SUSTAINABILITY REPORTING PART 4

A Compelling Case

BY
K. SADASHIV

In June 2016, the Singapore Exchange (SGX) joined other leading stock exchanges in requiring listed companies to issue a sustainability report annually. This move by the SGX recognises that sustainability has become a critical success factor for companies' long-term value creation, and the growing investor demand for transparency on environmental, social and governance (ESG) practices.

Understandably, companies that are new to sustainability reporting (SR) may view this as an added compliance burden. Many of them may be looking to put in just enough effort to meet the basic requirements.

The 2017 EY report, "Is your nonfinancial performance revealing the true value of your business to investors?" should convince businesses otherwise. The report found that investors have developed a greater appreciation for the value of ESG factors, as 68% said that nonfinancial information have played a pivotal role in their investment decision-making.

In that light, companies that seek to do the minimal for compliance sake may miss out on the benefits that SR delivers.

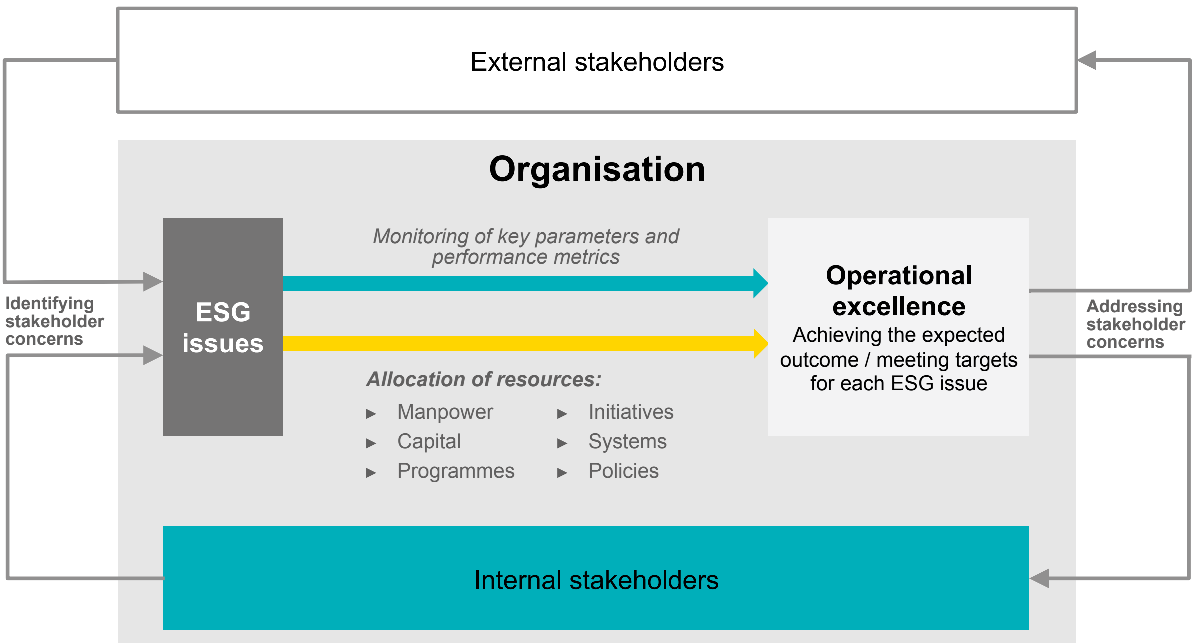
IMPROVE OPERATIONAL EXCELLENCE

SR requires organisations to gather information about processes or impacts that they may not have measured before. This new data can provide companies the necessary knowledge to improve their operational performance.

For example, through identifying stakeholder concerns, companies have a better overview of their ESG issues. They can then better monitor key parameters and performance metrics to align processes and allocation of resources to achieve the expected outcomes and targets for each ESG issue (Figure 1).

★
Sustainability reporting requires organisations to gather information about processes or impacts that they may not have measured before. This new data can provide companies the necessary knowledge to improve their operational performance.

Figure 1 SR provides good overview of a company's ESG issues



HELP INVESTORS MAKE INVESTMENT DECISIONS

Traditionally, investors have relied on financial information to gain insights into a company's performance, profitability and investment-worthiness. While financial information continues to be critical, it only tells part of the company's story.

With the Paris Agreement (COP21) entered in force in November 2016 and other stewardship codes being introduced, the pressure on companies from investors to report more consistent and verifiable ESG information is going to increase. Investors are seeking information that provides the confidence that management and the boards of their investees are thinking long term.

The heightened awareness of the impact of social and environmental practices makes the management of these aspects even more critical (Figure 2).

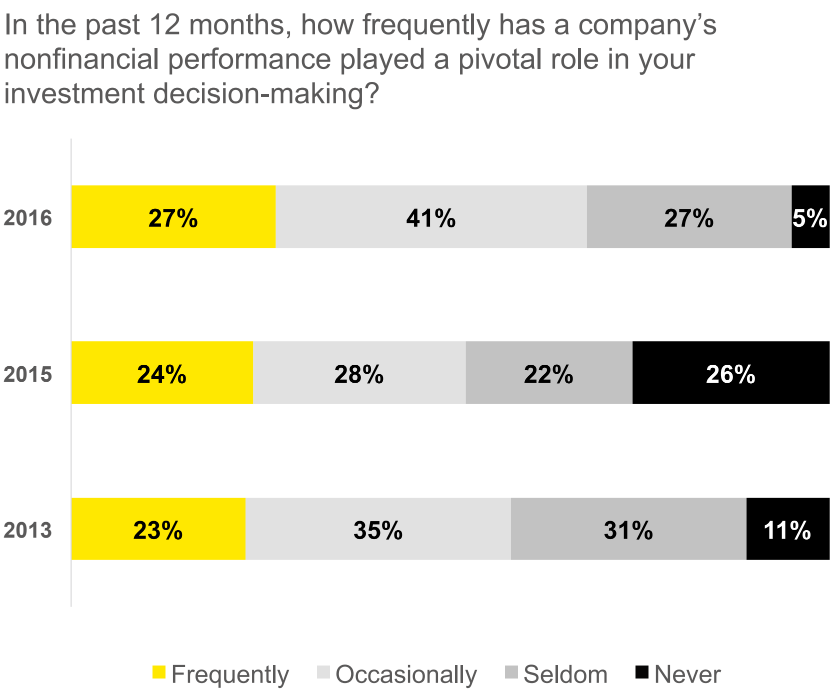
ACCESS SUSTAINABILITY-FOCUSED FUNDS

The introduction of the SR requirement by SGX can be seen as a proactive initiative to prepare listed companies for an emerging trend – responsible investing. Responsible investing incorporates ESG considerations into investment decision-making. In the US, ESG assets have almost doubled from US$4.8 trillion in 2014 to US$8.1 trillion in 2016.

★

A transparent approach towards disclosure of nonfinancial and ESG information will provide confidence to investors that the management of the business is astute and aware of the changing business environment and consumer demands.

Figure 2 SR focuses management/board attention on ESG practices



Through a sustainability report, companies have a platform to demonstrate their ESG credentials and attract investments from these funds. For example, in Singapore, City Developments Limited (CDL), which has been issuing an annual sustainability report since 2009, made its first foray into accessing these funds by launching Singapore's first green bond earlier this year.

ATTRACT TALENT AND REDUCE STAFF TURNOVER

Commitment to sustainability can also have a profound effect on the engagement and productivity levels of a company's employees. A good sustainability report that discloses employee welfare and development-related information is likely to be more attractive to talents in a competitive job market.

Research has shown that morale and loyalty at companies with effective ESG programmes are significantly

higher than those without or with inadequate ones. Those committed to sustainability observe a reduction between 25%–50% in turnover rates over time. In addition to lower turnover rates, responsible companies attract talents who are aligned with the company's motivations, which lead to a 3%–3.5% decrease in annual resignation rates.

BUILD CORPORATE REPUTATION

Three-quarters of the surveyed companies for the abovementioned EY report shared that corporate reputation was the top motivation for its nonfinancial and ESG reporting.

A consumer study by The Regeneration Roadmap, a collaborative and multifaceted initiative by GlobeScan and SustainAbility, found that two-thirds of the surveyed consumers in six countries, namely Brazil, China, India, Germany, the UK and the US, feel a sense of responsibility to the environment and society and would make their statements through their buying decisions.

A transparent approach towards disclosure of nonfinancial and ESG information will provide confidence to investors that the management of the business is astute and aware of the changing business environment and consumer demands.

ACHIEVE POTENTIAL INCREASE IN SHARE PRICE

Institutional investors surveyed by EY shared that they enjoy the recognition that comes when their firms are named in lists of ESG leaders or ESG-focused indices. Hence, these investors may be willing to pay a premium for stocks that are recognised for their ESG performance or practices. A 2012 study by the Harvard Business School also found that high-sustainability companies outperform their low-sustainability peers on return-on-assets and return-on-equity.

REPORTING QUALITY MATTERS

It is clear that SR is here to stay. Governments around the world have shown public commitment to sustainability through initiatives such as the United Nations Climate Change Conference, pushing ESG concerns to the fore of the global and national agendas.

For example, in Singapore, the government has committed to reducing greenhouse gas emissions intensity by 36% from its 2005 levels by 2030. This year, the Singapore government has also announced the introduction of a carbon taxation scheme, which will come into effect in 2019.

The current reporting requirements by the SGX builds a strong basis for disclosure, and provides recommendations on globally acceptable approaches to SR, as well as a practical reporting framework. In fact, the Small and Medium Capitalisation Companies Association has said that the reporting requirements are not too overwhelming, and give sufficient flexibility to companies in determining how they would prepare the report.

Having said that, companies must go beyond preparing disclosures solely with compliance in mind. The quality of SR is what will make a difference. SR can be a competitive differentiator but only if it is objective and transparent, and strives to address the material aspects that most concern stakeholders.

To that end, a quality sustainability report will require the commitment of the management and appropriate allocation of resources that cascade through all levels of business operations. SR is not a moment-in-time process; it is a journey and constant quest to move from good to great. ISCA

This is the fourth article in the ISCA Corporate Reporting Committee's series of articles on sustainability reporting to raise awareness and quality of sustainability reporting in Singapore. The first three articles were published in the October, November and December 2016 issues of this journal.

K. Sadashiv is Managing Director, Climate Change and Sustainability Services, Ernst & Young LLP.