IMPLEMENTING
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#3

LEADERSHIP DECISION-MAKING REIMAGINED

SUSTAINABILITY REIMAGINED

Unleashing the full potential of sustainability to drive transformational change

Sustainability is at the top of the strategic agenda everywhere. Trailblazing organisations are acting fast to reduce harmful impacts on people and the planet. And even those that have been slower to respond are being forced to act due to regulatory changes and stakeholder demands. Becoming more sustainable is now a given.

However, all organisations face a significant strategic choice: "Will sustainability provide us with the opportunity to rethink fundamental strategic approaches and change everything? Or will we address the issue through an isolated sustainability strategy to get on par?"

Faced with a proliferation of stakeholder requirements, there is a risk that many organisations are merely scratching the surface of sustainability as they try to keep up. But what if we used the sustainability agenda to profoundly reimagine why our organisation exists and how we operate?

We believe that, instead of a "sustainability strategy", organisations of the future will have a "sustainable strategy". Instead of taking incremental steps towards what is good for them, they will dare to unleash transformational change towards a brighter future that is better for all of us.

Let us explore the future together and reimagine sustainability.

#3

LEADERSHIP DECISION-MAKING REIMAGINED

What if organisations of the future **integrated multiple bottom lines** and externalities in all **decision-making processes** to make truly sustainable choices - and asked the finance department to never produce a simplistic financial business case again?

Myriad of decisions are made in every organisation each day. Some decisions are tactical and simple, typically based on straight-forward intuition and experience. Other decisions are strategic and complex, often demanding sophisticated problem-solving and careful testing of critical assumptions. However, looking at different types of decisions, as leaders we typically apply financial reasoning to make decisions. These range from 'please provide me with a rough, back-of-the-envelope calculation' to 'we need to do a detailed investment business case projecting future cash flow' to make decisions. Financial logic is omnipresent, informing and guiding decision-making.

Entering a new age of stakeholder value creation challenges the hardwired practices of making the final call based on simple financial logics. But several challenges to move forward towards a broader understanding of value creation spring to mind.

Challenging the dominant financial logic

Firstly, most business cases tend to be crude simplifications of a complex reality, in which profit maximisation or return on invested capital is often the overarching goal. A more nuanced analysis of both positive or negative externalities of the decisions being made is often absent or hidden. Some organisations are, for example, introducing the impact of carbon emissions, encouraged by the introduction of carbon taxes, and this is a great step in the right direction. But carbon emissions are only one sustainability factor among many. How about biodiversity, scarce resources, or social impact?

Secondly, complexity grows if we want to consider and account for all relevant people and ecological implications of decisions in addition to financial data. Decisions become hard to make and, in many cases, there simply are no tools, data or capabilities available to support decision-making, and attempts to come up with better answers become very time-consuming.

Thirdly, the advantage of a classic business case in helping us choose from alternatives is challenged as comparability becomes more complex. And when considering a range of organisations, this issue gets worse, as there is an evident lack of clear standards on how to make judgements and business decisions when including different aspects of sustainability. This is further amplified by the absence of price/market signals indicating the impact on sustainability.

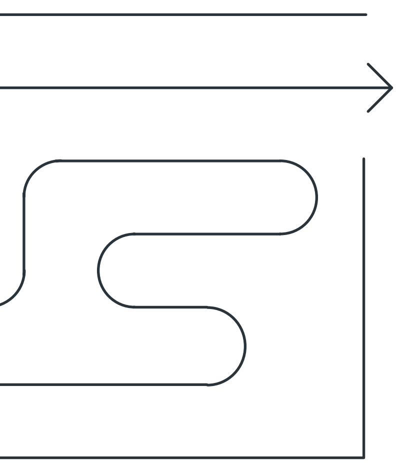
All of the challenges mentioned work against a fundamental shift in decision-making practices. But if we are to be serious about stakeholder value creation thinking, we must act decisively to overcome the challenges. It is tempting to lean back, wait for regulators to set the bar and enjoy the ride 'for free' until the true stakeholder value impact of our decisions is revealed by an external party. Think again and consider the risks. Is a company taking that approach likely to be a leading company in the future?

Bridging the gap to better decision-making

While the complexity of sustainable decision-making practices must be acknowledged, pathways are emerging to help companies transition to a new paradigm: focus, simplification and standardisation.

Focus emerges as an essential factor when it comes to navigating the sustainability landscape. Assessing all the potential factors related to sustainability will lead to confusion; from employee working conditions to waste management and from carbon emissions to societal value creation. That is why decisions should be made based on the most material factors according both to external scientific standards and stakeholder perceptions, as well as internal importance of long-term value creation and the strategic direction of a company. In financial services, trust, security and transparency are material factors, while sustainable water usage, for example, is less of an issue. The first step in navigating decision-making is reducing the long list of potential factors to a short list of high-impact factors in the given context.

To cut through complexity, the ability to simplify is an important skill. One approach to simplification is establishing clear rules about organisational non-negotiables; basic stop-go rules. Implement, for instance, does not work for the tobacco industry and this is a non-negotiable standard. Another approach is defining clear threshold values and limits that a decision cannot challenge or pass. A simple example is to make sure that any investment decision must always be in line with achieving the goals of the Paris Agreement in terms of reducing carbon emissions.



Another pathway to navigate the new realities of sustainable decision-making is standardisation. Standardisation can happen internally as the organisation develops decision-making tools and processes that can be scaled across a range of business decisions, taking more aspects into account. Such practices are well-established in mature organisations that have already moved from purely financial logic to more nuanced decision-making frameworks in which several aspects are evaluated in composite scoring models, thus maintaining comparable metrics. In addition to the financial impact, aspects such as the strategic importance, potential risk factors and fit with organisational capabilities are typically considered systematically. In the future, the impact on people and the planet should be included in such frameworks.

Standardisation can also happen externally when organisations are either forced to comply with certain standards through regulation or when they voluntarily commit to external standards, such as setting targets for carbon emissions according to science-based targets (SBTi) or similar emerging commitment standards. Across internal and external standardisation, data definition, collection, analytics, disclosure and availability are key enablers of making both effective and efficient decisions. And for this to be meaningful, it must be across the full value chain.

The science of organisational decision-making has progressed significantly in recent years due to advances in behavioural economics, helping to make leaders aware of the many unconscious biases at play when making great decisions. Taking the next step forward requires us to move beyond simplistic decision-making based on classic financial reasoning to a new level of awareness that will help us make better and more sustainable decisions.

Questions worth considering

Do you have a clearly defined approach for making major decisions that is used consistently across your organisation?

What elements of your organisational decision-making capability need to be upgraded to include relevant sustainability dimensions?

How will you navigate the complexity challenges of making more sustainable decisions in your specific organisational context?

RioTinto

Case in point:

Rio Tinto accounts for positive and negative externalities

Rio Tinto is among the largest metals and mining companies in the world, focusing on sourcing, mining and processing mineral resources. In 2021, Rio Tinto revamped its corporate direction, making the focus on sustainability an integral part of its overall corporate strategy.

The updated strategy unites three elements at its core: accelerating the decarbonisation of assets; developing products and technologies that help customers decarbonise; and growing in materials that enable the energy transition.

While focusing efforts on decarbonisation, Rio Tinto's general business objectives also aim to capture and account for efforts with wider societal impact. To this end, Rio Tinto developed an in-depth reporting tool for strategic KPIs, including measurements of the socio-economic impact created. Taking a broader perspective offers the potential to analyse the impact of different social and environmental externalities, as well as to support strategic decision-making and dialogue with stakeholders.

The socio-economic impact created in 2021 amounted to USD 66.6 bn, taking into account the total value of operating costs, employee wages and benefits, payments to providers of capital, payments to governments, development contributions, payments to landowners and community investments.

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