How **Sustainable** is your **Business?**

*Luke Manning & Andre Chanavat

If you go back to basics of what any business is trying to achieve, the first goal is survival and the second phase is to thrive sustainably.

Economic factors have always been, and will always be, the primary measurements of business success. After all, any business is sustained by generating and saving revenue. Most businesses have not been created with an altruistic purpose to improve the environment or social cohesion, and so in the bluntest of assessments the drivers of a business are not to focus on – or be driven by – these factors.

But if you look at the importance of addressing environmental, social or governance (ESG) issues in terms of economic impact to the company's long-term sustainable success, it is clear they are playing an ever-more important part.

A large part of this shift is due to the primary demands placed on businesses by wider groups – not just shareholders but employees, customers, regulators, industry bodies and society in general. In the US, the Business Roundtable recently changed its statement on the purpose of a corporation to incorporate these different stakeholder types.

Businesses can no longer afford to ignore environmental and social considerations, or not communicate about them. The impact an organisation has on the societies around them, the increased demand for transparency from customers to investors or employees, the fervent pace of technological innovation, and transitioning to a low-carbon economy are all mega trends.

The latter point is arguably the other key driver of the sustainability shift; the inescapable direction the world is moving in of de-carbonisation. The simple truth is the world will be powered, resourced and fed in a different way in the future. Only firms that have laid the foundations for surviving in this new environment will have any chance of surviving. Earlier this year Mark Carney, the Governor of the Bank of England, put it even more starkly, suggesting "'companies that dont adapt will go bankrupt without question."

This is a strategic change but sustainability can be assessed at a strategic, operational (external interaction) and tactical (internal interaction) level. Businesses rightly concentrate most of their time and resource into operational and tactical initiatives; this is what they control.

It is strong governance that underpins operational and tactical initiatives, and on this foundation there are ***five key pillars which determine the long-term viability, and sustainability, of a business: purpose, people, practices, performance and partners.***

The first of these, purpose, considers factors such as the mission of the business, its values, its reputation and ultimately the impact it has on society. Taking out values-based subjectivity on what a business does as 'good'; a successful business is a profitable one. And make no mistake, purpose can impact profitability.

Profitability depends on people or other businesses continuing to use their products and services, and having the ability to operate freely. Public, employee and political opinion can shift quickly and dramatically, and with it comes an impact to a business' sustainable success.

The environment in particular is a topic that is attracting considerable public, employee and political attention and businesses not seen to be on the right side of the debate are feeling the impact.

Just look at Amazon. More than 1,500 Amazon employees recently pledged to stage a 'walkout' protest against the company's environmental record - the first walkout by staff at Amazon's Seattle headquarters. Shortly after, Amazon CEO Jeff Bezos committed to making the company carbon neutral, and meeting the goals of the Paris climate agreement, by 2040.

For years choices have been taken by businesses to safeguard their reputations by adopting social positions in particular that are important to the stakeholder groups they serve – think issues such as pay, discrimination, diversity, human rights – but now environmental considerations are arguably moving to the top of the pile in terms of scrutiny, immediacy and pressure.

Environmental issues are deeply political, with different groups becoming more vocal, advocating the areas which impact their stakeholders the most.

But there are two key areas which have universal support – minimising pollution (i.e. everything from reducing greenhouse gas emissions through to stopping plastics choking our oceans and the wider food chain) and consuming less in a world of finite resource (i.e. halting land and sea degradation or biodiversity loss through to adopting a circular economy).

Regardless of individual or national stances on the environment, failing to adapt business purpose to reflect and support stakeholder attitudes to these trends will severely impact long-term business growth.

The second, and closely linked, sustainability pillar is people.

The ability to attract and retain the best talent is of course a key ingredient for any business' sustainable success, and is linked more inextricably to the values, culture and purpose of a business than ever before.

Environmental considerations, alongside the wider purpose of the organisation and how it supports local communities, are becoming increasingly important when people decide where to work – even, in some cases, beyond financial considerations.

The increased representation of Millenials and Generation Z in the workplace has seen a shift to an overall majority of employees now placing 'being dedicated to a cause' or feeling they are 'serving a greater good' as top career goals.

86 percent of millennials would consider taking a pay cut to work at a company whose mission and values align with their own, according to LinkedIn's latest Workplace Culture report.

These values form the beating heart of corporate culture and are represented through a myriad of factors, such a business' approach to diversity and inclusion, employee wellbeing, training, environmental impact and volunteering time to name but a few.

It could now be argued a greater emphasis on environmental and social considerations can give a business a competitive advantage just through the type of people it attracts and retains. The Refinitiv Diversity & Inclusion (D&I) index is a good case in point here, which measures relative performance against multiple factors that define diverse and inclusive workplaces. Blackrock has launched an exchange-traded fund (ETF) based on the index, and the Matterhorn Group at Morgan Stanley are first advisory team to use the D&I Index as an investment tool.

Interestingly, performance of the D&I Index is almost 10% higher over a five-year period than the S&P Global 100.

The next two pillars are also closely linked to each other – practices and performance – and this is where governance has a particularly critical part to play.

Practices relate to how a business structures itself, sets out its targets and frameworks, how it measures its impact and, crucially, what it discloses. Aside from simply being about strong corporate governance, which has long been considered a critical foundation for sustainable success, transparency has equally become a watchword for good corporate behaviour.

Transparency is a central tenet of sustainability – it creates accountability and provides the foundation for changing behaviours.

If you take an environmental lens, there is a steady shift towards mandating environmental corporate disclosures, alongside an increased prevalence of measures such as carbon pricing and taxing.

With an increasing number of disclosures and frameworks available (such as the Carbon Disclosure Project (CDP), Taskforce on Climate-Related Financial Disclosures (TCFD), corporate annual reports) the executive team and the board must have understanding and oversight of what is being communicated through voluntary and mandatory channels.

It's not just disclosure either where senior leadership need to factor in ESG considerations.

Failure to stay ahead of, and comply with, sustainability-related regulation and compliance will not only erode business competitiveness and stakeholder investment but ultimately impact profitability.

Different global regulation means that business response is evolving at varying rates in different regions - take India and the CSR 2% law as a prime example, where businesses with annual revenues of more than 10bn rupees (£105m) must give away 2% of their net profit to charity.

Performance, in the context of sustainable business, is a combination of establishing where the business is vulnerable in the transition to a low carbon economy, and also physically what is needed for it to perform day-to-day.

In the short-term, there are two sustainability truths which impact how a business uses its resources: the world is warming up and global population growth continues.

As the world warms, weather is becoming more unpredictable. More financial capital and human ingenuity needs to be reallocated to protect and mitigate against these changes.

It also means more resources, such as energy and water, are increasingly used in those attempts to stabilise the environment around us, whilst we continue to use the same finite resources to facilitate business growth. Over-use leads to scarcity, scarcity leads to premium prices. Premium prices again lead to capital expenditure or divestiture.

The questions businesses must now ask ourselves is how do we invest all resources with value, so they're not discarded? How do we operate more efficiently, keep more things in existence and avoid single-use of materials?

When it comes to sustainable performance from an economic standpoint, there is another sustainability truth: we must always remember the human impact. There will never be full global agreement, alignment or collective action on environmental initiatives unless there is a path to progress and prosperity along the way.

From a business perspective it means environmental and social factors should be considered as direct impacts to financial performance, rather than being considered alongside it.

The last pillar is partners, as businesses look beyond the boundaries of their own footprint, and into their wider ecosystem.

Businesses are reliant on a complex web of partners in the supply chain, including local communities and academia, to supply the talent and assets needed to 'keep the lights on' in their locations across the world. They need that eco-system of partners to also uphold the same pillars of sustainable success, otherwise the chain becomes more vulnerable. Big business has a key role to play in setting best practice examples to their partners, thereby creating a positive ripple effect.

Even though we at Refinitiv look at over 7,000 of the world's largest listed businesses representing more than 70% of the worlds market cap across 450 different ESG measures, the next level has to be influencing the behaviours and practices of the hundreds of millions private companies globally.

Our helps large listed businesses to understand the trajectory for sustainable success, by covering data points from carbon emissions to board diversity, to water usage. Equipped with these insights, the ESG dialogue companies are having can shift, not just with their stakeholders but with their partners too.

Data is just the beginning when it comes to shifting behaviour; it provides transparency and ultimately holds businesses to account. You need data to inform decisions, to focus action and to mobilise.

It's the first step in quantifying and codifying the recipe for success and shining a light on the ever-increasing importance of environmental, social and governance factors for the long-term health of any organisation.

So the one question that remains is, given this changing corporate landscape, just how sustainable is your business? ■

***Mr. Luke Manning** *is Head of Sustainability and Strategic Initiatives.*

***Mr. Andre Chanavat** *is Director of Product Management at Refinitiv, UK.*