# The Three Big Ideas behind Integrated Thinking and Reporting

How to start measuring, managing and communicating about your business in an integrated way

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## The Integrated Model - A Trend You Don't Want to Ignore

Companies today are subject to **conflicting pressures** from their shareholders, stakeholders and their own boards. On the one hand, they feel the need to **drive innovation, performance and corporate value** as never before. On the other hand, they are also being held **accountable for their effects on society and the environment**. Reconciling this conflict is almost impossible using traditional measurement and reporting. This is leading to innovative approaches to strategy and measurement using what is often called the "integrated" model.

The **integrated model is a holistic view** of the ecosystem in which a company operates and creates value. It examines how a company uses its capital (tangible, intangible and natural) to create value and profit today…while ensuring the sustainability of its capital and value creation capability for the future.

Embedded in this definition are three ideas around **capital, value and sustainability.** These three ideas are each important building blocks of the integrated movement so it bears putting each one into context.

This briefing paper describes each of these ideas together with examples of integrated reporting from GE, Southwest and DBS.

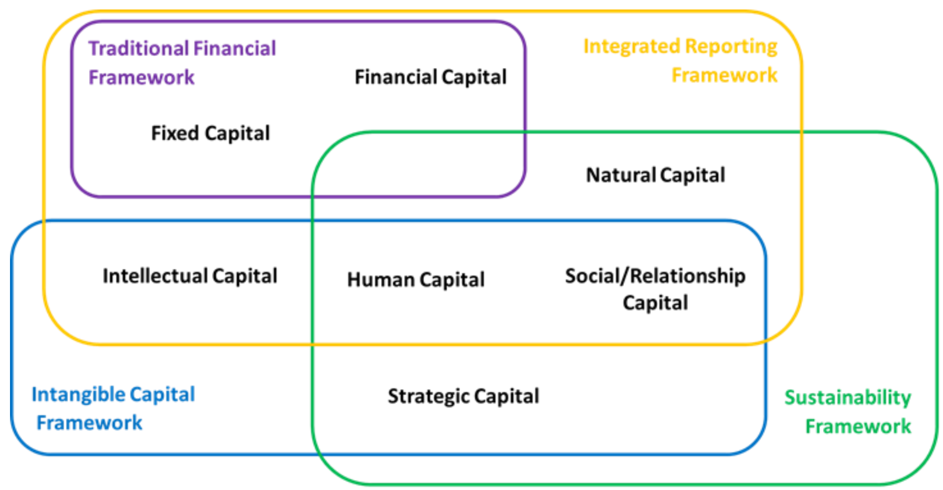
> The integrated model presents a holistic view of how a company uses its **capital** (tangible, intangible and natural) to create **value** and profit today…while ensuring the **sustainability** of its capital and value creation capability.

## 1 – Multiple Forms of Capital

**The first big idea is that a company needs multiple forms of capital to succeed.** Capital is a long-lived resource that a company can access to create value. The major types of capital used in integrated models include:

- **Financial** - cash, debt, equity, grants
- **Fixed** - buildings, equipment, infrastructure
- **Intellectual**- intellectual property and organizational capital such as knowledge, data, systems, procedures, protocols
- **Human** - competencies, capabilities, experience, motivations
- **Social/Relationship** - shared norms, key relationships, brand and reputation
- **Natural** - air, water, land, minerals, forests, biodiversity, ecosystem health
- **Strategic** - purpose, business model, governance, culture

As seen in the graphic here, there are a number of fields that use multi-capital frameworks. The **traditional financial** framework is grounded in accounting and recognizes owned, identifiable and tangible assets as well as a small amount of intellectual capital. The **intangible capital** model (like the financial model) is primarily viewed from the inside out. But it includes the long-lived resources that are mostly excluded from the financial model. This class of asset has grown dramatically as computerization has facilitated an explosion in knowledge capital of many forms. The third major set of frameworks are those that fall under the **sustainability** umbrella including Corporate Social Responsibility (CSR) and Environmental, Social and Governance (ESG) and Triple Bottom Line movements.




The exact name and makeup of individual capital categories are still somewhat fluid with different names being used by different companies and guidelines. But all the models recognize that companies draw on multiple forms of capital to succeed.

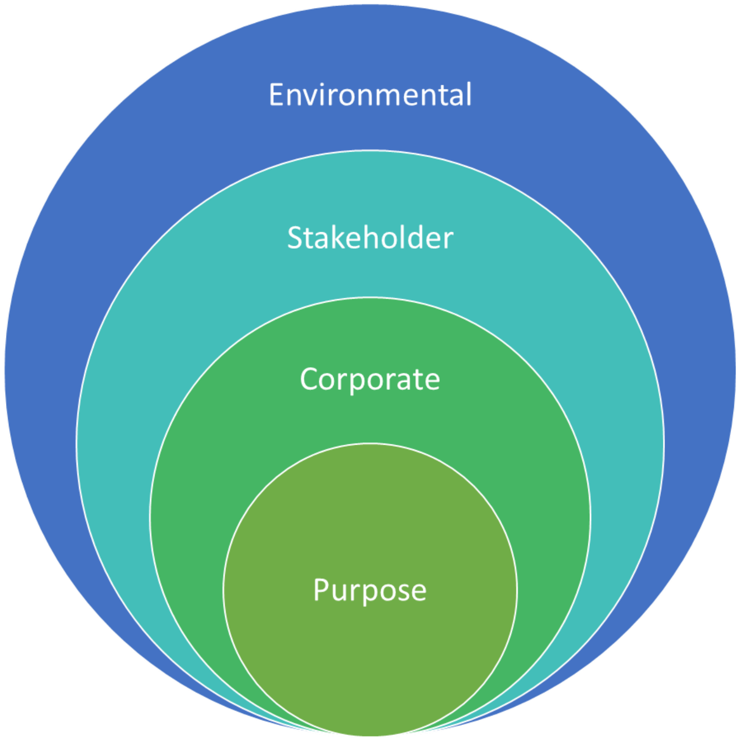
## 2 – Multiple Forms of Value

**The second big idea is that a company creates multiple forms of value**. The value created can take both monetary and non-monetary forms. Broadly speaking, there are three kinds of value flows that are considered in the integrated model:

**Corporate Value** –Corporations generate value by solving problems for their customers using a business model that generates a return. The greater and more reliable this return, the greater the value of the business. This is influenced by performance and profits today. But it's also influenced by the company's ability to generate performance and profits tomorrow. The ultimate measure of corporate value is still financial. But it's increasingly unwise and often impossible to create financial value without also creating stakeholder and environmental value.

**Stakeholder Value** – This includes the financial and non-financial benefits that stakeholders get from their interaction with a company—it solves their problems in a way that works for them. This applies to customers but also to employees, partners, and communities. Stakeholder value may be as simple as a financial transaction: payment for employees/suppliers, or delivery of a product/service to customers. But it is often more complex, bringing in forms of value like personal satisfaction, quality of relationships or the fulfillment of shared values. In today's increasingly transparent and connected world, the qualitative aspects of value creation can't be ignored.

**Environmental Value** – This includes the positive and negative externalities related to the organization's actions. In our industrial past, corporations did not generally consider the environment to be their responsibility. Of course this is changing and the past couple decades have seen the rise of global efforts to educate, drive change and hold companies responsible for their environmental impact. This includes use and/or conservation of natural resources such as water, energy, air, land and other elements of our physical environment. The drivers of corporate focus on environmental value can be negative (risk mitigation) and positive (driver of innovation, fulfillment of purpose or enhancement of reputation).



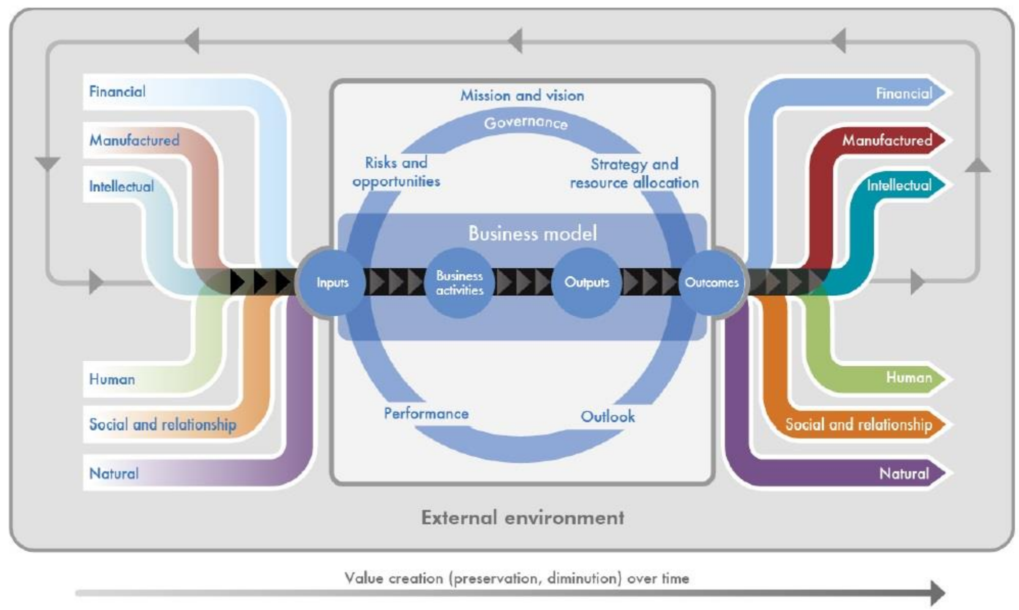
## 3 – Multiple Views of Sustainability

**The third big idea is the broad view of sustainability underlying the integrated model**. Today, the connotation of the word sustainability usually relates to external sustainability of the planet and of communities. The integrated model broadens the perspective to include **sustainability of the full set of internal and external resources**. The graphic at the right comes from the International Integrated Reporting Council (IIRC), an important advocate for use of the integrated model in corporate reporting.

The graphic seen here is from the IIRC Framework. It unites the multiple forms of value, multiple kinds of capital and multiple time frames needed to ensure sustainability of the entire ecosystem of a company. It's a great illustration of **sustainable value creation**. It shows that a company has access to a set of capital resources. It puts them to use in its daily operations. But the company also has to ensure that its underlying capital is preserved for future use.

This perspective highlights the **balancing act that management teams face**: To **create profits and shareholder value** today, a management team needs to **create value today** for customers, employees and stakeholders. But to make this value creation sustainable, today's value shouldn't decrease and should at least preserve or even better increase **the value of the capitals for the future**.

A simple **internal example** is the decision to lay off employees. This can lead to an immediate decrease in operating costs (increasing financial capital). But it can also potentially destroy the company's ability to create value tomorrow (decreasing human capital and potentially future financial capital). A simple **external example** of this is a company's release of dangerous chemicals into the air around a plant. It doesn't cost the company anything today financially (unless it is fined), but it can endanger its people, hurt its community support and/or reputation (human and relationship capital).



## Into the Mainstream

At first blush, these ideas about capital, value and sustainability can sound like the work of idealists working on the fringes of mainstream business. It may have started there, but it's quickly moving into the mainstream. To see this, you need look no further than the recent letter sent by BlackRock CEO Larry Fink to the CEOs of the S&P 500. BlackRock is the world's largest investor. So it's news when its leader calls for longer-term thinking in American companies. In the letter, Fink uses the word "capital" and the phrase "value creation" multiple times and calls for sustainable thinking (emphasis added):

> *We continue to urge companies to adopt **balanced capital plans**, appropriate for their respective industries, that support strategies for **long-term growth**….Generating **sustainable** returns over time requires a sharper focus not only on governance, but also on **environmental and social** factors facing companies today. These issues offer both risks and opportunities, but for too long, companies have not considered them core to their business – even when the world's political leaders are increasingly focused on them, as demonstrated by the Paris Climate Accord. Over the long-term, environmental, social and governance (ESG) issues – ranging from climate change to diversity to board effectiveness – have **real and quantifiable financial impacts**.*

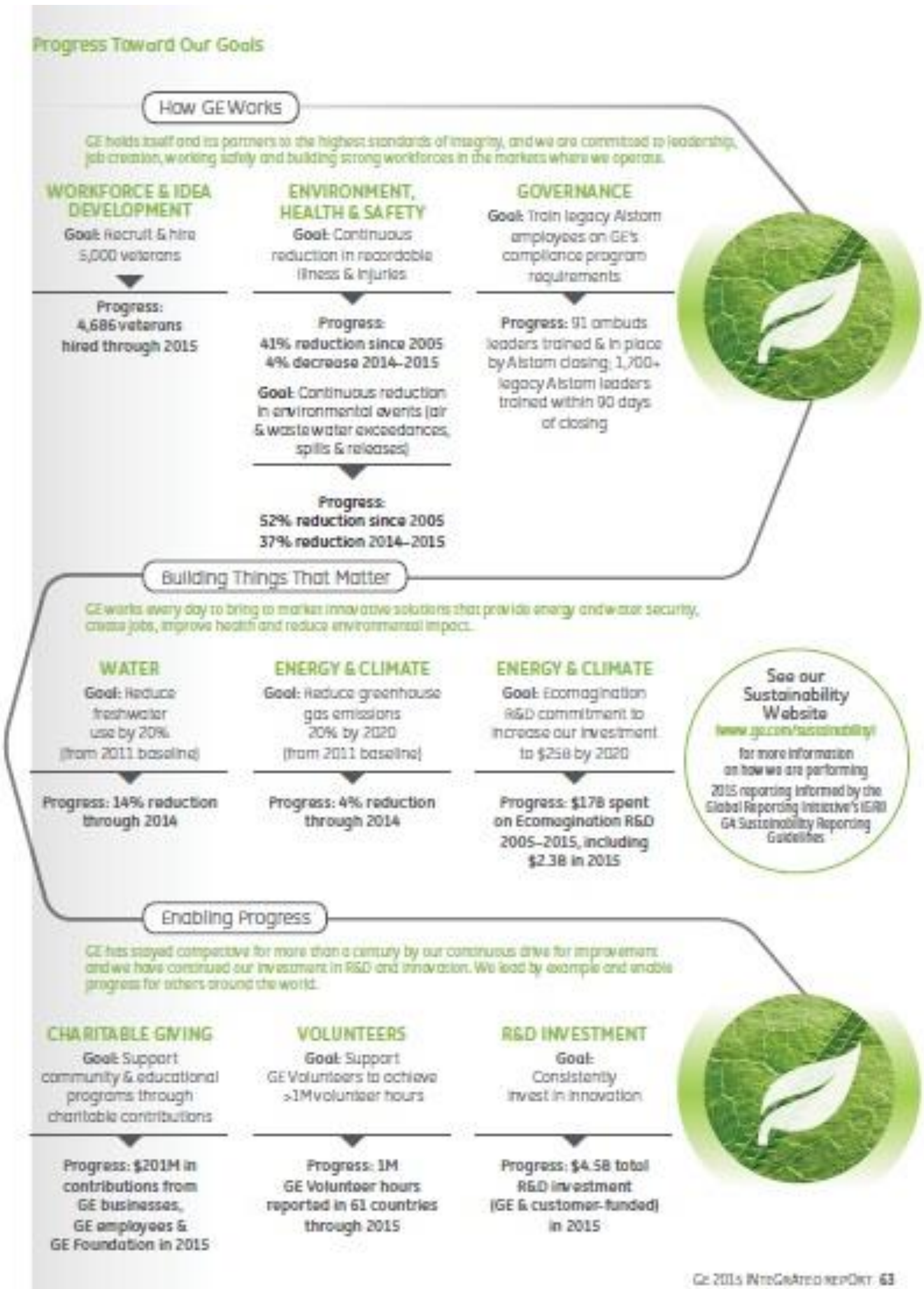
This letter reads as a call for use of the integrated model for both management and reporting purposes.

## General Electric

GE is a company famed for its hard-nosed management practices. So it's significant that they issued their first integrated report to shareholders for fiscal 2015. A statement from CEO Jeff Immelt explained,

> *Over the past several years, we have already been enhancing our reporting in response to feedback from investors, and they have told us how much they like it. This year, we are taking it even further.*

They called it an Integrated Summary Report. It's actually a completely new report that is positioned as a synthesis of the annual, proxy and sustainability reports. The 68-page summary report "shows investors GE through the lens of management," is highly strategic but still highly financial in focus. Nevertheless, it does include a section on sustainability at the end including the graphic summary seen here that includes measures related to human, natural and relationship capitals.



## Southwest Airlines

Southwest has been issuing an integrated report since 2010. The inspiration for their approach was the book *One Report* by Bob Eccles and Mike Krzus. The 2014 Southwest One Report is organized around a variant of the Triple-Bottom Line approach, highlighting Performance, People and Planet. Their report includes a summary table at the front of each of these three sections, each including multiple metrics that they have tracked over the course of five years. This table excerpt illustrates the key customer metrics that are included in the People section.

| Customers | 2014 | 2013 | 2012 | 2011 | 2010 |
|---|---|---|---|---|---|
| External Customer commendations | More than 75,000 | Nearly 70,000 | Nearly 65,000 | More than 65,000 | More than 65,000 |
| Ratio of external Customer commendations to personnel rudeness complaints | 4:1 | Nearly 5:1 | Nearly 7:1 | Nearly 8:1 | Nearly 10:1 |
| American Customer Satisfaction Index (ACSI) | 78 | 81 | 77 | 81 | 79 |
| U.S. Department of Transportation (DOT) Customer Satisfaction rating (consumer complaints per 100,000 enplanements) | 0.50 | 0.34 | 0.25 | 0.32 | 0.27 |
| Percentage of reported flight operations arriving ontime | 73.0 | 76.7 | 83.1 | 81.3 | 79.5 |
| Number of mishandled bags reported per 1,000 Passengers | 4.06 | 3.72 | 3.08 | 3.65 | 3.47 |
| Passengers denied boarding per 10,000 Passengers | 1.03 | 1.06 | 0.84 | 0.65 | 1.24 |
| Number of incidents involving the loss, injury, or death of animals during transport | 0 | 0 | 0 | 0 | 0 |

## DBS

The 2015 Integrated Report by DBS, a Singapore-based bank is a single report that replaces their annual, proxy and sustainability reports. It includes a 20-page Overview section that synthesizes a highly-graphical, full integrated view. This was their first year to fully implement the IIRC guidelines (something neither GE nor Southwest has yet done).

The graphic below is an excerpt from the table in the Overview section which presents specific metrics for the following resource groups: Brand, Capital, Funding, Employees, Customer Relationships, Technology, Society, Physical Infrastructure and Natural Resources. The example here addresses technology, something that neither Southwest nor GE includes in their report in a specific way.

The summary includes prior year metrics on the left and the current year on the right to show value creation. This resources table is followed by another graphical summary of the distribution of both financial and non-financial value. The approach is a direct nod to the IIRC capital-in and capital-out graphic.

| Resources | | 2014[2] | How we manage our resources | 2015[2] |
|---|---|---|---|---|
| **Technology**<br>The IT hardware and software that support our regional operations | Cumulative expenditure in IT – rolling 5 years[6] | SGD 4.1 bn | Our investments in technology ensure our IT platforms support our growing franchise in a resilient manner. Over the years, our spending has shifted from strengthening the core IT infrastructure to building up our digital channels to enhance the customer experience. | SGD 4.6 bn |
| | *Of which relating to specific IT initiatives*[7] | SGD 1.6 bn | As we pursue this, we are using modern cloud-scaled technology to componentise and automate our deliveries. This has dramatically reduced the time to market – from the time an idea is first developed until the technology is in the hands of our customers. | SGD 1.7 bn |
| | Number of CBG/ Wealth Management customers using<br>– internet platform<br>– mobile platform | <br><br>> 2.7 m<br>> 1 m | *Refer to "Customers" on page 28.* | <br><br>> 2.9 m<br>> 1.3 m |
| | Number of IBG customers using DBS IDEAL™[8] | > 137,000 | | > 150,000 |

## Start Your Company's Journey

These examples of the emerging practice of integrated reporting illustrate the three big ideas behind the model: recognition of multiple forms of value creation using multiple forms of capital over multiple time periods. Each company is at a different stage on its own journey to apply these ideas in their reporting. GE took a first step for 2015. DBS has been at it for several years and for 2015 started showing two years of data. Southwest has been at it since 2010 and showed five years of data in their 2014 report. When you see examples such as these, you realize that integrated thinking and reporting are not abstract concepts. They are a practical way of communicating the true drivers of revenue, profits, reputation and valuation. Modeling and measuring sustainable value creation is a great place to start on your company's journey toward integrated thinking and reporting.

*Smarter-Companies recently released a study of ten U.S. integrated reports*

Read The U.S. Integrated Reporting Journey

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