The PACE of Change
Insights into the Issues Driving Change

August 2020

Ethics Considerations in the New Normal

Ethics

2020 has seen unprecedented forced disruption from a global pandemic, the exit of the UK from the European Union, global political movements and an even stronger spotlight on climate change.

This has brought wider societal and global pressures into sharper focus for many businesses. The PACE of Change takes a research-led look at these issues in detail and explores key implications for businesses.

Corporate Behaviour and Values

Reputation will be key, as will corporate purpose, as calls grow for businesses to play their part in solving the problems of people and planet. Businesses will increasingly need to adopt a long-term stakeholder approach to their business models if they want to stay relevant.

In January 2020, when the COVID-19 pandemic was still in its infancy, the World Economic Forum launched The Davos Manifesto 2020: The Universal Purpose of a Company in the Fourth Industrial Revolution. The manifesto at the time recognised the rise of stakeholder capitalism and the Greta Thunberg effect. It holds more weight now as we enter into the "new normal". The manifesto sets out ethical principles to guide companies, with corporate purpose, behaviours and values at the heart of it. Redefining an organisation's reasons for being should extend well beyond financial gains and should stretch further than corporate social responsibility.

> "The purpose of a company is to engage all its stakeholders in shared and sustained value creation. In creating such value, a company serves not only its shareholders, but all its stakeholders – employees, customers, suppliers, local communities and society at large."
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> The Davos Manifesto 2020: The Universal Purpose of a Company in the Fourth Industrial Revolution

Incorporating non-financial considerations will become a mainstay of business planning and decision-making as more and more companies incorporate frameworks for environmental, social and governance (ESG) factors into their business models. For businesses, this means not only demonstrating ESG credentials, but also establishing a clear purpose, which is in line with the UN Sustainable Development Goals.

Going forward, the call for greater corporate transparency on ESG issues will only amplify as ESG factors prove themselves not just to be non-financial considerations, but also material drivers of financial performance and business resilience.

Pressure will continue to come not just from legal compliance, but also from customers, the workforce, supply chains, society and shareholders. Businesses will need to focus their attention on the following corporate behaviours:

- **Customers** – Delivering fair competition, reliable, trustworthy digital ecosystems and transparency around products and services.
- **Workforce** – Diversity and inclusion, employee wellbeing, upskilling and retraining, and fair executive remuneration.
- **Supply chain** – Developing partnership models, providing a fair chance for new market entrants and adhering to human rights across the supply chain.
- **Society** – Demonstrating support to communities and people's wellbeing, paying a fair share of taxes, validating ethical use of data and stewardship of the environment.
- **Shareholders** – Continuous innovation, sustained investments and sustainable shareholder returns.

Diversity and Inclusion

COVID-19 has undoubtedly put further emphasis on inclusion and diversity issues.

While the pandemic has highlighted existing inequalities by hitting the lower paid, black and ethnic communities harder, the Black Lives Matter protests following the death of George Floyd have catapulted racial inequality to the forefront as an issue needing visible and concrete action on the part of society, employers and policymakers.

The UN Principles for Responsible Investment is galvanising action on the part of investors and has called for "engagement on ESG issues which directly and indirectly perpetuate inequality". It goes further to say, "to hold corporations and policy-makers to account, we must push for public disclosure on racial diversity and related metrics by which we can assess progress against concrete outcomes."

The pandemic has also disproportionately affected women. Not only are working mothers more likely to have assumed extra childcare responsibilities and housework during lockdown, but they are also statistically more likely to be hit harder financially, with less job security. Their "traditional" roles are also more vulnerable to advances in AI and automation. Ensuring that advances in women's interests are not set back by the virus is a challenge companies will need to address, especially as reporting requirements are relaxed in jurisdictions such as the UK on issues such as gender pay.

The trends towards greater remote working may level the field and provide employers with opportunities to improve access for women, the disabled and other diverse groups. The prospect of accessing multiple talent pools unrestricted by geographical confines presents an exciting opportunity, but how employers attract, motivate and retain that talent will also depend on its employer "brand", in particular with the young as they seek a clearly defined "purpose" in their jobs. As governments invest in schemes to support opportunities afforded to the next generation, employers have a role to play in ensuring the skillset of their talent pool stays relevant and future proof.

Businesses need to have an action plan to drive equality at board level, a commitment to embedding this through their brand, and delivering it through corporate purpose.

Regulation and Governance

Investors are increasingly seeing non-financial considerations as material to companies' performance. The data is starting to demonstrate a positive correlation between strong ESG practices and financial performance.

Businesses with robust governance frameworks are able to manage their environmental and social factors and can better mitigate risks and increase productivity. At the same time, public discourse on climate change, social inequality and corporate governance failures has kept these issues at the top of the policy agenda, with more than 730 hard and soft laws underpinning ESG considerations worldwide.

ESG-conscious companies with sound governance and solid relationships with their suppliers, employees and stakeholders have been able to better account for long-term risks, shown greater resilience and outperformed during this period of intense volatility. Even before the pandemic, the largest review of studies into whether the integration of ESG principles had a positive effect on corporate financial performance showed that the business case for ESG was empirically well founded.

In addition, the increasingly complex regulatory regime has increased the exposure faced by businesses. This is particularly acute, as the regime extends to actions of third parties acting on a business' behalf, in particular within their supply chain.

The consequences for a lack of robust compliance programmes are very real, including unlimited fines, loss of operating licences and damage to the business' reputation. Businesses will require a well-designed and well-implemented compliance programme to help mitigate substantial risk, which is also able to detect/address systemic weaknesses.

Governance is critical and it has to be a boardroom issue. The boardroom must address all key business integrity risks, including:

- Anti-tax evasion (corporate tax offence)
- Bribery and corruption
- Data privacy
- Modern slavery
- Money laundering
- Reputation
- Sanctions
- Sexual harassment (safeguarding)

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