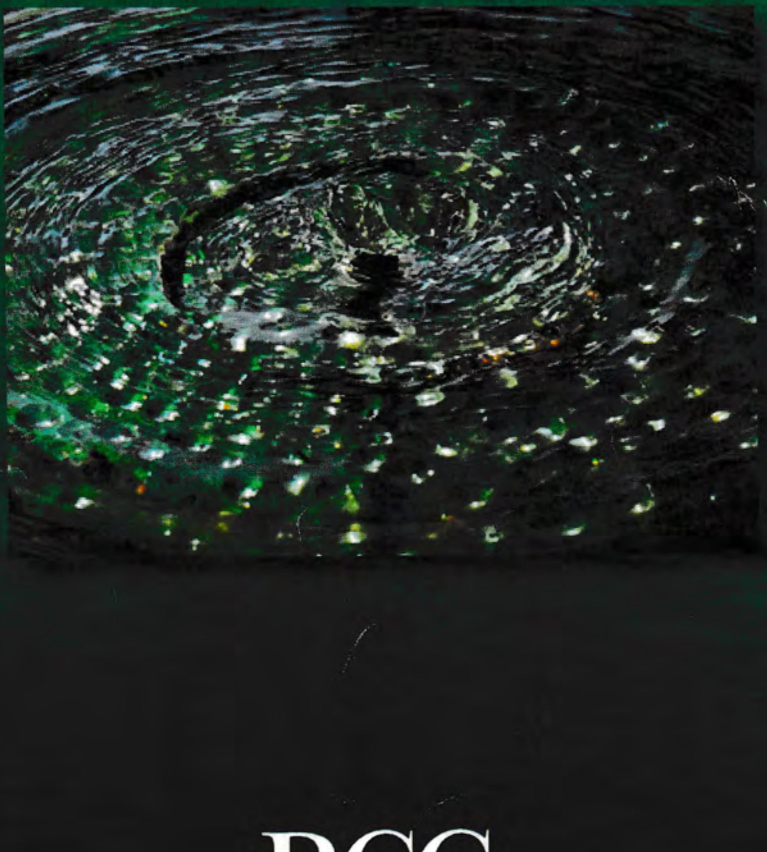
TOTAL SOC

Background research for working paper

IMPACT

A NEW LENS FOR STRATEGY

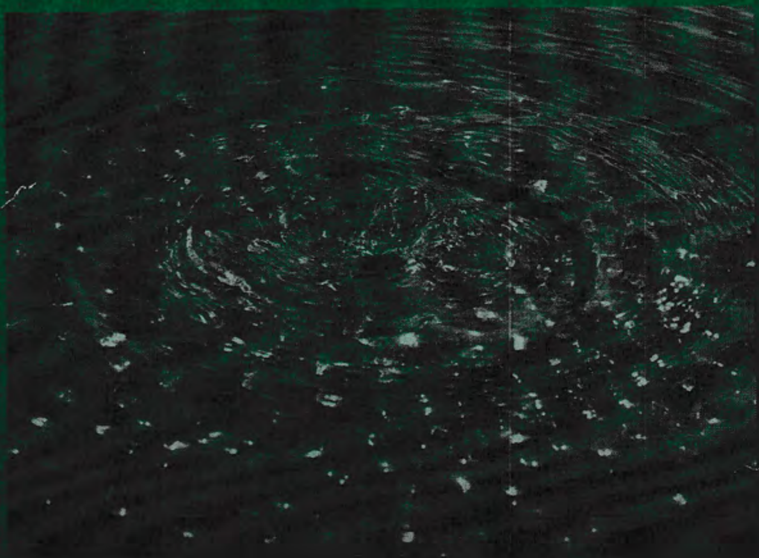
BCG, 2017



BCG

THE BOSTON CONSULTING GROUP

The Boston Consulting Group (BCG) is a global management consulting firm and the world's leading advisor on business strategy. We partner with clients from the private, public, and not-for-profit sectors in all regions to identify their highest-value opportunities, address their most critical challenges, and transform their enterprises. Our customized approach combines deep insight into the dynamics of companies and markets with close collaboration at all levels of the client organization. This ensures that our clients achieve sustainable competitive advantage, build more capable organizations, and secure lasting results. Founded in 1963, BCG is a private company with more than 90 offices in 50 countries. For more information, please visit bcg.com.



TOTAL SOCIETAL IMPACT

A NEW LENS FOR STRATEGY

DOUGLAS BEAL

ROBERT ECCLES

GERRY HANSELL

RICH LESSER

SHALINI UNNIKRISHNAN

WENDY WOODS

DAVID YOUNG

OCTOBER 2017 | THE BOSTON CONSULTING GROUP

CONTENTS

FOREWORD

THE BOSTON CONSULTING GROUP'S study of the impact of environmental, social, and governance (ESG) issues on company performance is an important addition to a growing body of research confirming the financial materiality of these attributes. But it also breaks new ground in trying to help companies capture the broader societal impact of their core businesses when it comes to global issues, such as drug availability and affordability, as well as important challenges related to economic, financial, and social inclusion. More important, it demonstrates how that approach can benefit total shareholder returns over the long term by improving margins and valuation multiples. The idea of a company's total societal impact (TSI), as the study describes it, and consideration of all stakeholders are areas many of the world's largest institutional investors are increasingly looking to measure and monitor.

As the third-largest investment manager in the world, we have been managing ESG strategies for more than 30 years.[1] Yet as the authors of this study suggest, we are at the dawn of profound new developments when it comes to thinking about ESG and impact investing. Investors have come a long way from the negative screening that characterized the early forms of what was initially called socially responsible investing (SRI). We have progressed toward positive, thematic ESG tilts such as State Street's gender diversity and carbon-neutral indexes and are now focusing on fully integrating ESG issues into our investment risk frameworks and those of our client institutions. That process has relied heavily on the insights and data provided by studies like this one. Efforts to quantify the financial implications of ESG factors help investment managers incorporate them into investment models, both as signals for identifying outperformance potential and as red flags for potential risks.

Still, we all have much more work to do, as the report indicates. A growing number of institutions around the world want to broaden their long-term investment objectives beyond traditional financial metrics to include the economic, environmental, and societal impact of their investment programs. This presents critical challenges for investment managers to come up with new kinds of performance scorecards that include attributes such as the carbon profile of an investment portfolio or scores related to workforce quality and supply chain sustainability. As the authors point out, many companies are able to measure the outcomes directly associated with their core businesses but have difficulty sizing their ultimate societal impact.

One of the most important preconditions for advancing to this new stage is access to high-quality and consistent data to assess these new factors when we are analyzing companies. As BCG notes, the ability to measure the impact of environmental issues such as water resource management or carbon intensity is more advanced than the means of quantifying the influence of more intangible issues such as purpose-driven work cultures or community impact.

Fortunately, many organizations are working to address this data challenge. For example, with its recommended disclosure standards, the Financial Stability Board's Taskforce on Climate-Related Financial Disclosures (TCFD) has provided a foundation for improving our ability to assess and price appropriately climate-related risks and opportunities. Investment managers like us are also encouraging companies to provide more robust and consistent reporting of environmental, social, and governance issues. As one of the largest ETF and index managers in the world, we have made sustainability issues around ESG a central focus of our active stewardship practice. Because we are near-permanent capital (if a company is included in an index, we must own it on behalf of our clients), we have, by definition, a long-term perspective on how ESG issues can impact a company's ability to deliver attractive returns. For that reason, we have called upon companies to analyze and report in detail how sustainability issues might impact their long-term strategy and capital allocation decisions.

The BCG study rightly distinguishes the effects across sectors. The oil and gas industry, as the authors note, will obviously have different opportunities and challenges than biopharmaceuticals, technology, banking, or consumer packaged goods. We believe more industry-specific and regional-specific research is still needed.

As the report suggests, institutional investors, both asset owners and asset managers, have a crucial role to play in helping to advance this next frontier in impact investing. Global institutional assets under management represent trillions of capital firepower to put behind increasing industry knowledge and understanding.

Undeniably, there is a growing appreciation that companies need to consider the interests of a broader group of stakeholders beyond shareholders alone, including society as a whole. This, we believe, is the future. Integrating these issues into corporate strategy can fundamentally change the way businesses think about what makes them successful. As this research vividly demonstrates, successfully managing total societal impact can measurably improve total shareholder returns by motivating employees, building loyalty and trust with customers, and strengthening relationships with policymakers.

—Ronald P. O'Hanley,
President and CEO, State Street Global Advisors

NOTE
1. All rankings according to State Street Global Advisors, December 31, 2016. Data updated annually.

For information or permission to reprint, please contact BCG at:
E-mail: bcg-info@bcg.com
Fax: +1 617 850 3901, attention BCG/Permissions
Mail: BCG/Permissions
The Boston Consulting Group, Inc.
One Beacon Street
Boston, MA 02108
USA

10/17

BCG

THE BOSTON CONSULTING GROUP

bcg.com