Corporate and societal value creation are increasingly connected, finds KPMG

18 September 2014, Johannesburg - Companies need a better understanding of the value they create for society in order to protect and create corporate value, according to A New Vision of Value, a global report published today by KPMG International.

A New Vision of Value identifies three key drivers that are closing the gap between corporate and societal value creation: new regulations and standards; the growing influence of stakeholders; and changing market dynamics driven by economic, social and environmental megaforces.

These three drivers mean that corporate externalities, which historically had little or no impact on cash flows and risk profiles, are bringing new risks and opportunities with significant implications for corporate value creation in the 21st century. Externalities can be positive or negative. A positive externality is an economic, social or environmental benefit that a company creates for society for which it is not directly or fully rewarded in the price of goods and services. Conversely, a negative externality is a cost a company imposes on society, for which it does not pay.

The report contains case studies which illustrate how new regulations, stakeholder action and market dynamics could affect the earnings of three model businesses if they do not adapt to these drivers: a gold mine in South Africa, a brewery in India and a plastics plant in the US.

It applies the KPMG True Value methodology to find that, in a 2030 scenario, the brewery could see its earnings margin of 5 percent turned into a loss of 4 percent. The gold mine could see its earnings margin reduced to a level of 1 percent that would make it financially unsustainable. The plastics plant by contrast was better protected from the internalisation of its externalities due to its location and sector-specific conditions.

“Corporate value measurement has historically largely excluded externalities, but today many South African corporates recognize that corporate and societal value creation are becoming more closely connected,” said Shireen Naidoo, Director of KPMG South Africa’s Climate Change & Sustainability practice.

Adrian King, Global Head of KPMG’s Climate Change & Sustainability practice said that, “Externalities are now part of every company’s value creation story. Business leaders and their investors need to be aware of these new dynamics in order to unlock value creation opportunities and manage risks. They need to identify and quantify externalities, recognise what is driving internalisation and understand the implications for corporate value."

The report also highlights how closer alignment between corporate and societal value creation is being held back by the current financial system in which many investors and business leaders are focused almost exclusively on the creation of short-term shareholder value.

It proposes a 6-point agenda for change:
1. Demonstrate leadership and tangible action
2. Clarify the concept of fiduciary duty
3. Improve understanding of the relationship between corporate and societal value
4. Change mandates and incentives
5. Improve the quality of data
6. Provide an enabling policy environment

To view the report, please visit: A New Vision of Value: Connecting corporate and societal value creation

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