17th Annual Global CEO Survey

Summary: Sustainability

Business success beyond the short term: CEO perspectives on Sustainability

1,344

CEOs in 68 countries

46%

CEOs agree resource scarcity and climate change megatrend will transform their business

74%

CEOs told us that measuring and reporting their total impact (financial and non-financial impacts) contributes to their long term success

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Contents

Sustaining business for the long term

We live in a world with a growing population, seeking a better lifestyle, to be delivered from a planet with finite resources, many of which are now rapidly running out. The implications are significant, but are the business models of today equipped to deal with this? If a business is focused purely on profit with a by-product of depletion and damage, is it sustainable?

For many, the starting point for understanding and taking action on sustainability has centred around 'doing good' with profits made and corporate social responsibility. It's tended to operate in a silo, separate from the strategic decision making of the business. But now, the focus for business is turning to a more holistic understanding of how it makes profit in the first place, the implications, consequences and benefits not only to it, but to society. So it's no longer a philanthropic afterthought or about installing low energy light-bulbs, but an approach to embed more forward thinking and responsible business practice in how a business produces and delivers its goods and services.

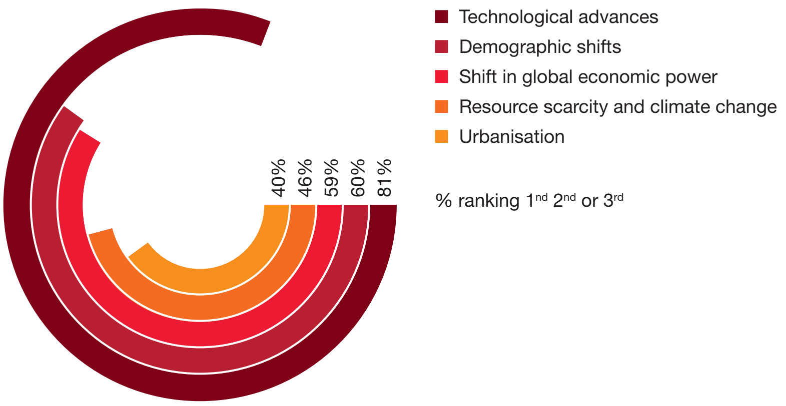
In PwC's 17th Annual Global CEO Survey, 75% of CEOs agree with this saying that satisfying societal needs (beyond those of investors, customers and employees) and protecting the interests of future generations is important. This is reinforced by consumers – in the Edelman Trust Barometer 2014, 84% of respondents believe that business can pursue its self-interest while doing good work for society. It's a green light to embed sustainability into everyday strategy.

Sustainability is becoming core to business success. Being 'able to sustain' business, with one eye on 'new' external risks and the other on future consequences of its decisions, underlies it. It's about managing, reducing and removing risks responsibly and investing to build in resilience.

This perspective is apparent in the latest PwC annual survey of CEOs. Resource scarcity and climate change, urbanisation and demographic changes feature regularly in the top three megatrends CEOs think will transform business (See Figure 1: Megatrends transforming business). In themselves, these megatrends aren't 'new', but it's the pace at which they're unfolding and the way they're colliding to create a completely different business environment, that is new. Coupled with increasing confidence in the global economy, will the transformation expected translate not only into growth opportunities, but also sustainable business and good growth?

Here, we look at the findings of our 17th Annual Global CEO Survey through a sustainability lens, sharing both what CEOs are thinking about sustainability issues and challenges, and the implications for business. For more CEO views from the main report, go to pwc.com/ceosurvey.

Figure 1 Megatrends transforming business



Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

Scarce resources and unpredictable extreme weather are impacting business

46%

CEOs agree resource scarcity and climate change mega trend will transform their business – what differences will we see?

Resource scarcity is fast becoming a priority on both the political and business with access to raw materials, water, land and energy increasingly a concern. Population growth, the speed of rising consumption in developing economies, and geopolitical and environmental factors that impact production and distribution are all intensifying the issue. The result is higher prices, market volatility and a changing supply landscape. (See Figure 2: CEOs are concerned about the impact of resource scarcity and climate change).

Finite resources

As production demands increase and natural resources are depleted, it makes sense that the extraction of minerals and metals will become tougher – finding new sites or exploring existing ones more deeply will incur costs. Governments are increasing their expectations of, and involvement in, business operations around extractive industries and granting licenses to operate. Conflicts around the world, particularly in areas with natural resources, are putting pressure on reliable distribution. Recent natural catastrophes have compounded the issues, putting pressure on reliable supply chain distribution. The results are often price increases and supply disruption, but quality issues and the possible emergence of new government policies and regulations to protect resources and maximize returns are likely too.

Water pressures

75% of the Earth's surface is water and it's expensive to desalinate, purify and move it. As populations increasingly live in and move to water-challenged areas, and the use of water in manufacturing, energy production and agriculture increases in line with demand, water has emerged as one of the most critical scarce resources, creating friction between business, governments and communities.

Water, energy and food are now so intertwined they're dependent on each other and getting the right balance between them has become crucial – one man's dam providing energy for 1000's is another's downstream destroyer of livelihoods. We all know it takes water to create food, but it's needed to create energy too (eg. to cool power plants). It takes energy to move and treat water, and energy to produce and deliver food, and sometimes we use food as energy (in biofuels). Business has an important role to play in understanding the balance between the three and maintaining it.

Climate driving disruption

Our changing weather patterns leave few parts of the planet untouched. Floods, extreme temperatures and higher wind intensities are happening more frequently or with an increased reach. They are disrupting business (preventing supply, delaying distribution, driving migration and damaging product) as well as lives.

What does this mean for business?

Competition for resources

Business is right to identify resource scarcity and climate change as a transforming trend. Because global markets must now compete for resources (like oil, water, land and agricultural commodities) there are new cost worries and concerns to consider eg. about achieving desired outcomes, increased competition for talent, and changing business models.

Adapt or mitigate?

The recent Intergovernmental Panel on Climate Change report on the science of climate change stated that it is 95% certain that the human-related greenhouse gases are the principle cause of global warming since 1950.[1] The challenge set by the Panel to limit greenhouse gas emissions, and therefore global warming to 2^{0}C by 2100, moved from monumental to enormous.

This is a business risk and planning issue about investments, sourcing strategy, security and costs of supply, insurance planning, workforce wellbeing, and whether the infrastructure we rely on is built to last.

Business sectors with revenues sensitive to changes in weather and climate, such as tourism, retail, agribusiness, energy and insurance, will be at the frontline. But in reality, because of the role of infrastructure and investment, for example buildings, transport and power, this affects all sectors, particularly those with high value, long lifetime fixed assets, which risk depreciating in value if under-prepared and located in areas of rising risk.

At a high level, talk is about adaptation and mitigation as a response to climate change. Adaptation is about treating the symptom, responding to the problem with a direct solution eg. build a water desalinisation plant when water gets scarce, build a flood barrier to reduce the challenges a rise in sea level brings. Mitigation addresses the condition and is often driven by regulation and voluntary action. We have seen emissions reductions take place at the source, eg. carbon emissions reduction, or offsetting initiatives that result in investments in reforestation and energy projects in developing countries.

Build in resilience – innovate and collaborate

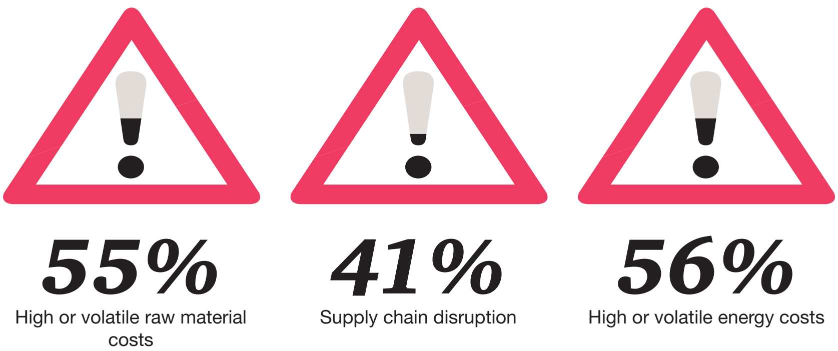
To reduce or remove the risk, new approaches are required to build in resilience. To get a handle on how scarcity will impact a business both now and in the future, the current and potential risks need to be identified and managed. Risk reviews need to be holistic so that solutions have the best chance to reflect the implications for all stakeholders. Innovation will be one route – developing new products that use scarce resources more efficiently or not at all. Collaboration will be another, both cross industry and amongst suppliers. Stronger relationships need to emerge cross-industry to invest in new solutions so all benefit from economies of scale and a joined up approach. Suppliers, working more closely together and with business, can build more integrity into the supply chain.

35%

CEOs think innovation in products and services is the biggest opportunity for business growth

Figure 2 CEOs are concerned about the impact of resource scarcity and climate change

Q: How concerned are you about the following potential economic and policy/business threats to your organisation's growth prospects?



Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

1 Source: IPCC, Climate Change 2013: the physical science basis

76%

of Energy and Power & Utility CEOs put resource scarcity and climate change in their top three megatrends with Mining CEOs not far behind at 62%.

The industry perspective on resource scarcity and climate change

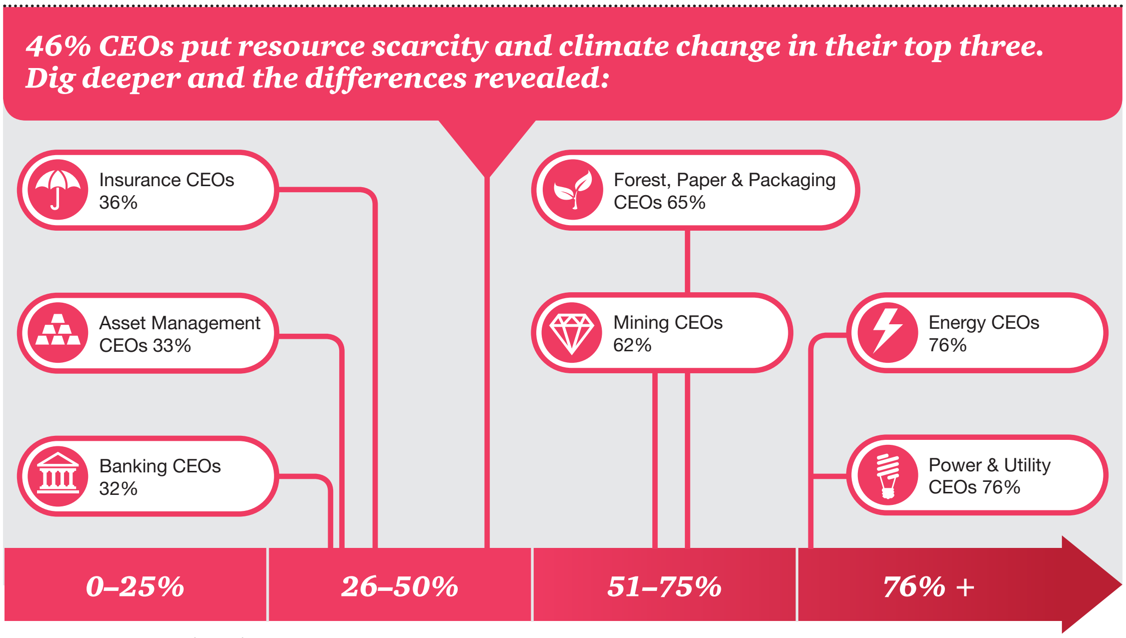
76% of Energy and Power & Utility CEOs put this megatrend in their top three with Mining CEOs not far behind at 62%. (See Figure 3: The perspective on resource scarcity and climate change differs by industry). These industries are already feeling the pressures of resource scarcity and the increased costs associated with it – everything from competition for new sites, deeper mines, extracting in or transporting across a war zone or area of conflict, to regulation and government intervention.

There's also stranded assets to consider. Many countries now have carbon budgets, limiting the amount of green house gases that can be emitted. If at some point the world adopted and rigidly enforced a global Carbon Budget (on current trends we will use up this century's carbon budget by 2034[2]), business would innovate to use and produce less carbon. When this happens, it's likely that fossil fuel prices will drop as demand falls away. In fact, if the world wants to limit its warming to just 2 degrees, then already between 60-80% of coal, oil and gas reserves of publicly listed companies are 'unburnable'.[3] Costs incurred to find it and extract it may not be recovered – a significant potential problem for all those directly involved, with implications throughout the supply chain too.

Interestingly enough, it's surprising to see that only 33% of Financial Services CEOs put resource scarcity and climate change into the top three megatrends that will transform their business. Although it might not have such a direct impact on their physical operations, they're in the business of insuring and investing in organisations that are impacted.

Figure 3 The perspective on resource scarcity and climate change differs by industry

We asked CEOs which global trends do you believe will transform your business the most over the next five years?



Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

2 PwC Low Carbon Economy Index 2013 http://www.pwc.co.uk/sustainability-climate-change/publications/low-carbon-economy-index.jhtml

3 Carbon Tracker http://www.carbontracker.org/wastedcapital

The business of changing demographics

60%

CEOs put demographic shifts in their top three megatrends that will transform their business in the next 5 years – buying behaviour, skills availability, markets are all changing rapidly

The global population is expanding; it will hit 8 billion in 2025. But this growth won't be uniform. By 2020, the median age in Europe will be 43, 38 in China and just 20 in Africa. The working-age population is undergoing major geographic shifts too. It's still growing rapidly in countries like India. But it's already peaked in China and South Korea, and has been falling for more than a decade in Germany.[4]

People are moving to cities. Over the next four decades the number of city dwellers is projected to rise by 72%. If the US is anything to go by, it's good news for business with urban households spending 18% more, and good news for workers, earning 32% more than rural counterparts.[5] In India, the contrast is more stark with the average urban earnings (monthly per capita estimate) 84% higher for urban dwellers than rural.[6]

But, with fast expansion comes infrastructure and health issues. For instance, fewer than 35% of cities in developing countries have treated wastewater, and half of the solid waste is not collected in most cities in low-income and middle-income countries.[7] Los Angeles experiences at least one extra day a year of smog that exceeds federal limits because of nitrogen oxides and carbon monoxide emitted by Chinese factories producing for export, drifting across the Pacific Ocean.[8]

4 Source: Population Division of the Department of Economic and Social Affairs of the United Nations Secretariat, 'World Population Prospect: The 2010 Revision'.

5 Source: Labor Statistics Consumer Expenditure Survey (CE), Beyond the Numbers http://www.bls.gov/opub/btn/volume-2/expenditures-of-urban-and-rural-households-in-2011.htm

6 Source: National Sample Survey Office (NSSO), Ministry of Statistics and Programme Implementation, June 2013 http://www.frontline.in/other/data-card/ruralurban-divide-in-spending-patterns/article5088969.ece

7 Source: WEF

8 Source: China's international trade and air pollution in the United States, University of California http://www.pnas.org/content/early/2014/01/16/1312860111.full.pdf

What does this all mean for business?

Engaging your workforce

Sustainability extends to people too. Without a healthy workforce with the right skills and good working environment, optimal production isn't achieved and reputational risks are exposed. Quality suffers. Turnover, absenteeism and recruitment costs soar, and workers health and safety is jeopardised. Business will need to factor people-related issues into its strategic thinking to reduce the risk implications. This could, for example, mean updating training practices, implementing health and safety programmes, meeting new or emerging market expectations or regulatory requirements. Factor in, as well, the implications of a multi-lingual workforce, the impact of immigration on the local community, and the need to review alternative site locations and distribution.

Increasing buying power

At the same time, one billion people are set to be better off and with a steady rise in the middle classes, consumer spending is set to increase. For business, this creates opportunities in sectors in which richer consumers typically spend, including culture, recreation, services and heathcare, with the resulting increase in potential new products and services.

Taking the strain

But what's the ultimate cost? As demand for goods increases, so does the demand for raw materials, water, energy and carbon that are involved in their manufacture and distribution, putting pressure on supply chains, communities, infrastructure and governments. Growth can come at a hefty price. So, how can you make sure your growth is 'good' ie. it is real, inclusive, responsible and lasting?

Sustainable growth strategies

Thinking about sustainability at the beginning of this growth phase will ensure an element of future proofing is built in and create a competitive advantage. Some companies are exploring ways to de-couple their growth from their resource use, building in efficiencies and innovating to reduce reliance and requirements for scarce materials and potentially reduce costs too. Some are developing closed-loop manufacturing practices, extending their control over more of their value chain with the aim to remove waste and recycle / reuse materials. The benefits here are numerous: e.g. reduction in carbon emissions, waste, water usage, pollution and energy consumption.

Thinking about your total impact as a business now will help identify strengths and weaknesses in your current set-up and flag where change needs to happen most.

40%

CEOs ranked urbanisation in their top three global trends that will transform business in the next 5 years – this shoots up to 61% for CEOs in South Africa

52%

CEOs are concerned about shifts in consumer spending and behaviour.

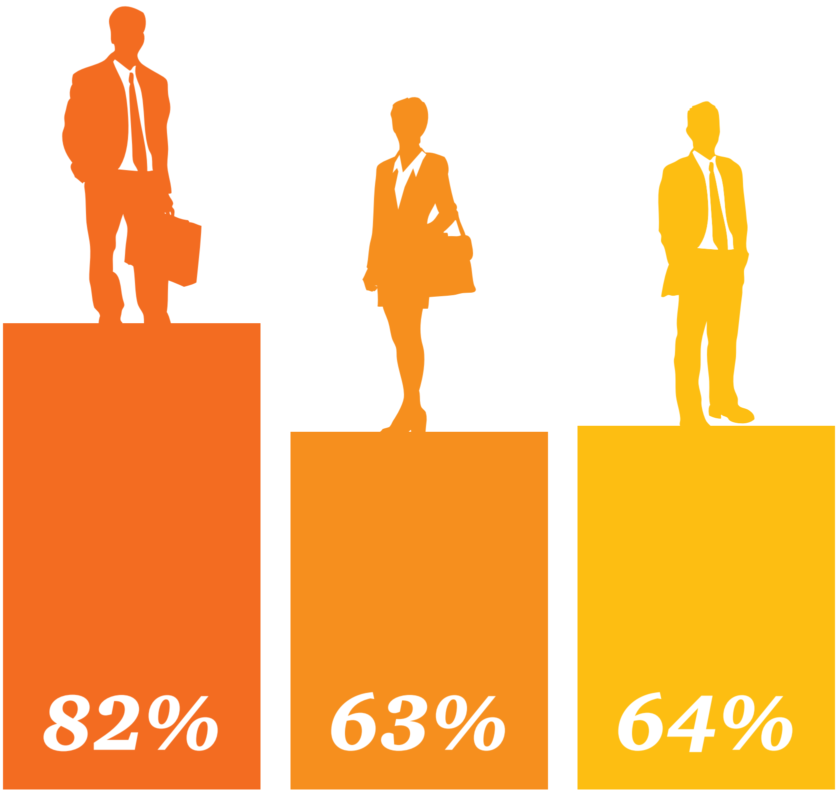
The industry perspective on demographic shifts and urbanisation

CEOs within people related industries, including Pharmaceuticals (72%), Healthcare (84%) and Insurance (73%), put demographic shifts in their top three megatrends more than others. Unsurprisingly, CEOs involved in infrastructure, including Engineering (56%) and Communications (56%), put urbanisation in their top three. There's a sense with both these groups that the transforming impact will be a positive one – CEOs seeing the opportunities new markets will bring.

"With the global middle class growing, we can all help to create solutions that use less water, less oil, less resources of all kinds… After all, our businesses can only be as strong and healthy as the communities that we proudly serve."

Interview with **Muhtar Kent**, Chairman and Chief Executive Officer, The Coca-Cola Company

Figure 4 **Concerns about the workforce are on the CEO agenda**



CEOs agree that improving workforce and board diversity inclusion is important for their business

CEOs concerned about the availability of key skills

CEOs focusing on creating a skilled workforce as a priority

Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

Do you have your eye on the ball?

5%

Only 5% CEOs say sustainability and climate change will be the next big thing to impact business

"[...] the purpose of the company isn't making money, that is the outcome of what we do for our shareholders. The purpose of a company like us is remarkably simple. It's about freeing people from the fear of uncertainty."

Mark Wilson,
Group CEO, Aviva

There are a growing number of companies who are embedding sustainability into their business models, seeing it as important not just to differentiate themselves or as a competitive advantage, but also as a way to achieve good growth. But it's surprising to see that so few see it this way.

Here's why. In ten years, according to the World Economic Forum (WEF) report, Global Risks 2014, extreme weather and environmental risk are the most likely risks facing the global economy, and amongst the top five of those with the most potential impact. So, a global systemic risk identified by experts as highly likely within ten years, isn't registering as a priority on CEOs' radar within five!

Often companies approach sustainability from a Corporate Social Responsibility perspective. Measuring and reporting elements of their impact is a good start and may be useful when communicating to stakeholders, but often it's produced separately from their financial reporting and not used by the rest of the business. By not integrating into the business and its strategic decision making, much of the value of this non-financial data is missed. In addition, few are managing their impact throughout their entire value chain and so most don't have the full picture.

Embedding sustainability thinking

Looking beyond financial performance and taking a holistic approach can help drive strategy. For instance, PUMA's Environmental Profit and Loss (EP&L) account results in 2011 (the first of its kind and supported by PwC) found only 6% of its environmental impact was head office related, 94% or €137 million was driven by its supply chain.[9] With this knowledge, PUMA developed its InCycle shoe with an environmental impact of nearly a third less than its conventional suede shoe - it used non-financial impact data to drive a new strategy.

Leading thinkers are seeking to find ways to create quality products and services in a net zero impact way.

In addition, some want to improve lives at the same time. This isn't just about philanthropy, there is a business edge to it as well. Increase sanitation levels or reduce malaria and you have thriving customers or a healthy workforce. Sponsor children through university or build schools or improve girls' education and you can extend your potential talent pool at the same time as lifting people out of poverty. In fact, taking care of the 'base of the pyramid' could be seen as a $5000billion market rather than a burden.[10]

Companies are looking at the impact their operations are having on the environment as well as the positive or negative impact on the communities in which they operate. Understanding these impacts can drive improvements in corporate strategy, day to day operations and ultimately in financial performance. They're moving away from sustainability as an afterthought or something that helps them put right a problem they've caused, to a way of doing business. They have a clear goal, thinking ahead to understand potential risks and identify solutions with longevity that better fit today's world.

9 Source: PUMA's Environmental Profit and Loss Account
10 Source: John Willman, 2008, former Business Editor, Financial Times

26%

CEOs say they are addressing the risks of climate change and protecting diversity as a priority over the next 3 years

91%

agree that it's important to them to ensure the integrity of their supply chain

21%

CEOs are focusing on reducing poverty and inequality as a priority over the next 3 years

"In principle, a company needs to be fair and honest with society. A company needs to face up squarely to society, and provide good products in a fair manner. The most faithless thing a company can do is to put fraudulent or low-quality products on the market. After all, product performance and reliability matter most."

Interview with **Shigetaka Komori,** Chairman and Chief Executive Officer, FUJIFILM Holdings Corporation

Total impact drives optimal business decisions

"It is very important to look at the stakeholder context when developing the business model and to see how we engage with government, with civil society, even at times with politics, but certainly with the business community as we expand our model going forward."

Arif Naqvi,
Founder and Group Chief Executive, The Abraaj Group

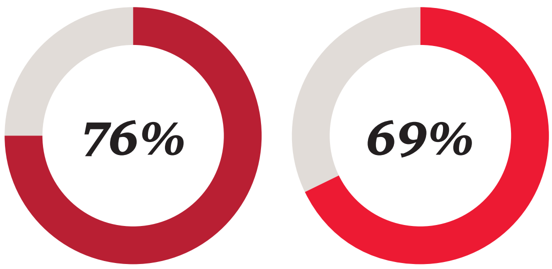
Believing sustainability is at the core of business success, means it's also at the heart of decision making. A focus on financial performance alone results in important considerations being missed. (See Figure 5: CEOs believe there is more to business than profit).

Public backlashes against businesses increasing profits are becoming more high profile, as consumers, campaigning groups and governments question whether a business is paying its fair share of tax, driving water scarcity, depleting resources or destroying natural habitats. The impact not only rocks reputations, but can damage revenues and leave the door open for competitors to step in.

CEOs know that their business activities are in full view and open to question, and this transparency extends beyond the balance sheet. (See Figure 6: CEOs recognise they have a visible impact). In the US, the last 12 months has seen a dramatic increase in CEOs believing it's important to measure and reduce their environmental footprint, up from 43% to 75%.

But it's not always straightforward to understand the implications of proposed activity or to get a balanced view from all stakeholders – some are more vocal and organised than others. Ultimately, rarely is new strategy or product development a clear cut choice between 'good' and 'bad'.

Figure 5 CEOs believe there is more to business than profit

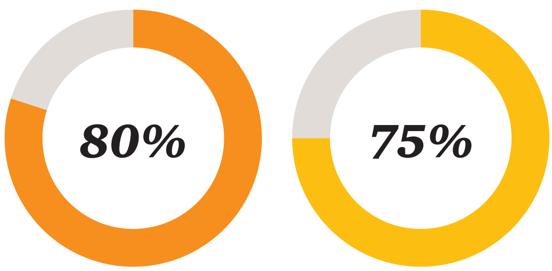


Believe satisfying societal needs (beyond those of investors, customers and employees) and protecting the interests of future generations, is important

Agree the purpose of business is to balance the interests of all stakeholders

Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

Figure 6 CEOs recognise they have visible impact



Believe it's important to measure and try and reduce their environmental footprint

Agree that being seen as paying their fair share of tax is important

Base: All respondents (1,344)
Source: PwC 17th Annual Global CEO Survey

We believe a total impact approach to making business decisions provides the holistic perspective business needs. In reviewing current thinking and the methodologies available, and working with clients and academics, PwC has developed Total Impact Measurement and Management.[11] By valuing social, environmental, tax and economic impacts, business is now able to compare the total impacts of their strategies and investment choices and manage the trade-offs.

74%

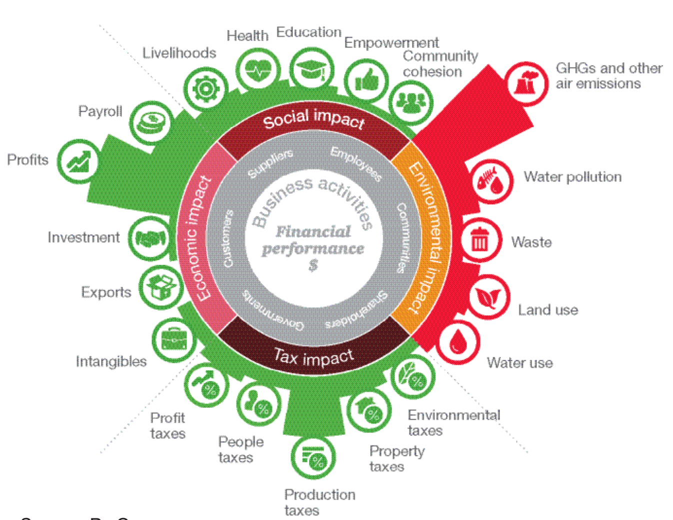
CEOs told us that measuring and reporting their total impact (financial and non-financial impacts) contributes to their long term success

Total Impact Measurement & Management (TIMM) – a different perspective for business

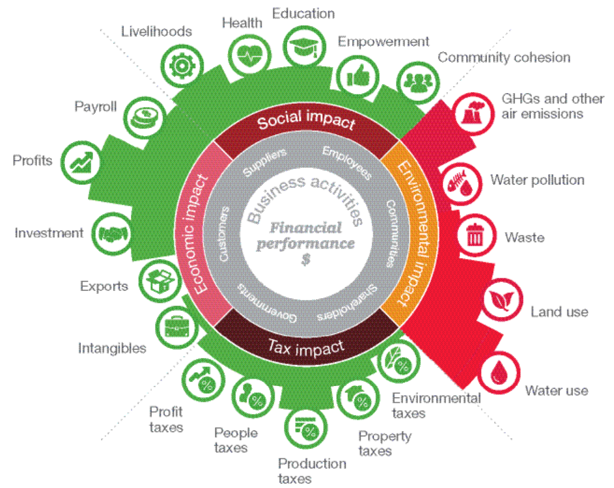
TIMM enables decision makers to develop a better understanding of the social, tax, environmental and economic impacts of their activities while still, of course, making a profit. It gives management the ability to compare strategies and investment choices, using quantified data, and evaluate the total impact of each decision and choice they make. This flexible framework will allow leaders to make sound business decisions, and at the same time better understand which stakeholders will be affected by which decisions, and why. With this total impact approach, you can see at a glance the impact you're making, and better still the trade-offs between alternative strategies. In effect, you can see the optimal decision for all your stakeholders.

Example: Imagine you're a brewer and you have a choice to import barley or grow your crop locally. Deciding which is the better option is complicated. But when the impacts are quantified and presented so that the trade-offs are easy to see, you're more likely to have the right conversations with the right people and reach an optimal decision.

Option 1 **Import barley**



Option 2 **Grow and source locally**



Source: PwC

11 Find out more at pwc.com/totalimpact

The industry perspective on total impact

There's a lot of violent agreement coming through from CEOs. We seem to be hearing that the shareholder is no longer the undisputed king, that there is more to success than financial performance alone and that it's not all about 'take' in the here and now. That's a positive message in itself.

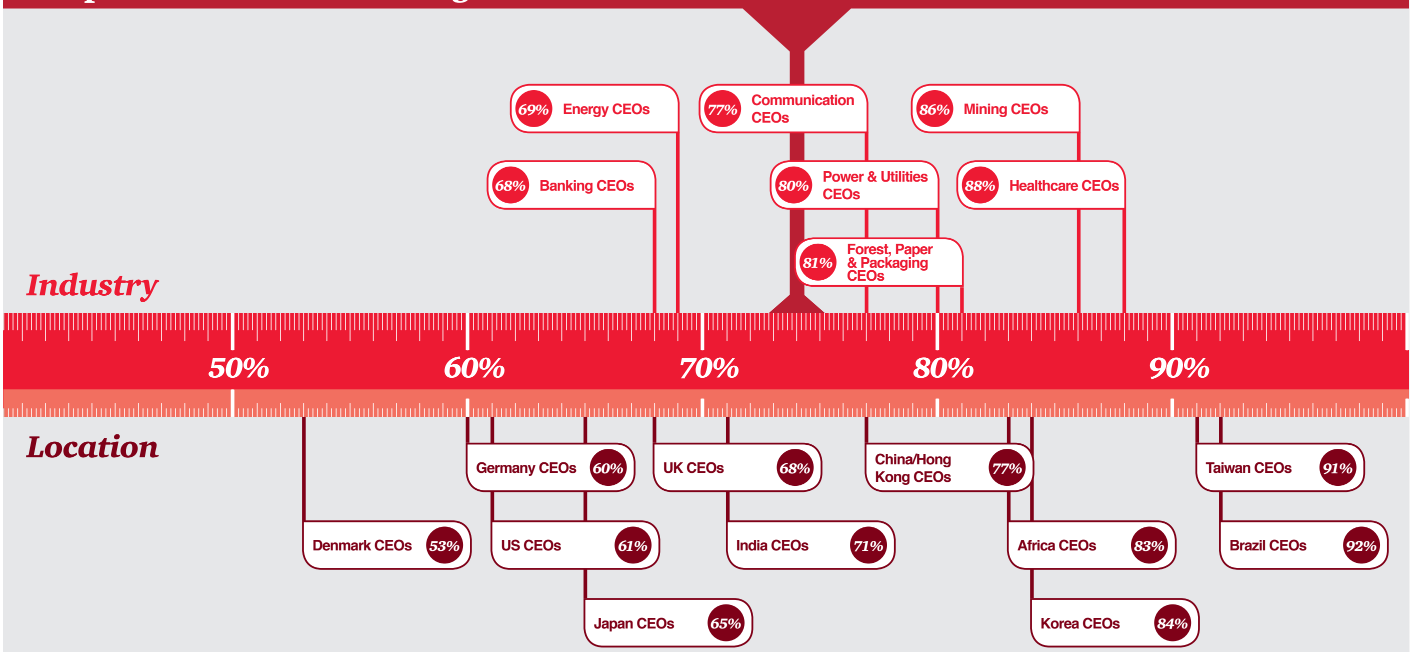
It's telling that more CEOs in industries and countries that are feeling the pressure of environmental issues or that are under closer scrutiny from the stakeholders, are in agreement that change is important. Whether it's to change what they measure and report, or to change their impact on the environment.

Figure 7: *Long term success driven by more than traditional metrics* shows how CEOs believe that measuring and reporting their total impact (financial and non-financial impacts) contributes to their long term success. Agreement is highest amongst Healthcare CEOs and lowest amongst Banking CEOs. With the recent financial crisis and current mistrust of the banking community in the West, this might be regarded as a missed opportunity. Interestingly, by country, CEO views differ markedly. 92% of CEOs in Brazil agreed that understanding their total impact contributes to long term success, compared to just over half in Denmark. In fact, there was less agreement on this amongst CEOs from Western economies compared to the rest of the world.

When looking at just the environmental quadrant, 80% of CEOs said that it's important to measure and try to reduce their environmental footprint, and this rose to 92% for Forest, Paper & Packaging CEOs and 91% for Chemicals CEOs. There's a lot of positive consensus here which is good news for the environment.

Focusing on tax, 75% of CEOs said that being seen as paying "our fair share" of tax is important. This increased dramatically amongst Mining CEOs (95%) and Banking CEOs (86%), but was lowest amongst CEOs in Power & Utilities with only 65% in agreement.

74% CEOs say that measuring and reporting their total (financial and non-financial) impacts contributes to long term success



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Source: PwC 17th Annual Global CEO Survey

Sustainability – is business equipped to change?

"Why is generating trust important? Because people who trust you work with you more, they buy your products, they lend you money and, as a result, you do better as a business."

Interview with
Badr Jafar,
Managing Director,
Crescent Group

Sustainability is so much more than energy efficient light-bulbs and recycling. It goes to the very heart of business strategy and its longevity. It extends beyond the confines of sustainability and CSR teams, into the territories of R&D, procurement, finance, risk, technology, investor relations, HR and strategy teams.

The significance of getting it wrong has many ramifications, not just in terms of customer reaction and reputation, but about:

- **Who will insure you?** In 2012, Swiss Re 'stopped' 23 business transactions going ahead because they failed to meet certain criteria around sustainability and corporate responsibility.[12]
- **Who will invest in you?** 71% of PE houses include Environmental, Social and Governance (ESG) management in their due diligence, to identify any issues before acquisition.[13]
- **Who will want you in their supply chain?** In 2012, Ikea dropped 70 suppliers for failing to comply with its Iway code of conduct - the main compliance challenges noted included working hours and overtime, safety instructions, storage, transport and handling of waste, wages, escape routes and emergency exits.[14]

What customers, suppliers, employees, governments and society expect from business is changing. We all want business to succeed, but not at any cost. But are the business models of today equipped to deal with this change? How business operates in the future will need to be transformed, and with a growing population seeking a better lifestyle from a planet with finite resources, business has to be smart to deliver and stay ahead. The challenge is to understand how these changes could, and perhaps should, lead to a fundamental shift in how businesses are run, and how they and their stakeholders measure success.

Thinking about your business:

How is sustainability embedded into your strategy?

Are your sustainability risks identified, monitored and actively managed?

How will your suppliers approach to sustainability impact your business?

12 Source: 2012 Corporate Responsibility Report, Swiss Re

13 Source: PwC Putting a price on value 2013

14 Source: IKEA Group Sustainability Report 2012 http://www.ikea.com/ms/en_GB/pdf/sustainability_report/sustainability_report_2012.pdf

Contacts

If you would like to discuss any of the issues raised in 'Business success beyond the short term: CEO perspectives on Sustainability', please speak to your usual PwC contact or

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