

## Looking Forward: Intergenerational Equity

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By Arthur Heinmaa, CFA, Chief Investment Officer

The last time I saw Peter Drucker, the founder of modern management, speak he made a comment that has stuck with me for decades - institutions are getting to be such large investors that they have no choice but to care about the companies they invest in. Inadvertently, he foreshadowed the eventual growth of ESG (Environmental, Social and Governance) investing. He argued that if a large sovereign wealth fund decides to sell its holding in a particular stock, for example, there are very few large investors that are able to buy a block of that size. Given the small pool of potential buyers, the eventual owner cannot simply assume that they can liquidate their position easily so they have no choice but to take an interest in how that company is run. As a result, investors become more like agents of change than passive observers. This idea has taken hold and now institutions are paying attention to ESG issues lest investors like Blackrock vote their proxies against management.

So the question is; what is the next evolution in corporate governance, ethics or values that will likely take hold in the future? We believe the next evolution will be towards incorporating intergenerational equity into both governance and investor expectations. Intergenerational equity is not a new concept but it has reasserted itself as populations start to focus on global climate change. This change in focus will not happen instantly but the incorporation of this concept into mainstream discussions will likely grow. As a starting point, the following describes the concept and the areas where this thinking will likely have an impact and where investors might look for opportunity.

The idea of intergenerational equity stems from the belief that future generations have rights in today's world. Setting aside the debate of whether someone who has yet to be born has any rights, consider for a moment the perspective of a parent. Many of us that are reaching, ahem, a certain age start thinking about the impact of the decisions we make today on future generations. Should my generation consume all of a particular resource and leave nothing for my descendants? Should future generations have rights to

clean air, water, and a stable environment? It seems that there is a subtle shift taking place over believing that we have a dominion over nature to the view that we are current custodians of our resources. There are two areas where this change will assert itself.

The first is national debt, a concept that is fraught with political partisanship. In general, the sound bite used by politicians and the press is that we have no right to pass on this tremendous debt burden our children. The issue of government debt dynamics is beyond the scope of this commentary but consider the following arguments. By choosing not to spend in order to balance the books, we are unconsciously making the decision to pass on deferred maintenance and a crumbling infrastructure to the next generation. Is that an appropriate result from the perspective of intergenerational equity? Moreover, if the cost of fixing the infrastructure has a real cost (after inflation) of less than zero, wouldn't that be a wise investment for future generations? If we are indeed the custodians of the economy for future generations, the decisions we make today have big implications for those unborn generations ahead. It is too simplistic to say that by balancing the budget and paying down the debt we are providing a meaningful inheritance to our children. There are other nuances to be considered to make an appropriate long-term decision.

Second is the issue of the environment and climate change. To what extent does the future population have a right to a stable environment and should their rights be explicitly recognized in today's policies? This issue is of particular interest because of the implications of the Intergovernmental Panel on Climate Change report issued this past August. The report concludes that if we take aggressive action now,

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climate change will be limited to 1.5% by 2050 and then decline thereafter. Essentially, if we make sacrifices over the next 30 years, the benefits will only start in the decades following. For anyone who has been involved with a condo board trying to make decisions today that will benefit owners after the current tenants' death, you will know it is a tough sell. So too will it be difficult for today's population to make sacrifices when they see no apparent benefit in their lifetime. It will likely be a battle between the rights of today's population to continue to produce externalities and the costs of which the next generation will bear.

Reframing the issue in terms of intergenerational equity gives voice to our future generations in today's policy debates and shifts the discussion from rights to obligations. What kind of obligation do we have to protect the commons for future generations? It was easier several hundred years ago where the tragedy of the commons was dealt with by enclosing your property from your neighbours. Unfortunately, this solution will not work today because the commons is not a piece of land but the air we breathe and the climate we share. The solution will require effort at all levels of society and some sacrifice. Hopefully the upcoming United Nations climate change conference in Glasgow will see some material forward progress.

We remain optimistic that these large complex problems will be addressed. We know that many of you share that belief and continue to ask how to best invest your portfolios to participate in this massive change and how to make an impact through investment choices. To this end, we have created both a concentrated energy transition portfolio and an impact investment portfolio, both of which should benefit as the world grapples with intergenerational equity.