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Executive Summary

This is the final report from a two-year EABIS funded research project. The purpose of the research has been to explore how the environmental, social and governance performance of companies might impact on the drivers of business success; how companies explain these linkages to investors, and how the investment community treats these data. The research project has been run in close contact with a parallel EU CSR Alliance Laboratory on "Corporate Responsibility and the market-valuation of non-financial performance". This Lab has been led by Lloyds Banking Group and Telecom Italia.

For many years there have been ultimately inconclusive attempts to prove that improved ESG (Environmental, Social, Governance) performance (frequently referred to as Corporate (Social) Responsibility [CSR] performance or, in brief, Corporate Social Performance (CSP)) affects overall business performance. This report argues that a more fruitful approach is to identify how improved ESG performance can improve individual elements of non-financial performance, and thereby, create future value. Specifically the report proposes that value is redefined in terms of 'sustainable value'. A 'value creation' framework is proposed. This Value Creation Framework – and an operationalised management version of it, developed by the EU CSR Alliance laboratory – can be used both by business itself to help embed a commitment to Corporate Responsibility and Sustainability; and by the investment community to refine their business valuation models. It should stimulate further dialogue between companies and investors. Growing sustainability pressures worldwide are likely to make these arguments even sharper in future.

The Value Creation Framework and other recent work on sustainable development and business challenge the existing dominant convention of shareholder value; and of how value is created or destroyed. As such, there are many obstacles both in business and in the investment community (owners, fund-managers, analysts) which would currently work against widespread adoption of this new approach.

Amongst the investor community, the obstacles include lack of evidence for or understanding of, the potential linkages; limited or non-existent data and certainly of anything which would be comparable across companies; confusion of terminology and shifting definitions; and few incentives to change.

For companies, the obstacles include all the above, as well as disconnects between Corporate Responsibility / Sustainability specialists and the Investor Relations function; perceived lack of investor interest; and lack of actual performance data.

During the research project, we identified, both through the consultations for the EU CSR Alliance Laboratory, and through studying practitioner reports produced since 2000, a number of organisations and initiatives to change investor community and business behaviour.

We have found a number of organisations interested in collaboration on implementation of the Value Creation Framework and / or providing access for follow-up research opportunities. As part speculation, part suggestion, we show how collaborative commitments might evolve over the next 1-2 years to create a critical mass of vanguard companies and investors prepared to use the Value Creation Framework to help explain the risks associated with not embedding sustainability, and the opportunities potentially accruing to businesses from doing so; and how this can be factored into investor valuation models. In particular, corporate CEOs whose companies have already started to embed CR and sustainability, and are seeing improved ESG performance, should be prepared to commit publicly that as a group they will each – within their 2010 results roadshows – explain these linkages and their impact on non-financial drivers of business success. There also has to be a change in the mindset of the mainstream investment community, which requires investor training, changes to how investors (individually and institutionally) are measured and incentivised; and to change time-frames from a fixation with quarterly earnings. Recommendations to the CSR Alliance laboratory, the EU Commission, companies, investors, business schools and EABIS are identified; and a number of further research opportunities are highlighted.

1

Introduction

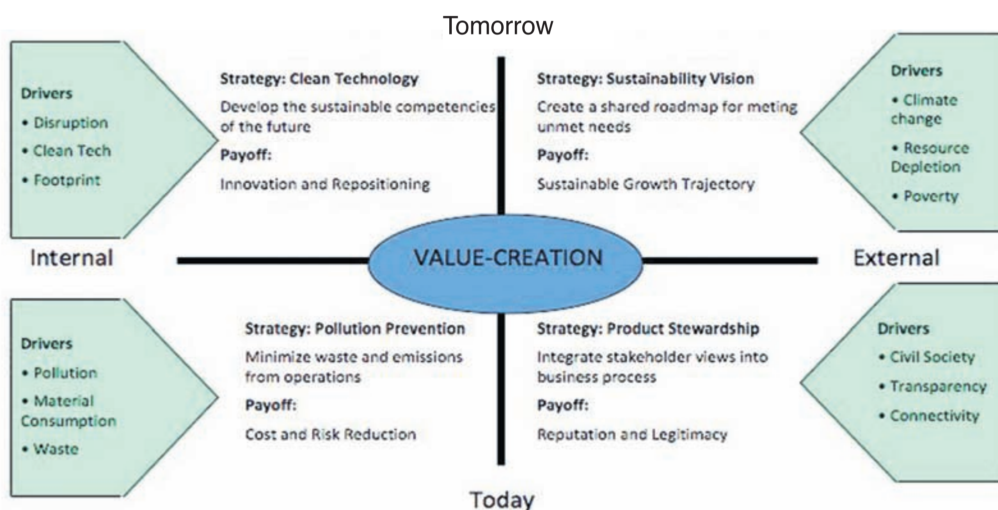
Business and society face multiple challenges: the immediate financial crisis which has triggered a wider economic crisis; and a deeper, longer-term sustainability crisis caused by climate change, pollution, resource depletion, burgeoning global population, and unsustainable production and consumption. These multiple crises intensify what was already an emerging debate about the purpose of business: how, and under what circumstances, business needs to internalise the externalised costs of doing business; and whether existing methods for calculating the value of a business are any longer fit for purpose.

For more than two decades, a dominant paradigm emanating from leading business people and business schools has been "shareholder value" and that the purpose of business is to increase shareholder value. We share the view of Ian Davis – the then global managing-partner of McKinsey and Co, writing in The Economist magazine (By Invitation, 26th May 2005) that: *"Paradoxically, the language of shareholder value may hinder companies from maximising shareholder value in this respect. Practised as an unthinking mantra, it can lead managers to focus excessively on improving the short-term performance of their business, neglecting important longer-term opportunities and issues. The latter would include not just societal pressures, but also the trust of customers, investment in innovation and other growth prospects."*

Instead, like the business leaders who produced the "Tomorrow's Global Company" report (June 2007), we see the purpose of business as: *"To provide ever better goods and services in a way that is profitable, ethical and respects the environment, individuals and the communities in which it operates."* (Tomorrow's Global Company: Challenges and Choices).

Some may see profits and sustainability as mutually exclusive. We believe that increasingly it will be understood that long-term profitability requires a commitment to greater corporate sustainability. Corporate sustainability has been defined *as a business approach that creates long-term shareholder value by embracing the opportunities and managing the risks associated with economic, environmental and social developments.*[1] A sustainable enterprise is one that contributes to sustainable development by delivering simultaneously economic, social and environmental benefits'[2]

Figure 1: Sustainable Value Framework



Adapted from "The Necessary Revolution", Peter Senge et al; Derived from: Hart, Milstein & Caggiano (2003)

[1] PWC/ SAM - The Sustainability Yearbook 2008.
[2] Prof Stuart Hart, Mark Milstein and Joseph Caggiano in an article in the Academy of Management Executive in 2003.'

In the aftermath of the financial and economic crises, various thinkers and opinion-formers have called for a "new capitalism," (Richard Sennett), "responsible capitalism"(Robert Reich) or "values-based capitalism" (Rosabeth Moss Kanter). It is argued that a core element of this renewed capitalism is corporate sustainability. Hitherto, the commercially successful sustainability corporate performers have been those minimising risks associated with the lack of sustainability (Accenture – forthcoming). Going forward, it might be expected that the commercially successful sustainability high performers will be those that exploit the opportunities from sustainable development. This is emphasised in two recent books. (Senge et al The Necessary Revolution 2008) and Adam Werbach Strategy for Sustainability: A Business Manifesto – 2009)

In parallel, the EU CSR Alliance established a Laboratory on "Corporate Responsibility and Market Valuation of Financial and Non-Financial Performance". It is the contention of the Lab and the EABIS research team working with the Lab that the markets do not fully understand the risks and opportunities associated with Environmental, Social and Governance (ESG) issues. Our central thesis is this virtuous circle: a better understanding of how improved ESG performance positively impacts on a business will lead to (a) mainstream investors proactively expecting ESG data from companies and understanding how to use these data; and (b) companies themselves measuring and reporting their ESG performance and understanding how to use these data. In turn this will mean that company-investor dialogues routinely incorporate ESG performance discussions. Then there is positive feedback as the dialogue further strengthens companies and investors in their understanding and use of ESGperformance data.

For glossary of terms see appendix 1.

Figure 2: Virtuous Circle

Achieving this "virtuous circle" will require new approaches to value risks and opportunities associated with the non-adoption or adoption of sustainability. Previously, researchers and practitioners have tended to focus on whether Corporate Responsibility – defined as commitment to improving environmental, social and governance performance by minimising negative environmental and social impacts, and maximising positive environmental and social impacts – helps improve business performance in terms of profitability and share price.

Several meta-analyses of individual studies have explored this link (see Figure 4 below).

Yet as The Economist magazine concluded (Just good business 18th January 2008 – The next question – does CSR work?): *"A new, exhaustive academic review of 167 studies over the past 35 years concludes that there is in fact a positive link between companies' social and financial performance—but only a weak one. Firms are not richly rewarded for CSR, it seems, but nor does it typically destroy shareholder value. Might cleverer approaches to CSR in future produce better returns?"*

Instead of asking *does* CR improve business performance, this research focuses on *how* CR *can* improve business success. Specifically, the research shows how improving aspects of ESG can positively impact on individual elements of what has traditionally been referred to as non-financial performance; and in turn, how these impact on the drivers of value-creation.

Game-Change – Changed Context of Global Crisis

The initiation of this project preceded the financial crisis. The crisis has, however, given added urgency and impetus to the project:

- Many are now looking for alternatives to short-term shareholder value which fuelled compensation rewards fundamentally misaligned with long-term interests of the business;

- There is a desire to unpick the generic "quality of management" assessment with more sophisticated indicators of factors both driving and exemplifying that "quality", which can be translated back into a numerical valuation of the business.

- The "sustainability crisis" and the international drive to a low carbon economy and conservation of natural resources requires new metrics to enable both companies and investors to evaluate companies well-placed for, or conversely those at risk from the transformation.

Whilst we recognise the vital importance of debates about the societal added-value that business can contribute, and the need for greater transparency and accountability required to meet societal expectations of business, we see this as a parallel debate to debates about how improving ESG performance can contribute to enhanced value for the firm. This study is focussed on the latter, and specifically on what needs to change within firms and within the investment community, and also within both together.

The close collaboration between the research team and the CSR Alliance Laboratory represents a different approach to much academic research. We summarise the key lessons for similar collaborations in the future in a separate note to EABIS.

This final report draws heavily on laboratory meetings, focus groups with investors held around the EU, 1:1 interviews with investors, companies and experts, and crucially on the working papers produced by the research team. These working papers are:

- Non-financial performance metrics for corporate responsibility reporting revisited (Malcolm Arnold)

- The Challenges of Mainstreaming Environmental, Social and Governance (ESG) issues in Investment Decisions A survey of practitioners' reports (Kenneth Amaeshi, David Grayson)

- Going beyond a long-lasting debate: What is behind the relationship between corporate social and financial performance? (Francesco Perrini, Angeloantonio Russo, Antonio Tencati, Clodia Vurro)

- The integration of ESG information into investment processes: Toward an emerging collective belief? (David Bourghelle, Hager Jemel, Céline Louche)

- Dialogues with the European investment community on the challenges of mainstreaming Environmental, Social and Governance (ESG) issues in investment decisions: Summary of findings from focus group discussions in: Rome, Frankfurt, Paris Stockholm and Utrecht (Kenneth Amaeshi)

These papers can be found at **www.eabis.org** and **www.investorvalue.org**. For a fuller description of the research project, including our operations timeline, research objectives and lessons see appendix 2.

With the publication of this report, this EABIS research project is concluded. Individual members of the research team will be continuing their work in this field; and the EU CSR Alliance Laboratory also envisages a new dissemination phase for its work. Details can be found at www.investorvalue.org

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2

Obstacles to Mainstreaming Environmental, Social and Governance Issues in Investment Decisions

Why are ESG issues not frequently represented in mainstream investment decisions? There is a growing awareness that investment decisions and the financial markets do not appropriately value ESG issues, despite the fact that these issues could be fundamental to understanding the performance of firms. Our research has identified a number of possible obstacles in the way of mainstreaming ESG in investment decisions. These are broadly grouped into obstacles (a) with the investor community and (b) inside companies, which are further summarised below.

2.1 Obstacles with the Investor Community

The obstacles to mainstreaming ESG issues in investment decisions on the part of the investor community are mainly to do with investors' mindsets, decision techniques, investment horizons and perceptions of ESG issues.

- **Investors' mindsets, decision techniques and investment time horizons**

It was noted through our multiple data sources that most investors, in line with their education and dominant economic worldview, are skewed towards quantitative analysis and short-termism in their investment decisions. This often comes with a slightly inflexible analytical framing of issues by investors, and is recognised as a deep and structural challenge. Given that ESG issues are much more geared towards qualitative analysis and long term investment decisions, sometimes, this inclination towards quantification and short-termism negatively rubs off on to ESG issues. And where data are collected on ESG issues, they are often undermined by inconsistencies and insufficiencies arising mainly from the differences of ESG data in terms of actors, industries, regions and countries.

- **Investors' perceptions of ESG issues**

Most investors tend to think that ESG issues are complex, expansionary, and, therefore, contestable. According to them, ESG issues present a very high degree of complexity, which makes them very difficult to articulate, assess and integrate into investment decisions. This complexity is particularly tied to the challenge involved in understanding the boundaries of ESG issues – i.e. what is in and what is out. This complexity is further intensified by a language confusion that has made it difficult to articulate what is meant by ESG and how to measure it. Some of the terms used to describe this practice include – ESG, non-financial performance; CR; extra-financial performance, sustainability.

The expansionary nature of ESG issues is also a source of concern for many investors. The issues are constantly evolving and as such difficult to pin down. For example, the issue of obesity and healthy eating has entered the corporate responsibility agenda in the developed economies, where it was not featured until the last decade or so. The same can be said of other issues such as climate change, water scarcity and even immunisation (e.g. PharmaFutures – www.pharmafurures.org)[3]. This fluidity, while necessary in identifying and internalising externalities arising from corporate actions and inactions, carries with it a significant amount of complexity and uncertainty. Some investors argue that the quest to unpack and address these complexities often leads to information overload.

In addition to the complexities engendered by ESG discourse and practice, they also constitute an arena for contestations and power relations. These contestations and power relations in turn express themselves through different interests and interest groups. Unsurprisingly, in the literature and sometimes in everyday professional conversations on ESG issues, the investor community is often considered and treated as a homogeneous group. This tendency, in itself, tends to conceal the differences in both interests and power relations that could exist amongst investors, and appears to stand in the way of mainstreaming ESG

[3] PharmaFutures brings larger pharmaceutical companies together with pharma sector investors, to explore what information is needed by investors that is not currently provided and how best to provide this.

issues in investment decisions. A participant in the Utrecht focus group session drew attention to the fact that: "We should be careful here to recognise that investors are not an homogeneous group. They are different and have different needs and therefore require different approaches".

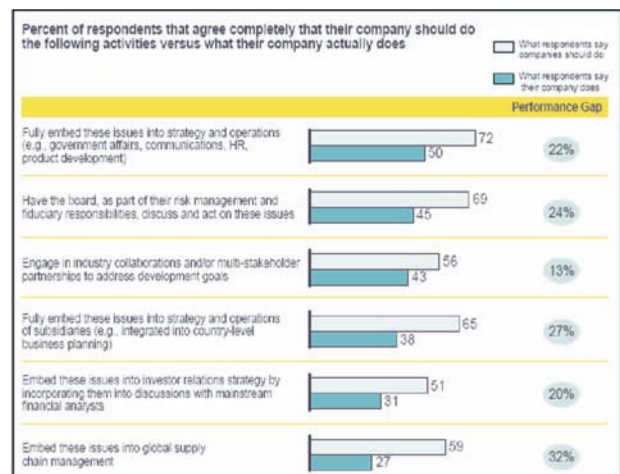
2.2 Obstacles inside Companies

Many of the same obstacles were identified as also applying inside companies too. Drawing an analogy with a pipe carrying water, leakages (obstacles) occur at numerous points in the pipe (achieving, measuring, reporting and communicating ESG performance).

- Companies are at different stages of CR maturity (and even within the same firm, may be more mature in certain parts of the business or on particular topics), and only some companies, therefore, will have significant improvements in ESG performance to be able to report;
- Even many of the more mature companies when it comes to embedding CR and sustainability have only recently made the explicit link between this commitment and their overall strategy; others have still to do so;
- Many have struggled with how to explain this linkage satisfactorily, in terms of how the failure to link creates corporate risks, and how making the link creates opportunities;
- Senior managers may not, therefore, yet appreciate the significance of ESG performance data presented to them in terms of potential or actual impact on business performance;
- Or they may understand the significance of the data but not yet trust their robustness and accuracy;
- Even where the data are available, these may be dispersed in different parts of the business, or held within a specialist CR / sustainability function which may be disconnected from the business;
- In particular, there may be a disconnect or outmoded thinking about the role and relevance of the specialist 'sustainability' / ESG performance data;
- This could apply particularly within the Investor Relations function with its well-established channels of communication and processes;
- Even where those responsible for communicating with investors (CEO, FD, Head of Investor Relations) understand the significance of the ESG performance data they have and this is positive, there may be a reluctance to share these data with mainstream investors due to seemingly justified or misplaced assumptions about the likely response of investors;
- There may, for example, be a feeling that the data are available in the Sustainability report and yet they get no questions from investors – not necessarily recognising that these reports (and even the main annual reports often nowadays) are not seemingly read by investors.

As a result, McKinsey & Co (see figure 3) found that CEOs of companies already committed to embedding CR and improving ESG performance, regard briefing mainstream investors about what they were doing as the least important of key requirements for embedding. What is not clear is whether interviewees rated briefing investors low because of their assumptions about investor indifference; their own concerns about the robustness of their ESG performance data; their knowledge about what their ESG data currently show; or because they did not regard mainstream investors as a significant driver or obstacle for embedding CR.

Figure 3: McKinsey survey: "Performance Gap"



Source: Feb 2007 McKinsey survey of 391 UN Global Compact participant CEOs

Whilst the research team did not conduct a separate detailed inquiry in academic or practitioner literature about these assumptions, nothing that we found in the literature or in focus groups, interviews and the stakeholder consultations, contradicted this description.

2.3 Underlying obstacle of lack of intellectual justification

For more than 35 years, research on the role and responsibilities of business in society has been searching for the Holy Grail represented by the business case for corporate responsibility. Therefore, an increasing number of studies on the Corporate Social Performance (CSP) – Corporate Financial Performance (CFP) link have been produced. CSP can be defined as the outcome of implementing CR activities and behaviours: it comprises principles of social responsibility, processes of social responsiveness, and policies, programmes and observable outcomes as they relate to the firms' relationships with stakeholders (Wartick & Cochran, 1985; Wood, 1991). In other words, CSP refers to the observable and measurable outcomes of corporate social actions.

Unfortunately, the traditional approach to the analysis of the relationship between CR, social performance and financial performance has led to inconclusive results: figure 4. (Barnett, 2007; Margolis and Walsh, 2003; McWilliams and Siegel, 2000; Orlitzky, Schmidt & Rynes, 2003; Rubbens & Wessels, 2004). In fact, the link between CSP and CFP is usually complex, not direct and not immediate, and is affected by many contingencies (Devinney, 2009).

Now, we have to recognise that there is no "silver bullet". However, this lack of evidence has often undermined attempts to fully integrate CR in managerial decision-making. It has also impeded evaluation practices of the "mainstream" investment community. If there is no clear relationship between CR and, for example, net income, earnings per share and market value, why should CR be taken into account in investment decisions?

The problem is that this approach is both simplistic and problematic. From a strategic standpoint, not integrating CR means for companies a dramatically limited understanding of their surrounding environment. For the investment community, not considering the possible impacts of CR means losing opportunities for more reliable and robust investments. Unfortunately, in this case, the financial dimension is still the prevailing criterion for performance assessment. But companies are too complex organisations to be evaluated internally and externally only in monetary terms. Complex organisations in complex times and in complex environments call for more refined and advanced methodologies and tools.

Instead of searching for the "silver bullet", empirical investigation needs to focus on a deeper understanding of what it means to succeed in CR, disentangling its specific dimensions.

Figure 4: Relationship between Social Performance and Financial Performance

Tabla 2
Resumen de los resultados con respecto a la relación entre rendimiento social y rendimiento financiero

	Griffin y Mahon (1997)	Roman et al. Mahon (1997)	Margolis y Walsh (2003)		Orlitzky et al. (2003)
Relación positiva	33	32	54	16+	27
Relación negativa	20	5	7	0+	2
Relación nula o no significativa	9	14	28	3+	-
Resultados mixtos	-	-	20	3+	23
TOTAL	62 (51)*	51 (46)*	109*	22*	52

Fuente: Adaptado de Allouche y Laroche (2006)
* El total de trabajos considerados no coincide con la suma de las diferentes conclusiones porque algunos de los trabajos ofrecen más de una conclusión según las variables utilizadas.
+ El rendimiento financiero es la variable independiente.

IESE Review of Academic studies of link between Corporate Responsibility and Financial Performance – 2006

Value Creation Framework

Starting from the analysis of existing literature on the link between Corporate Social Performance and Corporate Financial Performance, and deepening the different dimensions underlying the relationship between specific CR-related interventions and company performance, our research answered the call for a more detailed understanding of the mechanisms through which CR can impact on the performance of the firm (see Perrini, Russo, Tencati, & Vurro, 2009). There is no doubt that CR may be beneficial for committed firms. Less clear is what dimensions firms can leverage to improve their abilities to benefit from responsible behaviour.

In more detail, the obsession with the search for a unique "business case" has left unexplored questions about what firms are doing in response to their actual and perceived renewed role in society and with what effects.

In the real world, in many cases business practice shows how firms engaged in social and environmental activities are enlarging their sphere of responsibility and accountability, moving beyond simple monetary measures and a generic definition of CR to orient and manage their behaviour. Therefore, many companies tend to consider social and environmental performance not as univocal constructs (ie having only one unambigious meaning), but increasingly break it up into specific stakeholder-firm relationships and related CR areas.

In this sense, if CR is considered as a new strategic approach based on the crucial value of stakeholder relationships and on the capacity of a firm to meet stakeholder needs beyond mere legal compliance, then a clear understanding of CR performance consequences should identify possible different targets and investigate how specific activities translate into organisational, managerial or market gains according to a multiple-bottom-line thinking (Perrini & Tencati, 2006; Tencati & Zsolnai, 2009).

Trying to answer this call for reorienting business in society research towards a deeper understanding of the drivers of CR-related performance, recent research has taken account of the impact of CR at a different level of analysis (Aguilera, Rupp, Williams & Ganapathi, 2007) and in specific management areas and stakeholder interactions (Perrini, Pogutz & Tencati, 2006; Tencati, Perrini & Pogutz, 2004).

A broad and in-depth review of empirical and theoretical contributions allowed us to identify possible areas on which CR policies can impact (CR-related performance drivers) and the relationships of influence between these drivers and the financial (i.e., cost-related or revenue-related) outcomes.

The CR drivers are as follows:

- Organisational;
- Customer;
- Society (including the relationships with suppliers);
- Natural environment;
- Innovation;
- Corporate governance.

With regard to the financial outcomes, the revenue-related ones comprise the following:

- Growth opportunities;
- Competitive positioning;
- Brand equity.

The cost-related outcomes are as follows:

- Cost of labour;
- Operational efficiency;
- Cost of capital;
- Risk management.

According to this approach, the real case for CR has to be based on a different logic, in which:

(1) specific drivers of social performance are studied (in place of indicators of overall social responsibility);

(2) intermediate performance measures, such as operational efficiency, are analysed to point out the financial impact of CR (Pivato, Misani, & Tencati, 2008).

Figure 5 provides a summary picture of the main mechanisms linking CR-related drivers to specific performance areas, as emerging from the literature review carried out. We call this the Value-Creation Framework.

Though not exhaustive, Figure 5 allows one to define a taxonomy of the conditions under which one can expect certain results, as well as the mechanisms by which specific activities can relate to performance outcomes.

This theoretical framework provides an innovative perspective for both scholars and practitioners.

For academia, this work opens new research avenues: disentangling specific dimensions of the CSP-CFP link offers insights into the driving factors explaining the variability in corporate performance. Moreover, linkages among CR policies, CR-related drivers and financial outcomes need to be further studied: there is more than a single way in which improving company social and environmental performance can turn into performance differentials.

From the practitioner standpoint, and with a special focus on the relationships between firms and the investment community, this perspective provides an innovative and common framework through which companies and financial analysts and investors can communicate. Firms can adopt this framework to assess and orient their own behaviour. The investment community can use this approach to better read and appreciate the initiatives and efforts carried out by companies, and to better evaluate the real quality of management and the sustainability of the value creation processes developed by the firms.

Therefore, new managerial tools are needed to support firms and the investment community on the one side in performance management and evaluation and, on the other, in a mutual dialogue, and to complement and integrate with traditional financial methodologies.

The model advanced by the EU CSR Alliance Laboratory has exactly this purpose, that is, providing enterprises and the financial community with a tool able to improve the quality of the interaction between firms and investors and the corporate performance evaluation by adopting a more comprehensive and complete view – see www.investorvalue.org. The revised version of the Lab operational model can be found at appendix 3.

The Value Creation Framework is a research framework. It has been designed to illustrate a new, more complete and coherent approach to the analysis of the relationships between CSP and CFP. It is based on an extended academic literature review of more than 170 contributions.

Like every good research output it has managerial implications too. There is an evident lack of understanding between firms and the investment community. Firms are deploying broad value creation processes by targeting, involving and engaging stakeholders and constituencies but these efforts are not appreciated by the market.

More generally, the current financial crisis has further shown that the traditional financial methodologies are unable to capture the real value created by a company. Firm value and market value are only partially aligned. The perspective introduced by the framework tries to provide a positive contribution to solve this critical problem. But what is clear is that if we intend to foster an enhanced dialogue between firms and the investment community, then specific managerial tools are needed. From this standpoint, the Lab proposal is a methodology that is intended to fill the gap between the value creation processes generated by firms by leveraging ESG factors and the market appreciation of these activities.

Furthermore, the Lab model could be a promising starting point to establish a platform for dialogue between leading companies and representatives of the financial community to define a shared European framework/set of tools (including specific performance indicators) for valuing non-financial performance. This platform should be promoted, convened and supported by the European Commission as part of its multi-stakeholder engagement process – see recommendations section below.

Figure 5: The Value Creation Framework

CR values, beliefs & activities

ORGANIZATIONAL DRIVERS

Work content
Job design
Knowledge management
Safety and stability

Commitment
Satisfaction
Motivation

CUSTOMER DRIVERS

Transparency and reliability
Open dialogue
Mutual understanding
Quality and innovation

Trust
Reputation
Identification
Satisfaction

SOCIETY DRIVERS

Engagement and dialogue
Community development
Sustainable supply chain management

License to operate
Social capital

NATURAL ENVIRONMENT DRIVERS

Impact control, prevention and assessment
Managerial tools and strategies

Compliance
Reliability
Reputation
Sustainability

INNOVATION DRIVERS

Social and environmental programs
Operational changes

New product and process development

CORPORATE GOVERNANCE DRIVERS

Voluntary disclosure
Governance and engagement

Transparency
Reliability

REVENUE-RELATED OUTCOMES

Growth opportunities
Competitive positioning
Brand equity

COST-RELATED OUTCOMES

Cost of labour
Operational efficiency
Cost of capital
Risk management

Figure 5: The Value Creation Framework
Source: Perrini et al., 2009

How Companies and Investors might make use of the Value Creation Framework

The Value Creation Framework is a research framework: the Lab model is an operational tool, to make use of the Framework. The Framework provides a new perspective/thinking and the Lab model is a tool aimed at implementing that perspective in firms and in the investment community.

It is not expected that any one company will be able or will wish to demonstrate all the linkages suggested by the framework. Rather, a company would identify those linkages most appropriate for it (based on available, collectible metrics; positive results from previous company activity; alignment with current priorities for company attention). Over time, it is anticipated that more linkages will become apparent and susceptible to collection of positive metrics.

The Value Creation Framework and the associated Lab operational tool are an integral part of the processes and commitments required from companies to embed Corporate Responsibility and Sustainability, discussed in the EABIS Colloquium 2008 (www.eabis2008.info).

Within the investment community, it is not expected that the approach supported by the Value Creation Framework and associated Lab model would replace existing investment models. Rather they offer rich insights for refining existing models.

The next steps would be for some of the business-led CR coalitions such as the World Business Council for Sustainable Development and CSR Europe with its national partners network such as Business in the Community in the UK or Sodalitas in Italy; and other convening groups for responsible business leadership such as the Prince of Wales Accounting for Sustainability initiative, to promote the perspective provided by the Value Creation Framework and related Lab tool to member companies.

There needs to be a critical mass of vanguard companies committed to adopting the approach provided by using the Value Creation Framework and operationalised by the Lab methodology. They can then talk about the way that improved ESG performance is contributing to business strategy and value-creation, with innovative thinking helping the company to generate the data to demonstrate this. Focus groups convened by the WBCSD (2008) indicated that if (say) 200 top corporate CEOs spoke to investors with a new voice, it would make a significant difference to mainstream investors.

Simultaneously, the rationale of the Value Creation Framework needs to be incorporated into the training programmes for the investor community offered by professional associations such as European Federation of Financial Analysts Societies (EFFAS) and by business schools.

In parallel, it will facilitate understanding and adoption by both target groups: business and the investment community if:

- Worked examples become available of how companies are using the Value Creation Framework and the operational Lab proposal to stimulate the capture and deployment of data on the ways that improved ESG performance is contributing to business strategy and value-creation.

- Generic data are collected on some of the key metrics in the way that, for example, Towers Perrin as compensation and human resources experts have accumulated data on employee advocacy and business performance.

- Some early adopters are prepared to allow researchers to monitor their experience.

- Other levers – existing initiatives and organisations – can be pulled to advance awareness of the potential of the Value Creation Framework – for example the current revisions of the European Foundation for Quality Management (EFQM).

This is discussed further in section 6 below.

4

Changing Today's Dominant Convention in the Investment Community and Business

Financial market participants coordinate their actions through dominant conventions – i.e. some norms of behaviour that determine the normality of a situation and give saliency to implementing decisions shared and diffused across the market. The current convention does not generally incorporate ESG information into company valuation. But our contention is that the myriad of initiatives that have emerged over the last few years to encourage the integration of ESG information represent endeavours towards changing the current dominant convention of valuing companies.

4.1 ESG Integration: An emerging trend

The first claims and practices linked to the integration of ESG information into mainstream investment decision-making appeared publicly at the beginning of 2001. These were isolated projects launched by some pioneers convinced that ESG analysis can help asset managers and financial analysts to better assess the risks and seize the opportunities for companies. Nonetheless, in a short time period, the integration of ESG information into mainstream investment decision-making has created a growing interest within the financial community; and many other initiatives have emerged to encourage traditional institutional investors and research providers to consider ESG issues.

• ESG research providers' development

Since the 1990's, an increasing number of independent specialised research organisations have been created to provide investors with background data on ESG. Besides these independent organisations, many research teams have been developed inside investment management houses to support asset managers in managing ESG information.

At the beginning of 2000, the research on environmental, social and governance issues crossed a new stage with the creation of the first ESG research teams inside brokerage houses. In fact, the development of ESG research teams within sell-side companies symbolises the first concrete steps towards the mainstreaming of ESG information integration.

• Institutional investors' collaborations

ESG integration has rapidly moved from scattered initiatives to organised joint programmes. Among the most influential professional collaborations developed with the objective of promoting the integration of ESG information into mainstream research have been the Enhanced Analytics Initiative (EAI), now merged within the UN Principles for Responsible Investment (See http://www.unpri.org) (UNPRI) and the Carbon Disclosure Project (CDP), (see a more complete list below: Table 1)

Table 1: Examples of collaborative initiatives

Enhanced Analytics Initiative
The EAI "is an international collaboration between asset owners and asset managers aimed at encouraging better investment research, in particular research that takes account of the impact of extra-financial issues on long-term investment" [EAI, 2007]. The EAI was launched at the end of 2003 by a founding group composed of institutional investors[4] managing some $364 billion in assets. In October 2008 EAI was integrated within:

UN Principles for Responsible Investment (UNPRI)
The PRI were launched in April 2006 by former UN Secretary General Kofi Annan in collaboration with 20 major institutional investors. The initiative consists of six principles that provide a framework to incorporate ESG issues into mainstream investment decision-making and ownership practices. The six principles are not prescriptive, the signatories publicly commit to adopt and implement them, where consistent with their fiduciary responsibilities. By 2009, the PRI had grown into a coalition of more than 400 of the largest institutional investors and asset managers worldwide representing some $15 trillion dollars under management [Hobbs, 2008].
www.unpri.org

Carbon Disclosure Project
CDP was formed in 2000 as an independent not-for-profit organisation. It has 475 signatory institutional investors with $55 trillion in assets under management. The aim of the project is to assess the impacts of climate changes on company valuations. CDP sends out questionnaire each year to the 500 most important listed companies in the world in order to gather detailed information about the opportunities and risks that climate changes represent for them. The purpose is to encourage the development of a shared methodology for measuring greenhouse gas emissions and facilitate its integration in the broader analysis of financial investments.
http://www.cdproject.net/.

• Financial analysts' collaborations

The financial analysts' community has also witnessed the emergence of professional collaborations addressing the inclusion of ESG information. In France for example, some members of the SFAF, the French association of financial analysts, in 2002 founded a commission[5] to discuss and exchange ideas about the analysis of sustainable development information and to increase investment community awareness of the importance of this issue. At a European level, the EFFAS CESG (European Federation of Financial Analysts (EFFAS) Commission on ESG Environmental, Social & Governance (CESG)) was founded in October 2007 with the objective of "Facilitating the integration of ESG aspects of corporate performance into investment processes".

• Other professional initiatives

Many consultancy companies have positioned themselves in the emerging market of services related to ESG information and financial advice. Some of them rely on their skills in financial investment domains to propose new services combining ESG issues analysis and investment advice. The British consulting company Mercer is among the pioneering investment consulting firm that have developed such new services. Its newly-created division specialising in responsible investment is progressively striving for the extension of its services to mainstream investors. Several others consultancy companies have also launched services to help investors to develop investment approaches that integrate ESG issues within a fiduciary framework.

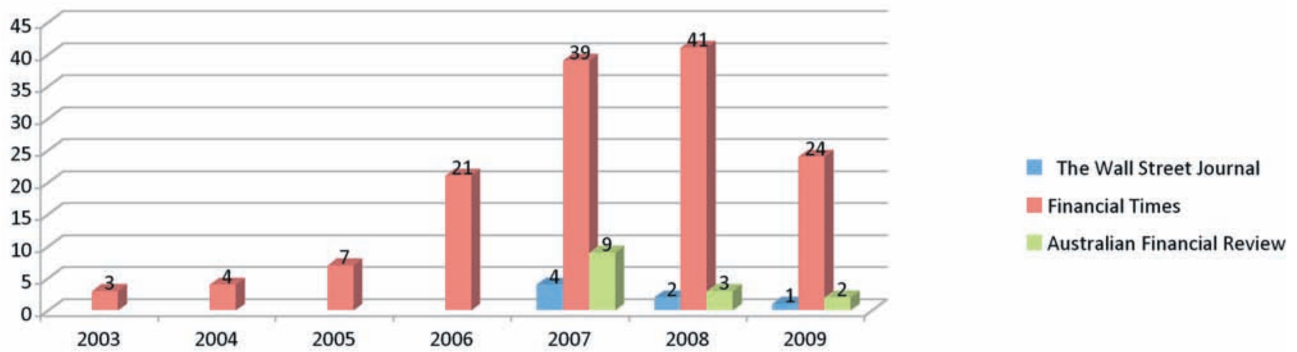
• Surveys, reports and publications

The number of reports, articles and surveys published in the last few years about ESG information, usefulness to the financial community and ESG integration into investment decisions, represents another indicator of the growing interest in these issues. [Our research team identified more than 80 such English language reports in the last decade alone.]

Similarly, the specialised Press has shown a greater interest in the inclusion of ESG issues in investment practices. A search in the Financial Times, Wall Street Journal and the Australian Financial Review reveals a significant increase in articles published on the topic since 2006-2007. "Environmental, social and governance" were used as key words.

[4] BNP Paribas Asset Management (France); PGGM (Netherlands); Deutscher Investment Trust (Germany); Dresdner investment management (Germany); RCM (UK) and Universities Superannuation Scheme (UK).
[5] La Commission Finance et Développement Durable.

Figure 6: ESG references published between 2003 and 2009 (as of 07 July 2009)



4.2 Influencing mechanisms

The myriad of initiatives – be they collaborative initiatives, research platforms or incentive systems – that have developed do not only demonstrate the growing interest in ESG but also contribute to the integration of ESG information into investment decisions[6].

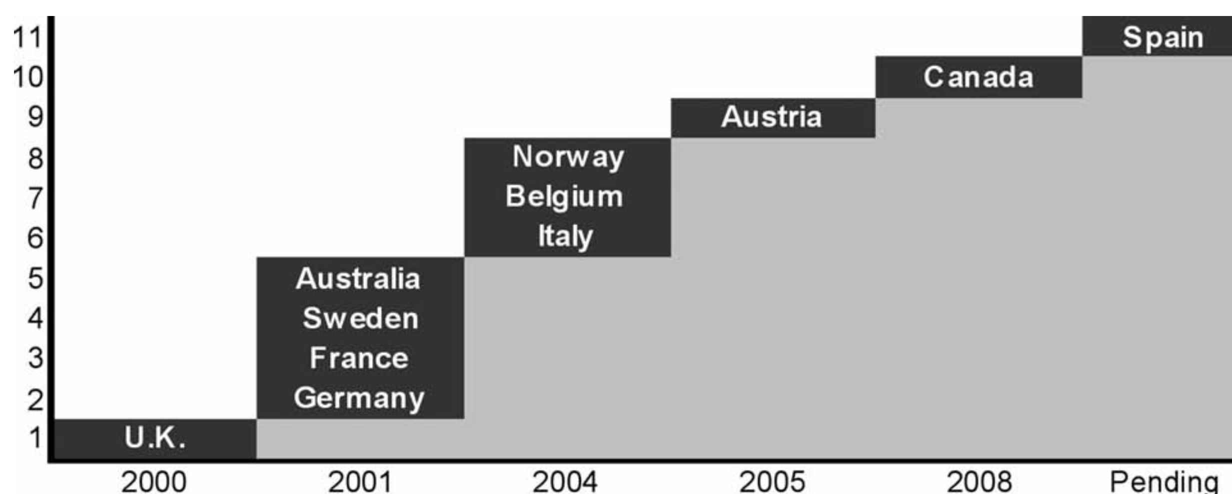
These initiatives include a number of institutional investors who are exercising pressures through contractual restrictions. Fund managers and sell-side financial analysts may be contractually required by institutional investors to integrate ESG issues in the management mandate. Over the last ten years, many institutional investors have launched calls for tenders for bond and equity mandates to include such a restriction. Indeed, such calls for tenders issued by major institutional investors, as for example the FRR[7] in France or the Norwegian Government Pension Fund-Global, have contributed to the development of extra-financial research within investment companies.

Over the last decade, many governments have launched new regulations to establish ESG disclosure requirements for pension funds. The first jurisdiction to establish a formal obligation for pension fund ESG disclosure was the United Kingdom in 2000. Following this pioneering initiative, many other governments have put similar rules in place. Figure 7 below recapitulates the regulations established worldwide up to February 2009.

[6] The research team's working paper The integration of ESG information into investment processes: Toward an emerging collective belief? David Bourghelle, Hager Jemel, Céline Louche discusses the mechanisms in terms of DiMaggio and Powell's 1983 framework of coercive, mimetic and normative mechanisms.

[7] FRR (Fonds de Reserve pour les Retraites) is the French pensions reserve fund.

Figure 7: Disclosure regulations for pension funds (Bourghelle et al., 2009)



A number of professional collaboration networks to create and share knowledge about ESG information such as the EFFAS Commission on ESG Issues[8] have been set up. The main objective of these initiatives is to facilitate the sharing of knowledge, methodologies and expertise among the investment community. Consulting firms, being viewed as experts, are also playing an important role by diffusing models, best practices, and solutions. Rankings and rewards such as such as the Thomson Extel Socially Responsible Investment Survey[9] (launched in 2003), the ESG Leaders Awards (launched in 2007) or the bi-annual EAI ranking (launched in 2004) reduce uncertainties as well by highlighting the efforts undertaken by the financial professionals in the domain of ESG integration. By putting them in the spotlight, they encourage many others to join the movement and provide legitimacy to those that are already involved.

Practices are also spread by financial analysts moving from one company to another. For example, in order to launch its extra-financial research activity in 2004, Citigroup hired the analyst who founded the ESG research team in HSBC. In the same way, Société Générale recruited two senior ESG analysts from CM CIC to initiate its ESG research activity in 2004. Those transfers are helping the diffusion of models among different organisations because individuals come with methods and practices developed with their original employer and tend to replicate them in the new company.

There are also external research initiatives: a good example is the creation of the AI CSRR (Association for Independent Corporate Sustainability and Responsibility Research). The AI CSRR has developed the first quality standard for corporate responsibility and SRI research and analysis. This standard named CSRR- QS 2.1 provides a general description of principles and requirements regarding the activities of the field of responsible research. It focuses mainly on the operational requirements of SRI-related products and services.

Several collaborations have also been developed between professional associations and academic groups to promote research linking finance with social responsibility and sustainability issues, such as the French SIF Award, the UNPRI Academic Network, or the European Centre for Corporate Engagement.

In February 2009, another similar initiative was launched in Australia. The Australian government announced $AU 2.5 million funding over three years to establish the Responsible Investment Academy. This Academy will be managed by the Responsible Investment Association Australasia (RIAA) and governed by an Australian and international Advisory Council. Its main goal is "to offer a range of premium Continuing Professional Development (CPD) courses as well as diploma and certificate courses[10]". The implementation of a specific academic course is another way to establish and legitimate the area of responsible investment.

[8] www.effas.com/en/cesg
[9] now Thomson Reuters Extel/UKSIF Survey
[10] http://www.responsibleinvestment.org

Table 2: Initiatives to promote ESG measurement, reporting and use

TO COMPANIES	TO INVESTORS	TO BOTH
Governments, EU, legal		
EU Modernisation directive A46 and Shareholder Rights Initiative	UNEP FI OECD draft pensions fund guidelines Sovereign Wealth Fund Institute	UNEP Green Economy
Business / business-led coalitions		
PWC Corporate Reporting Tomorrow's Company: how companies use sustainability reports internally		WBCSD Markets& Valuation Goldman Sachs SUSTAIN SAM/PWC Sustainability yearbook
Multi-stakeholder		
2020 Future of corporation	Geneva Sustainable Finance CERES lobby to US SEC	CSR Alliance Lab POWAFS Carbon Disclosure Project Aspen Principles GRI Reaching Investors: commercial valuation through ESG Disclosure
Investor		
	PRI / EAI South African SIF SAM Future of Finance Equator Principles Norwegian Institutional investors Sustainable Value Creation and report ESG Nordic Engagement Cooperation Initiative	
Professional bodies		
EUROSIF call for mandatory ESG reporting	EFFAS ESG Commission	
NGOS		
ECCJ call for mandatory reporting	Fair Pensions	
Training		
	Australian Responsible Investment Academy	
Academic		
		EABIS Value-Creation UNPRI Academic Network
Facilitating dialogue		
		Sustainability Pharma-futures Kuala Lumpur Dialogues Rockefeller Global Impact Investing Network

5

How Might Collaboration Evolve?

The table in section 4 immediately above – whilst not exhaustive – shows the ferment of activity now taking place from an increasing range of types of organisation and geographic approach, and at an accelerating pace. It is unclear, however, whether this has yet reached critical mass to achieve a tipping point – either with companies or the investment community.

What follows – as part suggestion, part speculation – is an examination of how the tipping point might be reached. It is based on: Lab stakeholder-engagement meetings, focus groups, analysis of practitioner reports and interviews conducted by the research team director.

John Kotter in 'Leading Change' (1996) suggests an eight-step process for understanding change which starts with a sense of urgency and of the need for change, see Table 3 below. The Inter-Governmental Panel on Climate Change, Stern Report to the UK Government, Al Gore's "An Inconvenient Truth", and numerous subsequent reports have created that sense of urgency on climate change and arguably on the broader issue of sustainable development. This is now coupled with the recognition that sustainability poses risks to business – and a dawning understanding that it also creates opportunities.

Table 3: Understanding change

1. establishing a greater sense of urgency,
2. creating the guiding coalition,
3. developing a vision and strategy,
4. communicating the change vision,
5. empowering others to act,
6. creating short-term wins,
7. consolidating gains and producing even more change
8. institutionalizing new approaches in the future.

Leading Change (1996) John Kotter

As previous sections of this report have shown, what is missing is widespread understanding of how this translates into corporate strategy, how to measure and report on ESG performance, and how to incorporate ESG performance in valuation of businesses.

Whilst we believe the Value Creation Framework and the related Lab operational tool can be a critical resource for the later step, there needs to be a sufficiently bold and high-powered initiative to break through the current obstacles (identified in section 2).

As discussed in section 4, there are a number of important initiatives already in play. The trick is not to create another – but rather to stimulate closer collaboration, and mutual reinforcement and division of labour between the existing initiatives.

It is suggested that separate gatherings of corporate CEOs this autumn/winter, e.g.:

- World Business Council for Sustainable Development (WBCSD) CEOs meeting, Washington DC, October 2009
- putative BITC leaders' gathering autumn 2009
- putative EU Commission's invitation to corporate CEOs
- Prince of Wales Accounting for Sustainability annual meeting December 2009

could each, within their own frameworks and in the context of their own previous work, issue similar statements of intent for signing by corporate CEOs. Specifically CEOs would be invited publicly to commit themselves to explain in the 2010 cycle of investor-roadshows, analysts' briefing, and CEO results presentations:

- The material sustainability challenges for their business and how this is impacting on corporate strategy
- How improving ESG performance affects extra or non financial performance and, therefore, long-term drivers of business success (according to the perspective provided by the Value Creation Framework)
- ESG performance and expectations of future improvements in ESG (ESG forecasts alongside 'risks and profits' forecasts)

Preferably the participating CEOs would give advance notification of their intentions directly to their investor community as well.

The international accounting firm PwC is currently analysing on behalf of the Prince of Wales Accounting for Sustainability (POWAFS) and for the WBCSD, the public domain, standard 2009 results presentations of WBCSD's 200 member companies to see what they are already saying about ESG performance and sustainability.

It is important that there be a similar exercise in 2011, extended to other companies involved through BITC, EU CSR Alliance, POWAFS which are not already included in the WBSCD sample. This would show how the explanations of ESG and sustainability had shifted from the 2009 to 2010 reporting cycles.

It would also be necessary for some of the initiatives to facilitate investor dialogues to assess the impact of such increased corporate briefing on ESG and sustainability; what had worked and what had not in these briefings, what improvements investors believe should be made; and what help – if any - investors needed (e.g. training, access to follow-up information) to optimise their use of the enhanced data.

A follow up survey of investors (owners, fund managers, analysts) should be conducted in 2011 to assess changes in behaviour, alongside a parallel survey of companies to assess changes in their own behaviour and their perceptions of changes amongst investors.

6

Recommendations

6.1 To the EU CSR Alliance Laboratory

We recommend to the Lab to:

a refine its model in the light of the research recommendations;

b use the fact that it is a finite initiative and, therefore, not a competitor to existing organisations, to pursue a dialogue with a number of the organisations that have convening power with corporate CEOs, to encourage them to seek CEOs' commitments to include in their 2010 results presentations to investors an explanation of why and how they are embedding sustainability within their corporate strategies (as outlined in section 5 above);

c in particular, to encourage the sponsors of the EU CSR Alliance – including the EU Commission itself – to invite corporate CEOs and investors to act.

6.2 EU Commission

We recommend:

a the convening by the new Commission of a meeting with vanguard corporate CEOs and investors willing to take a lead in publicly committing to explain how they are committed to improving and analysing ESG performance because of the risks in not doing so and the opportunities for value-creation in so doing;

b funding for an EU equivalent of the new Australian Government-funded Australian Responsible Investment Academy to provide training for analysts and investors in how to evaluate ESG performance as part of overall evaluation of quality of corporate strategy and management.

6.3 Companies

We recommend that companies:

a adopt and adapt the perspective provided by the Value Creation Framework and use the Laboratory's related operational tool as a vehicle for incorporating sustainability within overall corporate strategy;

b publicly commit at CEO level to include an explanation of why and how they have done this, as an integral part of their investor presentations for the 2010 results season;

c experiment with different approaches to empowering Investor Relations and CR functions in their business to work together, e.g. through internal secondments and participation in joint training in the adoption of the Value Creation Framework approach and in the use of the Lab methodology;

d encourage their Pension Fund Trustees to consider making ESG performance one of the factors in their mandates to their fund managers.

6.4 Investors

We recommend that investors:

incorporate the Value Creation Framework thinking in their models for assessing corporate value.

6.5 Business-Led CR and Sustainability Coalitions, Multi-Stakeholder Fora and Think-Tanks

Even if a critical mass of vanguard companies and investors respond positively to these recommendations, we believe that there is a need for "honest brokers" able to convene and facilitate structured conversations between companies and investors, adopting the Value Creation Framework perspective, as the think-tank/consultancy Sustainability has done with their Pharma Futures initiative, (see section 2.1 above). We support efforts by groups such as WBCSD and Accounting for Sustainability to build a critical mass of businesses accounting for and reporting to investors on sustainability impacts.

6.6 EABIS and European Business Schools

There is a critical role for business schools as educators of current and future managers through executive and graduate education programmes, and through the writings of faculty.

We recommend that:

a EABIS uses this report and initiatives, such as those to encourage schools to sign, and then embed the Principles for Responsible Management Education, to reach out beyond CR, sustainability and business ethics faculty, to promote these ideas to finance, strategy and management faculty (see http://www.unprme.org) and to encourage finance and strategy departments to develop teaching courses around ideas of long-term value-creation.

6.7 Recommendations for Further Research

Although this project has extended over almost two years and has involved an international research team from five countries, and input from a range of international perspectives, there are inevitably, a number of dimensions that have not been covered and could usefully be the subject of future research.

These include:

- The role of the ratings agencies has not been considered and they have not been involved. However, a number of commentators have emphasised that they could and should be incorporating ESG risks into their assessments.
- We have not explored the dialogue and relationships inside companies between the CR/Sustainability function and the Investor Relations function, and within the investment community between ESG analysts and financial analysts and how this can be improved. (Internal communication has come up several times as a barrier but it remains an under-explored 'black box'.)
- The Value Creation Framework represents an important breakthrough, but the next step would be to show the interactions between improvements to the individual drivers of non-financial performance with one another.
- Further exploration of communications between investors and companies in general and about ESG in particular, along the lines recommended in section 6.5 above.
- Behaviour change: understanding how investors work and function; how do they make decisions?

7 Conclusion

In the English language alone, we have identified almost 100 practitioner reports produced since the millennium on the obstacles to the incorporation of ESG performance into the mainstream investment community's valuation of business, and how these barriers can be overcome. Through this EABIS research project, we have had direct dialogue with more than 100 different organisations and initiatives working on these topics as well as various academic researchers. This is crowded territory.

Building on this rich foundation of academic and practitioner work, we believe we are contributing something new and positive: the definition of the Value Creation Framework; and the vision of how a network of contacts and collaborations with a range of influential individuals and organisations could create the opportunity for a wide dissemination of the Value Creation Framework, and associated thinking, to decision-makers and opinion-formers across the EU and beyond.

The research process itself has involved real-time partnership between academics and practitioners. Whilst not without difficulties and challenges, this approach to research also offers potentially better ways of working for subsequent EABIS research projects – see appendix 2.

Appendices

Appendix I

GLOSSARY – List of Abbreviations

ESG factors are a subset of Non-Financial Performance
ESG ⇒ This term has emerged globally, although mostly in the investment community, to describe the environmental, social and corporate governance issues that investors are considering in the context of corporate behaviour.

ESG integration ⇒ The active investment management processes that includes an analysis of environmental, social and corporate governance risks and opportunities to the extent they affect the economic performance of an investment. (FROM ***Translating ESG into Sustainable Value: a field guide for companies and investors based on a 2008 international study by the WBCSD and UNEPFI.*** Forthcoming 2009)

Corporate (Social) Responsibility is defined by the EU Commission as *"A concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis."*

It is the commitment to minimise negative environmental and social impacts and to maximise positive environmental and social impacts. (Doughty Centre for Corporate Responsibility). As such, C(S)R is a commitment to improving ESG Performance.

Sustainable development is development that *"meets the needs of the present without compromising the ability of future generations to meet their own needs."* (Our Common Future, Report of the Brundtland Commission, 1987).

Sustainable development & business *"... leading global companies of the future will be those that provide goods and services and reach new customers in ways that address the world's major challenges – including poverty, climate change, resource depletion, globalization, and demographic shifts."* (WBCSD, 2006).

Appendix 2

BACKGROUND – To CSR Alliance, lab and EABIS research project in support

The European CSR Alliance was formed by the EU Commission, Business Europe and CSR Europe in March 2006 as a voluntary initiative to improve Corporate Responsibility across the EU.

"The priority areas of the Alliance will be addressed by "open coalitions of cooperation" bringing together interested companies ready to tackle these issues in the form of "laboratory meetings" in order to explore and to develop joint operational projects, in partnership with relevant experts and stakeholders and with the backing of the European Commission."
(European Commission CSR White Paper: 22 March 2006)

One of the early laboratories to emerge through 2006 and early 2007 was one on measurement and communication of non-financial performance and how these data could be better used by businesses and investors. Early discussions amongst potential corporate members of this laboratory confirmed the need for research capacity to support their work. During spring/summer of 2007 this crystallised into discussions with EABIS about whether an EABIS-supported research project might run in parallel and close synergy with the laboratory. Over the rest of 2007/ beginning 2008, an outline research project and research team emerged. This team from Cranfield, Bocconi and Vlerick, has worked symbiotically with the Lab and CSR Europe: Table 4 and see timeline – Table 5. The project and the research team have worked in close collaboration with participating companies and other stakeholders. This is very much in the spirit of EABIS-supported research to be both rigorous, relevant and timely. Learning from this approach is summarised.

Research Methodology

The data for this study were drawn from multiple sources: an extensive academic literature review, semi-structured interviews, focus group discussions, stakeholder consultations, review of practitioners' reports since the start of the millennium, and a Delphi panel session.

Extensive academic literature review and semi-structured interviews

The empirical work consists of an exploratory research based on extensive academic literature review and semi-structured interviews and secondary data.

Academic literature review and development of the Value Creation Framework

The research working paper "Going beyond a long-lasting debate: what is behind the relationship between corporate social and financial performance?" is based on an extensive review (more than 170 contributions) of the relevant empirical and theoretical academic literature on the following topics:

- alternative perspectives on the integration of CR in the theory of the firm;
- relationship between CSP and CFP starting from the two comprehensive meta-analyses developed by Margolis and Walsh (2003) and Orlitzky et al. (2003);
- non-financial reporting and socially responsible behaviour of firms addressed also from the strategic standpoint;
- impacts of CR strategies, policies and activities on the different management areas (e.g., H.R.; innovation; the natural environment; and so on);
- impacts of specific CR drivers on operational performance;
- empirical and theoretical mechanisms driving the impact of CR strategies, policies and activities on specific areas of business and operational performance.

Interviews

25 face-to-face semi-structured interviews were conducted between July 2007 and April 2009 with financial and extra-financial analysts and fund managers in France. The primary objective was to identify the main initiatives and levers that encourage the integration of ESG information and assess their potential to become integrated by mainstream investment community. The interviews were transcribed and coded and analysed using the qualitative data analysis software program QSR NVivo.

A series of scoping interviews with influential individuals selected to illustrate different elements of the company and investor universe (Company secretary, head of investor relations, CR director, Finance director, Pension fund, institutional investor, fund manager, corporate reporting specialists) were conducted in London.

Focus Group Discussions

The focus group discussions were facilitated by a group of experts drawn from academia and industry; see table 4. Given the sensitivity around ESG issues – especially with regards to competitive, regulatory and civil society pressures – these discussions were conducted in a 'safe' environment to encourage honest conversations, i.e. openness and sharing of information. The focus group discussion sessions were governed by the Chatham House rule[10] and as such, were not recorded – but notes were taken by the experts from academia and industry who observed the different sessions.

Table 4: Focus Group Session Observers

Focus Group Sessions	Academics	Institutional Affiliations	Business	Affiliation
Rome	Antonio Tencati Francesco Perrini	SDA Bocconi School of Management	Paolo Nazzaro	Telecom Italia
Frankfurt	Antonio Tencati	SDA Bocconi School of Management	Paolo Nazzaro	Telecom Italia
Paris	Hager Jemel	Lille	Jan Noterdame	CSR Europe
Stockholm	Céline Louche	Vlerick Leuven Gent Management School	Paolo Nazzaro	Telecom Italia
Utrecht	David Grayson Céline Louche	Cranfield School of Management Vlerick Leuven Gent Management School	John Swannick	Lloyds Banking Group

The notes generated from the focus group sessions were then qualitatively analysed by NVivo – a qualitative research analysis software.

Review of Practitioners' Reports

The study searched for practitioners' reports in this field since 2000 – given that much of the momentum in this field has been, mainly, since the turn of the century - and identified 82 reports from accounting firms, investor associations, business coalitions, investment banks, multinational institutions, consultancies and think tanks, governments and multi stakeholder fora. A list of the 82 reports was sent to 36 experts in the field to advise on the relevance and impacts of these reports. The experts were also asked to identify other reports the study might have missed out in the process. The intention here was to meta-analyse these reports with the aim of identifying the major issues involved in integration of ESG risks in investment decisions.

18 responses were received, out of the targeted 36 practitioner respondents. A good number of the reports presented to them were considered relevant and impactful. 13 extra reports were suggested through this process, which were added to the mix. In total, they constituted well over 4,000 pages; however, a sample of 22 reports – those most mentioned by the respondents was analysed. These reports were then qualitatively analysed by NVivo – a qualitative research analysis software.

Delphi Panel Session

Following the outcomes of the extensive academic literature review, semi-structured interviews, focus group sessions and the review of practitioners' reports, a Delphi panel session was run in London on July 9, 2009, arranged with the assistance of the Lab members of the research project to share the findings of the study with experts in the field and also to get their feedback on how to improve on the research. The Delphi panel session drew about 30 participants from the mainstream investment community, boutique SRI community, academia, professional bodies, and the CR/ sustainability community. The researchers were all involved in the Delphi panel sessions and the suggestions/ feedback from the sessions were further discussed and reflected upon by the researchers and Lab members immediately after the sessions, i.e. the next day, whilst the feedback was still fresh on the minds of the researchers and the Lab members.

[10] The Chatham House Rule reads as follows:
1.1.1 "When a meeting, or part thereof, is held under the Chatham House Rule, participants are free to use the information received, but neither the identity nor the affiliation of the speaker(s), nor that of any other participant, may be revealed".
The world-famous Chatham House Rule may be invoked at meetings to encourage openness and the sharing of information.
http://www.chathamhouse.org.uk/about/chathamhouserule/ visited March 26, 2009

[11] The objective of most Delphi applications is the reliable and creative exploration of ideas or the production of suitable information for decision making. The Delphi Method is based on a structured process for collecting and distilling knowledge from a group of experts by means of a series of questionnaires interspersed with controlled opinion feedback (Adler and Ziglio, 1996). According to Helmer (1977) Delphi represents a useful communication device among a group of experts and thus facilitates the formation of a group judgement. Taken from: http://www.iit.edu/~it/delphi.html

Table 5: Timeline – EABIS research team and EU CSR Alliance laboratory – working together – a new approach to business – relevant, academic research.

Date	Lab	Research team	Joint	External developments[12] –
March 2006	European CSR Alliance announced.			The IFC's Communicating ESG value drivers at the company-investor interface – who cares wins annual event 2006.
	Lab on measurement and reporting non (extra) financial performance announced.			UNEPFI Report on ESG Show me the money: linking environmental, social and governance issues to company value (UNEPFI, 2006).
			Discussions CSR alliance – EABIS about funded research to support Lab.	UK Companies Act expands directors' duties and environmental reporting (2006).
		Informal discussions EABIS – Doughty Centre to reconstitute research project previously terminated due to departure of personnel.		USS Report on mainstreaming ESG. Enhanced analytics for a new generation of investor (USS, 2006).
June 2007			Milan stakeholder meeting: PwC corporate reporting initiative - at Telecom Italia.	Aspen Principles report Long-Term Value Creation: Guiding Principles for Corporations and Investors. (McKinsey report: most CEOs participating in UN Global Compact include ESG in core strategies (July 2007). GS Sustain (Goldman Sachs, 2007).
Sept 2007			London: Lloyds TSB HQ – stakeholder consultation.	Fund management transparency and engagement on environmental, social and governance issues (FairPensions).
Autumn 2007		Research team assembled.		
November 2007	CSR Europe Marketplace Brussels. Lab presentation – identified as significant project for EU CSR Alliance and for Commission.			
Jan 2008		Initial research team meeting in London hosted by Lloyds TSB.		
Feb 2008		Bilateral meetings with EABIS & research team member schools to refine project and agree brief.		Citi, JP Morgan Chase and Morgan Stanley adopt The Carbon Principles (February 2008).

[12] Promoting Corporate Environmental, Social and Governance (ESG) Policies with National Governments, International Organizations and Institutional Investors – memo periodically updated and circulated by Michael Kane of US EPA – edition Jan 2009

Date	Lab	Research team	Joint	External developments[12] –
Winter 2007-08		Initial interviews with French investors: Céline Louche and Hager Jemel. Scoping interviews London/Copenhagen with investors, company secretary, finance director of FTSE100 etc. consultancies.		Prince of Wales Accounting for sustainability Report (Prince of Wales Accounting for Sustainability).
April 2008			Lab leaders & research team meet Brussels to review how would work together.	Managing Responsible Business (CiMA).
Summer 2008		"Non-Financial Performance Metrics for Corporate Responsibility Reporting Revisited" by Dr Malcolm Arnold. Cranfield published work on obstacles to measurement, reporting and use of ESG data – practitioner studies – Kenneth Amaeshi. Does CSP improve financial performance – literature review – Hager Jemel.		Key performance indicators for environmental, social and governance issues (DVFA, May 2008).
July 2008		Initial work on Value Creation Framework.	Stakeholder consultation hosted by FORTIS Brussels.	
Sept 2008			Stakeholder consultation hosted by Cranfield, UK on Aspen Principles, PRI, meta-analysis.	The Promise of Private Equity Report (IFC).
			Focus group 1. Milan/Rome.	
Oct 2008			Focus group 2 Frankfurt.	
Nov 2008	Drafting of interim Lab report supported by research team.			Norwegian institutional investors create Sustainable Value Creation collaboration and release report on ESG performance.
Dec 2008	Launch of Lab interim report and endorsement by Commission Vice-president Verheugen.		EU CSR Alliance summit, Brussels. Focus Group 3, Paris.	
Winter 2008-09		Further development of Value Creation Framework and supporting academic justification. Revisions of meta-analysis.		
Jan 2009		Research team meeting, Brussels.	Focus group 4, Stockholm. Focus group 5, Utrecht.	Valuing corporate social responsibility (McKinsey, 2009).

Date	Lab	Research team	Joint	External developments[12] –
Feb 2009				EU multi-stakeholder Forum on CSR, Brussels – commission and stakeholders; Pharma Futures III – (Sustainability 2009).
March 2009				GRI Amsterdam Declaration.
April 2009			Joint Lab/research team review by conference call.	
Spring-Summer 2009		Defining 'Dominant convention' and strategies to change.		Communicating with the right investors (McKinsey, 2009). Reaching investors – communicating value through ESG disclosures (GRI, 2009).
July 2009			Final Lab summit – stakeholder consultation hosted by Lloyds Banking Group, London. Joint meeting of Lab and research team.	
		Research team strategy session final report – Brussels.		
Aug 2009		1:1 meetings with commentators.	e-consultation with invited respondents on final research report.	
Sept 2009	Launch of finalised report.	Launch of research report.	After action review of Lab-research team collaboration and lessons for future EABIS research projects.	EU commission round table 1. What data do stakeholders want from companies – 1 Investors.

Our Target Audiences for this Research Report

We have a number of key target audiences for this report.

- Companies which are already committed to embedding sustainability and Corporate Responsibility who want to be able to talk to their mainstream investors about how improved ESG performance and integrating CR and sustainability with overall strategy impacts on overall business performance. Companies yet to be convinced of the relevance of CR and sustainability to them, although these may find it useful to consult section 3 on how improving ESG performance impacts on non-financial drivers of business success.

- Mainstream investor community. (Although SRI investors may also find it useful to consult the Value Creation Framework model to consider whether it suggests any refinement of their own, existing valuation models.)

- European policy-makers at the EU and national government levels. The report is potentially relevant to those concerned with improving European competitiveness, as the EU Competitiveness White Paper (2008) postulated links between embedding CR and competitive advantage. It is also important for those EU national governments which have explicit strategies for promoting greater quality of Corporate Responsibility and sustainability such as Denmark and Spain.

- Business school academics – not just those working in corporate responsibility and sustainability, but particularly in the finance faculty who are responsible for research and teaching of today's and future members of the European investor communities.

Lessons from this Project for Future EABIS Research Projects

- The research team has worked closely with the EU CSR Alliance Laboratory to ensure managerial relevance and faster access to information. This has had a number of advantages such as enhanced access to practitioners through focus groups, stakeholder engagement meetings etc; and access to different policy-makers' networks. It has stimulated fresh thinking about dissemination channels and deliverables from the project. This has come with some challenges, such as different timescales of business and academia which had to be reconciled, and some uncertainty about the scope of the research project. With hindsight, access to companies through CSR Europe and its national partners, and from the EABIS founding partners could have been used much more effectively, for example in accessing heads of investor relations inside companies. Nevertheless, the overall experience has been positive and we recommend the approach is used by EABIS more in the future.

About the Research Team

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Appendix 3

EU CSR Alliance Laboratory Model

Primary objective

Market value

Financial drivers

Revenue growth	Operational efficiency	Brand equity	Cost of capital	Risk management

Core non-financial drivers

Human capital	Customer relations	Society	Environment	Innovation	Corporate governance
• Employee engagement	• Customer satisfaction	• Public perception • Supply chain management	• Carbon emissions • Waste management	• New product and process development	• Ethical integrity • Processes and procedures

ESG factors

Human capital	Customer relations	Society	Environment	Innovation	Corporate governance
• Absence rate • Staff turnover • Health & safety • Fair restructuring • Training • Performance management • Equality & diversity • Reputation • Commitment to customer • Talent recruitment & retention	• Customer loyalty • Retention • Reputation • Trust • Price, product, service quality • Competitive positioning	• Opinion former perception • Media coverage • Community investment • Stakeholder dialogue • Legal/regulatory breaches • License to operate • Inclusion • Social capital	• Energy efficiency • Deployment of renewables • Waste reduction • Recycling • Environmental impacts • Environmental breaches • Lifecycle assessment	• Value of patents • Customer perception • Talent recruitment & retention • Training • R&D expenditure	• Ethical code deployment • Board composition • Equality & diversity • Talent development • Audit processes • Reporting & transparency • Reputation • Shareholder interests • Anticorruption policy/practice • Competitiveness

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A fuller list of source materials can be found in each of the EABIS Research Project Working Papers.