Sustainable Business Practices: Managing Risk and Opportunity

A PwC Report by Andrew W. Savitz

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“Doing well by doing good” isn’t a new concept in business, but today it has taken on new meaning and urgency. The accounting and financial scandals that have rocked Corporate America underscore the connection between a positive corporate reputation and strong financial performance. Clearly, unethical or questionable business practices can cause customers to shy away and investors to flee. Not surprisingly, Wall Street is now concerned about what companies are doing to protect their reputations.

Increasing the pressure, a wide range of corporate stakeholders, from shareholders and investors to consumers and local communities, are starting to hold companies to a higher standard of corporate behavior. These stakeholders are focusing on sustainability—the long-term, overall impact of a company’s actions on the world. Key concerns include pollution, safe products and services, honesty in advertising, child labor, human rights, job creation, and the economic well being of host communities. As a result, companies are now examining the links between sustainability, reputation, and financial performance.

Sustainability: It’s Not Just About the Environment!
Why be concerned? Because, sustainability is a new, higher standard of performance that measures the social, environmental, and economic effects of business activities—the so-called “triple bottom line.” And because the Internet has intensified pressure to prevent “bad” corporate behavior. In a world where information is instantly available, bad news travels more quickly than ever. An incident in Peru, Portugal, or Prudhoe Bay can immediately reverberate throughout the global market place. Advocacy organizations with environmental, social or economic agendas are now experts at disseminating such information on the World Wide Web.

How well are American companies responding to this emerging challenge? Are they fully aware of the risks and liabilities they face if they fall short in satisfying these new standards of business behavior? To find out, PricewaterhouseCoopers (PwC) surveyed 140 large, U.S.-based companies in mid 2002. Of the respondents, 101 are listed in the Fortune 1,000; collectively, they account for approximately $2.5 trillion in annual sales. The largest study of its kind, the survey is both revealing and instructive.
The PwC 2002 Sustainability Survey

The single most important finding: Respondents are aware that the public now holds them even more accountable for their environmental, social, and economic activities—and their effects—but less than 30% have programs to systematically identify and evaluate these sustainability related risks.

The basic message: Companies without sustainability programs are flirting with disaster. A major misstep on a triple bottom line issue can have enormous ripple effects, ruining reputations and finances and endangering relationships with customers, suppliers, investors, and financial institutions. Despite this sobering reality, few corporations are responding adequately. Without a sustainability risk management program, companies are simply playing with fire. Other survey findings:

- 90% of the corporations responding indicated that enhancing and/or protecting their reputation was their primary reason for adopting sustainable business practices;
- 72% of those responding do not currently incorporate the risks and benefits associated with sustainability into their formal project and investment evaluations;
- 63% of those recognizing the link between sustainability and their corporate reputations are not assessing their potential risks and liabilities;
- 89% of all survey respondents expect that sustainability will grow in importance as a business issue over the next five years;
- 73% of those surveyed said they plan to begin issuing reports that measure corporate citizenship within the next five years, while only 32% do so today;
- 72% of the respondents rated the importance of sustainability to their companies as a six or higher on a scale of one to ten.

Emerging Risks and Liabilities

Our report also concludes that there could be serious downside penalties for failing to meet sustainability standards. The seven major financial and business risks identified are:

Lower stock prices and reduced shareholder value—shareholders and investors will withdraw financial support for companies based on perceived self-dealing, unfair or unethical behavior;
Loss or disruption of valuable customer and/or supplier relationships—resulting in lower sales and reduced operating capacity;

Project delays or stoppages—due to failure to anticipate and address community or regulatory concerns;

Labor unrest and disruption—based on workplace conditions or practices perceived to be unfair or exploitative;

Reduced access to, or higher cost of, capital—as a result of loss of trust and subsequent shareholder and investor flight;

Reputation-and-brand erosion—as a result of adverse public exposure and/or damages paid to shareholders or consumers for false claims, unfair labor practices, product liability/negligence;

Loss of operating freedom—as a result of disruptive government enforcement or litigation, based on environmental, workplace, or product safety issues.

Companies can take years to recover from such problems—and some may never succeed in weathering a major crisis in public and investor confidence. As noted earlier, recent events have underscored the close linkage between corporate reputation, financial health, and public perceptions of integrity or wrongdoing. As transparency and public trust become integral to a positive corporate image, the pressure to include sustainability guidelines in corporate reports will only increase.

Measuring Sustainability: The Global Reporting Initiative
One stumbling block to evaluating corporate track records on sustainability has been the lack of clear, consistent measurement tools. In 2002, this changed when the “Global Reporting Initiative” (GRI) was released at the World Summit on Sustainable Development in Johannesburg. The GRI offers a practical framework—a roadmap—for reporting the economic, environmental, and social effects of a company’s activities, products, and services. While not a code of conduct or a substitute for legal reporting or disclosure, the GRI is a powerful resource to help organizations assess their progress against sustainability goals, self-imposed standards, and voluntary initiatives.

Using the GRI will help a company identify and assess the actions it has taken to support sustainable development; the outcomes of those actions; and future strategies, projects, and goals. This type of comparable and consistent reporting offers many advantages. For example, it promotes:
• open, proactive communication on sustainability progress;

• ongoing dialogues with investors, customers, and suppliers;

• better interaction among internal functions, such as finance, marketing, and research;

• the use of early warning mechanisms to pinpoint trouble spots—or promising opportunities;

• transparency and financial stability; and

• recognition for corporate contributions to natural, business, and social capital.

The world business community is beginning to embrace the GRI guidelines and the United Nations’ endorsement of the guidelines in Johannesburg has increased the pressure on companies to use them and report the results. As the GRI gains wider acceptance, its value and precision will only increase. In addition, reporting frameworks designed specifically for major industry sectors are now being developed.

Good Corporate Citizenship: Real Business Benefits

According to our survey, sustainability isn’t a passing fad; it is rapidly emerging as a business reality. In fact, France and South Africa recently passed legislation that requires sustainability reporting as a precondition to being listed on their stock exchanges and the United Kingdom has appointed a cabinet-level sustainability minister. Today, many companies, especially in the United States, are grappling with the need to address sustainability issues directly and systematically. Understandably, concerns about risks and liabilities are center stage.

However, many leading companies are also looking at the upside opportunities that sustainable development offers—opportunities to open new markets, build strong labor pools, and reduce costs. Procter & Gamble, for instance, is researching ways to bring potable water to villages in Sub-Saharan Africa. Why? A high percentage of its products require clean water and until it is available, the African market won’t be viable.

As this example suggests, sustainability isn’t just about risk, it’s about value creation. Increasingly, corporate self-interest and major social issues will be intertwined. Sustainability represents a fundamental shift in how companies will be expected to conduct themselves. As you address this challenge in your own company, be alert to benefits as well as risks. Consider ways in which successful sustainable business practices can:
• protect your reputation and enhance brand value;

• strengthen internal and supplier relationships;

• build credibility and trust through increased transparency;

• reduce business exposure through crisis avoidance and stakeholder issue identification;

• decrease waste, emissions, natural resource use, and associated costs;

• increase innovation by proactively addressing high-impact issues;

• improve productivity and attract/retain top employees through high morale and open communication;

• support positive community relations.

Any one of these benefits can be vital to corporate well being. Taken together, they can help push your company to a new level of performance and profitability.

Andrew W. Savitz is a Partner in the Environmental and Sustainability Services group at PricewaterhouseCoopers LLP (PwC). This group specializes in strategic assessment, risk evaluation and the design and implementation of sustainability programs. The practice also provides traditional environmental services, including development of compliance-focused environmental management systems and litigation support. Andy has testified and provided support in a wide variety of environmental matters.

Andy has worked extensively on corporate governance, ethics, health and safety, consumer and communication issues. He was the Massachusetts General Counsel of Environmental Affairs and served as a staff member to the United States House of Representative’s Committee on Commerce, Consumer and Monetary Affairs, where he drafted legislation and organized hearings related to corporate governance, labor and consumer protection issues. He currently serves on the Steering Committee of the Harvard University, John F. Kennedy School of Government, Environmental and Natural Resources Program, the trustees of the Boston Zoos, and the Board of the Environmental League of Massachusetts.