INTEGRATED THINKING AND THE INTEGRATED REPORT

IFAC
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Presented by Mervyn E King SC
THE COMPANY YESTERDAY

- The primacy of the shareholders
- Wealthy families
- Single focus and bottom line
- Financial reporting – rear view mirror
- Prepare as if only user the investment analyst
- 100 years but IASB and FASB
YESTERDAY’S ECONOMIC MODEL

- Yesterday’s economic model was based on two false assumptions that:
  - there were limitless resources in nature and
  - that planet earth had an infinite capacity to absorb waste
- Take – make – waste
- Industrial revolution
- Until middle of 20th century
THE COMPANY TODAY

- New capitalists
- Stakeholders – inclusive – CSRO’s
- Legitimate NIE’s
- Moat of shareholders
- 100 largest economies
- Not in a vacuum – a triple context
- What are the specifics?
THE CHANGED WORLD

- Global financial crises
- Climate change crisis
- Ecological overshoot
- Radical transparency
- Greater expectations from stakeholders
- Population growth
- Cannot carry on business as usual
- Have to learn to make more with less
- Requires IT and innovation
DRIVERS FOR CHANGE

Drivers for Change

THE TECHNOLOGICAL REVOLUTION
THE ECONOMIC REVOLUTION
THE SOCIAL REVOLUTION
THE NET GENERATION

TAPSCOTT
COMPONENTS OF MARKET VALUE

S&P 500

<table>
<thead>
<tr>
<th>Year</th>
<th>Physical and financial assets</th>
<th>Other assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>83</td>
<td>17</td>
</tr>
<tr>
<td>1985</td>
<td>68</td>
<td>32</td>
</tr>
<tr>
<td>1995</td>
<td>32</td>
<td>68</td>
</tr>
<tr>
<td>2005</td>
<td>20</td>
<td>80</td>
</tr>
<tr>
<td>2009</td>
<td>19</td>
<td>81</td>
</tr>
</tbody>
</table>


Other assets: 17% of value in 1975, 32% in 1985, 68% in 1995, 80% in 2005, 81% in 2009.

Legend: S&P 500
# The Global 1000

<table>
<thead>
<tr>
<th>Time period</th>
<th>Sales ($B) of the top 1,000 firms</th>
<th>Employees (M) of the top 1,000 firms</th>
<th>GDP (current US$B) of OECD members</th>
<th>Population of 15-64 of OECD members</th>
<th>Top 1,000 firms' sales as % of OECD GDP</th>
<th>Top 1,000 firms' employees as % of OECD working population</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980</td>
<td>2,638.10</td>
<td>20.9</td>
<td>8,547</td>
<td>629</td>
<td>30.90%</td>
<td>3.33%</td>
</tr>
<tr>
<td>1990</td>
<td>7,126.30</td>
<td>31.4</td>
<td>18,079</td>
<td>702</td>
<td>39.40%</td>
<td>4.47%</td>
</tr>
<tr>
<td>2000</td>
<td>15,821.30</td>
<td>49.9</td>
<td>26,162</td>
<td>767</td>
<td>60.50%</td>
<td>6.51%</td>
</tr>
<tr>
<td>2010</td>
<td>31,196.30</td>
<td>66.8</td>
<td>42,809</td>
<td>825</td>
<td>72.90%</td>
<td>8.11%</td>
</tr>
</tbody>
</table>

The Information Age

Number of users, millions

Twitter: http://wewillraakyou.com/2012/02/dynamic-chart-shows-twitters-exact-growth/
The Power of the Internet

INTEGRATED THINKING (1)

- Integrated as opposed to “silo thinking”
- Every company dependent on relationships and resources
- Mindset change at board level
- Agenda item stakeholder relationships
- Knowledge of stakeholders’ legitimate NIE’s
- Greater stakeholder expectations
MINDSET CHANGE
INTEGRATED THINKING (3)

- Manage and strategize on a more informed basis
- Supply chain – suppliers stakeholder – code of conduct – impact reputation
- Traceability and monitoring
INTEGRATED THINKING (4)

- Identify sustainability issues material to business
- As water is to beverage manufacturer
- Embed sustainability into long term strategy
- In context of resources, relationships, risks, opportunities and global turbulence
Some numbers....

Integrated ESG information into investment decisions

- 79% of asset owners
- 95% of investment managers

(Source: UNEP Finance Initiative, UN Global Compact)
Tipping point to embed sustainability in core business strategies? (Acc. to CEO’s)

- Customers demand sustainable products  
  * 89%
- Educational reform to change mindsets  
  * 88%
- Accurate long-term valuation (incl. sustainability metrics)  
  * 86%
- Shareholders place more value on sustainability information  
  * 85%
- Boards hold directors accountable for practices  
  * 84%

(Source: UN Global Compact and Accenture)
INTEGRATED THINKING (7)

- Financial
- Manufactured
- Human
- Intellectual
- Natural
- Social
All organizations depend on a variety of resources and relationships for their success. These resources and relationships can be conceived as different forms of “capital”.

Source: Incite  *Sustainability 2.0: A Guide to Competing in a Changing World*
INTEGRATED THINKING (8)

- Management of risk
- Risk matrix informed by the levels of dependence on the resources and relationships
- Levels of risk tolerance more informed – opportunities
- Risk management plan more informed
- Risk responses more appropriate
INTEGRATED THINKING (9)

- Impacts
- Leverage
- Of company’s business model
- KPI’s and KRI’s fall under financial or non-financial?
INTEGRATED THINKING (10)

- Unilever
- Long term plan – re-engineer
- Productions and products
- Renewable power, recyclable materials, zero waste to landfill, consumer and supplier
- Lifebuoy and Pureit
INTEGRATED THINKING (11)

- Understanding, knowing and then planning:
- How the company makes it money?
- How the company will sustain value creation in the long term?
Companies consist of interacting, interrelated and interdependent operations, functions, relationships and resources

Take account of:

- the connectivity between these factors
- the changed world in which the company operates
- impacts
- leverage
Stakeholders expect that:
1. The company has not profited at the expense of the environment, human rights, a lack of integrity or society;
2. There are adequate controls in place to monitor and manage material risks and opportunities;
3. Remuneration is linked to overall performance which includes social, environmental and financial aspects;
4. There is an interactive communication with the stakeholders who are strategic to the company’s business; and
5. The company is conducting a sustainable business
INTEGRATED THINKING (15)

Business Model

How?

Risks

Resources

Opportunities

Stakeholders
THE OPEN KIMONO

- Reporting influences behaviour
- Integrated reporting – King III
- IIRC – formation 2010
- Informed assessment
- Discharge of fiduciary duty by trustee
SYSTEM OF REPORTING

- Is there one?
- Bolt on a division’s report to another
- Chairman’s statement
- Integrated report has a system
- The collective mind of the board
- FR impact on NF and how material sustainability embedded into strategy to sustain value creation
INTEGRATED REPORT
DRIVERS FOR INTEGRATED REPORTING

- State of planet
- The customer of today
- The new capitalist
- The identity & reputation of companies
- Competitive advantage – management more informed
- Market forces - external
PURPOSE OF INTEGRATED REPORT?

- Clear and understandable statement on “the state of play”
- Financial Report only part of “state of play”
- Nothing of impacts on society and environment
- Cannot make an informed assessment of the sustainability of a business
Guiding Principles

- **Strategic focus:** An Integrated Report provides insight into the organization’s strategic objectives, and how those objectives relate to its ability to create and sustain value over time and the resources and relationships on which the organization depends.

- **Connectivity of information:** An Integrated Report shows the connections between the different components of the organization’s business model, external factors that affect the organization, and the various resources and relationships on which the organization and its overall performance depend.

- **Future orientation:** An Integrated Report includes management’s expectations about the future, as well as other information to help report users understand and assess the organization’s prospects and the uncertainties it faces.

- **Responsiveness and stakeholder inclusiveness:** An Integrated Report provides insight into the organization’s relationships with its key stakeholders and how and to what extent the organization understands, takes into account and responds to their needs.

- **Conciseness, reliability and materiality:** An Integrated Report provides concise, reliable information that is material to assessing the organization’s ability to create and sustain value in the short, medium and long term.
Content Elements

- **Organizational overview and business model:** What does the organization do and how does it create and sustain value in the short, medium and long term?

- **Operating context, including risks and opportunities:** What are the circumstances under which the organization operates, including the key resources and relationships on which it depends and the key risks and opportunities that it faces?

- **Strategic objectives and strategies to achieve those objectives:** Where does the organization want to go and how is it going to get there?

- **Governance and remuneration:** What is the organization’s governance structure, and how does governance support the strategic objectives of the organization and relate to the organization’s approach to remuneration?

- **Performance:** How has the organization performed against its strategic objectives and related strategies?

- **Future outlook:** What opportunities, challenges and uncertainties is the organization likely to encounter in achieving its strategic objectives and what are the resulting implications for its strategies and future performance?
The integrated report is evolving
It is an evolution in corporate reporting
Integrated thinking is a revolution
A revolution in the approach to managing environmental and societal issues
Overwhelming support for integrated thinking
How are companies Doing?

- Annual reports now Integrated Report
- Detailed financial and sustainability information on line
- New Companies Act – section 29(3)
- Abridged financials
- Companies using diagrams, graphs and graphics
- All participants in the IR journey
- Some examples
How we measure our performance?

Our most important measure is what we call our Net Promoter Score (NPS). Vodafone uses this to monitor customer happiness in most of its markets. It is simply a measure of how likely our customers are to recommend us to their family, friends and colleagues – and how likely they are to recommend our competitors. We implemented NPS in South Africa and DRC in 2011. In the year ahead we’ll implement it in the other markets we operate in.

The great stuff we did this year

- Number one in NPS in all markets we measured
- Involved our executives in customer focus groups and customer days
- Improved our customer touchpoints
- Established active engagement with our customers on Twitter and Facebook
- Offered more value, bringing the effective price per minute down 18.0% across the Group
- Added 3.6 million new customers to bring Group customers to 43.5 million
- Launched Vodacom Change the World and Vodacom Red Alert initiatives with customers

The stuff we didn’t do well this year

- Delayed network rollout in some countries due to slow approvals and equipment deliveries
- Second place in Vodafone voice quality tests
- Limited progress in encouraging customers to dispose of handsets responsibly

Our 2013 goal

We aim to be No 1 in NPS in all our markets across all customer touchpoints.
Integration of Equator Principles into credit approval process

- Project initiation
- Registration and screening
  - Tool 1
- Project categorisation confirmation
- Pre-credit committee
- Credit application
  - Environmental and social assessment
  - Review of environmental and social impact assessment and management plans
  - Tool 2
- Gap analysis and action
  - Tool 3
- Legal documents
  - Tool 4
- Monitoring and evaluation
  - Tool 4

Standard Bank
USE OF SYMBOLS AND COLOURS

Easy referencing and usability features

Have we succeeded in our 2010/11 strategic objective?

Get more information online

Cross-reference information

Information contains GRI compliant information

This icon indicates more information available online at www.adcock.com

This icon indicates more information can be cross-referenced on pages within report sections

This icon indicates the information adjacent contains GRI compliance elements
CONVEYING KEY RELATIONSHIPS

Net working capital days:
- Accounts receivable
- Inventory
- Accounts payable

★ Multiple years
★ Arrow to indicate trend
★ Colour usage to distinguish

(ALTRON)
BUSINESS MODEL – HOW WILL IT ADD VALUE?

Our business model is designed to deliver sustainable growth in earnings. It is consumer-led and science-based.

How our business works

Consumers
Our success depends on really understanding the different profiles and preferences of our consumers. We invest in gathering comprehensive insights into smokers’ preferences and buying behaviour. This drives our marketing and allows us to promote our products to adult tobacco consumers in ways that satisfy their preferences, while responding to stakeholder expectations about how we should market our products.

Sourcing
We have a significant interest in tobacco growing and we work directly with around 70 per cent of the farmers who supply our leaf. We manage our whole supply chain responsibly and work with our suppliers to create a shared understanding of our social, environmental and economic impacts. This enables us and our suppliers to manage risks better, while ensuring that we are agile and flexible, so that we can use our resources as effectively as possible.

Building sustainable value

Science-based R&D
For over 50 years, we have had an extensive scientific research programme. More recently, we have been focusing research on modified cigarettes and low-toxicant smokeless tobacco products. We are committed to helping develop the scientific and regulatory framework we need to deliver a varied portfolio of products in the future, including alternative regulatory-approved nicotine products, to meet the evolving needs of adult smokers.

Brands
We have a successful brand marketing strategy based on innovation, responsibility and consumer choice. We recognise that our business starts with our consumers and our brand portfolio is designed to meet key consumer needs, especially in our strategic consumer segments. Our four Global Drive Brands – Dunhill, Kent, Lucky Strike and Pall Mall – and our other international brands account for more than 50 per cent of our total cigarette volumes.
**WHAT IS MATERIAL TO STAKEHOLDERS**

<table>
<thead>
<tr>
<th>Stakeholder</th>
<th>What matters most to them</th>
<th>Ways we engage</th>
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</thead>
<tbody>
<tr>
<td>Customers</td>
<td>Better value offerings</td>
<td>Call centres and outlets. Extensive focus groups and customer interviews.</td>
</tr>
<tr>
<td></td>
<td>Faster data networks and wider coverage</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Making it simpler and quicker to deal with</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Converged solutions for business customers</td>
<td></td>
</tr>
<tr>
<td>Employees</td>
<td>Clear career paths</td>
<td>Weekly emails, intranet, top management/CEO roadshows, webcasts and dedicated employee call centres.</td>
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<td></td>
<td>More knowledge sharing across the Group</td>
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<tr>
<td></td>
<td>Building the coaching capability of leaders</td>
<td></td>
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<tr>
<td></td>
<td>Better understanding of reward structures</td>
<td></td>
</tr>
<tr>
<td>Business partners (VODACOM)</td>
<td>Fair treatment across the board</td>
<td>Dedicated call centres, trade bulletins, allocated business managers, annual business partner conference.</td>
</tr>
<tr>
<td></td>
<td>Top management involvement</td>
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CASE STUDIES

★ Unilever
★ P & G
★ SAB Miller
★ Siemens – sustainability should be viewed not from the viewpoint of risk and compliance only but that which drives business expansion
★ Walmart
DUTY OF CARE

- Centro judgment – Australia
- What do you know or ought you to know?
- What are you aware of or ought you to be aware of?
SOME CONCLUSIONS

★ Tell your stakeholders what you do, do what you tell them, and write it down in your Integrated Report

★ Companies cannot solve 21st century problems with the same mindset their boards used when they created them

★ We cannot solve 21st century corporate challenges with 20th century decision making or reporting
INTEGRATED REPORT

- Reporting influences decision making
- A concept, fit for purpose
- Whose time has come
- Because of the changed world
- Financial, natural, human, society, manufacturing, intellectual capital
- Critical interdependencies
- The decade of stupidity 2000 – 2010
- The decade of change 2010 -2020
THE FUTURE

- Mindset changes
- Advanced IT
- The net generation
- Sustainable capitalism
- Civil society – great expectations
- Integrated reports and financial stability
- One certainty - change
Man and nations

Helen Keller: “The only thing worse than being blind is having sight and no vision”

We have the light

Why grope in the dark?
THANK YOU

Prof Mervyn E King SC