GOVERNANCE

December 2019 Issue 304

Engaging boards with climate change

'The consensus around our table was that non-execs have several very important roles to play in this, by: challenging their boards to develop appropriately ambitious CO2 reduction plans; scrutinising the delivery of those plans; using their networks to transfer good practice from one board to another; and communicating with the investor community.'

David Archer and Alex Cameron

Sustainability

'Overall, the business case for addressing sustainability is compelling – and companies can no longer afford to avoid embedding sustainability goals into their strategic thinking. ESG concerns have reached the boardrooms and are topping agendas. We are seeing this play out across all markets as businesses respond to increasing expectations among customers, shareholders, and civil society.'

Robert King

Content

Feature

Sustainability

Robert King considers a major global survey which finds that businesses are struggling to turn sustainability ambitions into action.

Sustainability is now firmly on the agenda for business management teams of all sizes, but only a minority have a clear understanding of how they are performing and as a result, they are feeling the pressure.

This is what we found in our new HSBC survey, '*Navigator: Now, next and how*', exploring the views of over 9,100 companies in 35 countries and territories.

It shows that almost all businesses (96%) are under pressure to become more environmentally and ethically sustainable, but many are struggling with barriers – such as their ability to finance change (35%) and free up resources to implement that change (31%).

Over a quarter of businesses say they are frustrated by a lack of clear environmental, social and governance (ESG) measurement criteria, meaning they simply aren't sure what to focus on.

There is also a consistent gap between indicators companies identify as relevant and those they measure. For example, 24% of firms recognise that energy usage is relevant to their operations, but only 15% are actively measuring it.

Translating sustainability ambitions into measurable practices is the core challenge for these businesses – and they are not finding it easy.

ESG guidance is issued by a range of organisations, from the UN to stock exchanges. Identifying which guidance best applies to their business is a challenge for management teams. Our Navigator findings show that clearer common reporting frameworks would be welcomed by these business leaders.

While 26% of businesses want to become more sustainable to improve their efficiency and 23% think it will help boost sales, 8% are measuring their carbon emissions. Overall, in terms of social and governance metrics, 13% say they measure the fair treatment of employees and 14% track the effectiveness of their anti-bribery and corruption controls.

Pressure to become more sustainable in the next five years is coming from multiple sources including from competitors (36%), end consumers or customers (34%), and governments (32%).

On competitor pressure, we have seen examples, in the UK, where HSBC clients have observed the competition accessing the green finance market – a form of lending dependent on the borrower fulfilling environmental criteria – and have rapidly tried to follow suit. This may be motivated by a desire not to be seen publicly to be left behind, or a genuine curiosity to understand how the facility was structured and appetite to replicate it.

So, we've found through our experience that this is a big motivating factor for companies.

Overall, the business case for addressing sustainability is compelling – and companies can no longer afford to avoid embedding sustainability goals into their strategic thinking.

ESG concerns have reached the boardrooms and are topping agendas. We are seeing this play out across all markets as businesses respond to increasing expectations among customers, shareholders, and civil society.

It is becoming more pressing for suppliers to change – as the alternative is being left out. We see this as becoming an increasing issue over the coming years. Suppliers not taking sustainability seriously can become vulnerable in the marketplace.

Increasingly, it is driven by end-consumers who care about how goods are manufactured and the ESG impact. Another outcome is a reduced financial risk profile, as they are positioned more favourably by financial institutions and investors.

Technology also has a big part to play in sustainability goals for companies and their leaders. Over the next five years, a third of businesses expect to invest more in technology, innovation and infrastructure to improve sustainable production. The focus for 31% of them will be to promote employee health, wellbeing and safety, while for 29% it is to reduce waste generation and improve energy efficiency.

Service companies are more likely to be investing in promoting employee health, wellbeing and safety (32%), reflecting the importance of their people. Goods companies, meanwhile, are focusing investment on reducing waste generation (31%).

Another massive challenge, therefore, for businesses and their decision-makers is access to finance to make the investment required to become more sustainable.

In the next five years, it is considered the main challenge they will face in improving their sustainability practices, along with resource pressures.

Feature

So how does HSBC help our corporate clients access finance to make these kinds of investments? We are continually developing sustainable finance products, including green loans, sustainable supply chain financing and green bonds.

We are starting to see the market develop standards for sustainable finance products. For example, with the Loan Market Association (LMA) developing principles and guidelines for green loans and sustainability-linked loans, where the margin paid by the borrower is dependent upon meeting pre-agreed sustainability metrics.

At HSBC, we have aligned our green loan proposition to the LMA Green Loan Principles. We have also designed a process which provides us with disclosures and information from the client so we understand the asset and the positive environmental impact it is going to have, whilst recognising the need to eliminate unnecessary reporting.

We are also looking at some of the transition risks facing some of our clients arising from policy, market and technology shifts, as we move to a low or zero-carbon world. Financial institutions will increasingly start to ask themselves difficult questions on the impact of transition risk upon clients.

At HSBC, we believe that we will be able to support our clients more effectively through staying close to them and understanding the challenges and opportunities they are facing. It's something we do all the time and is key to supporting them in some of these investments.

But, we understand it's a two-way process, so for many of our clients it's really important that we are walking the walk on sustainability and we mean what we say as a bank. HSBC has committed to being a leader in sustainable finance and has made a number of sustainable finance commitments, including the provision of USD100bn of sustainable finance and investment by 2025 and sourcing 100% of our electricity from renewable sources by 2030, with an interim target of 90% by 2025.

We are passionate about leading and shaping the debate on sustainable finance and investment and in 2019 we were named the World's Best Bank for Sustainable Finance at the Euromoney Awards for Excellence.

Sustainability is also viewed as a big growth driver for businesses surveyed for the Navigator research. As we have found, it is no longer viewed as a tick-box exercise, with most companies now regarding it as a key contributor to their success, long-term survival and ultimately their growth.

When asked about their main motivations to becoming more sustainable, around a quarter cite improving operational efficiency (26%), sales growth (23%), meeting buyer expectations and securing competitive advantage (both 23%).

A similar proportion are becoming more sustainable to meet regulatory standards (24%), improve transparency and traceability and gain reputational advantage (21%), and just over one in five even say becoming more sustainable is essential for their survival (also 21%).

Meanwhile, a majority of businesses believe they have a responsibility to deliver UN Sustainable Development Goals (SDGs). The figures are revealing: 63% of leaders say they have a role to play in achieving the SDGs, with a quarter believing they play a significant role. The vast majority (82%) of high-growth businesses believe they have a responsibility here.

In the UK, 75% of British businesses believe they have a role to play in delivering the UN's SDGs. Only one in ten companies globally do not think they have a role to play at all.

The most relevant and highest-rated SDG goals among businesses tend to be the ones where companies feel they can make a direct, tangible contribution on: affordable and clean energy, good health and wellbeing, industry innovation and infrastructure, decent work and economic growth, as well as responsible production and consumption.

Banks can help to initiate action through SDG-linked financing. For example, HSBC led the way in launching the first SDG bond in 2017. This was followed in 2018 by the world's first SDG sukuk – an Islamic financial certificate, or sharia-compliant bond. Strong investor demand saw both bonds oversubscribed.

So, as our research shows, now is the time for companies to embrace and promote their sustainable ambitions and HSBC is at the forefront of helping them to do so. It's an exciting challenge and we are up for it, as are our customers, clients and partners.

It's such a fast-moving market and we're all continually learning. It has changed so much, even in the last two or three years – and it will continue to change.

We know we need to be engaged with third parties. We need to be open and connected, as we state in our values, to understand how the market is changing. And we know we need to hear the views from experts in the market to better inform our approach. We're already looking forward to what we'll uncover and help to develop – sustainably – in 2020 and beyond.

Robert King is the Sector Head of Sustainable Finance at HSBC.

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