TRANSFORMING BUSINESS PRACTICE THROUGH IMPACT VALUATION

Imagine social, environmental, and governance (ESG) impacts were systematically integrated into every business decision, without the need for abstract sustainability narratives. Companies completely integrated sustainability into their corporate culture because sustainability is fully ingrained in their incentive systems. Investing in projects with negative stakeholder value is as undesirable as to invest in a venture that leads to a financial loss. Our decisions are holistic.

By Sonja Haut and Denise Weger

We would start to see ESG not as a cost factor but as a driver of growth, a chance to work on new products and business models that would be both profitable and serve society. At Novartis, we believe that achieving this form of stakeholder capitalism is not only feasible but necessary to solve the massive challenges our society is facing as described by the United Nation's Sustainable Development Goals. We believe that the concept of "Impact Valuation" will help get us there, and we therefore started to design a methodology.

What is Impact Valuation?

Impact Valuation is a new method to perform monetary assessments of the economic, ecological, and social impacts of business activities along the value chain. Historically, most of these impacts were considered "externalities", which had little or no consequences on how companies run their business. The main reason was that the costs of these "externalities" were taken up directly or indirectly by other stakeholders or the society at large. The most prominent example is CO_2 emissions. New regulations, growing stakeholder influence, and changing market dynamics are forcing businesses to internalize these "externalities".

Impact Valuation looks at impacts from very different fields (e.g., emissions, health, human capital) and converts them into a common unit. This way, they can be more easily compared, and trade-offs are made transparent and thus can be considered. This way, Impact Valuation helps quantify what previously seemed unquantifiable.

Monetization is a vital step to gain relevance

To lift the considerations of stakeholder impacts from niche conversations to the leadership and executive level, a monetization of economic, social and environmental impacts is necessary. Money is the language of business; translating impacts into monetary terms makes them compatible with existing management frameworks. Using money as a leveling language enables people who are not experts in these various fields to engage with subject matter specialists and empowers leaders to get further guidance on how these impacts can be integrated into business steering and decision-making.

Impact Valuation at Novartis

At Novartis, we have been exploring Impact Valuation since 2015 on a project, country and corporate level. We have established calculation models that reflect economic, social, and environmental impacts of our most material issue are as along their impact pathways. Through these models, we capture our most relevant positive and negative externalities, whether they are caused intentionally or unintentionally. By mapping out our externalities' effects on the environment and on society (e.g. on human health), we derive valuation factors that determine the price, or value tag, of each impact factor. We apply this methodology for the direct impacts of our operations as well as for impacts of our entire value chain.

As an annual output, we report monetized impacts across all our established Impact Valuation indicators internally as well as on a consolidated level in our sustainability report (Novartis in Society).

Creating awareness

Despite our long experience, we still see significant challenges before Impact Valuation will be fully embedded in central business processes at Novartis. While we can already offer impact data for our most material issue areas, the model is not yet complete as many impact factors still need to be addressed. Where results are available, they are often based on valuation models that rely on macroeconomic data. In addition, international standards and commonly accepted definitions are missing. Our approach to Impact Valuation therefore requires explanation, and we need to train work colleagues as well as external stakeholders such as investors to use it. The data would be more accepted and more comparable between different companies if it were based on internationally recognized standards rather than a proprietary solution.

Creating an international standard

To support the global standardization of Impact Valuation, Novartis co-founded the Value Balancing Alliance in collaboration with seven other multinational organizations as well as the support of the "Big Four" accounting firms. The Value Balancing Alliance is mandated to identify a common method for assessing and monetizing a corporation's total impact in a manner that is scalable and applicable to companies of any size. To do so, the alliance collaborates with experts from accounting, finance, and sustainability as well as subject matter experts from the different impact areas. It aims to initiate a dialog and public discourse on methods, critical assumptions, the required micro- and macroeconomic data, as well as the correct positive or negative valuation factor for each of the different impacts.

Get involved

A first draft of the Value Balancing Alliance's work – a standardized framework – will be presented this year. We are convinced that the alliance will inspire more and more companies to pilot and implement Impact Valuation and report their results. We believe it is time for the corporate sector to step up and take responsibility in contributing to solving society's challenges – Impact Valuation is a step in the right direction.

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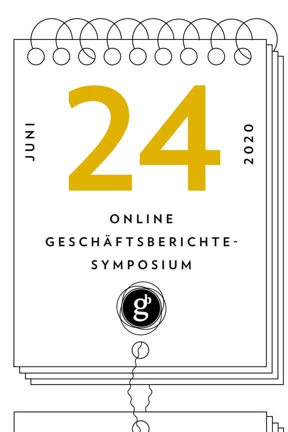
DENISE WEGER
joined Novartis in 2012. In Global Health and Corporate Responsibility she leads the company's Materiality Assessment at corporate and country level. In her role as Senior Manager she supports the Strategic Measurement and Materiality Team in various other strategic initiatives such as Novartis' Impact Valuation efforts. Denise Weger formally represents Novartis at the Value Balancing Alliance to standardize Impact Valuation internationally.



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Give externalities a financial value
The success of a business is no longer defined by its bottom line alone, but includes value created for a variety of stakeholders. As a consequence, additional information which is nonfinancial by nature, is required to describe and understand business performance. This is the ambition of the newly formed "Value Balancing Alliance", co-founded by Novartis and SAP who present their case studies.