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ESG: the new global imperative

Keynote Address

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With climate change upon us, required regulatory emissions disclosures are just around the corner, and beyond the “E” of ESG, stakeholders are increasingly asking for transparency and good practice on Social and Governance aspects: ESG has swept investment markets in the northern hemisphere as a new way of guiding investment strategies. Trillions of dollars of investment funds flowing into ESG active funds can’t be wrong, with major firms such as BlackRock leading the global charge in this regard, to what they call “ESG Integration”.

Boards will need to decide whether to embrace ESG into their values and organisational purpose and seek to gain advantage from their actions, or to take a minimalist approach and merely comply, viewing ESG disclosure as a cost of doing business. No doubt we will see all positions on the spectrum between these extremes, yet there is now clear evidence that proactively pursuing ESG related improvements can lift performance, reduce risk, and engage stakeholders.

The evidence-backed case for using ESG as a force for competitive advantage is strong. When ESG is sound and indeed strong and improving, costs have been reduced, such as costs of packaging and energy consumption, customers are loyal, regulators are satisfied hence reducing “license to operate” risk, and investor attraction is raised. These benefits go well beyond what a “compliance only” approach brings to an organisation.

How are leading companies pursuing ESG-based advantages? First up is to rigorously acknowledge where they are starting from by doing a strategic ESG evaluation. There are two major problems that first need to be overcome. My research has shown that the multiple global standards in current use are overly bureaucratic and compliance oriented, and while they might improve over time, just as quality management standards did, it is possible to engage with the requirements of global standards and still be a poor performer on E, S and G. It is unacceptable that standards should have a low bar. The second problem with ESG and Sustainability reports is that many of them, often around 100 pages long, are poorly structured “show and tell’ reports of all the things that readers should marvel at, lacking a strategic connection or structured improvement approach.

It is possible to cut through the bureaucracy and focus on performance. We have adapted the American Business Excellence framework to the ESG domain, assessing and quantifying core elements of ESG, including assessing for each category in the illustrative example shown here, the depth, breadth, strategic alignment, learning and innovation of these elements.

For a world-leading manufacturing company, the summary shows the structure of their scores on a 1000-point scale. This company is a very high performing business and ESG is well integrated into its strategy, leadership, and all aspects of its practices, activities, operations and improvement initiatives. In contrast, I have evaluated a Chinese company that has grown remarkably quickly, that scored less than 200 on the 1000 point scale. Recently that company was censured by its home government and required to change its ways. A major bank in Australia that we evaluated scored right around 500. There is much to be gained by all that bank’s stakeholders once it implements initiatives that will get it to, and beyond, 600. These ESG category scores should be of high importance to boards wishing to de-risk and drive their organisation’s performance.

The key reason for boards to take a proactive rather than minimalist or compliance approach to its ESG profile, values, strategies and activities is that there is advantage to be gained from this! Nobody loses when stakeholders are engaged, emissions are audited and reduced, societal requirements are integrated into operations, and governance is sound. At best, an evaluation such as shown for a globally leading automotive company becomes the beginning of a long term commitment to ESG performance improvement: that is surely in the interests of boards, shareholders, customers, employees and suppliers, and in aggregate, society.

This quantitative evaluation must always be accompanied by a descriptive report, that qualitatively describes practices and initiatives, performance goals and recommended strategies for ESG improvement. ESG can only then become “mainstreamed” as part of the organisation’s values and strategies.

AutoCo: Summary scores

1) Planning and Leadership of ESG	**163 / 200 points**
1a) ESG within organisational values and strategic intent **1b)** Alignment of stakeholders with ESG approach **1c)** Senior leadership commitment and involvement **1d)** Planning for ESG progress **1e)** ESG throughout the organisation	32 / 40 points 30 / 40 points 31 / 40 points 36 / 40 points 34 / 40 points
2) Environmental Practices and Initiatives	**166 / 200 points**
2a) Lowering emissions and pollution **2b)** Reduced use of water/exhaustible resources **2c)** Preservation of natural environment, ecology **2d)** Contribution to reduction, recycling and reuse **2e)** Environmentally focused products/services, business models and processes	36 / 40 points 30 / 40 points 36 / 40 points 34 / 40 points 30 / 40 points
3) Social Practices and Initiatives	**145 / 200 points**
3a) Respectful treatment of stakeholders **3b)** Contribution to community wellbeing **3c)** Contribution to diversity and human rights	70 / 80 points 45 / 60 points 30 / 60 points
4) Governance Practices and Initiatives	**158 / 200 points**
4a) Board practices **4b)** Accountability and transparency **4c)** Ethical standards and Business Integrity **4d)** Executive and management structure/practices **4e)** Governance specific processes	32 / 40 points 26 / 40 points 30 / 40 points 36 / 40 points 34 / 40 points
5) ESG Results	**148 / 200 points**
5a) Leadership (of ESG) results **5b)** Environmental results **5c)** Social and community results **5d)** Governance results **5e)** ESG measuring and reporting quality	32 / 40 points 22 / 40 points 32 / 40 points 30 / 40 points 32 / 40 points
Total	**780 / 1000 points**

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