

THE DAILY CHECK-IN WITH GOLDMAN SACHS

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LIZ BOWYER: Hi John.

JOHN GOLDSTEIN: Hi Liz.

LIZ BOWYER: You're Head of the Sustainable Finance Group, which is responsible for expanding Goldman Sachs' capabilities when it comes to inclusive growth and the climate transition. As we near the end of 2020, what are some of your biggest takeaways this year?

JOHN GOLDSTEIN: Well, you know, I think the biggest is really that this is a field, sustainable finance, ESG, environmental social governance investing, that got a stress test, inarguably a stress test it needed, and it passed. Right? Heading into the end of 2019 there was a lot of enthusiasm, but there was a lingering question: is sustainable finance, is this growth in ESG a bull market luxury? And importantly, what will happen when times get tough? Right? Will it melt? Will this fade away?

And in Q1 times got tough. And ESG really held in quite, quite strongly. I mean, just for instance, in the first quarter, 44 percent of ESG funds were in the top quartile relative to peers. 11 percent in the bottom quartile. 24 out of 26 ESG passive options outperformed their active counterparts. And significantly, the biggest driver of that wasn't, say, an energy underweight or a tech overweight, although those helped. It was actually security specific backers.

Then the question was, could it keep up that performance during a recovery? And it did. Right? And so, year to date really what we're seeing is, you know, 40 percent or so of ESG funds are in the top quartile, about ten percent in the bottom quartile. You know, I was talking to someone at BlackRock the other day, 94 percent of their passive options have outperformed, the ESG versions, have outperformed their non ESG counterparts. So, that performance was really rewarded with flows. And assets momentum really continued. And year to date, ESG equity funds have gotten

120 billion of net inflows. Non-ESG have had 125 billion of net outflows. In the passive market, the market share of ESG for inflows into passive instruments has grown from 1 percent in 2017, 3 percent in 2018, 14 percent in 2019, to almost 40 percent year to date.

LIZ BOWYER: And what about the S in ESG? We've heard many times on this show that 2020 is the year that the social part of ESG really took hold.

JOHN GOLDSTEIN: Yeah. And you know, I think it's interesting in the sense of when David Solomon announced our \$750 billion sustainable finance target in December, we laid out these two pillars: climate transition and inclusive growth. And you know, people were happy about the announcement. But we got some questions that, we understand the climate transition pillar. But inclusive growth, is that really going to be a significant factor?

And we find ourselves almost a year later having worked to navigate a health crisis and an employment crisis, you know, very visible manifestations of continued racial inequity in the US. And this continued focus as the world has really become, frankly, much more aware of the importance of the inclusive growth side of the work. And so, it's interesting, no one's asking us now why we have both of those pillars as we come to the end of this year.

LIZ BOWYER: So, as inclusive growth has become more prominent, does that mean that climate transition is taking a backseat?

JOHN GOLDSTEIN: Yeah, that was interesting. One of our senior leaders, we were talking about this, you know, in the middle of the year. And said, "Okay, so has E taken a backseat to S?" And I think the way we describe it is S climbed into the front seat with E.

Environmental considerations haven't slowed down one bit. And in fact, in some ways they've accelerated. And we've seen this from companies, the important, ambitious pledges from companies as diverse as, you know, BP, Walmart, Apple, and Google that have significant impacts up and down their supply chains. We've seen countries, you know, net zero targets on a national basis from China, from South Korea, from Japan. And investors making pledges around their portfolios and how their focus on climate is growing and accelerating. And we, certainly, have seen the

same thing in our investing in terms of, you know, creating new products, making investments to accelerate this across our portfolio. So, I think it's certainly not that environmental considerations have receded. But I think the social plank of this has really risen to take its due next to the climate transition pillar of our work.

LIZ BOWYER: So, you mentioned conversations that you're having with corporate leaders and investors across the spectrum about what the ESG evolution means to them. What sort of advice are you giving them, maybe starting with investors?

JOHN GOLDSTEIN: Yeah, look, we're really lucky because we get to spend time talking to people, really, across this chain from companies to asset managers to asset owners. And for investors, I think what's interesting is, look, the statistics we talked about earlier, if this is where money is going into active management and is a growing share of passive management, it's clear why for investors this is a significant focus, but the question is what to do. I think we see a couple of key steps. I think, number one, you know, really is there's a lot of noise, a lot of jargon and really a lot of preconceptions about this that get in the way of having a real investment conversation. Sometimes it almost feels like a philosophical conversation.

So, we say a critical step is clearing the underbrush. You know? Recognize that to some degree, some people are too predisposed to love sustainable financing and ESG. And some people are too predisposed to not like it. That, in our view, is not a constructive way to approach the investment question side. Let's roll up our sleeves, let's look at the data, and let's think. So, clear away the underbrush that gets in the way of having the right conversation.

I think the second thing is that right conversation for us is grounded really in what we like to say is hopefully a post acronym world. It's not about E or S or G. It's about why this matters economically. And for us, we break it down now into the acronymic elements. But into the levers of economic impact in terms of risk, growth, or efficiency. Right? Losses, growing the top line, or margins. And I think grounding in this thesis, and for us we talk about where the world is going, the secular themes that are increasing to have an impact on companies, the economy, and on markets, investors need to do the same on theirs. What is their thesis? And then you do what we do with any other important investment question, you roll up your

sleeves and you do the work.

LIZ BOWYER: So John, a key question for investors is whether this surge in ESG is driven by the market, or if it reflects part of the real economy. What do you think?

JOHN GOLDSTEIN: I think that's a centrally important question. And frankly, one that gets glossed over. It's why I talk about my aspiration for a post acronym world. Because I think one of the things, and we went through our own analysis, we had to do this, right? The first question I got was, is there something real here? Right? Or is this just caving to investor preference?

And when we did our analysis and looked under the hood, what we found are the drivers underlying this are more diverse, have deeper ties to the real economy, and intersect with each other in ways that gives us comfort that these trends, these themes, and the underlying economy are significant and are going to continue to grow.

So, for example, employees. Right? You know, people talk about investor preferences, but they don't talk as much about employee preferences. I talked to a CFO of a company recently. They on board 100 new people a day. And they said even a 2 percent change in their retention rate for employees makes a massive economic difference. And what do their employees care about? They care about sustainability. They care about how the company conducts itself. And so, employee preferences in the war for talent matters tremendously.

Number two, corporate preferences. You know, when a company like, as I said, say a Walmart, makes a supply chain pledge to be net zero, whether you have a carbon target or not, if you want to sell your products to Walmart, congratulations, in effect you have a target. We see these pledges up and down the supply chains that affect for more than just the companies making the pledges themselves.

We see governments getting into the action in terms of things like Green New Deal in Europe. You know, and what's important is all of these interact. Right? When you have individuals, not just as investors but as consumers buying different things, as employees wanting to work for different kinds of companies, when companies themselves make commitments that stretch up and down their supply chains, and that gives a hook for government to build on. That gives a resilience of these themes not just in

markets, but in the real economy.

LIZ BOWYER: So let's talk more about corporates and the conversations that you're having with them.

JOHN GOLDSTEIN: Yeah. You know, for corporate clients, there's an important, but not always easy transition of these issues. In some cases it's on the periphery to the core, right? And right now, we like to say sometimes this field is in its adolescence. It's growing fast. It's awkward. And there are a whole lot of pain points. And frankly, those pain points didn't matter much when this was marginal. But with the growth, with the assets, with the focus on it, those pain points are, in fact, painful. This society is not academic.

And so, for companies the challenge is several fold. Number one, don't be distracted by the noise. There are labels and ratings and reportings. I talked to one CFO recently who'd been asked for 2,000 different ESG data points in the last 12 months. So, the key thing there is to realize the swirling mess of scores and rankings, that's not how you're going to win. The key is to make sure you don't lose. And do that by focusing on a smaller number that are more important. And they're not always what you think, right? Some are from commercial data vendors. Some may be small civil society groups that are very significant and influential with investors. So, step one, do the work to not necessarily win with the data and with the scores and with the rankings, but try to make sure you do the things to not be disadvantaged. You know? Don't lose there.

From there though, tell a real business story core to your strategy and integrated to your corporate purpose. Right? And in our case, we've gone through the same process. Our purpose is sustainable, economic growth and financial opportunity. Underneath that we see these two core pillars: climate transition and inclusive growth. And there are three tools we have to pursue that - what business we do: our products and services. How we do it: our people, our organization, our culture, our operations. And how we tackle the things we can't do on our own: philanthropy, partnerships, collaboration.

And so, companies need to find their version of that. What does it look like to have something tied to your purpose and core to your strategy at the center of your business? From there, tell that's try with numbers. Ideally numbers that tie to common credentializing frameworks, things like SASB, the Sustainable Accounting Standards Board. Or TCFD, the Task Force on Climate

Related Financial Disclosures.

And finally, find ways to lift it up and take something that on the one hand is deeply integrated to your core business, but lift it up and make it visible. And for some companies, that means investing their corporate cash with diverse broker dealers. For others, it could mean issuing a green bond, social bond, a sustainability bond. You know? A whole host of ways to take this deeply integrated thing and really lift it up for your investors, for your employees, and for your stakeholders to see.

LIZ BOWYER: So finally, John, just looking out to 2021, what's your outlook for ESG?

JOHN GOLDSTEIN: So, I think a couple of key things when we look ahead. I think, number one, you know, I talked about this, this data adolescence. I hope we make progress. Right? And I think there are some intriguing initiatives on the horizon. Things like the work that IFRS is doing to really figure out as we have different standards, different metrics, different acronyms for groups, how do we take that and converge? Because ultimately, we need a world where we have better data on fewer things that matter more, reported by companies. You know? Data and information is the life blood of markets. We need more of it. And we need it to flow freely. And I think, hopefully, we'll make real progress on that, I think, number one.

You know, number two, I think that to some degree people can get past the labels and get down to the real hard work of execution. Right? The day to day work of taking this strategic clarity about the importance of it, understanding the drivers, but then incorporating into the work and doing what you do with any other business investment question. You know? Work hard at it. You pick your head up from time to time, reflect on what you're learning. And get back to work and try to keep doing it better every day.

And I think, finally, that we're going to continue to lean into the hard to solve problems. Right? I think about the hard to abate sectors, you know, sectors that have really critical roles in the economy, but are hard to decarbonize. I'm thinking about, you know, basic materials, steel, the energy sector. And that we apply our creativity and ingenuity to come up with solutions. And really lean into those problems, lean in with those clients and help them on their journeys.

LIZ BOWYER: Thanks John.

JOHN GOLDSTEIN: Hey Liz, thanks so much for having me.

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