

**SUSTAINABILITY**

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# **Sustainability and Your Investors**

Findings from the 2016 Sustainability & Innovation  
Global Executive Study and Research Project.

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## About the authors



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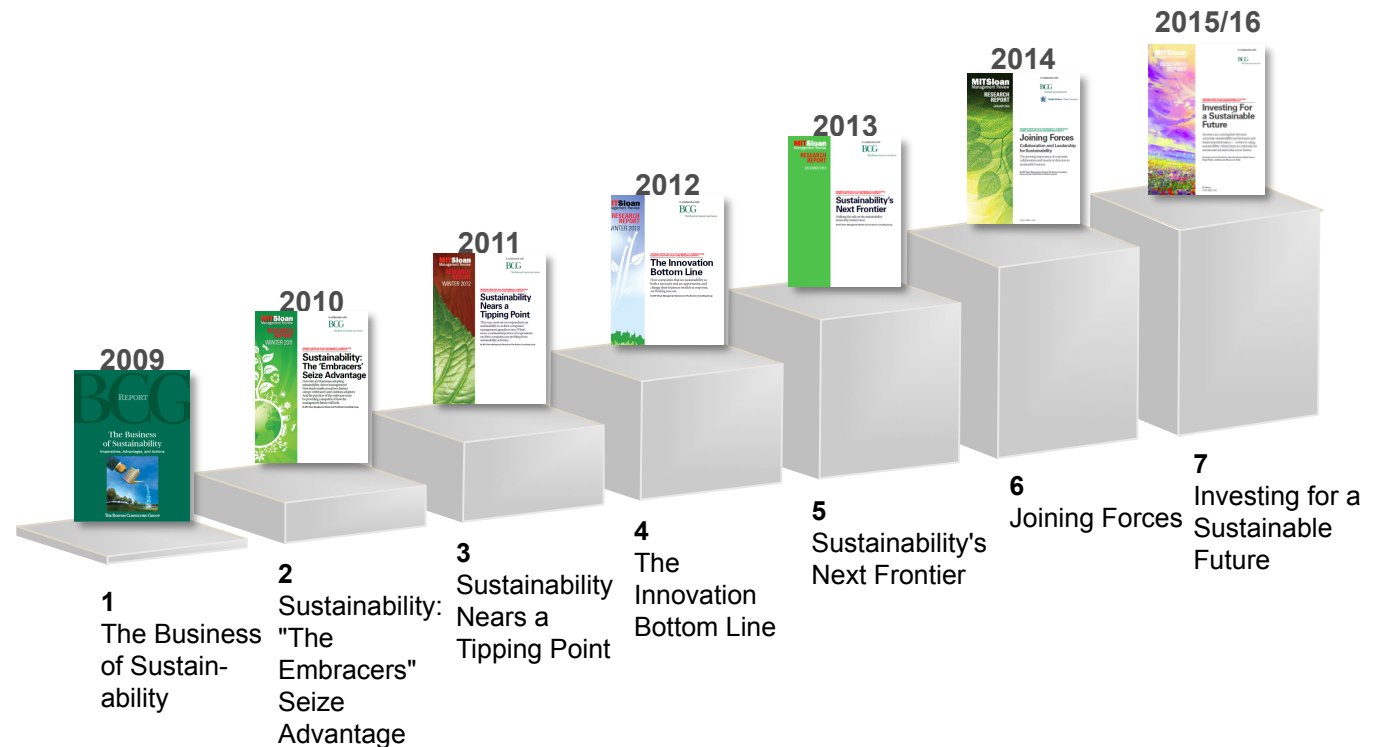


# Since 2009, *MIT SMR* and BCG have collaborated to examine sustainability impact on managers around the world



**BCG MIT Sloan**  
Management Review

- Joint undertaking
- Started in 2009
- Focuses on how challenges and opportunities of sustainability affect corporate strategy



## Core of the study is the sustainability survey

- Since 2009, > 45,000 executives, managers, and thought leaders responded
- More than 117 different countries represented
- Companies from 1 to > 100,000 employees

Besides the survey, the study incorporates insights from interviews, case studies, and academia

# This year's survey focuses on investors and corporate attitudes toward investors

## Large representative study on sustainability...

- **> 7,000 people engaged** and **> 3,000 respondents** in commercial dataset
- Respondents from total of **117 countries** – U.S. represent 36% of respondents
- Respondents from **~20 different industries** plus non-company entities
- **~40%** of respondents' companies operate on a **global scale**
- **~30%** of respondents are **board members** and c-suite executives
- **> 500** of respondents are **investors**

## ...with investors as main focus

### Lead question:

*"How are executives' decisions to act on corporate sustainability influenced by investors' perceptions about the value of corporate sustainability?"*

# Key finding: Investors care more about sustainability than many executives believe

*"Companies have been complaining that nobody cares about Sustainability, but investors care and companies need to up their game."*

*Robert Eccles, chairman of Arabesque Partners and professor of management practice at Harvard Business School*

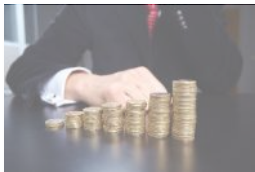
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## **Investors believe that sustainability creates tangible value, yet companies underestimate investors:**

- 75% of top executives in investment firms agree that a company's good sustainability performance is materially important to their firm when making investment decisions.
- Yet, only 60% of managers in publicly traded companies believe good sustainability performance is materially important to investors when making investment decisions.

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## **Investors are willing to divest for sustainability reasons:**

- 57% of investment firms' board members state that they exclude or divest from companies with poor sustainability performance.

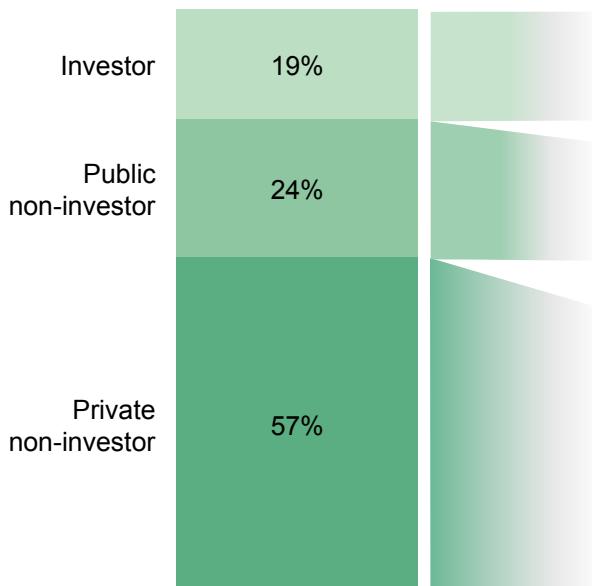
# Good sustainability performance has an impact on investor decision-making

*"Because we think that drivers have changed, the context of business has evolved, and because we know that sustainability or difficult-to-quantify factors are relevant to the long-term success of business, it is an investor's fiduciary duty to include it. It's not a nice to have; it's a requirement to fulfill your obligations as a fiduciary."*

David Blood, Senior Partner Generation Investments

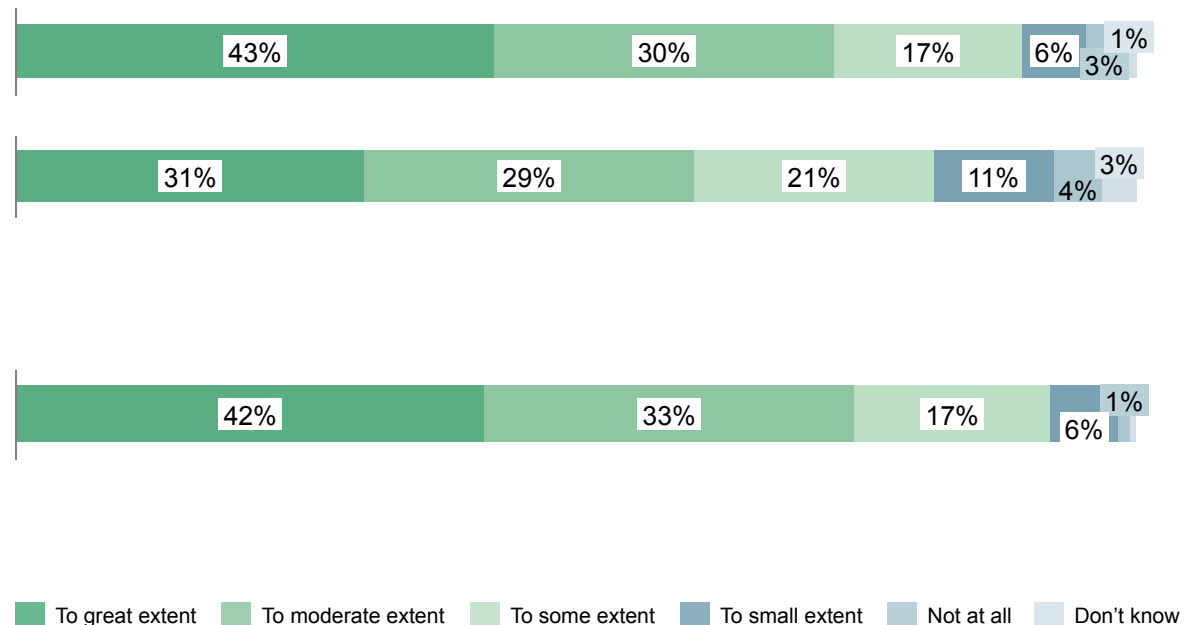
## Respondent's type of company

% of respondents



## 60% of public firms regard sustainability's impact on investment decisions as moderate or great—lowest share

Q8, Q13, Q28—To what extent do you agree with the following statement: A company's good sustainability performance is materially important for investors when making investment decisions



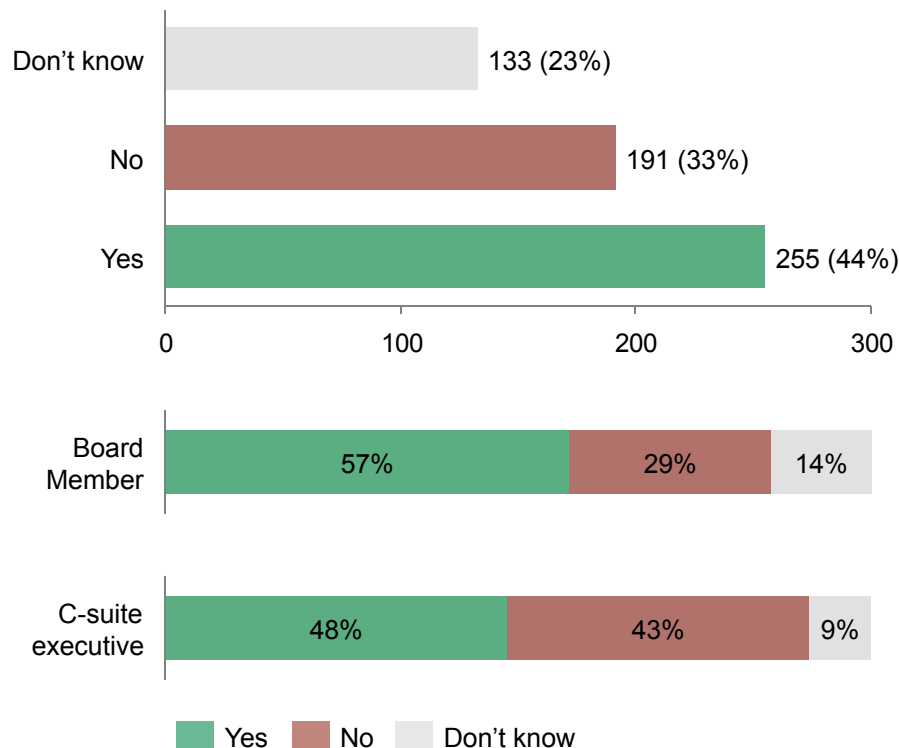
Note: Rounding errors might occur

Source: BCG-MIT SMR 2015 Sustainability Survey (based on commercial data-set with 3,057 responses); BCG analysis

# Investors are willing to divest from companies with poor sustainability performance. Example: energy sector

## Nearly half of all investors divest from companies with poor sustainability performance

Q17—Does your firm exclude or divest from companies that have a poor sustainability performance?



## Fossil fuels as an example

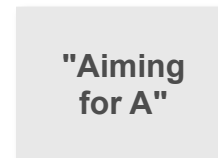
To date, more than 400 institutional and 2,000 individual investors in 43 countries have committed to divesting more than \$2 trillion in assets from fossil fuel companies



- Norway's largest pension fund with total assets of NOK 200 Billion
- Decided to divest from all companies that earn more than 50% of their revenues from coal-based activities



- One of the world's largest insurance companies
- Will divest from any company that generates more than 30% of revenue by mining coal or bases more than 30% of its energy production on coal



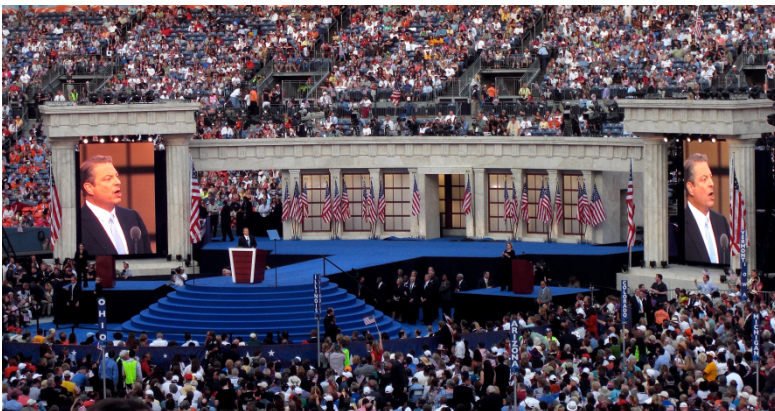
- Coalition of around 100 investors with \$4 Trillion in assets
- Increases pressure on companies, e.g., in mining industry to lessen the impact of climate change on their business models



- 6 UK institutions (e.g., councils) with GBP 180 Billion under management
- Use their pension funds to make "impact investments" in areas that reflect their economic, ethical and environmental interests

# Was losing the election the best thing to happen to Al Gore?

## Al Gore – not becoming a president ...



## ... but a very successful investor

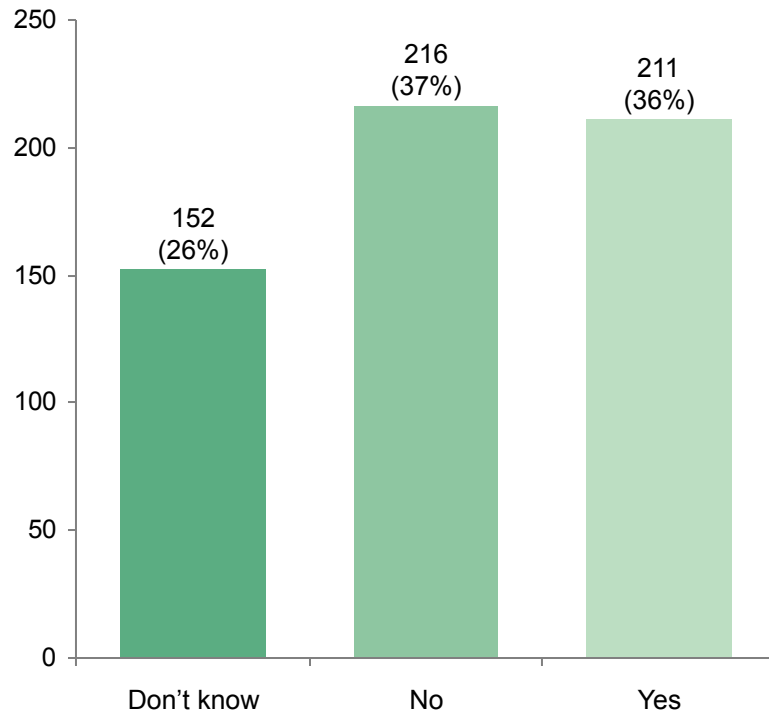
### GenerationIM

- Generation Investments with ~\$12Bn AuM
  - Strong performance for 10 years with >12% ROI, which outpaced the MSCI World Index by more than 500 basis points
  - GI's 10-year average return ranked it number two among the 200 global equity managers (Mercer)
  - E.g. due to sustainability KPIs his firm divested from BP just before the oil spill in the Mexican Gulf
- ▶
- **GI's fundamental premise is that standard financial metrics provide only a small picture of a company's real prospects → GI includes sustainability into its models**



# Sustainability ratings provide limited guidance to investors and are used infrequently for investment decisions

Only 1/3 of investors considers sustainability ratings for investment decisions



Agencies and investors currently developing their own tools

- **U.S.:** the Sustainability Accounting Standards Board is working to develop rules governing public disclosure of financially material corporate sustainability information
- **Europe:** Project Delphi is convening investors and financial analysts to develop quantitative sustainability indicators that can predict overall company performance
- **Others:** currently also working on standardized reporting tools

# Unsustainable business behavior can lead to disastrous consequences and destroy value for investors

## Deepwater horizon explosion



"The disaster has now cost BP \$54.6B since 2010"<sup>1</sup>

theguardian

## Volkswagen emissions scandal



"The company has already set aside \$7.3B but some experts estimate the bill could ultimately be five times as large"<sup>2</sup>

U.S. News

1. Article from June 2015 2. Article from October 2015  
Source: The Wall Street Journal; The Guardian; U.S. News; BCG analysis  
[sloanreview.mit.edu/sustainability2016](http://sloanreview.mit.edu/sustainability2016)

# Sustainability has become a billion dollar business proposition

## The green giants

- Generate > \$1Bn revenue with sustainable products or services
- Stocks return 11.5% more than a selection of comparable competitors over past 5 years
- Stocks outperform S&P500 by 6.8% on average



**Sustainability boosts the bottom line as well as shareholder returns**

## Three steps to success with sustainability focus

1. **Commitment of the CEO**
2. **Investment to drive disruptive innovations**
3. **Engagement of mainstream customers**

## Selected examples



- Commercialized first high-end electric vehicle ahead of American and German luxury car competitors
  - Plans to build a "gigafactory" for low cost batteries
- ➔ Best performing stock on Nasdaq in 2013



- Created Ecoimagination product line providing energy efficiency and cost savings
  - Invested ~\$15Bn in R&D over last ten years
- ➔ Cumulative revenue of ~\$180Bn <sup>1</sup>

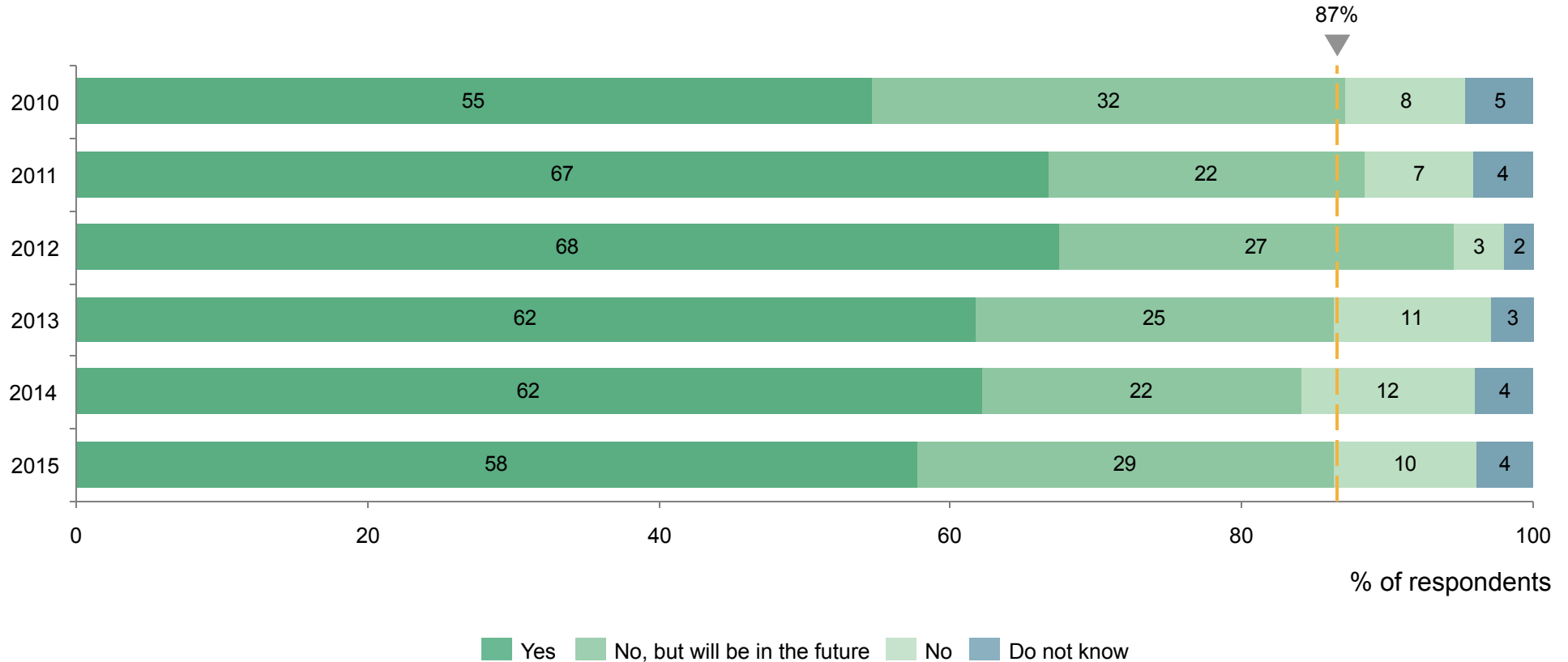
➔ **"Sustainability ... is no longer going to cost or lose money; it's the new way to make it."**  
Freya Williams in The Street

1. Already by end of 2014 within the first 10 years of operations

Source: The Guardian: "Meet the nine billion-dollar companies turning a profit from sustainability" Jan. 2, 2016; The Street: "7 Companies Making Billions with Sustainability" Sep. 2, 2015; BCG analysis

# A sustainability strategy is necessary to be competitive

Q46 — Is pursuing a sustainability-oriented strategy necessary to be competitive?



**Constantly, a share of ~60% of respondents see a sustainability-oriented strategy as necessary to be competitive already today**



# Top Challenge: Develop value creation story for sustainability

*"Many companies still base sustainability efforts on values, but it is the business case that really matters if we're talking to the investment world."*

*Cary Krosinskyi, advisor at the Principles for Responsible Investment<sup>1</sup>*

**90%**

of companies consider a sustainability strategy as important

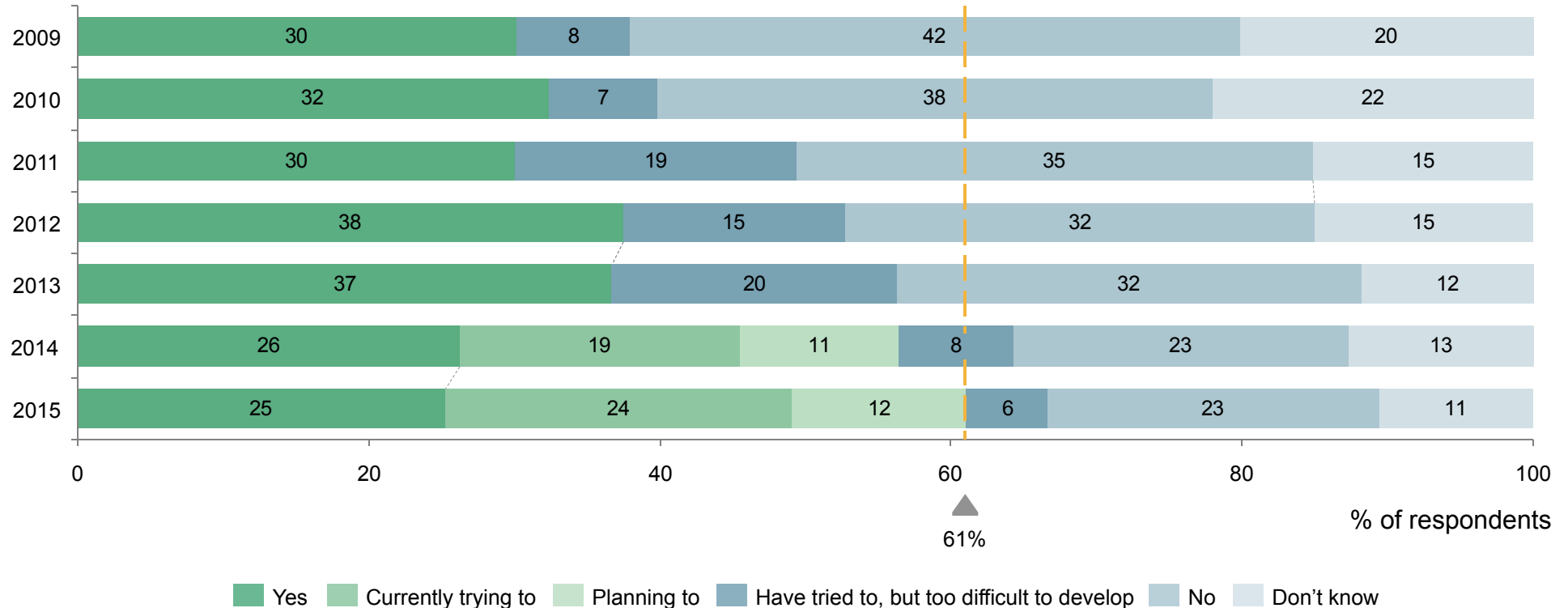
**60%**

of companies incorporate sustainability in their strategy

**25%** have business case for sustainability

# Companies still struggle with value proposition

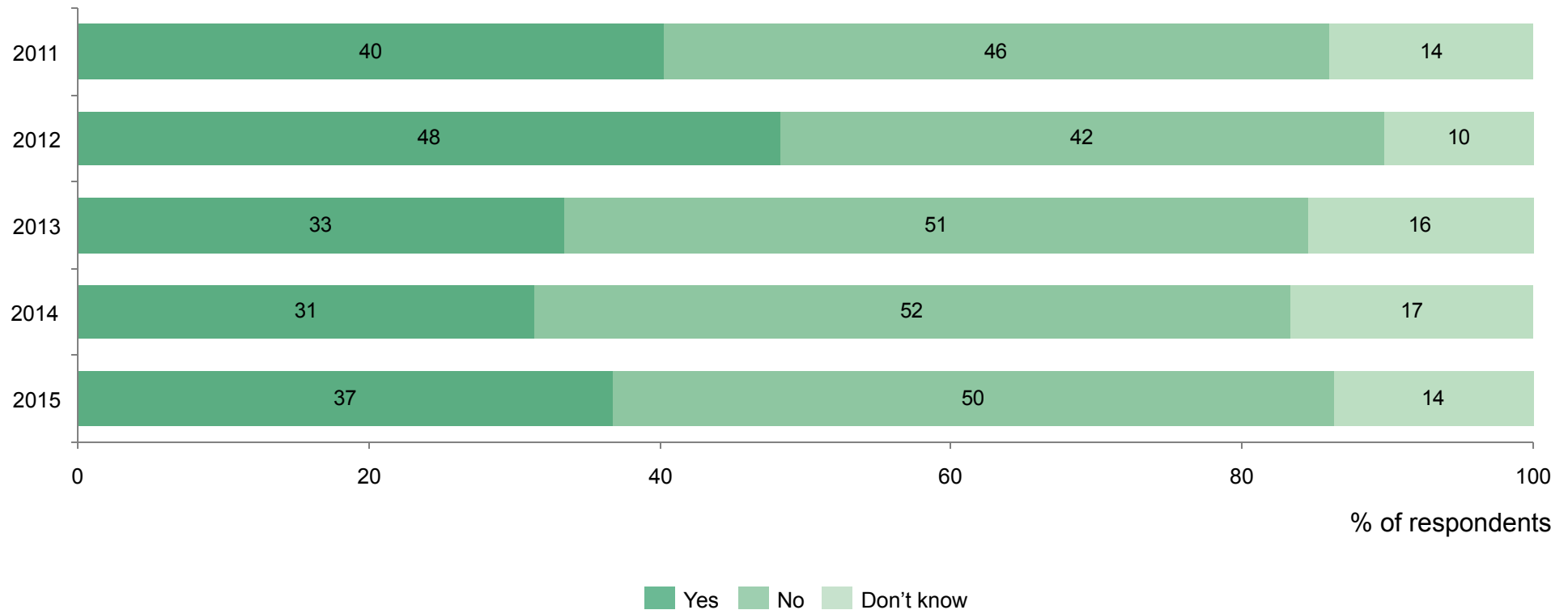
Q49 — Overall, has your organization developed a clear business case or proven value proposition for its approach to sustainability?



**Since 2009 respondents not having a business case for sustainability decreased systematically from 42% to 23%**

# Sustainability drives business model changes

Q48 — Has your organization's business model changed as a result of sustainability?



**Increase as compared with 2013/2014 still remains significantly below 2012 level**

# Example: Some investors are willing to pay M&A premium



## Premium paid explicitly for good sustainability performance

**Mitsubishi invests \$1.1B to acquire 20% stake in agricultural trader Olam**

**Mitsubishi justifies premium of ~55% with demand to grow food sustainably**

**Olam practices sustainable and traceable sourcing of products it trades**

**Olam considers care of environment, efficient resource use and quality of life of farmers and society**

Source: Business News: Sime Darby Plantation completes acquisition of Papua New Guinea's NBPOL, Mar. 2, 2015; Bloomberg Business: Sime Darby Offers \$1.7 Billion for New Britain Palm Oil, Oct. 9, 2014; The Abraaj Group Sustainability Report 2014/2015, Case Study: Fan Milk; Reuters: Danone to join The Abraaj Group in the acquisition of Fan Milk International, a leading dairy products player in West Africa, Oct. 24, 2013; Financial Times: Danone expands in Africa with 49% stake in dairy, Oct. 24, 2013; Reuters: With strong new backer, Olam gets what Noble needs, Aug. 28, 2015; Financial Times: Mitsubishi seeks Olam's sustainable approach, Oct. 28, 2015; BCG analysis



# Lack of communication poses challenges

## Knowledge of sustainability only trickles down the value chain...

### Investment firms

"Company engages in sustainable investing"

Board members

80%

Middle management

73%

Front line

62%

### Corporations

"Fully informed about organization's sustainability efforts"

C-Suite

85%

Senior mgmt.

51%

Middle mgmt. & front line

31%

## ...and is still not considered key for investor relations communication

Only **24%** of IR professionals are asked to tell investors about the value of sustainability to the company's bottom-line

Nearly **40%** aren't given direction on sustainability reporting at all

Nearly **80%** don't regularly include sustainability talking points in investors presentations

Almost **half** don't believe that sustainability strategy is necessary to remain competitive in their industry

Barely **one fifth** of U.S. companies were integrating sustainability into their investors communications; in Europe the share was just **over half**

# Conclusion and recommendations for companies



INVESTING FOR A SUSTAINABLE FUTURE  
Investors care more about sustainability  
than executives think



## Conclusion and recommendations for companies

- Do not underestimate the importance of sustainability to investors
- Incorporate it into your corporate sustainability strategy in 6 steps
  1. Build **awareness** for sustainability challenges and topics
  2. Analyze material issues and **align for integrated response**
  3. Focus on tangible and **measurable outcomes** rather than optimize ratings
  4. Translate sustainability measures into **sustainability strategy**
  5. Incorporate sustainability measures in **corporate strategy** creating a **clear business/proof of value** case
  6. Engage **investors** in your sustainability strategy discussions

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## Conclusion and recommendations for investors

- Consider mid/long-term investment strategies in the context of sustainability issues
- Integrate sustainability into their investment strategies
- Develop valuation methods that account for nonfinancial sustainability issues
- Avoid relying on sustainability indices, which can be misleading
- Actively engage in discussions on sustainability topics with companies and make your expectations transparent





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