The What, Why and How of ESG Dashboards

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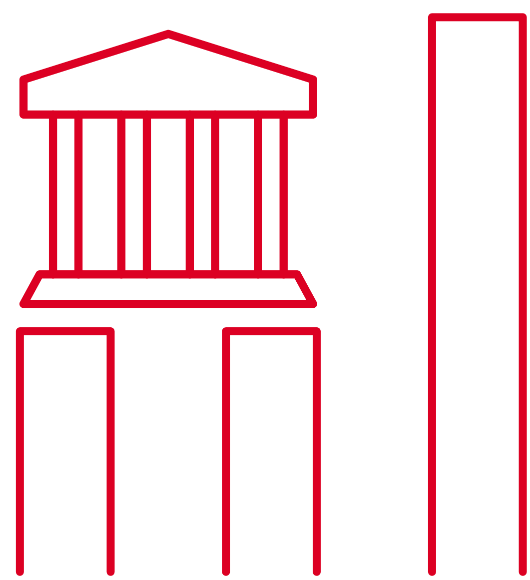

ESG is a hot topic × Companies striving to build long-term value for their stakeholders, the community and the environment often integrate ESG indicators into their business models. ESG stands for environmental, social and governance metrics – both qualitative and quantitative – to highlight how well or poorly a firm is doing in terms of long-run sustainability. Just as the dashboard of a car provides real-time information on speed and mileage, and alerts us when things such as engine oil or gas needs our attention, ESG dashboards provide a company with information on a variety of sustainability metrics such as CO_2 emissions, water usage, fatalities, etc. It alerts us to environmental and social risks that pose threats to a company's future operations and well-being. On the flipside, however, ESG has been vilified by some and the space has become quite difficult to navigate. Elon Musk recently tweeted "ESG is a scam" to former Vice President Mike Pence's comments that ESG is politically driven. Another example is the state of Texas, which has barred local governments from doing business with banks that don't support oil, gas and guns.

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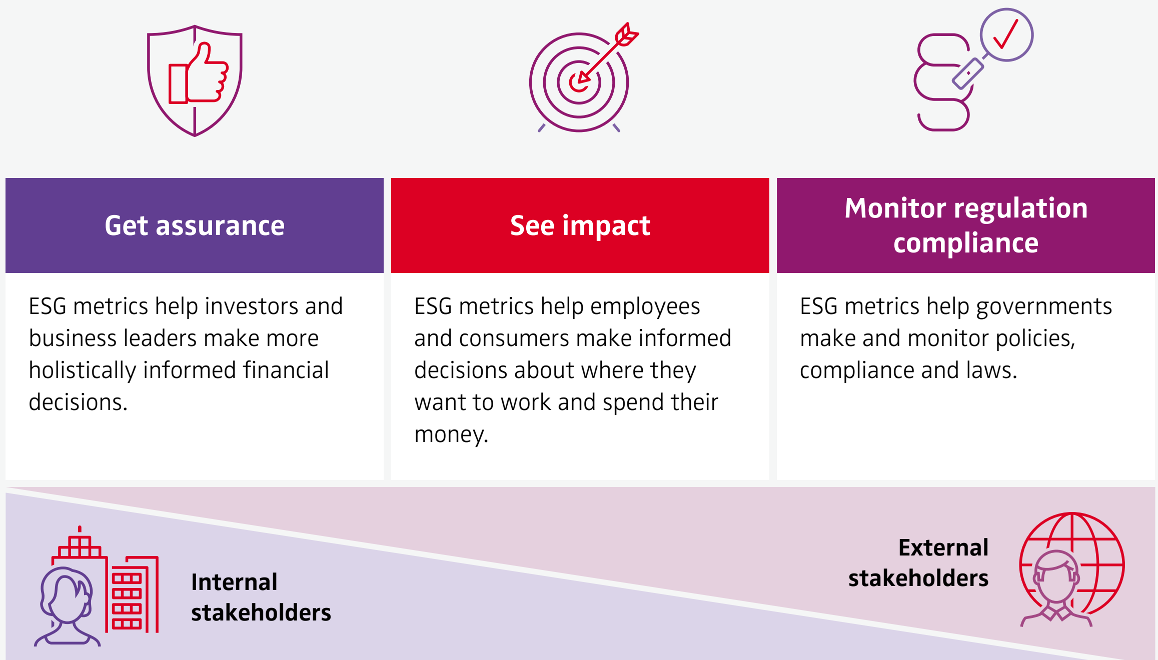
Many stakeholders welcome ESG reporting × Despite this controversy, many businesses have turned to ESG reporting to satisfy the informational needs of their external and internal stakeholders. Investors and governments as well as customers and employees are becoming more and

FIGURE 1 > What stakeholders seek from ESG dashboards



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more concerned with ESG issues. Environmental metrics include a company's efforts to battle global warming, reduce carbon emissions, enhance water quality, manage waste and control other emissions. Social KPIs provide information on what a company is doing to better the lives of its customers and employees, including how it supports diversity, encourages employee involvement, protects human rights and upholds labor standards. And finally, governance measures cover issues such as the steps an organization takes to be accountable for its sustainability targets, combat corruption and guarantee the longevity of its financial investments.

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Beyond its use by investors, rating agencies and other external parties, there are several internal benefits to developing and using an ESG dashboard.

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BOX 1

The special role of the ESG assurance function: the concept of "double materiality"

ESG dashboards ideally provide two types of information: "inside out" and "outside in." The first perspective refers to a company's environmental and social impact on people and planet. The second one refers to the impact of people and planet on the company and indicates its future profitability – typically described in terms of risks, vulnerabilities and resilience. This dual use of ESG metrics and thus the dashboard has given rise to a concept called "double materiality." Companies can use the concept of double materiality to examine both the financial and non-financial effects of their actions to develop a more thorough ESG strategy.

The "double materiality" concept has been built into new European regulations, where disclosure is required from the point of view of the environment and society's financial impact on the company – the financial materiality – and conversely of the company's impact on society and the environment – environmental and social materiality. It recognizes that opportunities and risks may be significant from both a financial and a non-financial standpoint and acknowledges that businesses are accountable for the current and potential negative effects of their activities on individuals, society and the environment.

ESG criteria are becoming more and more popular among investors for assessing investment opportunities. They can give much-needed legitimacy to a company that wants to showcase its sustainability prowess to investors. Foremost, however, ESG metrics and analysis are intended to be "a means to an end, and that end is a planet that is livable – and lives worth living, a strategy that explicitly acknowledges that investors have a role to play in providing these outcomes to the world," says Amy Domini, the founder and chair of Domini Impact Investments and a pioneer in the ESG field, in an interview in the New York Times. In reality however, investors and ratings agencies have mostly ignored this part and Wall Street's current system for ESG investing, which is designed almost entirely to maximize shareholder returns, falsely leads many investors to believe their portfolios are doing good for the world. Recent initiatives such as promoting the understanding of "double materiality" that look at both sides of the coin can provide valuable course correction.

What stakeholders expect from ESG reporting × The various internal and external stakeholders have different motivations for using ESG dashboards. Expectations typically fall into one or more of the categories presented in Figure 1. Stakeholders either seek assurance for their decision-making or are interested in sustainability impact or regulation compliance. ESG reporting needs to consider these different functions. ESG for assurance is all about adjusting for financial risk and making better financial decisions, while the aspect of driving sustainable business transformation remains in the background. ESG reporting in that sense helps investors, board members and chief executives monitor potential risks to the financial bottom line – for example, a lawsuit for non-inclusive hiring practices, or decreased future earnings as natural resources become less available. In this context, the new concept of "double materiality" is emerging, which is presented in Box 1. ESG for impact monitoring is about leveraging ESG to drive more sustainable business models and creating positive social and environmental value. ESG further serves to demonstrate compliance with laws and requirements imposed by outside authorities – like national governments or the U.S. Securities and Exchange Commission. Regulation can differ across countries or regions like the EU and should mostly facilitate the adoption and comparison of specific standards across industries and regions.

» *ESG dashboards are useful tools for showcasing to internal and external stakeholders that a company's sustainability projects are real and not just greenwashing.* «

The internal benefits of ESG × Beyond its use by investors, rating agencies and other external parties, there are several internal benefits to developing and using an ESG dashboard.

- **Making company progress on sustainability transparent** × ESG dashboards are useful tools for demystifying and showcasing to internal and external stakeholders that a company's sustainability projects are real and not just greenwashing, vague promises or lip service. It shows whether the company is on track to achieve its goals and gives the company legitimacy and credibility in stakeholders' eyes. Verifiable KPIs in the dashboard can also make it easier for the business to handle legal difficulties when they arise.

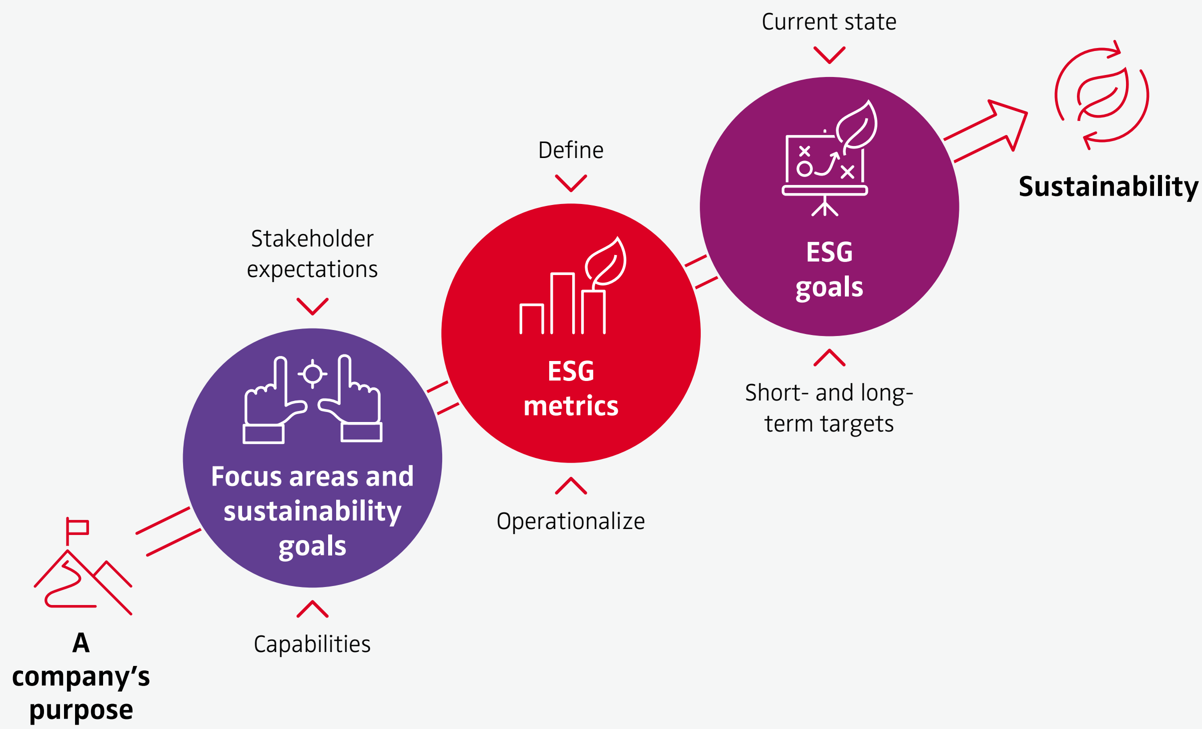
- **Having all the ESG data in one place makes the task of ESG reporting easier** × There are myriad reporting frameworks with their own idiosyncratic requirements – Global Reporting Initiative (GRI), Carbon Disclosure Project (CDP), Taskforce on Climate-related Financial Disclosures (TCFD), Sustainability Accounting Standards Board (SASB) and the like. Often, different stakeholders – investors, policy makers, NGOs, regulators – rely on different disclosure frameworks, and having good data collection mechanisms in place makes it easier for companies to comply with such requirements.

- **Fostering accountability and improving decision-making** × By showing the performance of sustainability initiatives vis-a-vis targets spanning issues, geographies and departments, the ESG dashboard fosters accountability on the part of senior management and improves decision-making. For example, the ESG dashboard can help managers use quantitative analysis to demonstrate to their employees, C-suite and board members the effectiveness of their sustainability strategy, which in turn informs company decision-making and resource allocation internally.

- **Allowing compensation schemes based on ESG performance** × Tying ESG performance to variable compensation of employees is increasingly popular as it provides additional motivation to integrate sustainability into one's daily work routine and accelerates sustainability progress overall.

- **Enlivening the "sustainability culture" of an organization** × ESG dashboards play a key role in developing a sense of "sustainability ownership." Companies that are successful in the sustainability space use key metrics to

FIGURE 2 > Steps toward clear ESG goals and more sustainability



communicate incessantly to their employees and other stakeholders – via hallway tickers, computer pop-ups and the dashboard itself.

How to build ESG dashboards for more sustainability

While monitoring ESG metrics is beneficial for companies, failure to comprehend value and inappropriate measurement methodologies might result in mediocre or even negative performance. ESG reporting is a complicated area, and companies who report to different stakeholders with different requirements may find it challenging to stay on top. As Perez et al. aptly put it in their McKinsey article, "ESG is a process, not an outcome." Figure 2 shows the important steps in such a process.

The first point to note is that the ESG dashboard is idiosyncratic to a company and ought to be tightly coupled with the company's purpose, its raison d'etre, or the answer to the all-important question of "why do we do what we do?" Is a car company's purpose to sell more cars or to provide mobility? The answer to this question will undoubtedly feed into its sustainability strategy and ultimately to the metrics displayed in the ESG dashboard.

Once purpose is clear, the next step in deciding the sustainability strategy is to define a set of concrete or "material" focus areas and goals for the company, the idea being that sustainability is a big playing field and all companies do not have to run after the same goals. For instance, while reducing CO_2 emissions may be material for a cement manufacturer like LaFarge Holcim, financial literacy and inclusion may be more material for a bank like ING. Materiality analysis entails assessing key stakeholders' expectations of the company's sustainability efforts and juxtaposing those with the managers' assessment of the company's ability to deliver on those goals. Footprinting, impact screening and traditional

FIGURE 3 > Examples of ESG metrics

Environmental

- Carbon emissions
- Tons of toxic waste
- Percent of energy reduction
- Percent of water reduction
- Percent of sustainably sourced products
- Amount of pay tied to climate response targets

Social

- Percent of racial/ethnic group representation at all levels
- Gender pay gap
- Investment in upskilling per employee
- Employee satisfaction and retention
- Number and types of employee wellness initiatives

Governance

- Number of female directors
- Number of minority directors
- Board involvement on climate issues
- Alignment of executive compensation with sustainability goals

SWOT analysis are all part of the process of defining a set of concrete sustainability goals for a company.
In a third step, ESG metrics are defined and operationalized in the defined focus areas of the company. Figure 3 provides examples of ESG metrics for a hypothetical company.
On the basis of such metrics, companies can set clear goals in a fourth step. Ideally, they will follow the ESG metrics with a baselining exercise (where are we today) and a visioning exercise (where we want to be by 2030 or 2040), which enables them to set year-on-year targets for those metrics. Data collection on the metrics typically happens through the Enterprise Resource Management (ERM) systems that most companies have in place, and then visualization platforms such as Tableau by Salesforce are used to bring the dashboard to life.

ESG dashboards are a means to an end × In essence, the ESG dashboard metrics serve as a means of accountability for all parties concerned and contribute to ensuring that the business adheres to its ESG commitments. Companies should use a purpose-driven approach with strong commitment from management and use cross-functional teams from

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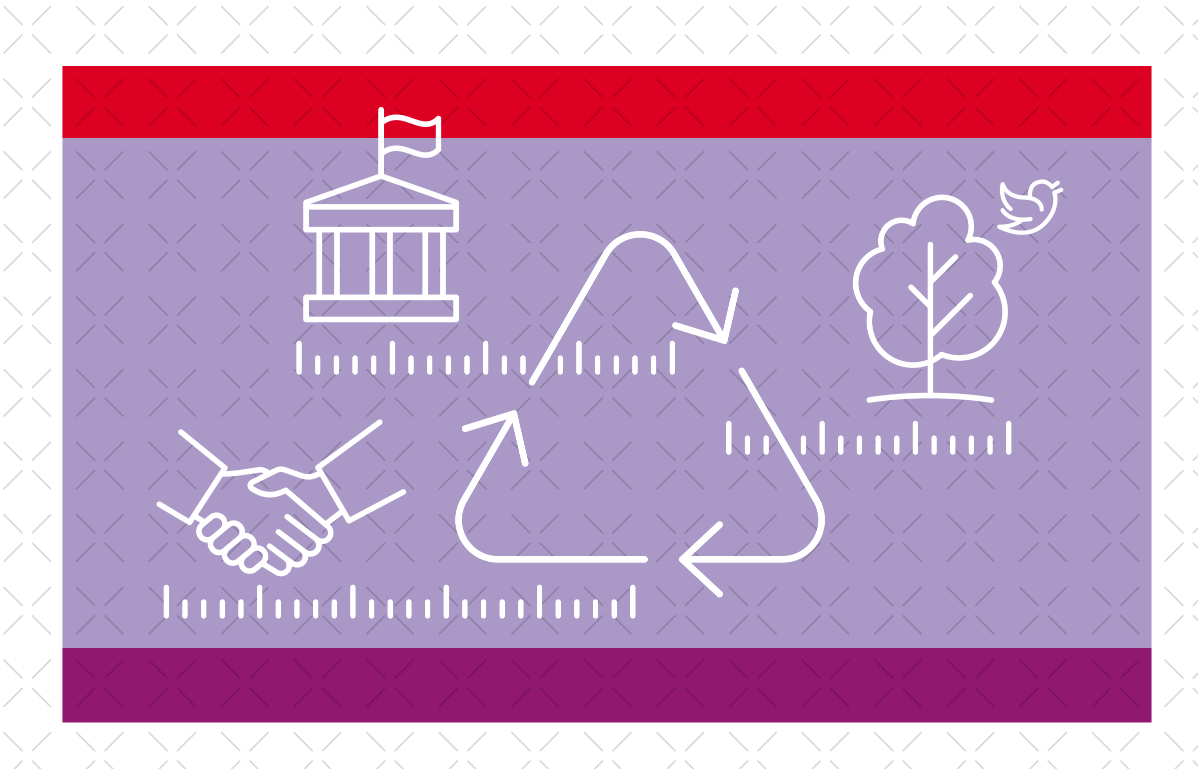

areas including supply chain, technology and infrastructure to formulate a plan to integrate ESG metrics for reporting and identify gaps and deficiencies in current practices. Identifying emerging technologies such as automation, blockchain, AI and data analytics can lead to improved efficiencies in ESG reporting. Although ESG impact is sometimes inherently more difficult to measure, the degree of difficulty ought not to be a deterrent. If a company's purpose authentically aligns with social, environmental and governance causes, it leads to a clear view of ESG metrics and gives guidelines to create a more reliable and actionable ESG dashboard – and a better planet.

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