Catalyzing Change: ESG Integration in the Global Economy for a Resilient and Responsible Future

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Abstract

Considering the global state of the current economy we can notice a slowdown across both developed and developing countries, most of them facing the risk of recession.

This paper aims to explore the intersection of ESG, and the pressing challenges confronting the global economy. The article will emphasize the significance and urgency of addressing these challenges to foster sustainable growth and resilience. The study seeks to analyze potential benefits that the integration of ESG norms can bring to the global economy and highlight the reasons why it has become so crucial. The research methods employed provide an overview of the key issues with the greatest impact that are shaping the present global economy as well as how ESG - Environmental, Social, and Governance factors have emerged as catalysts for change by mitigating risks, capitalizing on opportunities, and driving long-term value. The findings of this study serve as a foundation for developing more viable and resilient practices, enabling informed decision-making, and ensuring the long-term sustainable growth of the global economy overall.

Key words: environmental social governance (ESG), climate change, global economy, technology, sustainability
J.E.L. classification: M14, M16, M48, F01, F21

1. Introduction

There are multiple issues shaping the present global economy but the ones with the biggest impact, there are COVID-19, digital transformation, climate change, global trade tensions, protectionism and the matter of inequality and social justice.

Transformative effects of emerging technologies in the present global economy such as automation, AI artificial intelligence, and blockchain have the potential to transform industries, the labor market and improve productivity.

The global economy is undergoing a transformative phase, influenced by a growing emphasis on Environmental, Social, and Governance (ESG) considerations.

Considering ESG – environmental, social, governance as a catalyst of change refers to the fact that integrating ESG factors is no longer just a matter of corporate social responsibility rather it became a strategic imperative for businesses and investors alike. By aligning their financial goals with sustainable practices organizations can reduce risks, seize opportunities, and drive long-term value creation.

Through ESG programs we can help businesses grow, attract new investors, increase, and maintain their customer's loyalty, and entirely transform their operations by making them more sustainable resulting in gaining a competitive edge.

2. Theoretical background

Due to the climate change phenomena that happened worldwide, people started to become more responsible and aware of the role of ESG. Although there is still a big gap between believing in its benefits and implementing it within organizations. While some studies have suggested its positive long-term benefits such as increased rate of attracting new investments, enhanced reputation, brand value, innovation, and competitive advantage, there is still a need to better explore the benefits. This study aims to address this gap and provide a more comprehensive understanding of the opportunities and benefits it can bring to the global economy.

This research draws attention to how to manage crisis damages to create a more sustainable future and growth.

According to McKinsey & Company (2022) resilience is part of the key to success as it said back in 2022 “Resilience should be seen as the ability to deal with adversity, withstand shocks, and continuously adapt and accelerate as disruptions and crises arise over time” (Brende et al, 2022). They see the actual crisis as disruptions that are pushing us to a global transition to a low-carbon emission economy.

A study made by GSIR (2020) – Global Sustainable Investment Alliance gives us a short overview of the rising trend of investing in sustainability and the impact of these investments on the global economy.

The World Bank reports, and live graphics are also important references showing us the importance of ESG integration and how can it contribute to a better sustainable future.

Even if we report more granularly than the global economy and look a little towards the European one, there are data that indicates the good performance of ESG implementation. Thus, according to the statistical data available at the EFAMA (2021) - European Fund Asset Managers Association level, at the end of the first quarter of 2021, the most performant companies are those who aim to fulfill the best they can, the ESG criteria. Along with these companies, another type of business with high performance and profits is the investment funds that invest in these companies.

ESG factors encompass a range of environmental, social, and governance considerations that can affect the long-term performance and sustainability of businesses. Environmental factors include issues such as climate change, resource depletion, and pollution. Social factors encompass labor practices, human rights, community engagement, and diversity. According to Inderst G, Stewart F, (2018), governance factors refer to the structure, transparency, and accountability of corporate decision-making processes. ESG integration involves systematically incorporating these factors into investment analysis, decision-making, and risk assessment processes.

Studies have shown that the integration of ESG can lead to better financial performance, risk mitigation, increased stakeholder trust and enhanced brand reputation.

Regulatory frameworks and reporting standards, such as the United Nations' Principles for Responsible Investment (PRI), the Global Reporting Initiative (GRI), and the Task

Force on Climate-related Financial Disclosures, TCFD(2022) has played a crucial role in driving the adoption of ESG practices. Institutional investors, including pension funds and asset managers, have also recognized the importance of ESG integration in their investment strategies, leading to a growing demand for ESG-related products and services.

Despite the progress made until now, there are still challenges that remain to achieve integration at a global scale. These include issues such as quality standardization of reporting frameworks, data availability and the need for robust impact measurement methodologies. However, all these challenges also offer opportunities for innovation and collaboration among stakeholders to develop and implement more effective ESG integration practices.

3. Research methodology

The research methodology used to approach ESG integration in the global economy for a Resilient and Responsible Future is the type of mixed methods research combining both qualitative and quantitative elements. During the research were collected and analyzed both numerical and non-numerical data to gain a comprehensive understanding of the research question. Approach which helped in triangulating findings and providing a complete picture. Qualitative research helped for a better understanding and interpretation of social phenomena from a more subjective point of view. Meanwhile, quantitative research was based more on the collection and analysis of data which are helpful to answer many questions and hypotheses.

It was also based on studying different in-depth interviews with key stakeholders, such as industry experts, corporate executives, investors, policymakers, and representatives from non-governmental organizations – NGOs. The interviews explored their perspectives on ESG integration, the challenges faced, the strategies employed, and the potential for catalyzing change.

There was collected quantitative data from different sources including reports from different reference companies, financial databases and agencies specialized in ESG ratings.

The research was conducted following ethical guidelines and principles. All the information given in this paper is public information that can be revealed to the public. It adheres to ethical standards of data collection, analysis, and reporting.

The used research methodology provides a comprehensive understanding of the catalyzing effects of ESG integration in the global economy. It allows for the exploration of stakeholders' perspectives, the identification of challenges and strategies, and the examination of the relationship between ESG integration and financial performance.

4. Findings

4.1. Most important issues which are shaping the global economy

According to OECDiLibrary, (2021), what was known as the famous COVID-19 pandemic continues to have a major negative impact on the global economy. Among the major problems created, there is disruption of the supply chains which led to a lot of frozen industries and permanently closed businesses, which in the end, caused severe economic contractions in many countries. The recovery and long-term effects of the pandemic remain uncertain, posing challenges to global economic stability and growth.

Digital transformation is reshaping the global economy as well. Technology is advancing at lightning speed worldwide, especially in areas such as AI artificial intelligence, process automation and digital platforms that are completely transforming industries and the way of work. While at first sight digital transformation must seem like a huge opportunity for efficiency and innovation it also has a more controversial side and raises concerns about job displacement, income inequality, and data privacy. Managing digital transformation and ensuring its benefits are widely shared are pressing challenges for the global economy.

Addressing climate change and promoting environmental sustainability is also a critical global issue. There is an urgency of transitioning to a low-carbon economy and to do so we need to reduce greenhouse gas emissions and adapt to the impacts of climate change. The impacts of climate change such as extreme weather and increased sea levels pose risks to economies and societies worldwide. Certainly, a good way to fight all this is by investing in sustainable practices that can create economic stability and resilience.

Trade tensions between major economies, such as the United States, China, and the European Union, have escalated in recent years. The imposition of tariffs and trade restrictions has disrupted global supply chains and created uncertainty for businesses. Protectionist measures and trade disputes pose risks to global trade, investment, and economic cooperation.

Social inequalities, including income disparity, gender inequality, and access to education and healthcare, continue to be pressing global issues. Addressing these inequalities is not only a matter of social justice but is also essential for sustainable economic growth and stability. Promoting inclusive growth, reducing poverty, and enhancing social mobility are key areas of focus for policymakers and organizations.

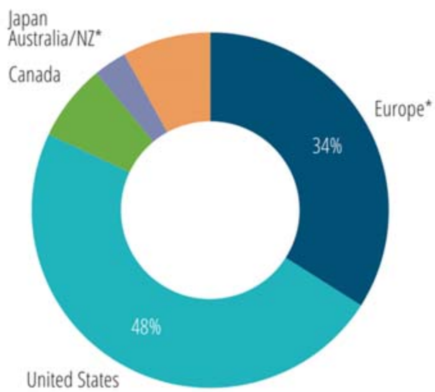
4.2. How does ESG impact the present global economy?

In the last couple of years, across industries, geographies and company sizes, organizations have allocated more and more resources toward improving their ESG standards.

According to Pérez L, Hunt D. V, Hamid S, Nuttall R, Biniek K (2022) nowadays more than 90% of the S&P 500 companies such as Amazon. Microsoft, Nvidia, and Apple are publishing their ESG reports and making reporting either mandatory or under consideration.

The popularity of ESG which has become a hot topic across the globe, has become more evident in investments as well. Even though the rate of investments has recently been decreasing, inflows in the sustainable investment funds have increased from $5 billion in 2018 to almost $70 billion in 2021 and gained nearly $120 net billion after the second quarter of 2022. In the middle of 2022, the sustainable assets were about $2.5 trillion.

Figure no. 1 Proportion of global sustainable investing assets by region 2020



Source: Global Investment Sustainable Alliance

"While historically ESG investing was regarded as a niche category, there has been a dramatic shift toward mainstreaming ESG integration and engagement in the last few years" (Garrett R.H et al 2020). The environmental component of ESG and the responses to climate change across the globe have played a major part in ESG's popularity. Apart from these 2 aspects, the social dimension was another component that has been gaining prominence. Also, the war in Ukraine and the human tragedy that followed as well as the entire geopolitical and economic aspects that came next helped the ESG importance to reach its peak.

As Lawder D. (2023) reported in Reuters, it is IMF that warns about geopolitical fragmentation that could raise financial stability risks and reduce cross-border investment and asset prices.

Another point of interest is the specific present issues resulting from the convergence of the global economy and ESG with a focus on key challenges faced in different sectors such as energy transition, responsible supply chain management, board diversity and corporate governance, labor rights and climate risks.

- Energy transition – A significant high-interest issue is represented by the transition to a low-carbon and sustainable energy system. Now the global economy relies on fossil fuels which have a huge negative contribution to climate change. The shift we need to take towards renewable energy resources, decarbonization and energy efficiency poses real challenges regarding infrastructure investments, technological progresses, and policy frameworks. Although the need for economic growth exists, balancing it with the need to mitigate climate change is a huge challenge for both the global economy and the energy sector. However, according to (UNFCCC Paris Agreement) by the year 2030, sectors responsible for more than 70% of global emissions could witness the competitiveness of zero-carbon solutions.
- Responsible supply chain management – Supply chain management is important to achieve business objectives. Though, responsible supply chains became a matter of interest as much as supply chains have become increasingly complex and globalized. They started to raise a

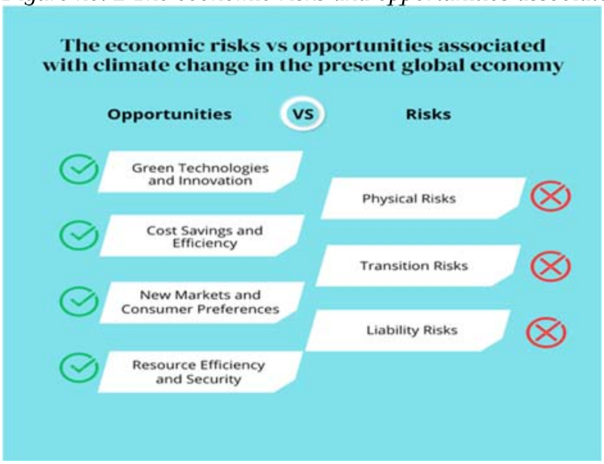
series of concerns regarding environmental and social impact, issues such as human rights abuses, pollution, deforestation, and child labor becoming the main reason that generated the need for responsible supply chain management. That's how ethics has become an increasingly important aspect of supply chain management, so much so that a set of principles called supply chain ethics was born. Ensuring transparency, traceability, and ethical practices throughout the supply chain is a pressing challenge businesses must face with. They also have the task along with the suppliers to identify and address sustainability risks and to promote responsible practices.

- Board diversity and corporate governance - According to Landaw J, Barington Capital Group LP (2020), board diversity and effective corporate governance are crucial for ensuring accountability, transparency, and long-term business success. The lack of diversity in corporate boardrooms, particularly in terms of gender and ethnic representation, remains a persistent issue. Enhancing board diversity and promoting inclusive decision-making processes can bring fresh perspectives, improve risk management, and enhance business performance. Strengthening corporate governance practices is essential for maintaining stakeholder trust and fostering sustainable economic development. Also, studies have shown that diverse personal experiences such as living or working abroad can bring new perspectives, higher productivity, and greater creativity. That's why companies should improve gender, racial and ethnic diversity on their corporate boards.
- Labor rights – As I already mentioned above, labor rights, fair wages, and decent working conditions are integral components of the ESG agenda and are an important issue of the present global economy. As Bourgeot R, Devine M, Panitsas K, Andretta C, Klaas de Vries, (2023) showed us in a paper, numerous challenges persist globally including forced labor, inadequate treatment of workers, and poor worker protection. Creating a proper balance between economic growth and respect for labor rights requires businesses to prioritize employee well-being, have a fair recruiting process, and maintain close relationships and a good dialogue with labor unions and advocacy groups. Respecting labor rights is essential for economic growth.
- Climate risks (Bloomberg M R., TCFD Status Report 2022) – Depending on the activity profile, climate changes can become a significant financial risk for both businesses and investors. Extreme weather conditions, natural calamities, and lack of resources along with risks associated with shifting regulations and market preferences can impact the stability and growth of a company. Assessing, identifying, and managing climate-related financial risks and incorporating them into decision-making are critical challenges for businesses or any financial institution.

4.3. The economic risks and opportunities associated with climate change in the present global economy

Like any change in the world, climate change presents both economic risks and opportunities and to address and overcome all the challenges the transition to a low-carbon economy by managing resource scarcity and adopting sustainable development practices is required. In the lines below we will explore the economic opportunities and risks associated with climate change and what sustainable practices can we adopt to overcome the risks.

Figure no. 2 The economic risks and opportunities associated with climate change



Source: Author's own elaboration

Among the major economic opportunities, there is to mention:

- Green Technologies and innovation. Opportunities for the development and adoption of green technologies, renewable energy, sustainable infrastructure, and energy-efficient solution are created by the transition to low-carbon economies. This is also an opportunity that can create new industries and generate more jobs.
- Cost Savings and efficiency. The development of sustainable practices such as energy efficiency measures, waste reduction and resource optimization can lead to cost savings for businesses worldwide. To reduce the dependence on volatile fossil fuel prices and to be able to provide long-term cost stability investments in renewable energy are examples of good practices.
- New markets and consumer preferences. To start driving demand for eco-friendly products and services, growing awareness, and concern about climate change among consumers is a must. We can already see that for businesses that are embracing sustainability and offer low-carbon alternatives, it is easy to tap into new markets, attract environmentally conscious consumers and build brand loyalty.
- Resource efficiency and security. What presents challenges but also drives innovation is resource scarcity, including water scarcity and raw material shortages. The adoption of sustainable practices that can optimize resources and reduce waste can mitigate risks from scarcity, improve long-term resilience and enhance resource efficiency. Resource scarcity, including water scarcity and raw material shortages, presents challenges but also drives innovation. Adopting sustainable practices that optimize resource use and reduce waste can enhance resource efficiency, mitigate risks from scarcity, and improve long-term resilience.

Among the major economic risks, there are:

- Physical risks. Extreme weather events such as hurricanes, floods, and droughts are results of climate change that can damage infrastructure, disrupt supply chains and lead to increased insurance costs and business interruptions.
- Transition risks. According to Thesing G (2023) article about the green investments made by global leaders, we can remind of the industries heavily reliant on fossil fuels which are at high risk due to the transition to a low-carbon economy. Considering all this, in the current global economy the profitability and competitiveness of businesses that fail to adapt are impacted by regulatory changes, carbon pricing, and shifting consumer preferences.
- Liability risks. If a company's operation contributes to climate change or if they fail to disclose climate-related risks to investors, they can face legal and financial liabilities. Lawsuits related to climate change impacts are on the rise, imposing significant financial risks on businesses.

4.4. Transformative effects of emerging technologies in the present global economy

Automation including RPA (robot process automation) had a big boom in the past couple of years. We all know the incredible story of UiPath the first Romanian unicorn back in 2018 that provided a platform that allows organizations to automate repetitive and rule-based tasks through software robots or bots. Overall automation technologies including robotics and process automation offer various benefits such as streamlining operations, cost reduction, and enhance productivity in multiple industries. One of the biggest benefits of automation is that it can produce repetitive tasks with higher precision than a human could ever do, freeing up human workers to channel their abilities on more complex and creative work than simple repetitive tasks. Among the industries that are already experiencing the biggest effects of automation, we can mention manufacturing, transportation, and logistics. Reskilling programs and lifelong learning initiatives become crucial to equip the workforce with the necessary skills for the evolving job market.

AI with its capabilities of automating processes, improving efficiency, and enabling new business models is revolutionizing industries worldwide. According to an article by Katzenstein K, Newman B, Robin J. S, Wilson J, (2023) 75% of companies already use AI tools and technology especially for HR purposes.

When we are thinking about the labor market AI artificial intelligence is the one reshaping it from scratch by automating routines and repetitive tasks. While some might think that this is leading to job displacements in some areas which is completely true it is also to consider that at the same time is leading to new job opportunities that can replace the old ones. AI trainers, explainability experts, and data scientists are just a few examples of new roles that will be in high demand.

Taking into consideration OECD Background report for the Canadian G7 Innovation Ministers' Meeting, (2018) blockchain technology is another important pillar that creates new job opportunities in the labor market in areas such as blockchain development, security, and governance. Regarding blockchain technology, there is also a huge gap between industry-specific requirements and technical knowledge that can be filled by people with experience in blockchain technology.

It has the potential to transform industries such as healthcare, supply chain, and finance by enabling secure and transparent transactions, eliminating intermediaries, and reducing costs. It can also enhance traceability and accountability by providing an immutable number of transactions.

4.5. European Union legislation on sustainable investments

According to the declaration of Popovici. D (2022) for the Wall Street Journal, with the advent of EU Regulations UE 2088/2019, ESG investments are growing exponentially as more and more investors and issuers use ESG tools and climate data to inform their decision-making investments.

Therefore, we can observe that the ESG stock indices performed better than the general indices of the market in the last 5 years. The big problem in making sustainable investments is given by the lack of information related to this topic. Under these conditions, several external data providers have emerged covering a number important of listed companies that have a significant input in the provision of relevant information about these companies.

One such data provider is MSCI, through its MSCI ESG Ratings service. Of course, besides this, there are other providers of ESG data. MSCI ESG Ratings are designed to help investors understand risks and ESG opportunities and integrate these factors into the construction and management process of their portfolio.

Graphic no. 1 S&P 500 ESG vs. S&P 500

Source: wall-street.ro

Graphic no. 2 MSCI ACWI ESG Leaders vs. MSCI ACWI

Source: wall-street.ro

5. Conclusions

In conclusion, ESG integration in the global economy has emerged as a catalyst for change, offering the potential to drive sustainable development, resilience, and responsible business practices. By considering the theoretical foundations and key concepts discussed in this paper, researchers, policymakers, and practitioners can better understand the importance of ESG integration and its role in shaping a more sustainable and responsible future.

ESG integrations also drive significant opportunities for promoting sustainable development, addressing societal challenges, and fostering responsible business practices. The research conducted underscores the importance of recognizing the business case for ESG integration, establishing robust regulatory frameworks, addressing challenges, and promoting stakeholder engagement. By integrating it, businesses and society can work together towards a resilient and responsible future, creating value for both present and future generations.

Technological progress also becomes an important factor that is reshaping the global economy and plays a significant role in catalyzing change and enabling ESG integration. Technological innovations are driving the development and adoption of sustainable solutions such as renewable energy technologies, energy-efficient systems, smart grids, and circular economy models.

All these progresses especially advancements in transportation, infrastructure, clean energy, and the optimization of resources are helping businesses worldwide to reduce their environmental impact and enhance sustainability.

Meanwhile, automation, artificial intelligence, and machine learning algorithms are not only reshaping various industries of the global economy, but they can efficiently analyze ESG data, identify patterns, and generate insights for decision-making. This enables both businesses and investors to make more informed and data-driven decisions.

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