WORLD ECONOMIC FORUM

Stakeholder Capitalism Metrics: The Investors’ Case

COMMUNITY PAPER

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Introduction

Investors are increasingly using environmental, social and governance (ESG) considerations to identify material risks and growth potential, leading to better-informed investment decisions. Yet an accurate assessment of these risks and opportunities is hampered by the plethora of overlapping ESG standards. Corporate reporting of ESG factors is in its infancy compared to traditional financial reporting, especially since no assurance is yet required by law on non-financial information.

Over the past year, increased dialogue among a number of standard setters, capital market regulators and policy-makers has built momentum for global reporting standards. Despite this, there remain no mandated global standards and the voluntary standard setters have only recently started to align. It is likely to take several years before global standards are established and widely adopted – whether voluntarily or as mandated by regulators.

In the meantime, the World Economic Forum's Stakeholder Capitalism Metrics (SCM) provide a stepping stone for companies to build their capacity and capability for improved ESG reporting. These metrics are collated from existing standards and standard-setting bodies, such as the Sustainability Accounting Standards Board (SASB), the Global Reporting Initiative (GRI), the Task Force on Climate-Related Financial Disclosures (TCFD) etc. Ultimately, the Stakeholder Capitalism Metrics are offered as a market-led set of business-critical metrics – a building block to be employed by a future global sustainability standard setters.

This paper sets out an overview of the SCM and how investors can support the acceleration of a global solution to ESG and sustainability reporting standards.

> **SASB applauds this [International Business Council] effort, which will significantly accelerate progress towards a globally accepted system of corporate reporting – one that presents a coherent, comprehensive view of financial and sustainability performance.**
>
> Janine Guillot, Chief Executive Officer, The SASB Foundation

1 The evolution of the Stakeholder Capitalism Metrics initiative

In September 2020, the World Economic Forum, in collaboration with members of the International Business Council (IBC) and the "big four" accounting firms, published a set of recommended universal ESG metrics and disclosures (referenced as Stakeholder Capitalism Metrics). The recommendations reflect the perspective of global chief executive officers on the issues they believe most relevant for all industries in creating long-term sustainable value for their shareholders.

The initiative was designed to achieve three goals:

1. Improve the consistency and comparability of ESG information reported by companies

2. Increase the adoption of ESG reporting by companies

3. Inspire convergence on a global sustainability reporting solution

The year-long process engaged with 200-plus companies, investors, organizations, standard setters and regulators to scan more than a dozen existing ESG standard setters and frameworks (including GRI, SASB, TCFD) and selected only those metrics most critical to sustainable value creation. The metrics are organized around four pillars: people, planet, prosperity and principles of governance.

The recommendations set out a baseline of 21 core metrics and disclosures representing the most universal (e.g. industry-agnostic) ESG factors that all companies in all sectors should be able to report against. The SCM also present 34 expanded metrics that encompass a wider value-chain scope or convey impact in more tangible, monetary ways.

The recommendations have received strong support from member companies of the IBC, with around 80 global corporations committed to incorporating the metrics in their reporting. Given the profile of and leadership displayed by these companies, many other companies are planning to adopt the recommendations, too. This critical mass of collective action is driving improved corporate reporting and adding to the momentum towards the ultimate goal of a global ESG standard setters and globally accepted reporting standards.

> **We are working with the World Economic Forum's International Business Council to help harmonize the many reporting metrics. Getting to a common set of reporting standards will be a big step in the ESG effort.**
>
> Lim Chow Kiat, Chief Executive Officer, GIC, Singapore's sovereign wealth fund

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The investors' case for supporting the Stakeholder Capitalism Metrics initiative

The case for improved reporting on the risks, impacts and opportunities arising from ESG factors is growing stronger by the day. There are immediate financial and fiduciary implications to improved ESG reporting.

Investors and the 'licence to operate'

It can be useful to think of ESG factors as a social licence to operate.[1] Unlike a legal licence to operate, the social licence is granted by stakeholders but extends beyond shareholders. Companies cannot create long-term value without running their businesses for the benefit of, and minimizing harm to, all of their stakeholders, which include customers, employees, the societies in which they live and the planet as a whole.

ESG factors are increasingly finding their way on to boardroom agendas due to employee pressure, reputational concerns or the increasing negative impacts on society. This corresponds with greater public attention on the global sustainability agenda. It is particularly important for long-term institutional investors, such as pension funds, which have a broad stakeholder base to consider. This stakeholder base includes, for example, pensioners and many millennial investors who are increasingly desirous to allocate their money in a socially responsible way.

Alongside this, there is also growing scrutiny of ESG factors and how capital is allocated. Capital market sentiment and investment practices have changed significantly in response to the rise of sustainable investing.

In the face of greater stakeholder scrutiny, the SCM provide a mechanism to enable accountability and transparency so that capital markets can respond and drive a sustainable future.

Enabling comparability, efficiency and accountability on ESG progress

Asset owners and asset managers seek to optimize the returns on their portfolios by balancing downside risk with upside opportunity. Comprehensive analysis of company performance is at the core of the investment process. Investors expect companies to factor in material ESG risks, impacts and opportunities to their corporate strategies and to embed execution in their businesses and operating models.

Government policies and consequent laws and regulations are also influencing materiality considerations (e.g. decarbonization, human rights, diversity and inclusion). Investors want to understand how companies are managing material risks, impacts and opportunities in relation to ESG.

However, the array of choices and possible ESG metrics for companies to adopt can be bewildering. The result is that far too few companies are reporting often enough, while the information from those that do report more comprehensively is often not comparable with information from other companies, including those in the same sector. The differences in reported data and the lack of harmonization on common metrics has led to an alphabet soup of overlapping standards and frameworks, which makes it difficult for investors to form a clear view of ESG performance. Investors often engage huge teams to extract more specific information from investee companies.

Adoption of the SCM, in the absence of global ESG reporting standards and assurance, will improve comparability and the reliability of information reported. There will also be efficiency gains for investment firms due to this consistency and reliability.

Building company capacity as a stepping stone to future global sustainability standard-setting

While many companies do an excellent job of reporting their ESG performance, there are many more that report little or nothing. A significant amount of corporate ESG reporting is based on disclosing policy statements, with relatively little comparable, numerical data.

Investors are particularly interested in enterprise value (financial impact) and how companies are managing industry-specific risks and opportunities. The SASB Materiality Map and associated industry-specific standards, for example, are highly regarded and endorsed by investors. Investors also want to see how companies are managing risks associated with their licence to operate through impacts on and from wider stakeholders (e.g. workforce, customers, communities, the planet). The GRI standards are widely respected and used by companies to demonstrate how they are creating value for their stakeholders (including investors) and how they are considering the business impact on the economy, environment and people, which will affect stakeholders and enterprise value.

Investors need companies to continue improving their ESG reporting – and the reporting needs to be high-quality and focused to be valuable. The SCM provide a stepping stone for companies to build their capacity and capability for improved ESG reporting:

- For companies already reporting material industry- and company-specific ESG information (e.g. using SASB), the SCM provide useful, supplementary and comparable information – especially on stakeholder impact – to inform investment decision-making.
- For companies not currently reporting ESG information, the SCM represent a relatively easy starting point that can be developed over time.

Add weight to the critical mass of collective action

During the SCM consultation process, different investors requested varied information on ESG, but many said they would like to see a global ESG reporting standard-setting body develop a comprehensive set of standards that focuses on comparable and numerical data where possible.

For example, the World Economic Forum is working alongside SASB, IIRC, TCFD and the Climate Disclosure Standards Board (CDSB) in the working group set up by the International Financial Reporting Standards (IFRS) Foundation to lay the groundwork for the possible establishment of an International Sustainability Standards Board (ISSB).

Investors are encouraged to throw their weight behind the IFRS Foundation's initiative, which has committed to build upon existing convergence initiatives.

However, it is likely to take several years before global standards are established and widely adopted – whether voluntarily or mandated by regulators. In the meantime, the SCM provide a stepping stone for companies to help build their capacity and capability for improved ESG reporting.

Encouraging companies to adopt the SCM will add weight to the critical mass of collective action driving momentum towards a global solution, while offering the SCM as a building block in creating that solution.

Conclusion

For companies, investors and other stakeholders, the SCM enable more consistent and comparable communication of ESG factors by amplifying a set of priority disclosures, based on established standards.

Investors can support the acceleration of a global solution to ESG and sustainability reporting standards by encouraging companies to adopt the Stakeholder Capitalism Metrics – a stepping stone for now, a building block for the future.

> **I welcome the work of the World Economic Forum's International Business Council in creating a set of common metrics for reporting sustainable value creation … I encourage governments, regulators, the official accounting community and voluntary standard setters to work with the IBC towards creating a globally accepted system of sustainability reporting based on this project's groundbreaking work.**
>
> Mark Carney, former Governor, Bank of England; UN Special Envoy for Climate Action and Finance

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Endnote

1. Jan, O., "The Board and ESG", Harvard Law School Forum on Corporate Governance, 25 February 2019: https://corpgov.law.harvard.edu/2019/02/25/the-board-and-esg/ (link as of 11/6/2021).

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