KPMG

Driving industry transformation through ESG reporting standards and metrics

ESG voices podcast series

Musical intro

Announcer:

Hello and welcome to another episode of ESG voices! This podcast series addresses the opportunities and challenges within ESG, through interviews with ESG and IMPACT specialists from KPMG and beyond. Throughout this series, we will discuss a broad range of environmental, social and governance issues, aiming to support governments, businesses, and communities in creating an equitable and prosperous future for all.

Environment, Social and Governance considerations has become a top priority on investors' and corporates' agenda. Boards and executives are increasingly seeing ESG as an imperative to long-term value creation and as such ESG reporting standards and metrics are becoming more widespread. For today's episode, I am delighted to be joined by Richard Threlfall, Global Head of KPMG IMPACT, KPMG International, Maura Hodge, Audit Partner, National ESG Assurance Leader, KPMG in the US and Andries Terblanche, Executive Director, KPMG International who will be discussing how organizations can drive industry transformation through ESG reporting standards and metrics.

Thank you all for joining me today.

Richard perhaps to kick of the conversation today could you describe how the topic of ESG including the race to net-zero has driven organizational transformation?

Richard:

I think significant numbers of organizations all over the world are now recognizing that ESG is, is not just a reporting, exercise. It's not just about telling the world what your environmental, social and governance footprint is. It needs to be much deeper than that, because this is about embracing stakeholder capitalism, this is about adapting the way your business operates. So that it's not just for the pursuit of profit but is in the interests of your employees, customers, or suppliers, and the communities as a whole in which you operate as a business. And that means that it is driving organizations to actually change the way they operate, not just the way they report on a new set of metrics.

Announcer:

Thanks Richard, how is ESG reporting standards and metrics driving transformation? Perhaps we could start with you Andries and then turn to Richard?

Andries:

We've learned and it's only fairly recently from about 2017, that the literature has been published, that we're going through the cycles, economic cycles, and they are profound cycles. Every 40 years, we seem to change in quite a different direction. And the past 40 years was total shareholder return where the main focus used to be just on the profitability of organizations. Now, what is really interesting is that this narrow focus on profitability alone was all along regarded as an outlier. Some even call it a sect in economic thinking. And so in many ways, as Richard has pointed out, we're returning to what business always was, which is a more altruistic behavior. And now we are pivoting from only profit and the assumption that it's the net present value of my future profitability alone, that drives my market capitalization, to a recognition that other factors are at play as well. Factors like governance and planet and people and prosperity, supply chains and customers. So, what we've seen and what we are living through is a re-establishment of the importance of these values. This is not a nice to have, but it is an essential in the determination of future capital flows.

Richard:

One of the most exciting things that's happened over the last 24 months or so is the way in which whether it's in Europe, or in the US, there's a regulatory push to require organizations to report against a broad range of environmental, social and governance metrics. Now, I'm really excited about what this is going to mean. Because I think the disclosure is going to force those businesses that haven't have themselves recognized how they need to change will now do so. Because when their customers can see if a business is sustainable, when suppliers can see if the business they're operating with is sustainable, when those who are looking for work, choose to go to businesses that are sustainable, that is going to change the way that businesses work.

That's why I think the reporting against ESG standards is going to have such a big impact.

Announcer:

Maura, could you share your perspectives on why companies should consider implementing ESG reporting standards and metrics in their own organization?

Maura:

There is the age old quote you can't manage what you don't measure. And so, having data and metrics is absolutely critical to be able to understand how and if the strategy that you've put in place is successful. And if you're making progress against that strategy, or against those commitments that you've made. What I think is really important about the standards is that you can only measure and make sure that you're making that progress, if the way that you're doing the measurement is consistent period over period or year over year. And what we've often seen around ESG data or other types of non-financial metrics, is that because the world is evolving so quickly around it, the definitions that are used often evolve and change as well. And so, we need to be moving to a place in order to get either investor grade data around this information, or even just the concept of comparable consistent and reliable data by the use of standards. And so that's why I'm really excited about some of the regulatory considerations that are coming out from the US and the European Union, as well as the International Sustainability Standards Board. But I don't think that it solves all of the problems that we're facing today. And so, companies need to both contemplate those standards that that we're seeing being developed. But also making sure that when there is no specific standard out there, that they're also doing their own definitions, making sure that they're documented and that they're being consistently applied every time period over period.

Announcer:

Thanks Maura that's very insightful. Is it important to have a common set of guiding metrics or principles to implement and report against? Richard?

Richard:

Over the last few years, there's been a lot of concern about greenwashing by organizations. And one of the things that helps drive greenwashing is having such a number of different standards sets that organizations can pick and choose the ones that most suit them. That's why KPMG is so keen on the idea of having a common set of ESG reporting metrics adopted by regulators across the world, it's not only going to be easier for businesses, who will have to grapple with less and fewer systems, but it also means that there will be much greater ability to compare businesses across the globe in terms of their environmental, social and governance footprint.

Andires:

Well, in the past 40 years, we've seen unprecedented globalization, and that includes aspects like foreign direct investment, capital flows. And even though we de-globalizing to a degree now, we are still more interconnected than we've ever been before. And global capital flows required standardized metrics. And that's why it's important for us to have a common set of principles. If we don't, if they are discrepancies in how we measure it introduces friction into capital flows, and that slows the global economy down. It's almost like a in financial terms, a Tobin tax, and so it detracts from future economic growth which every soul on the planet needs to lift out of poverty, to be able to feed them to be able to live their dream and invest in their children. So yes, it's really important the way I think about it to have a common set of principles as we go forward.

Announcer:

Richard, building off of the previous question, could you share some practical steps organization can take to implement standards and metrics within their own company?

Richard:

Time and again as KPMG is asked to advise on reporting against environmental, social and governance metrics, the first challenge organizations find is the access to the data they need in order to be able to make that disclosure. And of course, it's not just about the data of the organization itself, it normally requires the organization also to report on what is happening within its supply chain, I don't think I can overemphasize just how difficult this is. So, the sooner that companies can make a start in terms of setting out for their suppliers, what they will be expecting of them, and give them a year or two to be able to put the necessary reporting measures in place, and then put in place the systems within the company itself, so that they can take on board that data and analyze it and start to drive really value enhancing decisions from the use of that data.

Announcer:

Maura turning back to you, what are some practical steps leaders can undertake to strengthen governance of the standards and metrics that they have implemented?

Maura:

What we're finding is that it's absolutely critical that we have cross functional and inter- organizational groups that are working together on putting the right governance structures in place. So when we think about where to start practically, we often talk about needing a project management organization, they really serve as the driver of all of the initiatives that are going to be undertaken, and really the nucleus of everything that ultimately gets created. I think historically, we have seen sustainability departments or ESG departments that have been responsible for everything. They've done, both the development of the identification of the topics and the issues to be addressed. The strategy around those, the execution on that strategy, as well as the reporting on the information. And what we're finding today is that to actually be successful in developing and executing on that strategy, as well as having reliable information to help evidence progress, it takes a lot more people to be involved. And it really takes people who have access to investment, access to resources and the ability to execute to be a part of that discussion. So, to go back to talk about really how the governance works, is I think you continue to have a sustainability group or a department that is responsible for the issue identification and the strategy setting. But then that's where some of the operational parts of the organization need to come into play and start to understand how they can functionally build that into the business. So, I work with a clothing retail company. And one of the things that's been so fun to see as they've evolved over time, is that they have a group that set their strategy. After they've set their goals and commitments, they have gone into the supply chain team, and into the design team, and explained what they're trying to do. So for instance, they're rolling out an eco-friendly line of clothing. And by talking to the designers, and the designers hearing that this is a commitment that the company was planning on making, they got really excited, and were able to brainstorm and come up with ideas of new products that they could launch or new materials that they could use, that would meet the definition of eco-friendly as the company had defined it. They're also starting to have those conversations with their marketing team. And helping the marketing team understand how they want to brand themselves from a sustainability perspective. And then marketing, being able to take that information and go out and develop their products and their communications around it. So, once you have the strategy and the execution, you need people who know how to do reporting, and make it investor grade quality. So that means development of process and controls over the information, which also includes the review of that information and making sure that it's fit for external consumption, and that it fits within the requirements of legal or compliance considerations that you might see once this data has to be submitted for regulatory purposes. In order to really have all of that come together, what we're seeing from a governance structural perspective, is that project management organization that I had mentioned, right off the bat, a cross functional working group, where there are representatives across the organization to really implement so I had mentioned in, in my example, the marketing team, the design team, the supply chain team, and the reporting team, like finance or accounting.

And then on top of that, we're starting to see a layer of what we're calling a steering group. So, these are executives that have access to budget, access to investment and ability to make decisions, as well as ability to hold the organization accountable for making progress on their goals. And that steering group is really there to both move any roadblocks that you're identifying as you're going through. And you're working groups are trying to make progress, as well as to unlock that investment and engage with the C suite or the board or investors at a level that helps them understand how the organization is moving around ESG.

Announcer:

Thanks Maura. Richard, how can implementing ESG reporting standards and metrics set organizations up for success as they drive transformation in their own organization?

Richard:

I believe there's something really important about the process that an organization goes through, as they start to look at what they need to do in order to report against a broad range of environmental, social and government standards. Simply having to stand back and recognize what it is about the way that the organization operates. What impact does that organization have on the planet in terms of, for example, its carbon emissions? To what extent is the organization really a role model for inclusion and diversity? Is the business really certain that its human rights record, is as good as it could possibly be throughout the entirety of the supply chain? Just asking these questions, we see time and time again, encourages businesses to go further and start on a process, on a journey of transformation.

Announcer:

To wrap up our conversation today, can I ask each of you to pass on some advice to our listeners?

Andries:

Well, as I've said before, we seem to go through transformation, significant transformations, every 40 years, they do happen, literature is quite clear about that, so I want to underline that we're not dealing with a fad or a passing wave of popularity. Time and again, when we go through these deep shifts, the early adopters seem to benefit significantly, whilst those that lag seemed to inherit a tag of being a laggard. And these differences have a cost. It pertains to the cost of your capital, it pertains to the availability of finance and the cost they have, and also to your customers, because loyalty wanes in these pivots. And even long-standing customers might pivot to other organizations that are more aligned in terms of governance, and sustainability, and the environment.

So, embrace it, and be quick, speed has a cost, or an or an advantage.

Announcer:

Maura?

Maura:

The number one piece of advice that I always give when I'm talking to clients about ESG is that it takes all the different skills that we have built up in our careers and in our work life to apply to ESG. Said differently, ESG needs to be a lens through which we do all of our work. My role as an auditor and the skills that I've learned and developed in that role at KPMG has been absolutely critical in my success and being able to provide assurance over ESG information, as well as help clients understand how to report on this in a rigorous and timely and comparable way. And I believe that that's true for any part of the organization that, that you work in, take the skills that you use every day, and look at them and use them through the ESG lens.

Announcer:

And finally, Richard?

I think the most important piece of advice I can give everybody involved in business today is really recognize the responsibility and the power that businesses have to be able to safeguard the future of our planet. We are facing an existential climate crisis in the world. And we only have just over seven years before the world burns through the 1.5 degrees of global warming above pre-industrial levels and get to a position where we start to see serious detriment to our planet, and knock on effect for our people. I think there's something really powerful about the leaders of organizations and organizations as a whole, putting themselves forward as being hand in hand with the efforts of the world to try to confront this crisis. And I think if we start with that mindset at the top of the organization, we know that we will really succeed in being able to avoid the worst possible outcomes that could come from climate change.

Announcer:

Richard, Maura and Andries, thanks again for speaking today, you've given our listeners a lot to think about and we look forward to hearing more about the many topics discussed today in future podcasts.

Join us again next time for more insights from ESG leaders and innovators. You can also find our latest insights covering a range of ESG topics by visiting home.kpmg/IMPACT. Thanks for listening!

Musical exit

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