



One Report: Better Strategy through Integrated Reporting

Q&A with: Robert G. Eccles and Michael P. Krzus

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Author: Martha Lagace

How can managers better identify, describe, and confront the issues of environmental and social sustainability that their companies increasingly encounter? One answer is One Report, a method of integrating information about financial and nonfinancial performance into a single, jargon-free document.

There are two main reasons to use One Report, according to its originators, Robert G. Eccles and Michael P. Krzus: First, such integration allows companies a clear view of risks to and opportunities in their own strategy. Second, One Report speaks with one voice to all stakeholders, who can even engage with the company via Web 2.0 tools and technologies. One Report is thus an essential element of demonstrating and building transparency and trust.

Why is One Report important now?

"The capital markets and our planet have simultaneously reached a fork in the road. One path continues the status quo. The other and new path is a commitment to a better society, stronger financial markets, and a healthier environment," say Eccles, a senior lecturer at HBS specializing in corporate reporting, and Krzus, a public policy and external affairs partner with Grant Thornton LLP. They recently authored *One Report: Integrated Reporting for a Sustainable Strategy*.

"This new path isn't easy," they continue. "We are trying to solve a collective action problem where many actors must collaborate together, including companies, investors, accounting firms, sell-side analysts, regulators and standard setters, and NGOs and civil society itself. We all have a responsibility for making integrated reporting the dominant practice."

In an e-mail interview, they explain why company adoption of integrated reporting is essential for sustainable strategies and society.

Martha Lagace: How do you define One Report?

Robert G. Eccles and Michael P. Krzus: One Report is the integration of information about financial and nonfinancial performance in a single document. By "nonfinancial" we mean the kind of information that is typically provided in a company's corporate social responsibility or sustainability report regarding its performance in environmental, social, and governance terms.

But One Report doesn't mean "only One Report," since a company can use the Internet to provide more detailed information of interest to specific stakeholders. Through Web 2.0 tools and technologies, a company can engage with all stakeholders in a meaningful dialogue that includes listening as well as simply reporting or talking. By listening, the company learns about the needs

and expectations of all stakeholders, how well it is meeting those needs and expectations, and what information will be most useful in reporting on this.

Q: What is deficient about current reports?

A: The King Code of Governance for South Africa 2009 [PDF] describes the problem in a way that is applicable to every listed company in the world:

"The market capitalisation of any company listed on the [Johannesburg Stock Exchange] equals its economic value and not its book value. The financial report of a company, as seen in its balance sheet and profit and loss statement, is a photograph of a moment in time of its financial position. In buying a share on any stock exchange, the purchaser makes an assessment of the economic value of a company. The assessment considers the value of matters not accounted for, such as future earnings, brand, goodwill, the quality of its board and management, reputation, strategy and other sustainability aspects. The informed investor assesses the quality of the company's risk management and whether it has considered the sustainability issues pertinent to its business."

Q: What are the benefits of more integrated reporting?

A: We see four primary benefits to companies:

1. Greater clarity about the relationship between financial and nonfinancial key performance indicators. This will help managers understand and confront the trade-offs necessary to balance financial and societal demands.
2. Better management decisions. As noted by the creators of the Balanced Scorecard, HBS professor Robert S. Kaplan and David P. Norton, there is compelling evidence that better measurement, and therefore better information, leads to better decision-making.
3. Deeper engagement with the broad stakeholder community. First, it will help shareholders focus on more than short-term returns and better understand the investments necessary to ensure long-term viability. Second, other stakeholders will begin to appreciate the need for a company to make a profit if it is to create value over the long term.
4. Lower reputational risk resulting from integrated reporting. Stakeholder engagement leads to better mutual understanding. Clear and consistent communications about a company's financial and nonfinancial performance will be the basis for a constructive two-way conversation.

Q: What challenges do managers face by encouraging more transparency?

A: Transparency is not the challenge. Globalization, the Internet, and instant communications combine to subject every corporate action to scrutiny whether the company communicates or not. This reality puts every company's reputation and brand at risk. The challenge is whether every corporate CEO has the courage of his or her convictions to accept their intergenerational responsibility for the quality of life in our society and at the same time deliver long-term profitability.

Q: What company or companies are leaders in conducting and communicating integrated reporting, and why?

A: The Dutch health-care and electronics company Philips; the Danish pharmaceutical company Novo Nordisk; the Brazilian cosmetics company Natura; and the U.S.-based technology and aerospace company United Technologies all come to mind. All have done a very good job of demonstrating and explaining the relationship between financial and nonfinancial performance. Perhaps more importantly, all have created robust Web sites to provide stakeholders with additional information not included in their printed reports. And all are deeply engaged in an ongoing dialogue with their stakeholders.

Q: How should companies take the first steps to adopt integrated reporting?

A: The experience of the German chemical company BASF provides an excellent model to follow.

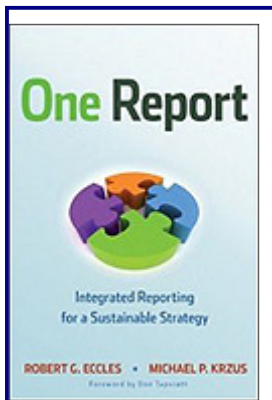
1. Understand stakeholder information needs—that is, answer the questions, What information do stakeholders need? What information do companies provide that stakeholders do not use?
2. Based on dialogue with all stakeholders, create an information gap analysis, develop and implement necessary methodologies for creating missing content, and consult with the board to determine an "optimal level of transparency."

The foregoing two steps will identify what needs to be done to align the organization to support One Report in terms of measurement methodologies, processes, policies, structure, compensation, internal reporting, and external reporting.

Excerpt from **One Report: Integrated Reporting for a Sustainable Strategy**

By Robert G. Eccles and Michael P. Krzus

The Case for One Report



There are two main reasons why companies should adopt One Report in their external reporting. The first is that it is a key element of taking sustainability seriously, once the company has created a truly sustainable strategy, by responding to the risks and opportunities created by the need to ensure a sustainable society. The second reason is that the simplification from One Report's single message to all stakeholders is a key element of improving corporate disclosure and transparency. Philips cited both of these reasons in its explanation for why it decided to produce a single, integrated report for 2008.

Of course, One Report is not a panacea or silver bullet solution to making sustainability more than a public relations campaign or resolving the complex issues regarding improving corporate disclosure for all stakeholders. Really taking sustainability seriously requires understanding the risks and opportunities created by environmental and social issues and trends and responding to both in a meaningful way. When and where a sincere commitment to sustainability and transparent disclosure exist, an integrated report becomes a cornerstone to improving both, since it provides a point of focus and discipline.

Some simple and pragmatic guidelines can be used to make the company's reporting as useful as possible to all stakeholders. By simplifying the language and avoiding the use of jargon or "legalese," the narratives in One Report are made more accessible to a broad spectrum of readers. Quantitative information in tables that stand out and use of color ensure that the key points of the data are clear and also helpful.⁷ Easily navigable corporate Web sites make it easy to find information online, as do internal and external links to related information. By leveraging the spatial qualities of the Internet with drill-down capabilities in which summary data are provided, the company enables the user to get more detailed data one or two levels down. Data presented in an XBRL format make it easy to download and analyze.

It is certainly true that a company can be clearly committed to sustainability without producing One Report. Ricoh is a good example of this. Sustainability is at the core of the company's strategy and how it is managed, yet Ricoh produced three external reports: annual, environmental sustainability, and corporate social responsibility. It is also true that a company can be committed to as earnest disclosure and transparent reporting as possible without being committed to sustainability. In this case, the company would have a classic shareholder-only financial focus and would be striving to do the best job possible in reporting and explaining its financial results.

But *if* a company is truly committed to sustainability (a claim being made by more and more companies) and if a company is truly committed to as transparent reporting as possible (another claim being made by more and more companies), then the case for One Report is a compelling one. The assertion "What gets measured gets managed" applies here. Just as the Balanced Scorecard provides for better internal management and implementation of strategy by focusing on both financial results and the factors that produce them, One Report adds the discipline that comes from external reporting to the discipline that comes from internal reporting. Reporting on both financial and nonfinancial performance to all stakeholders strengthens management's desire to show good results, particularly if financial and other incentives are tied to these results and commitments are in terms of future goals and targets. This was the case at Natura and UTC; both companies were candid about whether or not past targets had been achieved.

Practicing integrated reporting brings four major benefits to the company. First, it provides greater clarity about relationships and commitments. Second, it leads to better decisions. Third, it deepens engagement with all stakeholders. Fourth, it lowers reputational risk. Taken together, these benefits make the development, implementation, and reporting of a sustainable strategy for a sustainable society mutually reinforcing processes. We discuss each of these benefits in turn next.

Greater Clarity about Relationships and Commitments

It is easy for a company to make the sweeping statement "We believe that sustainability is good for our shareholders" or "By pursuing sound environmental, social, and governance policies we are creating value for our shareholders, all other stakeholders, and society at large." Of course, sustainable strategies are not that easy. Investments to improve energy efficiency and reduce carbon emissions can have a positive return on investment but hurt earnings and cash flow in the short term. Some commitments may actually result in a wealth transfer from shareholders to another stakeholder group, such as paying a "living wage" that is above market labor rates—although this can ultimately benefit shareholders by attracting customers who support this. A sustainable strategy with a multi-stakeholder perspective means that sometimes trade-offs must be made. As Joshua Margolis and James Walsh point out, "Managers face a vexing reality. They must find a way to do their work even as seemingly financial and society demands intensify."⁸ Rather than ignoring them or pretending that they do not exist, managers need to directly confront these trade-offs and be clear on the choices they've made and why—recognizing that some stakeholder group will inevitably be disappointed in the decision.

One Report begins with identifying the most important financial and ESG metrics for the company in its given industry and the strategy it is pursuing to achieve its goals. In some cases, revenue growth may be critical; in others, earnings growth is more important. In some cases, reducing carbon emissions may be the most important environmental objective, and in others it may be reducing the amount of water used. Racial and gender diversity can be a priority, but so too is ensuring some minimal amount of training for all employees every year.

The real essence of One Report is in describing what management believes the relationships between these key financial and nonfinancial metrics to be. Most companies have a great deal of work to do in this area. A 2008 KPMG CSR survey found that "Only a minority 16 percent of G250 companies quantified the value of corporate responsibility performance specifically for their analyst and investor stakeholders," an issue that needs to be addressed in order to convince mainstream investors of the company's sustainable strategy.⁹ Quantifying the value of CSR starts by answering the following questions: Which ESG topics represent opportunities to improve financial performance, such as through increased revenues for green products or decreased costs through greater energy efficiency? Which ESG topics represent risks and cause spending to protect against the downside in terms of the destruction of shareholder value? Which ESG topics are not risks, but the company is committed to making investments to create value for other stakeholders even if this is at a cost to shareholders? Obviously the dividing lines between these categories of risks, opportunities, and "other commitments" are not well defined. Over a

sufficiently long period of time, what looks like an "other commitment" might turn out to be value-enhancing for shareholders, particularly since the state of the world will change in unpredictable ways. One Report gives management the opportunity to clarify the dividing line and explain how other commitments have become value-enhancing activities.

As management develops a better understanding of the relationships between financial and nonfinancial performance through modeling and analysis, improving internal systems and measurement methodologies as necessary, it can re-evaluate what is included in its categories of risks, opportunities, and choices. One Report challenges management to be much more granular about how they are "doing well (for shareholders) by doing good (for stakeholders)." It challenges them to be as explicit as possible in a cause-and-effect sense of how good outcomes on a particular aspect of ESG lead to good outcomes on a particular financial metric. Ideally, the lag times and functionality (e.g., linear, asymptotic, or exponential) will also be specified, although data limitations typically make this very hard to do. Many ESG metrics are still being developed and have not been in place for most companies long enough to explore time-series relationships; we envision that this will change over time. As it does, the capability of companies to develop and implement sustainable strategies for a sustainable society will improve.

Better Decisions

As management attempts to be as explicit as possible about the relationships between financial and nonfinancial outcomes, it inevitably finds that for some, good metrics do not exist, and for others, they are very hard to develop. This can be an excuse for not doing the hard analytical work necessary to specify and validate the relationships that are believed to exist. The better response is to improve poor measurement methodologies and invent new ones for useful metrics that do not yet exist. The result will be better information for better decisions.

In some cases, better information comes from simply combining data that already exist in the firm but are spread across different parts of the company. Some metrics, such as customer satisfaction (like the Net Promoter Score used by Allianz), require going outside the company's boundaries to gather the necessary data. Different measurement methodologies will need to be used, including aggregating data from transactions (e.g., number of calls from whistleblowers), measurement of physical processes (e.g., carbon emissions), and surveys (e.g., of customer and employee satisfaction).

Kaplan and Norton's voluminous body of work on the Balanced Scorecard provides compelling arguments and evidence for how better measurement leads to better management decisions. When information is reported externally, the standards for its reliability are especially high. The higher quality metrics required for external reporting provide higher-quality internal information and this results in higher quality decisions. The external transparency of the results of these decisions adds an additional incentive for making them good ones.

Developing greater clarity about the relationships between financial and nonfinancial information, developing the supporting metrics to test and validate these relationships, and then pulling all of this performance information together in One Report requires a high level of internal collaboration across functions and business units. As each unit sees its role in a broader context and begins to better understand the consequences of its decisions on other units, better decisions that craft and reinforce a sustainable strategy will be made for the company as a whole.

Deeper Engagement with All Stakeholders

As companies realize the benefits of better decisions from higher levels of internal collaboration, they will naturally seek to obtain these same benefits from higher levels of external collaboration through stakeholder engagement in order to better understand their expectations, obviously useful for internal decision making. The 2008 KPMG survey found that "understanding key stakeholder

expectations" was the most important reason cited for stakeholder engagement by 59 percent of the respondents.¹⁰ External stakeholders can provide useful input to the decision-making process. Initially, collaboration will be between individual internal units and their external counterparts, but eventually this collaboration will become cross-functional and cross-stakeholder in nature.

The implicit theory behind having annual reports that focus on financial performance and separate CSR reports that focus on nonfinancial performance is that these reports are audience-specific and meet each reader's information needs. However, in our world, where companies are facing the demands of many stakeholders, it is essential that every stakeholder understands how its interests are related to those of others and to the factors that contribute to the level of performance that is being met. A single-issue focus by a stakeholder is as irresponsible as a company's singular focus on short-term profits for shareholders. Just as companies must take a more integrated approach to their external reporting, stakeholders must take a more integrated view about how their interests are related to others' interests.

One Report eliminates the artificial and unhelpful analytical distinction between shareholders and stakeholders. The former are simply one particular type of stakeholder, and all stakeholders have convergent and competing interests to varying degrees. We disagree with the argument that a separate CSR report "empowers" other stakeholders by treating them as a separate and distinct audience deserving of its own report. Instead, it marginalizes them by putting this information in a separate report from the official document that must be audited and filed with the appropriate regulatory agency.

A separate CSR report also marginalizes the importance of nonfinancial information to shareholders. While Socially Responsible Investment (SRI) funds pay some attention to them, primarily for screening rather than resource allocation purposes, most investors find the reports unhelpful because they contain little in the way of information useful for investment decisions. Ricoh is a case in point.

Putting all performance information into One Report in an integrated way challenges all stakeholders to take a more holistic perspective. Shareholders cannot just focus on short-term profits; they need to understand that a company's ability to earn profits over the long term will require investments that come at a short-term cost, or even value transfers that preserve its legitimacy and continued existence in order to earn profits in the future. Conversely, other stakeholders need to understand that companies need to make a profit in order to survive and grow. Failure to do so means that eventually they will not be able to fulfill the needs of other stakeholders or may even fail to survive.

Additionally, One Report ensures that a coherent and consistent message is going out to all stakeholders. It creates the platform for one conversation in which all stakeholders can and must participate. While it is natural for particular stakeholders to want to engage with their corporate counterparts due to a common issue focus—such as environmental groups with environment, health, and safety; consumer interest groups with product development and marketing; and community groups with human resources—it runs the risk of creating "splinter groups" or factions along issue lines that make it difficult for the company to communicate and act in a coherent way. The result is often mixed messages to external parties and internal confusion about priorities.

Engagement is not easy. It takes time and effort. It requires listening as well as talking. But it is through engagement that companies remain aware of the interests of their different stakeholders and how these interests are in alignment or conflict with each other. A great deal of engagement is already taking place today in many companies, initiated both by them and by their various stakeholders. Examples include the kind of engagement that comes from active investors—such as on issues of corporate governance, executive compensation, and climate change—and from NGOs—such as on human rights and climate change. Engagement provides the basis for an ongoing dialogue between the company and its stakeholders. The company should also encourage


engagement and dialogue among the various stakeholders to help create a single collective conversation rather than many separate and disjointed ones about society's expectations for the company.

Lower Reputational Risk

Not surprisingly, as corporate social responsibility and sustainability have increased in importance, so has managing reputational risk, which is now seen as one of the most important and difficult risks to manage. A survey of senior executives by The Economist Intelligence Unit found that, as a priority, reputational risk ranked first and distinctly ahead of regulatory risk and human capital risks, which tied for second. It also found that the key reasons cited for difficulties in managing reputational risk were the lack of established tools and techniques; no identified person with responsibility for the issue; poor coordination between the board, risk management, and corporate communications; and poor communications with external stakeholders.¹¹ All of these difficulties can be overcome by the process and communication that necessarily go hand-in-hand with CSR reporting. Leslie Gaines-Ross, Chief Reputation Strategist of Weber Shandwick, commented that "In today's multi-stakeholder and multi-channel society, CEOs are increasingly concerned about reputational risk, both for their company and themselves. Now is the time for CEOs to carefully explain their companies to stakeholders, engage in productive two-way conversations, and clearly communicate their contributions to the market and society. If stakeholders are left on their own to unify all the information they need about an enterprise, companies could find themselves vulnerable to misinformation and hearsay and put their reputations at risk."¹²

Robert G. Eccles, Scott C. Newquist, and Roland Schatz cited three major determinants of reputational risk: a reputation/reality gap (the company's external reputation is greater than its ability to consistently meet expectations through actual performance), changing beliefs and expectations (actions considered acceptable become unacceptable as social norms and values change), and weak internal coordination (actions by one group create expectations that another group cannot meet). To manage reputational risk, they cite three corresponding actions¹³ and for each of them One Report can play a meaningful role. First, to address the reputation/reality gap, the company needs to objectively assess reputation and reality. An integrated view of the company's financial and nonfinancial performance, provided by One Report, will help identify areas at risk, since it will make clearer the areas where a company's reputation is based on overlapping performance outcomes.

Second is the need to assess and accept the impact of changing beliefs and expectations. These can happen suddenly (such as a major accident that is a catalyst for new safety standards) or emerge more slowly over a long period of time (such as the gradual crescendo of concern about carbon emissions over the past few decades). Through constant monitoring of trends, social attitudes, and the media, the company can improve its awareness of how social norms and values are changing. Through the deeper engagement process, One Report facilitates a dialogue that can identify new themes and concerns across more than one stakeholder group, helping the company become more aware of early-stage changes in expectations that will become more widely held and supported.

Finally, the solution to weak internal coordination is to put a well-defined process in place that includes all of the groups (e.g., investor relations; public relations; corporate communications; marketing; environment, health, and safety (EH&S); operations; and risk management) whose input is necessary for managing reputational risk. One person needs to be explicitly put in charge of this process to ensure that it works in a collaborative, cross-functional fashion. Similarly, producing One Report requires an integrated process that involves all of these groups and the same degree of collaboration. Given the close relationship between integrated reporting and managing reputational risk, these processes should be coordinated to avoid redundancies and confusion. 

Footnotes:

7. For more on the visual representation of data and information, see: Tufte, Edward R. *The Visual Display of Quantitative Information*. Cheshire, CT: Graphics Press, 1983; *Envisioning Information*. Cheshire, CT: Graphics Press, 1990; *Visual Explanations: Images and Quantities, Evidence and Narrative*. Cheshire, CT: Graphics Press, 1997; and *Beautiful Evidence*. Cheshire, CT: Graphics Press, 2006.
8. Margolis, Joshua D. and Walsh, James P. "Misery Loves Companies: Rethinking Social Initiatives by Business," *Administrative Science Quarterly*, v. 48, is. 2, 2003: 268-305, p. 296.
9. KPMG. *International Survey of Corporate Responsibility Reporting 2008*, p. 31.
10. *Ibid.*, p. 31.
11. The Economist Intelligence Unit. *Reputation: Risk of Risks*, white paper, December 2005, p. 5, 22.
12. Leslie Gaines-Ross, e-mail correspondence with Robert Eccles, September 22, 2009.
13. Eccles, Robert G., Newquist, Scott C., and Schatz, Roland. "Reputation and Its Risks." *Harvard Business Review*, v. 85, is. 2, 2007, pp. 104-114.

About the author

Martha Lagace is the senior editor of *HBS Working Knowledge*.

[Integrated Reporting.org](http://integratedreporting.org)

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