

# Corporate Sustainability

Creating long term value for  
Japanese companies



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# Introduction

PwC has published reports on corporate sustainability since July 2016, making this report the third publication on this theme. In these reports, we advocate the importance of moving on from CSR to corporate sustainability. But how far have Japanese companies actually come in the move from CSR towards corporate sustainability?

In order to achieve the Sustainable Development Goals (SDGs) that were adopted in September 2015, not only are the efforts of each national government important, but so too is the active participation of private companies. Furthermore, the Japanese Business Federation has proposed the initiative “Society 5.0” which is the fifth evolutionary step of human society within the different stages of societal development. Society 5.0 advocates for the widespread implementation of cutting-edge technology to bring about both economic development, as well as solve societal issues, and thus achieve the SDGs. Encouragingly, private sector businesses in Japan are actively adopting initiatives and seeking to contribute to solving societal problems in the mid- to long-term. We can also see that Japanese companies are shifting their approach to long-term issues from conventional CSR to Corporate Sustainability. Since the Japanese Government Pension Fund signed up to the UN Principles for Responsible Investment (UNPRI), ESG investment in Japan has been growing rapidly. This change in behaviour from investors also supports companies greatly in their efforts on sustainability.

To shed light on the progress of the move to corporate sustainability, PwC conducted a survey of employees of listed companies. Whilst gaining a grasp of their awareness of CSR and corporate sustainability, we examined the changes in trends over the past few years as well as differences within industries, by comparing with similar surveys conducted in the past.

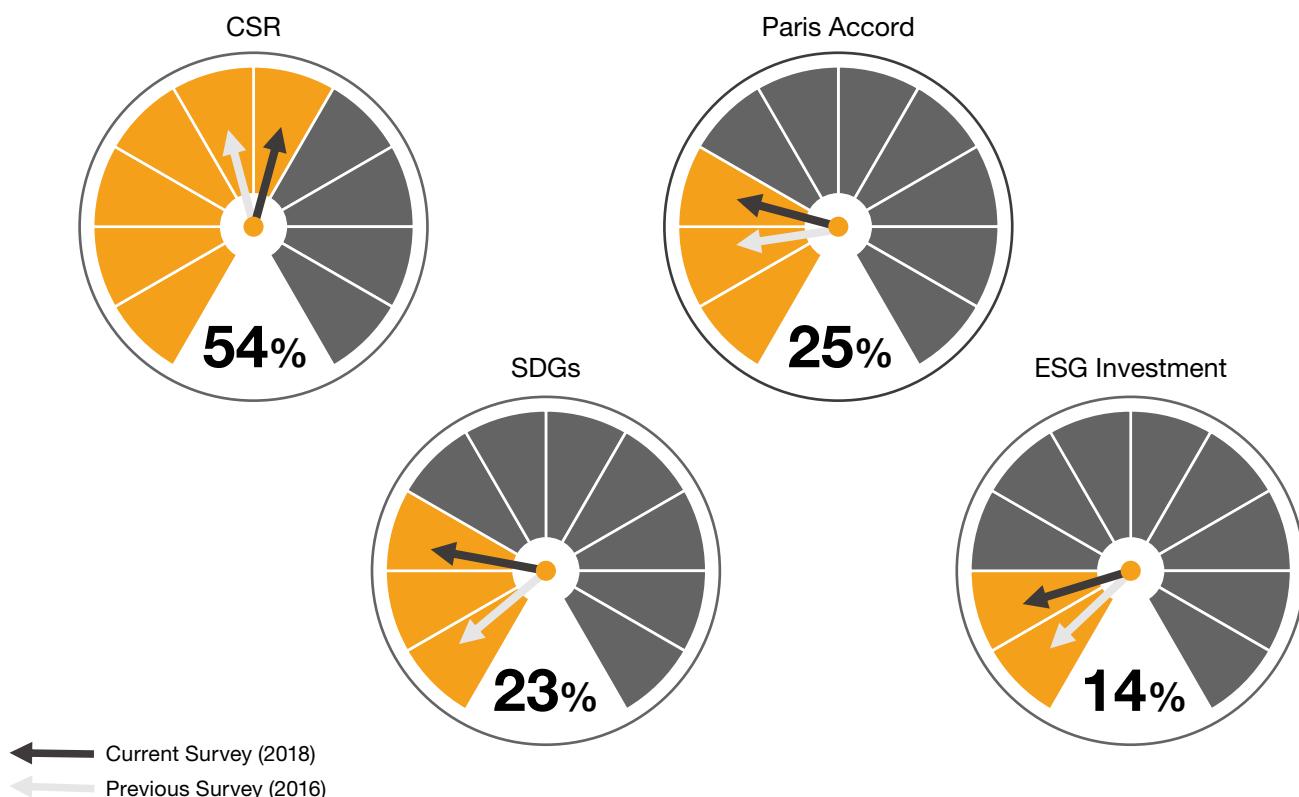
PwC believes that corporate sustainability will require assessing mid- to long-term societal changes (megatrends), devising strategies, taking action, measuring performance, conveying results, providing feedback, making improvements and implementing reforms. As society changes in the long-term, global firms are being required to adopt a corporate sustainability approach. We hope that this report will support the implementation of corporate sustainability, and at the same time, we would like to once again, express our gratitude to those who responded to the survey which enabled us to prepare this report.

# A snapshot of corporate sustainability

## The Level of Awareness of Corporate Sustainability

The awareness of sustainability-related matters has increased over the past two years. In particular, there has been a significant increase in awareness of the Sustainable Development Goals.

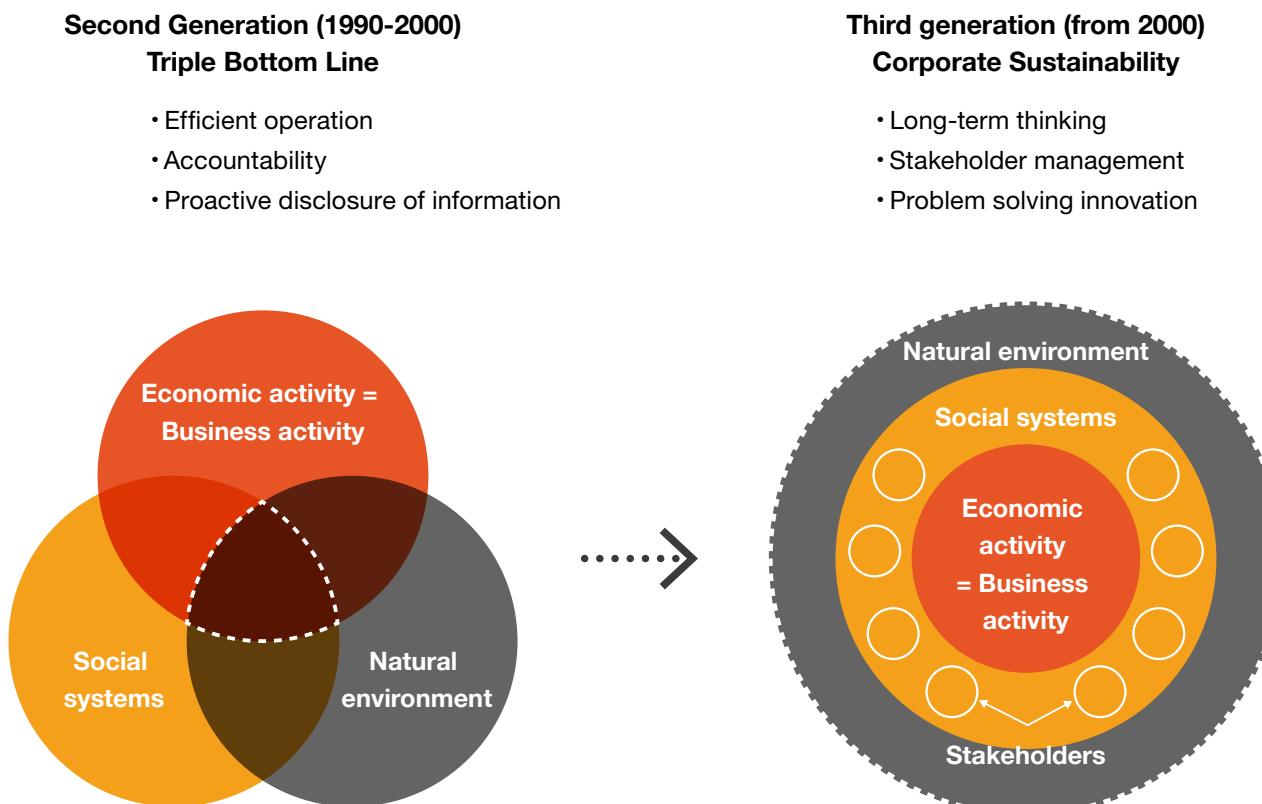
**The share of respondents from selected listed companies who answered,  
“I know enough about the topic to explain it to someone else”**





## What is Sustainability to Japanese Companies?

For Japanese companies, sustainability means a focus on strengthening corporate governance and the environmental impacts of operations. Many Japanese companies are in the process of shifting to third generation corporate sustainability from the second-generation Triple Bottom Line CSR concept.



The dotted line represents the area considered to be CSR/Sustainability by companies.

# Chapter 1

## –Megatrends facing Japanese Companies

### 1.1 What are Megatrends?

Megatrends are social and economic shifts, which have the power to re-shape the world, as we know it. This way of thinking about megatrends itself is not new. Even if the term “Megatrend” is not currently used very frequently, the majority of companies have, for some time and in some way and shape, developed strategies to respond to major contemporary trends. Purpose-driven companies pay attention to megatrends, because they seek to remain relevant in the long term. So what megatrends are companies facing, and what influence will these megatrends have on them?

### 1.2 Five Megatrends and their potential impact

As an example, the makeup of the human population will continue to change drastically with the support of advancements in medical technology. As a result, the way people work and the essential makeup of societies too will change. Backed by population growth, production and consumption will continue to increase in developing countries, and global economic power will continue to shift away from western economies. Expansion in production and consumption will no doubt lead to a situation where we must fundamentally reexamine our lifestyles, as we rely on finite fossil fuels and natural resources. Could the innovative technology that we are developing provide the solution? Below we will examine the 5 megatrends that PwC has identified and their underlying impacts on companies.

#### Megatrends:

American Futurologist, John Naisbitt proposed the concept of Megatrends in his 1982 book, titled, “Megatrends”. At PwC, we perceive Megatrends as “macroeconomic and social forces that are shaping our world, and our collective futures in profound ways.” We recognize megatrends based on our understanding of reality, and often have the backing of evidential data.

Figure 1-1: Five Megatrends



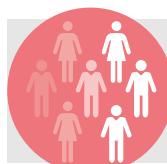
#### Rapid Urbanisation

The urban population in Asia and Africa is growing. Migration from rural to urban areas is accelerating this.



#### Climate Change and Natural Resource Scarcity

Due to extreme weather and rising sea levels, traditional agricultural, fishing, and hunting methods are becoming unfeasible.



#### Demographic and Social Change

Due to ageing populations in developed countries, and a lack of skilled human resources in developing countries, the supply of labour is becoming more globalized.



#### Shift in Global Economic Power

Following the growth and expansion of emerging markets, ties between many developing countries are deepening through trade and investment.



#### Technological Breakthroughs

Completely new fields of business are created, and the scale and composition of global manufacturing and high tech industries will drastically change.

Source: PwC

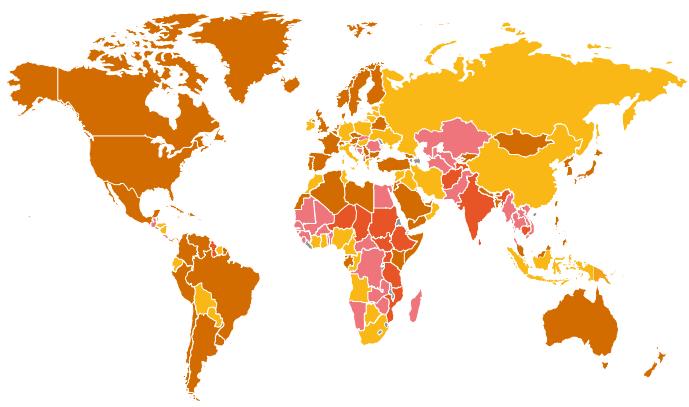
## Megatrend 1

### Rapid Urbanisation

In 2010, more than half of the global population lived in urban areas, and every week 1.5 million people move to urban areas. By 2020, it is estimated that 4.9 billion out of the 8.3 billion global population will live in cities. There are currently 22 megacities with populations of over 10 million people, with 17 of them being located in developing countries. These new cities emerging in developing countries must prepare infrastructure in order to accommodate their rapidly expanding populations.

In other words, large-scale megaprojects will become necessary for building urban infrastructure. These projects will require infrastructure to accommodate for the flow of goods, education, medical services, public security and the employment of people, which will create new business opportunities for companies. There are also many voters living in megacities, and so these cities have powers rivalling those of national governments. In other words, for companies involved in the development of these megaprojects, local municipalities will possibly be just as important stakeholders as national governments.

**Figure 1-2: The proportion of the population living in urban areas by 2030**



Over 80%   60-79%   40-59%   20-39%   Less than 20%   No information

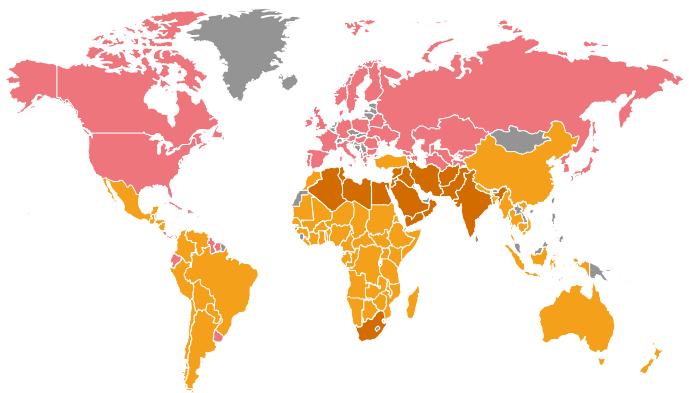
Source: United Nations Department of Economic and Social Affairs/Population Division, World Urbanization Prospects: The 2014 Revision

## Megatrend 2

### Climate Change and Resource Scarcity

As populations increase, energy demands are expected to increase by 50% compared to 2012, total water withdrawal will be 40% greater, and the demand for food will increase by 35%. Greenhouse gas emissions stemming from energy consumption will make extreme weather more frequent and cause a change in rainfall patterns. By 2050, it is predicted that there will be water shortages south of the 35th parallel, which will reduce Africa's food production productivity by a third in the coming 60 years. Confrontation over resources and political tension will increase due to a change in the allocation of food and water. Regulations in response to climate change are to be expected, as well as increased and strengthened indirect regulations, such as taxes, and incentives, which are sure to change the business environment. New production techniques will most likely be developed in response to energy and resource scarcity, and existing manufacturing systems will likely be reformed.

**Figure 1-3: Estimated water scarcity by 2025**



Physical Water Shortage   Economic Water shortage  
Possibility of Water Shortage, but probably not the case   No Data

Source: International Water Management Institute, World water demand and supply, 1990 to 2025: scenarios and issues

1 PwC analysis of United Nations, Department of Economic and Social Affairs, Population Division (2013)

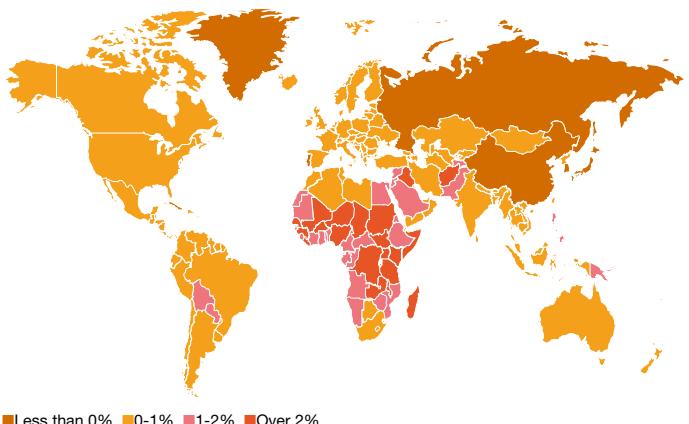
2 Intergovernmental Panel on Climate Change (2007)

3 UNEP/GRID – Arendal Maps and Graphics Library

### Megatrend 3 Demographic and Social Change

The global population will continue to grow, but the growth will not be uniform, and demographics, such as age, religion, and economic strength will continue to change. By 2025, the global population will reach 8 billion, of which 3 billion people will be aged over 65. Therefore, due to rapid population ageing, in some countries the share of the population of working age will decline. On the other hand, labour forces and consumer markets are emerging in developing countries on a scale never seen before. Young peoples' attitudes to work practices and family composition are also rapidly changing. In addition, economic disparity is widening, and going forward around 70% of the world's population will be living in countries where inequality is expected to increase. Creating employment in particular for elderly people and the poorest groups in society is becoming an increasingly pressing issue. Companies will be required to look for labour on a global level, and it will likely be necessary to strategically manage human resource development in order to both attract capable young workers, whilst also retaining older workers.

**Figure 1-4: Annual rate of population growth from 2010-2050 (average estimate)**

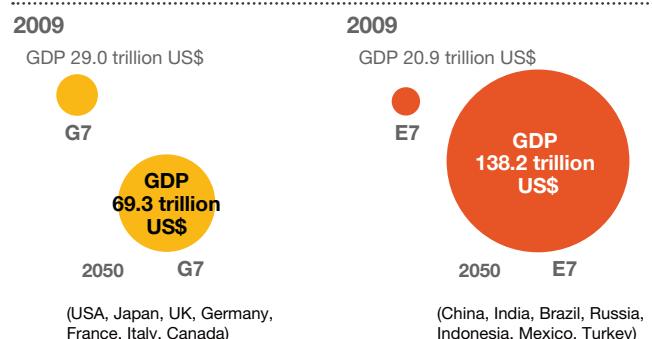


Source: Pew Research Center, The Future of World Religions: Population Growth Projections, 2010-2050

### Megatrend 4 Shift in Global Economic Power

The western dominance over the world economy is a relatively recent phenomenon, and the present shift in the centre of the global economy is considered as a kind of rebalancing of the overall world economy. Against this backdrop, in addition to the impact on the economic development of developing countries with rapid population growth, this shift will also have an impact on the proportion of the population that receives higher education. For example, it is estimated that the number of college graduates in the E7 (comprised of the seven major developing economies) will rise to a level three times that of the G7. The young people who receive higher education in developing countries will likely push for economic growth in their home countries. In addition, trade within the E7 is expanding at five times the speed of the G7, and so the presence of developed nations will likely continue to diminish. Europeans and Americans are likely in charge of a great majority of global firms, however the strength of regional and local players in the world will increase, and a shift to a multipolar world will likely continue. Mature industries will lose out in terms of influence and capital strength, and because their attractiveness to workers and business will grow weaker compared to what it used to be, firms will need to rethink their business strategies.

**Figure 1-5: G7 and E7 purchasing power (GDP) in US Dollar**



Source: PwC Analysis

4 UN Population Division, World Population Prospects, the 2015 Revision

5 PwC Next Gen: A Global Generational Study (2013)

6 PwC analysis based on OECD, UNESCO, the Chinese National Bureau of Statistics, NASSCOM (2010-2013)

7 PwC analysis based on data from UNCTAD (2013)

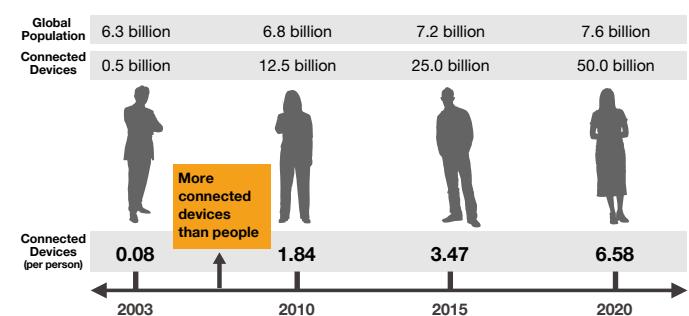
## Megatrend 5 Technological Breakthroughs

Technological innovation is accelerating. Innovation in Information Communications technology is taking place at a particularly exponential rate, with 90% of current technology having been developed in the last 2 years. Internet, mobile devices, data analytics, cloud computing, and artificial intelligence are all being integrated and will continue to change the world. In addition, we are seeing rapid advances in nanotechnology and energy technology. In response to these changes, firms in all industries must deal with issues such as changing consumer expectations, how to interact with customers and understanding what type of business models are best for operations in this current climate. Furthermore, given that systems and information will be more easily accessible, management models based on a flat organizational structure will become possible. Additionally, in project management, real-time data gathering and analysis will not provide a competitive edge; rather it will be an essential requirement.

Once more, let us reflect on the meanings of these 5 megatrends.

Population growth and rapid urbanization will inevitably bring about long-term growth in the real economy. However, whilst the shift in global economic power and population ageing in certain countries has created geopolitical dynamics not witnessed until now, it is also transforming the nature of production and consumption. Naturally, a prolonged increase in demand conceals the likelihood that it will dramatically worsen climate change and resource depletion. Given this situation, the importance of technology is evident. However, the likelihood that large 20th century companies of the developed world (including Japan) will be at the heart of the development and spread of technology decreases day by day. Through the economic policies and development of business and enterprises in the E7, and later with the emergence of other developing countries, the map of influence in the dynamics of market competition will be dramatically redrawn.

**Figure 1-6: The emergence of the Internet of Things**



Source: Cisco Internet Business Solutions Group, The Internet of Things: How the Next Evolution of the Internet Is Changing Everything April 2011

# Chapter 2

## – Corporate Sustainability

### 2.1. Sustainable Development and the Role of Companies

How must companies respond to the various issues brought about by these global megatrends? In order for companies to achieve sustained growth, the society in which companies exist, and the environment in which society exists, must be sustainable. So what does it mean for society and the environment to be sustainable? In addition, when striving towards realizing sustainability, how is the role of companies changing?

#### 1st Generation Compliance: Risk Management CSR

Since the industrial revolution, large-scale energy and resource consumption, and industry-related atmospheric pollution, water pollution, soil pollution and noise pollution have had a negative effect on people living in neighbouring communities – this disturbance is a major societal issue. In order to reduce the impact, many environment-related laws and regulations were introduced, to which companies responded. As part of their social responsibility, companies were required to be compliant and exercise risk management with regard to the surrounding environment. However, these local environmental issues eventually became more and more severe, and cross-border pollution, such as acid rain, developed into issues that countries could not solve on their own. In 1972, the UN hosted the Conference on the Human Environment (known as the Stockholm conference), the first meeting where world governments gathered to discuss the relationship between environmental problems and societal development.

### 2nd Generation Triple Bottom Line CSR

The focus of environmental issues shifted from issues such as atmospheric pollution to problems relating to the loss of biodiversity as a result of the destruction of the Ozone layer, global warming, and rainforest deforestation, and people became increasingly concerned about protecting the environment. The “World Commission on Environment and Development” (known as the Brundtland Commission) which was established by the UN in 1984, introduced the concept of ‘sustainable development’ in 1987 via their report “Our Common Future”. Furthermore, the United Nations Conference on Environment and Development (known as the Rio Summit) in 1992, held 20 years after the Stockholm Conference, is well-known for the UN adopting the Framework Convention on Climate Change and the Convention on Biological Diversity as a global response to environmental problems. A major feature of the Rio Summit was, that in confronting society’s mid-to-long term environmental issues, there were participants not only from national governments, but also from international organizations, NGOs and the business world. This development is also reflected in the formation of the World Business Council for Sustainable Development (known as the WBCSD) in 1995, the establishment of ISO14001 in 1996, and the creation of the Global Reporting Initiative (known as GRI) in 1997. Since that time, Corporate Social Responsibility has transformed from mainly being about compliance and risk management to focusing more on efficient operations (such as energy and resource saving), as well as companies’ responsibility to provide proactive disclosure of information. The “Triple bottom line” concept, focusing on the three main outputs of corporate activities, financial, environmental and societal, also started gaining attention.

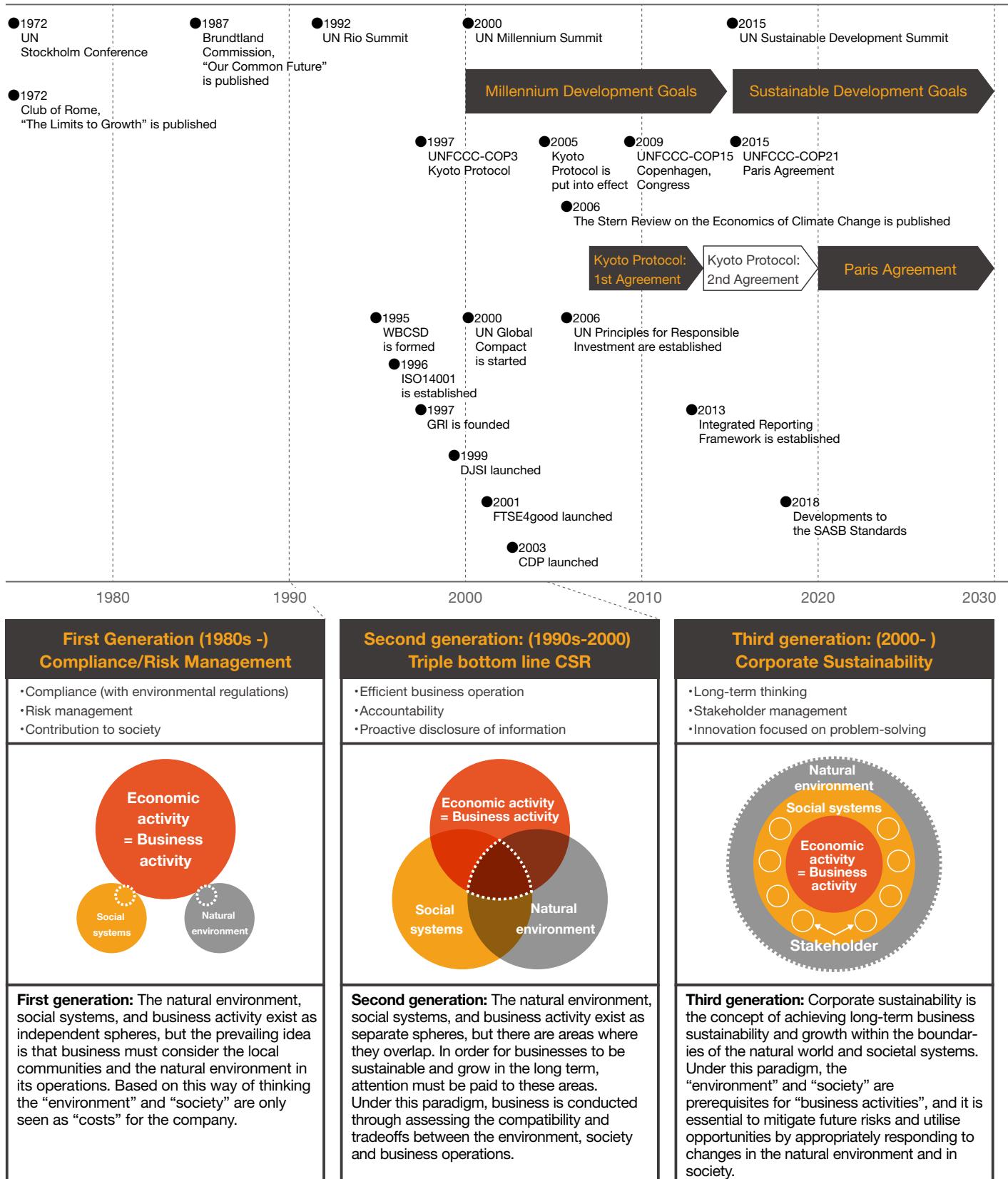
#### Sustainable Development:

The concept proposed in the report released by the Brundtland Commission – Our Common Future - defines sustainability as “development that meets the needs of the present without compromising the ability of future generations to meet their own needs”

#### Rio Summit:

In addition to over 170,000 members of national governments, 2400 NGO representatives participated and discussed the environment and sustainable development. As a result, three non-legally binding agreements were adopted: “Rio declaration on the Environment and Development”; “Agenda 21”; and “The Forest Principles”, and two legally binding international treaties “United Nations Framework Convention on Climate Change (UNFCCC)” and the “Convention on Biological Diversity”.

**Figure 2-1: Sustainable Development and the Changing Role of Businesses**



The dotted lines in the above chart show areas which companies perceive to be the areas relevant for their CSR/Sustainability activities.

Source: PwC

### 3rd Generation Corporate Sustainability

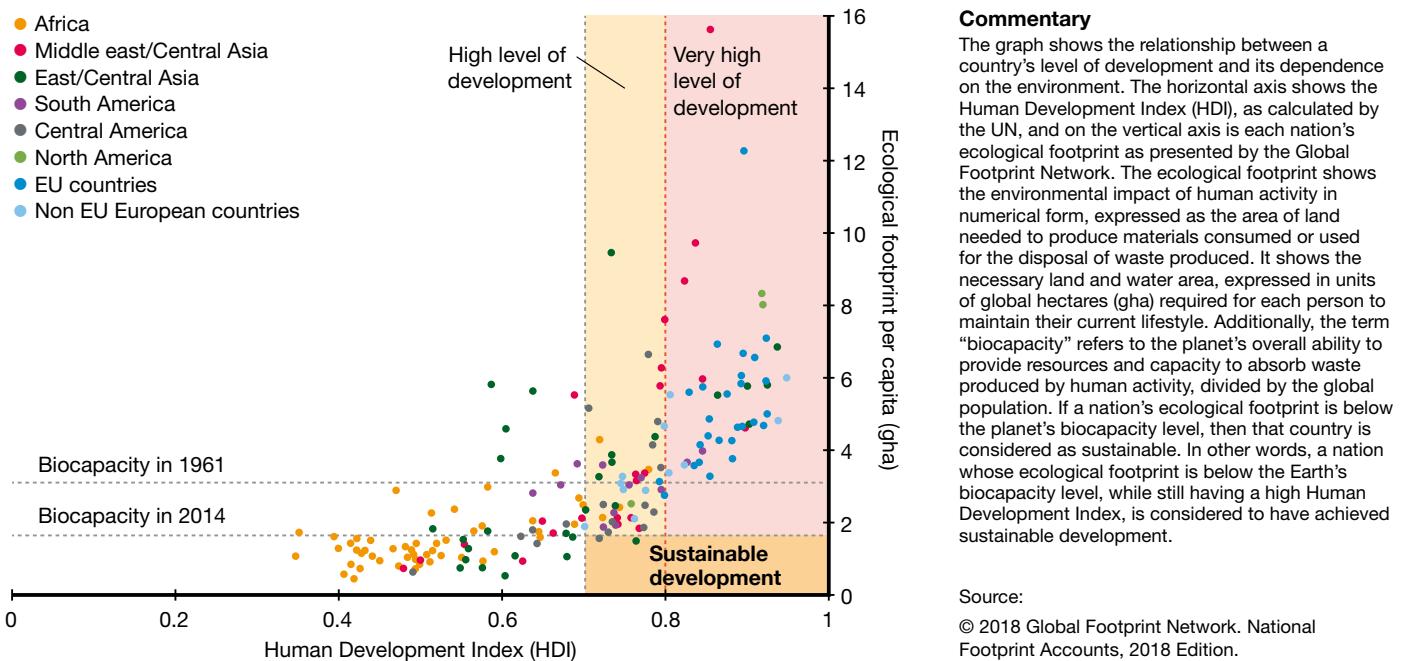
In the year 2000, at the UN Millennium Summit, the UN adopted the Millennium Declaration as the target for the international community in the 21st Century. The Millennium Development Goals (MDGs), which also included previously discussed goals, were unveiled as an integrated framework for international development. Around the same time, the UN launched the UN Global Compact (UNGC) as an initiative to further sustainable business practices, and through this initiative, a stronger link between environmental issues and sustainable development on the one hand and private business on the other was established. In short, the notion that business activity can contribute to solving environmental problems and achieve sustainable development gained acceptance and influence.

Subsequently, in September 2015, at the UN Sustainable Development summit “The 2030 Agenda for Sustainable Development”, including the Sustainable Development Goals (SDGs), was adopted as the next phase of sustainable development after the MDGs. While national governments were the main contributor to achieving the MDGs, all organisations that make up our society, including businesses, are expected to contribute towards the achievement of the SDGs. Furthermore,

at the 21st UN Climate Change Conference (COP21) in December of 2015, the Paris Accord was reached, with the objective of keeping global warming to well below 2 degrees compared to pre-industrial times. Since the 2009 Copenhagen Summit (COP15), international discussion on climate change had slowed down, but the progress made towards establishing a new policy framework beyond 2020, reached in Paris is expected to have a big impact on the environment and private business.

Economic globalization is accelerating at an increasing rate, and whilst there are many companies that take pride in the fact that their sales amounts are boosting the GDPs of entire nations, society's expectations towards businesses and their contribution to realizing sustainable development are growing. In addition, against the backdrop of population growth, private businesses are expected to contribute with innovative solutions to solve issues such as how to effectively utilize limited natural resources, and how to raise the living standard of people all around the world (Figure 2-2: The relationship between a country's level of development and its dependence on the environment).

**Figure 2-2: The relationship between a country's level of development and its dependence on the environment**



## Sustainable Development Goals

The successor to the 2015 Millenium Development Goals (MDG) are the Sustainable Development Goals, which include targets for sustainable development for 2030, and are comprised of 17 goals and 169 targets. Below are the 17 Global Goals.



## 2.2 Changes in the Company-Stakeholder Relationship

Just as expectations of global companies grow, the companies' stakeholders are also changing. In general, customers that consume goods and services, employees engaged in the company's business, shareholders who invest capital, and suppliers who provide inputs needed for developing goods and services, are considered the most important stakeholders for a company. These stakeholders directly influence the operations of businesses, and they will continue to remain important. However, in addition, rating agencies/institutional investors, NGOs/community groups, international organisations, and the media are also, in a long-term perspective, having a considerable impact on businesses.

### Rating agencies/Institutional investors

In recent years, the trend towards responsible investments has accelerated, with institutional investors such as pension funds playing a central role. Responsible Investment (also known as Socially Responsible Investments) dates back at its earliest to the 17th century, and originated with groups, such as religious organisations in western countries that chose their investments so as not to support industries such as gambling and alcohol. Subsequently, against the backdrop of environmental protection and anti-war movements this further expanded, and so this type of "negative screening" – excluding certain industries from investments – was for a long time the main focal point of responsible investment strategies. However with the launch of the Dow Jones Sustainability Index, developed by American company Dow Jones Indices (subsequently renamed S&P Dow Jones Indices) and Swiss investment management

firm Sustainable Asset Management (later renamed Robeco SAM), in 1999, the development of Sustainability Ratings of companies quickly started to grow. Moreover, the UN Principles for Responsible Investments (UNPRI) were adopted in 2006, with many financial institutions endorsing this way of looking at investments and becoming signatories of the principles. In June 2019, over 2200 financial institutions were signatories of the UNPRI, and the sustainability/ESG rating agencies that investors use as a tool for making responsible investment decisions are said to exceed 100. According to research by the Harvard Business School, the stock values of companies implementing environment and social-oriented policies (defined as high sustainability companies in the research paper) in the 1990's, was two times that of companies that had not done so (referred to as low sustainability companies) by 2014. (Figure 2.3 – relationship between a company's sustainability and its share price).

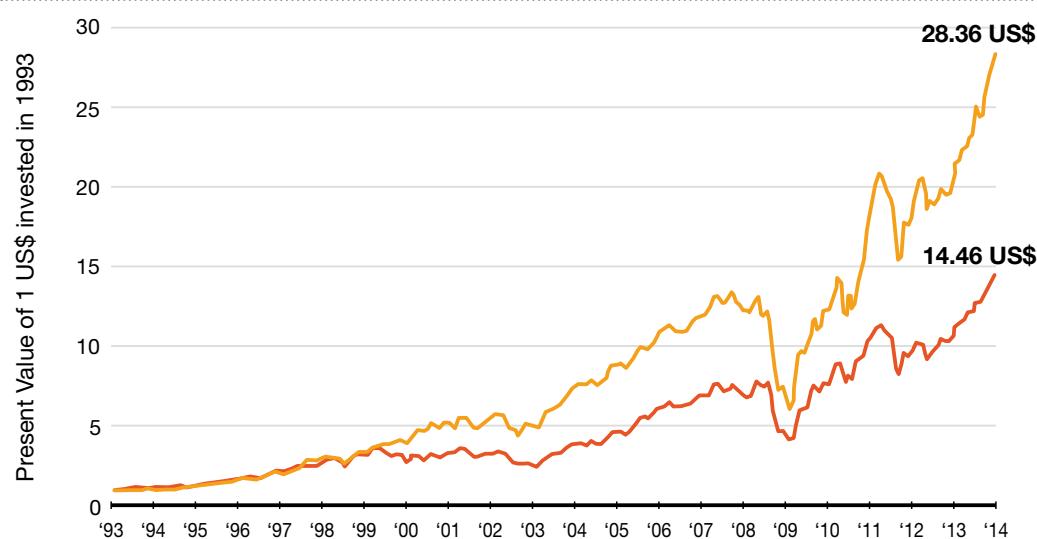
#### Responsible Investment:

The UN Principles for Responsible Investment defines responsible investments as, "taking into account a wide range of factors when making investment decisions, including the soundness and stability of economic and environmental systems, societal value and society's expectations, with the target of continuous long-term return on investments."

#### Sustainability/ESG rating:

Businesses are not assessed based on financial performance but rather on how they manage non-financial aspects such as environmental protection, corporate governance, human resource development, diversity, and brand management. Companies are rated based on factors that support their long-term growth but which at present are not shown in the financial statements.

Figure 2-3: relationship between a company's sustainability and its share price



#### Commentary

This graph shows the return on one USD invested in a portfolio made up of companies that perform well on material sustainability-related topics (yellow line) compared to an investment made in a portfolio comprised of companies performing poorly on the same topics. Which topics are considered as material varies from industry to industry as defined by the Sustainability Accounting Standard Board.

Source: Mo Khan, George Serafeim and Aaron Yoon. Corporate Sustainability: First Evidence on Materiality. HBS working paper, 2014 quoted in Serafeim (2014). *Turning a Profit While Doing Good: Aligning Sustainability with Corporate Performance*. Harvard Business School.

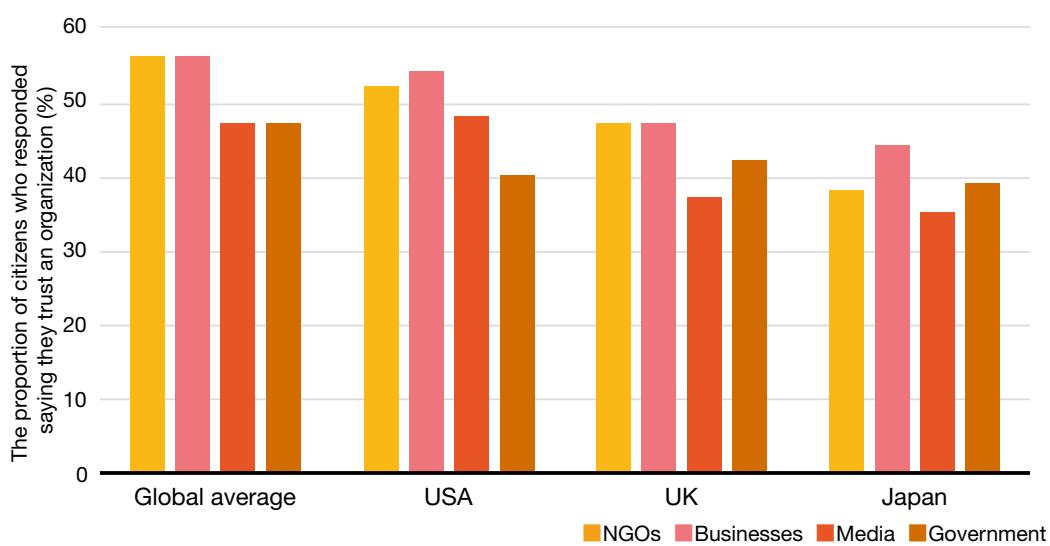
1 Mozaffar Khan, George Serafeim, and Aaron Yoon (2014) Corporate Sustainability: First Evidence on Materiality.

## NGO/Community groups

In many American and European countries, NGOs play an important role. NGOs have a long history, tracing their origins back to colonial times. At the 1992 Rio summit, NGOs were positioned in partnership with national governments, which gave NGOs a major influence over sustainable development, and more specifically environmental issues. Also, due to economic globalisation, as the awareness of the role that global companies play in solving international and societal issues increased, NGOs started calling for global companies to implement long-term business strategies. Well known cases of how NGOs have changed corporate behaviour are for example the call for the boycotting of American sports apparel companies, due to exploitative low wages and unfair working conditions in their overseas factories (often described as sweatshops), and the call for a boycott of a major oil company due to its dumping of materials from its platform in the North Sea, both of which took place in the late 1990s. In recent years, the development of information technology and the spread of the internet has also shown how influential the voice of NGOs can be.

According to British research and consulting company Sigwatch, which provides statistical data on the activities of more than 7,000 NGOs globally, around 6,000 NGO campaigns are initiated yearly, and the number is increasing. A recent report points out that companies targeted by NGO campaigns change and tend to conform to international discourse. Especially concerning climate change, NGOs traditionally targeted Oil companies in the energy sector but over the past few years NGOs have shown that campaigns targeting consumer brand companies are the most effective to bring about fast and pragmatic change of multinational corporations. Why is it that NGOs can change consumer behaviour? The answer is because in many countries, NGOs enjoy the same or even a higher degree of trust from society.

**Figure 2-4: which organisations does society trust?**



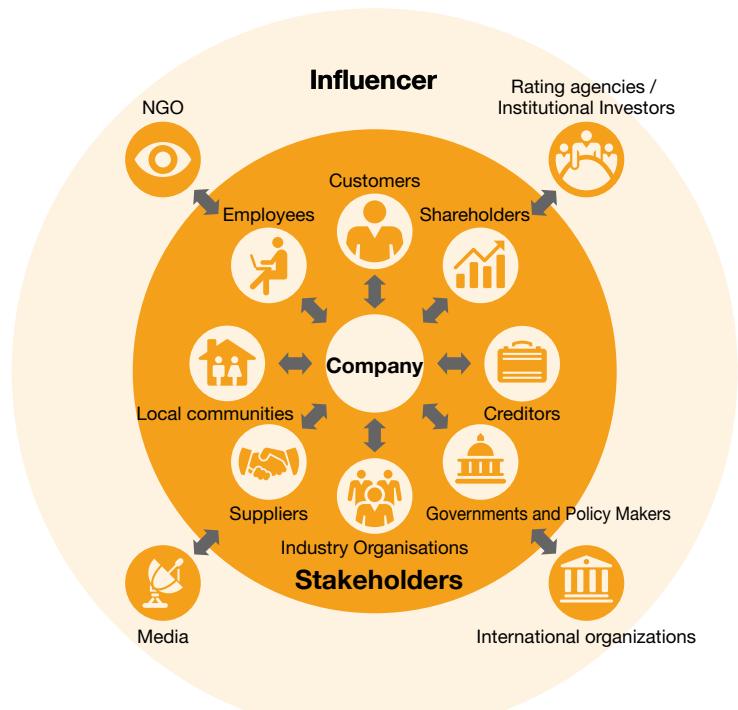
Source: Edelman(2019) Edelman Trust Barometer

## The Emergence of Influencers

Sustainability rating agencies and NGOs do not necessarily have a direct stake in companies. Instead, they affect the actions of the stakeholders with a direct interest in companies and so are considered as “influencers”.  
(Figure 2-5: Relationship between companies and stakeholders). As the indirect impact that these influencers have on companies increases, corporations are now expected to identify their primary stakeholders, as well as the influencers affecting these stakeholders, and actively manage these relationships.



Figure 2-5: Relationship between companies and stakeholders



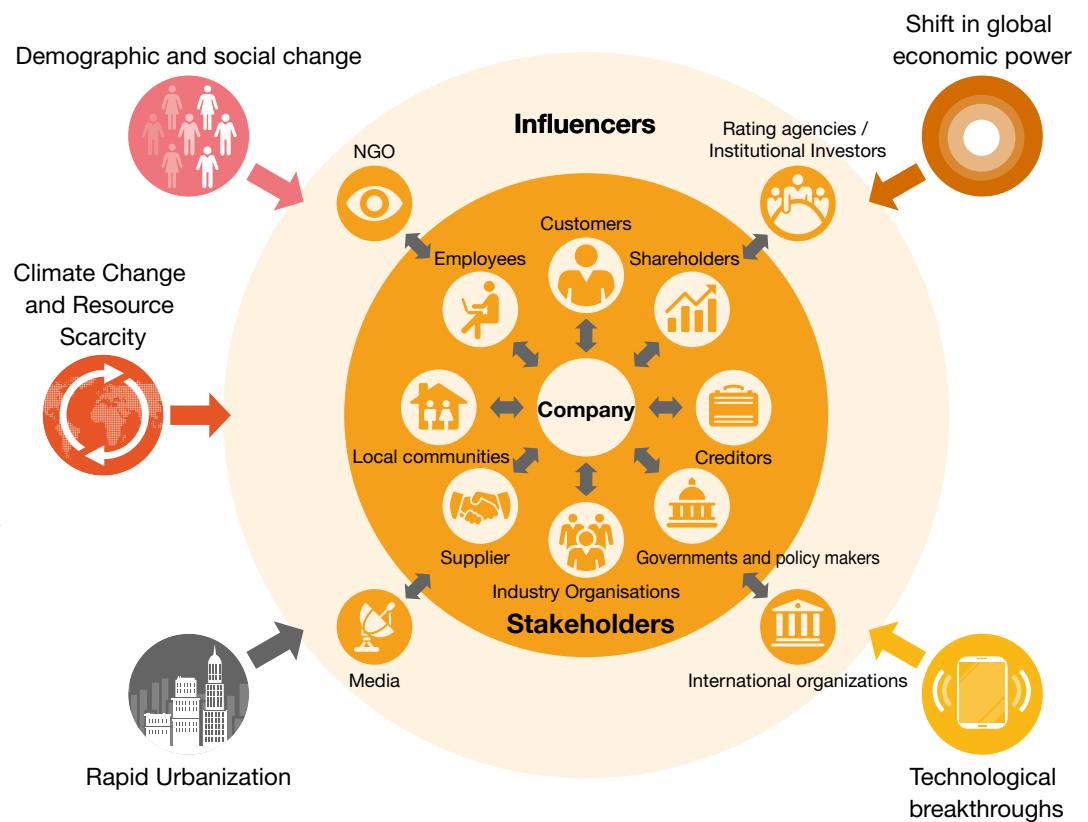
Source: PwC



## 2.3 What is Corporate Sustainability?

Even as companies are striving towards the realization of sustainable development, the expectations on them continue to increase and their stakeholders continue to change. Against this backdrop, not only is the first generation's CSR focus on compliance/risk management insufficient but we have now entered an age where also the second generation's proactive disclosures and efficiency-focused business is not enough. So, what are companies expected to do today? The answer, they need to integrate ways of approaching environmental and social issues into their business. We call this way of thinking 'Corporate Sustainability'. It means that companies need to formulate and implement strategies to grow within the bounds of the environmental and societal systems in which they exist while also responding to global megatrends such as demographic changes, shifts in global economic power, climate change and resource depletion. These megatrends will influence stakeholders and change the behaviour of influencers. Therefore, in implementing strategies for corporate sustainability, it is essential for companies to recognize the actions and viewpoints of company stakeholders and influencers.

**Figure 2-6: Corporate Sustainability**



**Japan's weak NGO movement has enabled Japanese corporations to mostly avoid the kind of criticism regularly dished out to their American and European counterparts. But Robert Blood, founder of SIGWATCH, argues that this has to change now that Western activists have discovered how to project their influence across the world via cooperative global financial institutions, and this is damaging Brand Japan.**

In the summer of this year, Britain's largest asset manager Legal & General announced that it would remove a major Japanese corporation from its \$6.7billion Future World index funds. Moreover, any of its funds that still held shares would be instructed to vote against the re-election of its chairman. L&G justified the move by saying that company had "shown persistent inaction" to address climate risk.

The company was reportedly shocked at L&G's initiative, which came after a year of L&G questioning the management of leading companies on their climate policies. However, it should not have been a surprise. Pressure on global financial institutions from US and European activist groups to divest from "extreme carbon" such as coal and oil sands has been building for over a decade. Inevitably, once Western financial institutions began divesting from their own funds, they would also evaluate the policies of their investments, regardless of which country they were located in.

The attack on Japanese institutions funding coal has not let up. Just this September, the Japanese wing of one of the world's leading climate action groups, 350.org, attacked several leading Japanese banks for allegedly providing over 60% of all the credit provided by Japanese institutions to coal development projects. Several of Japan's largest insurance companies have also been cited as major coal financiers.

Meanwhile in the U.S., despite operating in a political environment that is hostile to the very idea of climate change and officially 'coal-friendly', six of its largest banks have all announced coal exits. Almost all of Europe's leading banks, and several of its biggest insurers and reinsurers, have done the same.

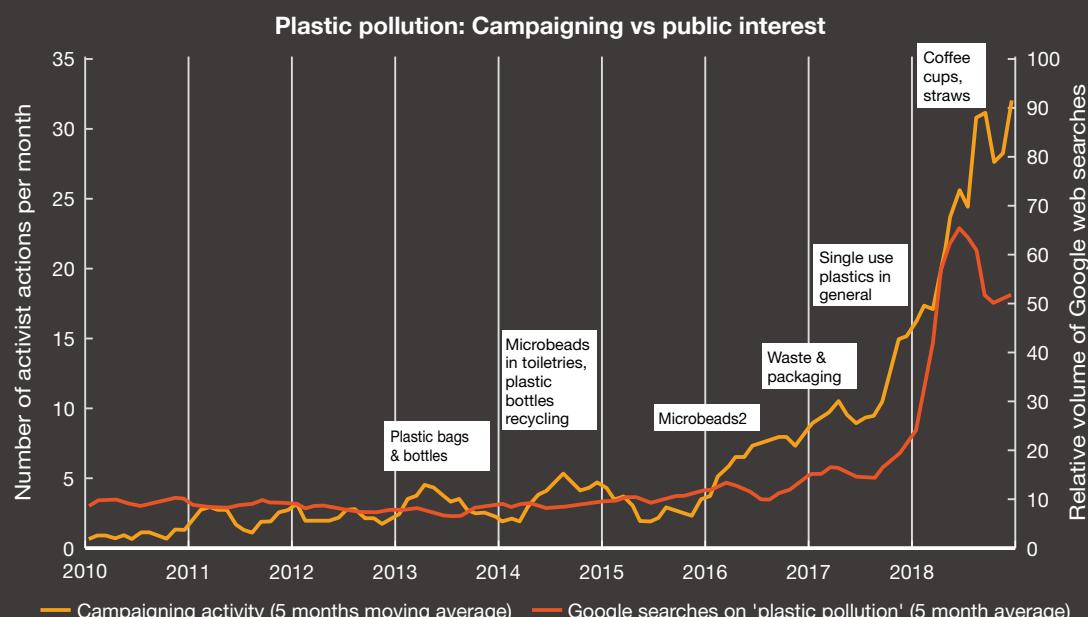
The reason? High profile and often embarrassing campaigns by skilled environmental activists to make them change policies, initially targeting US college endowment and pension funds and their fund trustees and professional investment advisors. These campaigns were modelled on the politically charged campus divestment battles of the 1980s which were intended to undermine the economy of apartheid South Africa. Arguably they achieved little in direct business terms, but they helped to make South Africa a pariah investment in the USA for many years.

This is how a policy made in America, adopted by a financial institution in Britain, can end up punishing a major institutional investor on the other side of the world, in Japan.

The 'global ripple' of NGO campaigning that discomfited the former L&G holding is unlikely to stop at carbon. Western activists have learnt from the climate divestment movement that sympathetic financial institutions are a highly effective way to give a campaign "bite".

### Chart 1

**NGO campaigning drove public concern on plastics, but it took some years to really take effect**





**Robert Blood**  
SIGWATCH  
Founder and managing director

In the early years only the SRI and ethical funds were interested in working with NGOs on policy matters, but of late, mainstream funds have joined too. This is due, in part, to pressure from political stakeholders and customers, particularly in relation to the institutions' own funds, to take intangible risks such as human and indigenous peoples' rights more seriously. The financial crash of 2008 was doubtless also a major stimulus. Many banks at that time, suddenly bereft of their political friends, felt a need to address their deep unpopularity, and beefing up their environmental and social governance (ESG) policies and engaging with NGOs was an obvious way to achieve this.

As well as human and indigenous rights, many other issues such as sustainability, environmental responsibility, labour standards and even animal rights will become more important for global financial institutions, as they develop ever more expansive policies and standards under pressure from NGOs and other stakeholders. By implication, as with carbon already, these moves will have major implications for the firms and industries in which these institutions invest.

A good example is the plastic pollution issue. Less than two years ago it had barely registered on the public consciousness – it was a non-issue, at least politically. Today it is a major public concern, getting heavy media coverage, persuading governments to draw up legislation on plastic waste and companies to rethink their packaging and single-use plastics policies. Chart 1 shows how the plastics issue has jumped massively in public awareness since mid-2017 (as measured by the relative volume of Google searches), within months of a major uptick in NGO campaigning activity, driven by Greenpeace, Friends of the Earth, WWF and a broad swathe of the environment movement across the world.

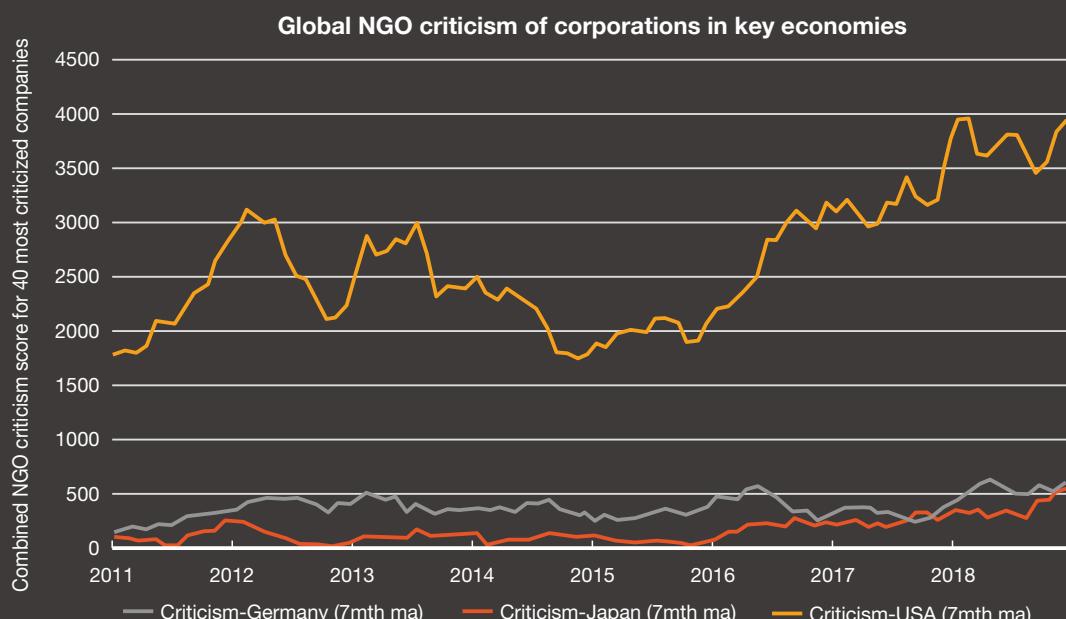
We have seen the same predictive association between NGO campaigning and public awareness on other issues, such as shale gas (fracking) and the environmental cost of meat consumption. There can be no doubt that NGOs really do make the political weather on many issues. Now, this power has been combined with the NGOs' ability to project their influence globally through supportive financial institutions. Japanese business, particularly brands with a significant international presence, can no longer realistically hide behind a weak local NGO movement to avoid acting on issues that are already forcing change on their rivals across the world.

Chart 2 reveals how NGOs have been paying increasing attention to the behavior and policies of Japanese corporations in the last few years. Note that their criticism of Japan's leading companies has been rising steadily over the last three years. Today it is the same as the combined criticism of the leading companies of Germany, a similarly export-oriented economy of a similar size. However, whereas German firms are forced to operate in the heartland of European environmentalism, their Japanese counterparts are rarely troubled by their country's weak and fragmented environmental movement. The reason criticism of Japanese firms is as high as German ones is because of NGOs based outside Japan.

Japan, a country, which has made an art out of combining economy and efficiency with elegance and style, is failing to communicate these environmentally positive qualities to the outside world. NGOs are sharp critics, but they are also quick to acknowledge 'earth-positive' behavior when they see it. That they are not doing so for most Japanese corporations is damaging Brand Japan. This is something that should worry all globally trading Japanese companies.

## Chart 2

### NGO criticism of corporations is increasing most in the US and Japan



# Chapter 3 – Corporate Sustainability in Japanese Companies

## 3.1 Corporate Sustainability awareness at Japanese Companies

Corporate sustainability involves devising strategies, taking action, measuring performance, communicating results, and, based on feedback, making improvements and implementing reforms based on mid- to long-term changes in society (megatrends). Consequently, as a first step on the journey to realizing Corporate Sustainability, understanding of these long-term societal developments and changes in the behaviour of influencers is of great importance. PwC has looked into to what extent Japanese companies are aware of, and understand the meaning of major sustainability-related agreements and conventions such as the “Paris Accord” and the “Sustainable Development Goals” (SDGs), as well as concepts necessary to realize the internationally agreed goals such as “ESG investment” and “Integrated reporting”.

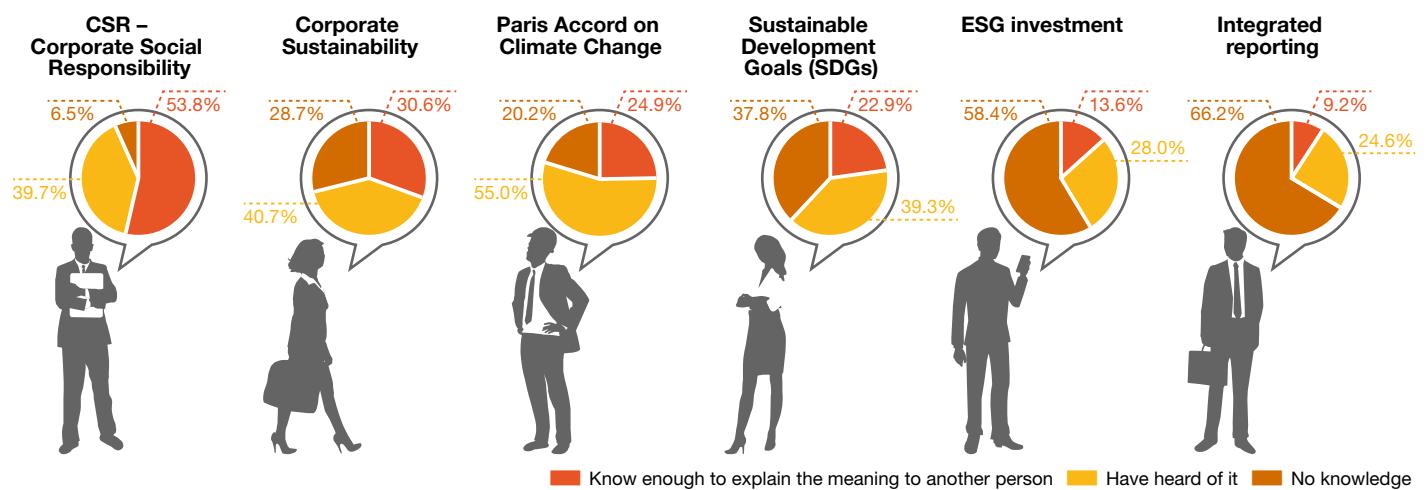
Before inquiring into these topics, we have carried out surveys since 2016, asking employees of Japan’s largest companies about their level of awareness of broader topics such as Corporate Social Responsibility (CSR), and Corporate Sustainability. In PwC’s most recent survey, conducted in 2018, over half of the people responded that they “know enough to explain the meaning to another person”, when asked about their

understanding of “CSR” and if you add the share who answered they “have heard of it” the share is about 95%. Although awareness on Corporate Sustainability is lower compared to that of CSR, 70% of people still answered that they either “know enough to explain the meaning to another person”, or that they had “heard of it”. In other words, it was quite clear that the awareness for Corporate Sustainability/CSR among people working at large listed Japanese companies is fairly high.

However, there were large differences in awareness depending on age and job rank with people of higher age and in more advanced positions showing a greater level of awareness. For example, for department or section managers the proportion of people answering that they “know enough to explain the meaning to another person” was 77% for CSR, and 55% for corporate sustainability. However, for deputy managers and regular employees, the proportion was only 41% and 19% respectively. One can perhaps say that a big challenge for Japanese companies is to increase awareness on long-term issues such as Corporate Sustainability among younger employees who will be in charge of running the companies in future.

So, what level of awareness is there on key concepts within the broader concept of Corporate Sustainability such as the “Paris

Figure 3-1: level of awareness of Corporate Sustainability/CSR at Japanese companies



Source: PwC

Accord on Climate Change", "Sustainable Development Goals (SDGs)", "ESG investment", and "Integrated Reporting" While the awareness of these aspects are not as high as it is for CSR and Corporate Sustainability, the level of awareness has increased since our last survey in 2016. Especially for key words such as "SDGs" and "ESG investment", we can see a big change. In our last survey the share of people who responded that they had "no knowledge" of these concepts were 54% and 73% respectively, but in this year's survey these numbers had fallen to 38% and 58% respectively. (figure 3.2 Comparison with previous survey results).

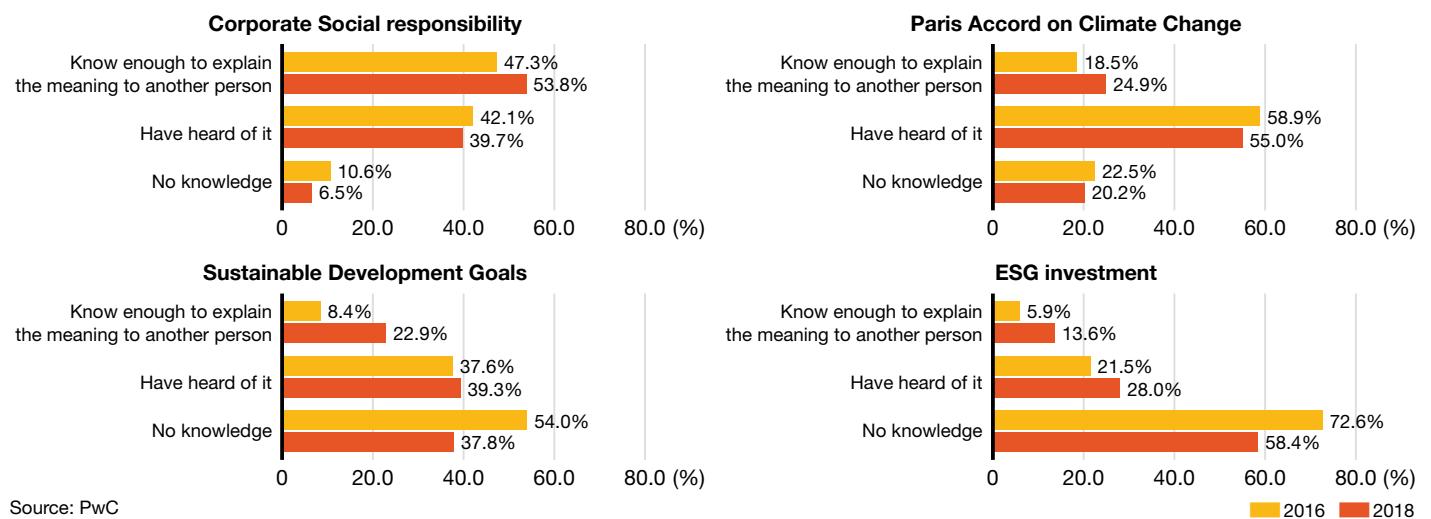
Since their adoption in September 2015, Japan as a country is actively working towards the Global Goals, and the Japanese government has established an SDG promotion head office in Japan, formulated guiding principles for implementing the Goals and, since 2018, has been adopting yearly action plans. In response to these initiatives, the Japanese business community is also taking action towards realizing the SDGs. In particular, the Japanese Business Federation, Keidairen, has advocated for the concept of "Society 5.0", where innovative technology is used to its fullest extent to contribute to both economic development and solving societal issues. The active promotion of activities, such as sharing good practices that contribute to the achievement of the SDGs seems to have contributed greatly to raising the awareness of the SDGs among people working in

Japanese companies.

According to the latest biannual research conducted by the Global Sustainable Investment Review, the growth rate of Sustainable/ESG investment in Japan was 308% over the 2 years from 2016 to 2018, and sustainable/ESG investment's share of total assets under management, rose rapidly from 3.4% to 18.3%. It is widely understood that the Japanese Government Pension Investment Fund (GPIF) becoming a signatory to the UN Principles for Responsible Investments (UNPRI) in September 2015, and the subsequent expansion into ESG investments by the GPIF has largely contributed to this development. Given this situation, we believe that the level of awareness of ESG investment has increased amongst Japanese companies because their daily exposure to ESG related information is growing.

Furthermore, starting from this year, PwC's survey also includes questions on whether or not the responders know if their company publish a sustainability or an integrated report, and, if they do, if they have read it. Our study shows that 70% of respondents were aware that their company had published a sustainability report/integrated report, and amongst those, 80% had read it. These reports likely also play an important role in increasing the understanding of Corporate Sustainability among employees of listed corporations.

**Figure 3-2: Comparison with previous survey results**



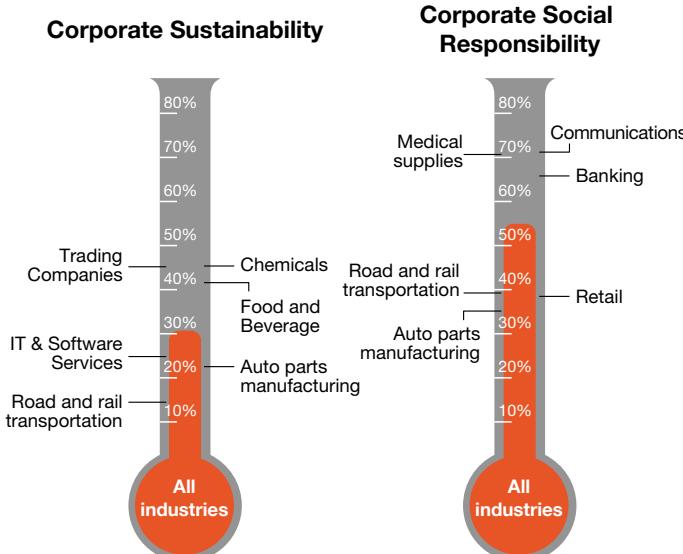
Source: PwC

## Industry differences

Although the level of awareness of corporate sustainability/CSR in general has been increasing amongst employees of listed corporations, this does not mean that the awareness level is the same across all industries. For example, in communications, and pharmaceuticals, where awareness of CSR was highest, over 70% answered that they “know enough about the topic to explain it to someone else”. In contrast, the corresponding figure for those industries with the lowest levels of awareness - transportation, retail, and automotive manufacturing - was less than 40%. As for Corporate Sustainability in chemical-, trading- and food and beverage industries, where the level of awareness was highest, 40% responded that they “know enough about the topic to explain it to someone else”, compared to the transportation industry, where the corresponding figure was just 14% (figure 3.3: Industry differences regarding corporate sustainability/CSR awareness).

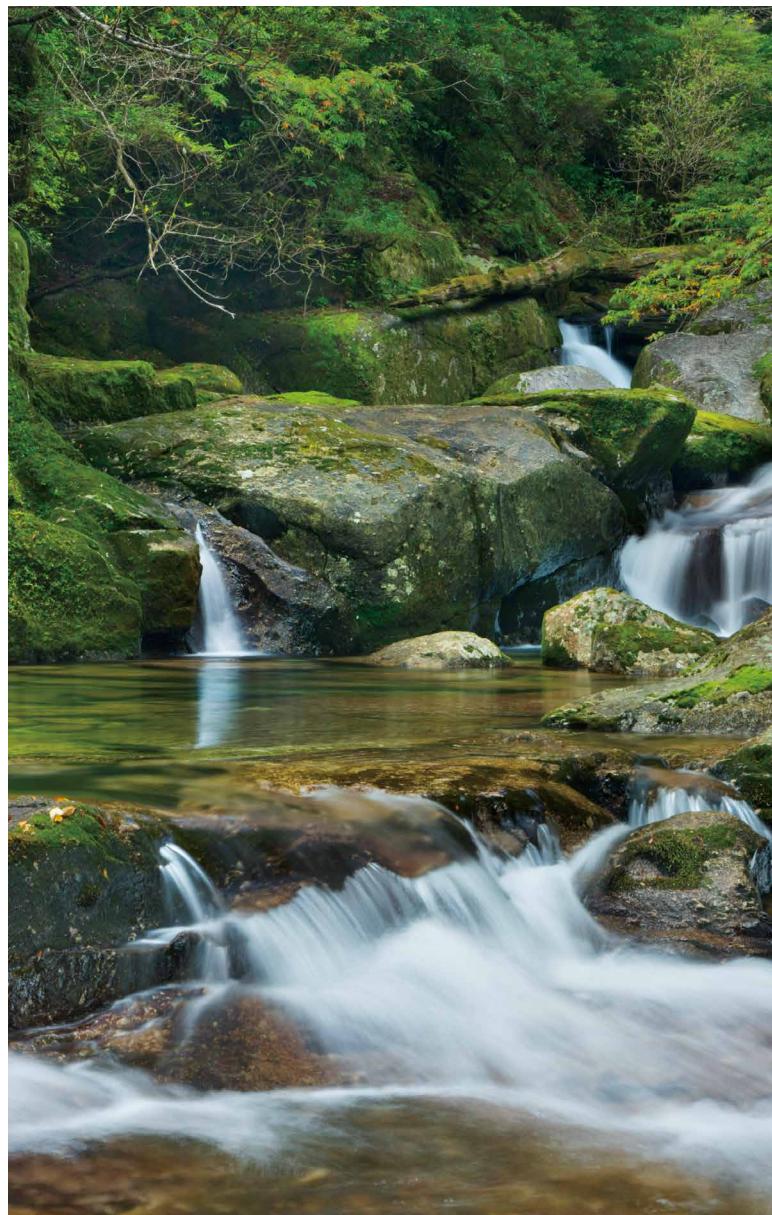
When it comes to keywords such as the Paris Accord, ESG investment, and Integrated Reporting, we can see a similar trend with awareness being relatively high in industries such as

**Figure 3-3: Industry differences regarding corporate sustainability/CSR awareness**



Source: PwC

chemical, banking, trading, and diversified financial services (non-banks and securities). On the other hand, in transport, auto manufacturing, and auto parts manufacturing industries, awareness levels are relatively low. If one looks at the past two years, in industries with little awareness, to begin with there has been little change in awareness, but there has been a remarkable increase in awareness among financial institutions, such as banks and financial services companies. As mentioned previously, ESG investments have seen a rapid increase in Japan and the importance of the role financial institutions play in promoting sustainability among corporations can clearly be seen in the results of our study.

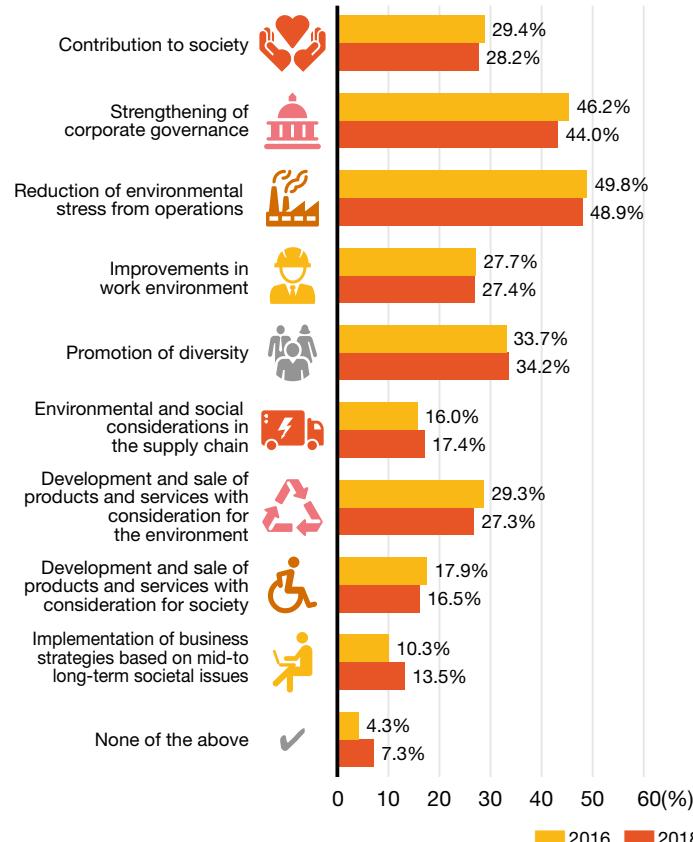


### 3.2 What is Corporate Sustainability/CSR to Japanese Companies?

As explained in Chapter 2, the role that companies have been expected to play in creating a sustainable society has been changing over time. About 90% of people at major corporations know of corporate sustainability/CSR but what is their perception of what this concept means and what companies are expected to do? PwC presented ten topics encompassing the different viewpoints from first generation CSR (compliance/risk management) to third generation Corporate Sustainability and asked what the respondents considered to be the most appropriate in describing corporate sustainability/CSR. The results show that approximately half of employees at major corporations consider Corporate Sustainability/CSR to mean “Reduction of environmental stress from operations” (such as energy saving in offices/manufacturing sites, reduction of CO<sub>2</sub> emissions, waste material produced and water consumption).

**Figure 3-4: What is corporate sustainability/CSR to Japanese companies?**

Respondents could pick up to three definitions that they felt best described the meaning of Corporate Sustainability/CSR

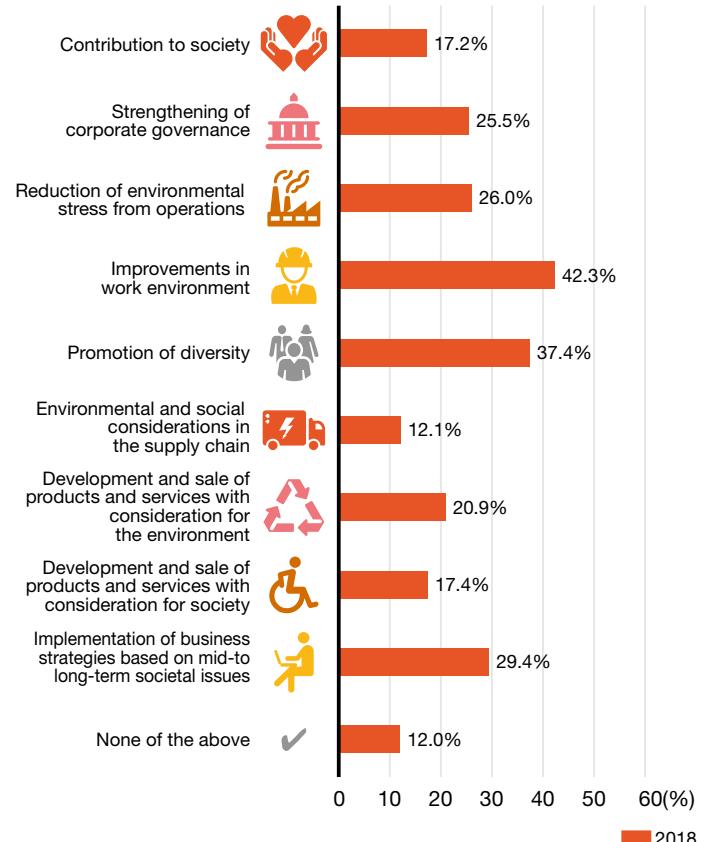


A similar share of people see it as “the strengthening of corporate governance”. The third most mentioned topic was the “promotion of diversity”. There were no noticeable differences in terms of gender, age, or job position, and compared to the same survey carried out two years ago we see almost no changes in results. (Figure 3-4: What is Corporate Sustainability/CSR to Japanese companies).

Since the International Organisation for Standardisation (ISO) established the international standard relating to environmental management systems (ISO14001) in 1996, many Japanese companies have acquired ISO14001 certification, and have been making progress in reducing the environmental burden from their offices and factories. At present China has the most certified companies, but Japan still remains in second place. Many companies are having environmental protection at the core of their CSR efforts so it is not particularly surprising that nearly half of respondents said that CSR means the “Reduction of environmental stress from operations”.

**Figure 3-5: Issues facing Japanese companies**

Respondents could pick up to three issues that they considered necessary for their companies to manage in the future.



In Japan, the Tokyo Stock Exchange launched the Corporate Governance Code in June 2015. Through this code, having the subtitle “For sustained business growth and mid- to long-term growth in corporate value”, listed companies are required to disclose information in their corporate governance reports about their implementation of the Code, and they are becoming more aware that it is becoming increasingly essential to strengthen corporate governance to sustain mid-to-long term growth. In similar ways, major corporations are incited to strengthen their efforts on diversity as a result of the Ministry of Economy, Trade, and Industry (METI) and the Tokyo stock exchange launching the annual selection of “Nadeshiko Brands” (listed companies that are outstanding in terms of encouraging the empowerment of women in the workplace) since 2012. Against this backdrop we gather that many respondents chose “strengthening of corporate governance”, or “promotion of diversity” in response to the question, “what Corporate Sustainability/CSR means” to them.

Some believe that the perceptions that Japanese companies have of Corporate Sustainability/CSR have changed over time but many respondents still chose topics associated with risk management when asked about the meaning of Corporate Sustainability/CSR, indicating that they are still looking at the concept through the lens of the second generation CSR (Triple Bottom Line CSR).

However, in addition to the question of “what represents CSR or Corporate sustainability best”, we also asked, “What are the issues that your company should deal with in the future?” (Figure 3-5: Issues facing Japanese companies). The results show that in third place, after “improving work environment” and “promoting diversity”, about 30% of respondents chose “Implementing business strategy based on the mid- to long-term societal issues”. This is no doubt, “Third Generation Sustainability”, which means that people working at major Japanese companies already recognize its importance. However, it is possible that as far as they are aware, these types of issues are not currently being included in their companies’ CSR/Sustainability efforts. Still, in the last 1-2 years, the CSR departments of major companies have changed their names to “Sustainability Department” or “Sustainability Strategy Department” and considering that they are revising their roles and positions within the corporate structures, a future where Japanese corporate employees’ way of thinking has shifted from second generation CSR to third generation Corporate Sustainability might not be too far away.

**Figure 3-6: The meaning of Corporate Sustainability/CSR (by industry)**

Respondents could pick up to three definitions that they felt best described the meaning of Corporate Sustainability/CSR. Below are the top five most selected topics for each industry

Auto manufacturing:	Banking:	Construction:	Retail:	Insurance:	IT services/ Software services:	Electric/ electronic products:	Land Transport:	Electric and Gas:	Communications:
Reduction of environmental stress from operations 	Strengthening of corporate governance 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Strengthening of corporate governance 	Strengthening of corporate governance 	Promotion of diversity 
Strengthening of corporate governance 	Reduction of environmental stress from operations 	Strengthening of corporate governance 	Strengthening of corporate governance 	Strengthening of corporate governance 	Promotion of diversity 	Strengthening of corporate governance 	Improvements in work environment 	Reduction of environmental stress from operations 	Strengthening of corporate governance 
Development and sale of products and services with consideration for the environment 	Promotion of diversity 	Promotion of diversity 	Promotion of diversity 	Promotion of diversity 	Strengthening of corporate governance 	Development and sale of products and services with consideration for the environment 	Reduction of environmental stress from operations 	Promotion of diversity 	Reduction of environmental stress from operations 
Improvements in work environment 	Contribution to society 	Improvements in work environment 	Improvements in work environment 	Contribution to society 	Development and sale of products and services with consideration for the environment 	Promotion of diversity 	Promotion of diversity 	Improvements in work environment 	Improvements in work environment 
Contribution to society 	Development and sale of products and services with consideration for the environment 	Development and sale of products and services with consideration for the environment 	Development and sale of products and services with consideration for the environment 	Improvements in work environment 	Contribution to society 	Contribution to society 	Contribution to society 	Development and sale of products and services with consideration for the environment 	Contribution to society 

Source: PwC

## Industry differences

At present, “Reduction of environmental stress from operations” and “Strengthening of Corporate Governance” are perceived as topics that represent the meaning of Corporate Sustainability/CSR in almost all industries. (Figure 3-6: The meaning of Corporate Sustainability/CSR [by industry]). However regarding which issues one’s own company should deal with in the future, responses differed by industry, and it seems that these issues are strongly correlated to the unique features of each industry (Figure 3-7: Issues facing Japanese companies). For example, looking at the topic of “Improvements in work environment” (which includes reducing working hours, prevention of harassment etc), a little less than 30% of all respondents selected the topic as relevant but more than 50% of respondents working in construction, transport and retail selected it as an upcoming issue. Furthermore, with regards to “Promotion of diversity”, compared to the 42% average across all industries, 50% of respondents in insurance, chemicals, and communications answered that it was the most important issue. An especially strong correlation between industry and topics selected can be seen in the automotive manufacturing and vehicle parts manufacturing sectors. Here “Development and sale of products and services with consideration for the environment”, was picked as the most important topic, whilst employees in banking and diversified financial services chose

“Implementation of business strategies based on mid-to long-term societal issues” as their most important issue. Lastly, although gaining in importance on a global level “Environmental and social considerations in the supply chain”, did not get into the top 5 most important issues in any of the industries covered in this survey.

**Figure 3-7: Issues facing Japanese companies**

Respondents could pick up to three issues that they considered necessary for their companies to manage in the future. Below are the top five most selected topics for each industry.

Auto manufacturing:	Banking:	Construction:	Retail:	Insurance:	IT services/ Software services:	Electric/ electronic products:	Land Transport:	Electric and Gas:	Communications:
Development and sale of products and services with consideration for the environment 	Implementation of business strategies based on mid-to long-term societal issues 	Improvements in work environment 	Improvements in work environment 	Promotion of diversity 	Improvements in work environment 	Improvements in work environment 	Improvements in work environment 	Improvements in work environment 	Promotion of diversity 
Reduction of environmental stress from operations 	Improvements in work environment 	Promotion of diversity 	Promotion of diversity 	Improvements in work environment 	Promotion of diversity 	Implementation of business strategies based on mid-to long-term societal issues 	Promotion of diversity 	Promotion of diversity 	Improvements in work environment 
Improvements in work environment 	Promotion of diversity 	Strengthening of corporate governance 	Strengthening of corporate governance 	Implementation of business strategies based on mid-to long-term societal issues 	Implementation of business strategies based on mid-to long-term societal issues 	Promotion of diversity 	Reduction of environmental stress from operations 	Implementation of business strategies based on mid-to long-term societal issues 	Reduction of environmental stress from operations 
Promotion of diversity 	Strengthening of corporate governance 	Implementation of business strategies based on mid-to long-term societal issues 	Implementation of business strategies based on mid-to long-term societal issues 	Strengthening of corporate governance 	Reduction of environmental stress from operations 	Development and sale of products and services with consideration for the environment 	Strengthening of corporate governance 	Reduction of environmental stress from operations 	Implementation of business strategies based on mid-to long-term societal issues 
Implementation of business strategies based on mid-to long-term societal issues 	Contribution to society 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Reduction of environmental stress from operations 	Strengthening of corporate governance 	Development and sale of products and services with consideration for society 	Implementation of business strategies based on mid-to long-term societal issues 	Strengthening of corporate governance 	Strengthening of corporate governance 

Source: PwC

### 3.3 The UN Sustainable Development Goals as Perceived by Japanese Companies

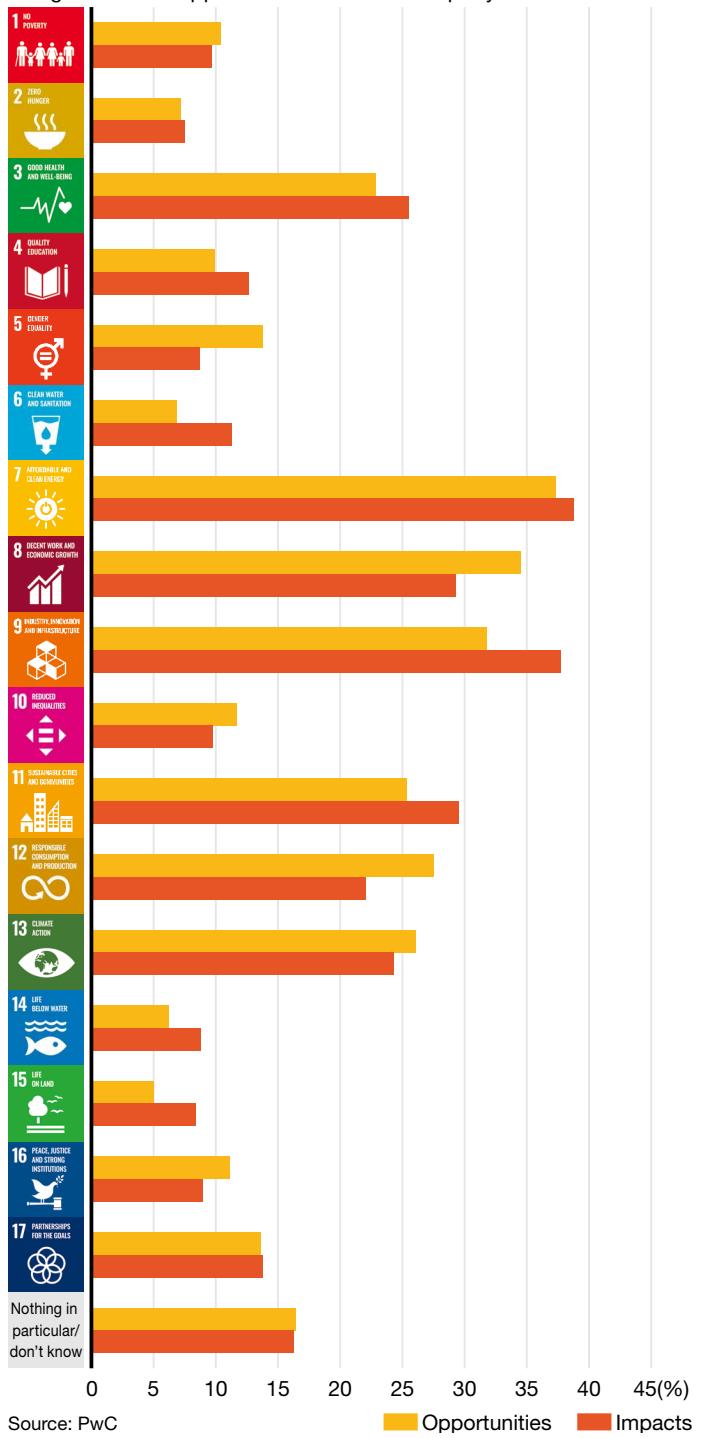
At the sustainable development summit held in September 2019, UN member states adopted the “2030 Agenda for Sustainable Development”, which includes the Sustainable Development Goals (SDGs). Before this event, in the Summer of 2015 PwC conducted research on SDG engagement covering 986 companies worldwide and 2,015 members of the general public, with a large number of Japanese companies and citizens participating (For detailed results of this survey, please refer to “Make it your business: Engaging with the Sustainable Development Goals” PwC April 2016).

4 years have passed since PwC conducted the survey, and as Figure 3-1 shows, companies’ understanding of the SDGs have changed considerably. However, how do people at major companies really look at their company’s relationship with the Global Goals?

PwC asked people to choose the five Goals that they believe will influence (impact) the company where they work (both for good and for bad), and which Goals they believe will deliver business opportunities in the future. Looking at both impacts and future business opportunities, the most selected SDGs were SDG7 (Affordable and clean energy), SDG8 (Decent work and economic growth), and SDG9 (Industry, innovation, and infrastructure). Particularly from a business opportunities perspective, out of these three, over 35% of people believed SDG7 and SDG9 will be material. Subsequently, after these three, SDG3 (Good health and wellbeing), SDG11 (Sustainable cities and communities), SDG12 (Responsible consumption and production), and SDG13 (Climate action) were chosen most frequently. SDG3 and SDG11 were more often selected from a business opportunities perspective while SDG12 and SDG13 were the most selected from the perspective of business impact. (Figure 3-8: Impacts and Opportunities from SDGs for Japanese companies). Out of the 17 Goals, it is apparent that people are aware of the importance of 7 of them, whilst the business relevance of the other 10 is just starting to be understood.

**Figure 3-8: Impacts and Opportunities from SDGs for Japanese companies**

Respondents could pick up to five Goals that they considered their company to have impact on or be impacted by, or that they believe brings business opportunities for their company.



Source: PwC

2 “Make it your business: Engaging with the Sustainable Development Goals” PwC (April 2016)

## Industry differences

In nearly all of the industries covered by this survey, SDG7 (Affordable and Clean Energy) made the top five in terms of SDGs connected with future business opportunities. Particularly in industries such as automobile manufacturing, construction, machinery, precision equipment, diversified financial services (non-banking, securities), mining and metals, chemicals, IT and software services, electric/electronic products, transportation, and utilities, it was selected as either the most or the second most important in terms of future business opportunities. For other Goals these varied according to the industry. Goals that varied in popularity depending on industry were SDG2 (Zero Hunger) which the food and beverage industry found relevant, and SDG1 (No poverty), which was seen as relevant by companies in the diversified financial services industry. SDG6 (Clean water and sanitation) was highlighted by the chemical industry and SDG18 (Partnership for the goals) by companies in the pharmaceutical industry. All these goals made the top five list of their respective industry but not in any other industry. It is likely that each of these industries will place importance on these goals as future growth areas. (Figure 3-9: top five SDGs connected to business opportunities [by industry])

**Figure 3-9: Top five SDGs connected to business opportunities (by industry)**

Auto manufacturing:	Banking:	Construction:	Retail:	Insurance:	IT services/ Software services:	Electric/ electronic products:	Land Transport:	Electric and Gas:	Communications:
7 AFFORDABLE AND CLEAN ENERGY 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	11 SUSTAINABLE CITIES AND COMMUNITIES 	8 DECENT WORK AND ECONOMIC GROWTH 	3 GOOD HEALTH AND WELL-BEING 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	7 AFFORDABLE AND CLEAN ENERGY 	7 AFFORDABLE AND CLEAN ENERGY 	7 AFFORDABLE AND CLEAN ENERGY 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 
9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	8 DECENT WORK AND ECONOMIC GROWTH 	7 AFFORDABLE AND CLEAN ENERGY 	3 GOOD HEALTH AND WELL-BEING 	8 DECENT WORK AND ECONOMIC GROWTH 	7 AFFORDABLE AND CLEAN ENERGY 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	8 DECENT WORK AND ECONOMIC GROWTH 	13 CLIMATE ACTION 	8 DECENT WORK AND ECONOMIC GROWTH 
12 RESPONSIBLE CONSUMPTION AND PRODUCTION 	11 SUSTAINABLE CITIES AND COMMUNITIES 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	11 SUSTAINABLE CITIES AND COMMUNITIES 	13 CLIMATE ACTION 	8 DECENT WORK AND ECONOMIC GROWTH 	3 GOOD HEALTH AND WELL-BEING 	11 SUSTAINABLE CITIES AND COMMUNITIES 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	11 SUSTAINABLE CITIES AND COMMUNITIES 
8 DECENT WORK AND ECONOMIC GROWTH 	7 AFFORDABLE AND CLEAN ENERGY 	12 RESPONSIBLE CONSUMPTION AND PRODUCTION 	12 RESPONSIBLE CONSUMPTION AND PRODUCTION 	11 SUSTAINABLE CITIES AND COMMUNITIES 	11 SUSTAINABLE CITIES AND COMMUNITIES 	11 SUSTAINABLE CITIES AND COMMUNITIES 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	11 SUSTAINABLE CITIES AND COMMUNITIES 	3 GOOD HEALTH AND WELL-BEING 
13 CLIMATE ACTION 	3 GOOD HEALTH AND WELL-BEING 	13 CLIMATE ACTION 	7 AFFORDABLE AND CLEAN ENERGY 	9 INDUSTRY, INNOVATION AND INFRASTRUCTURE 	13 CLIMATE ACTION 	13 CLIMATE ACTION 	Nothing in particular/ don't know	8 DECENT WORK AND ECONOMIC GROWTH 	4 QUALITY EDUCATION 

Source: PwC

"The only thing we know about the future is that it will be different."

Quoted from prominent business management consultant and author Peter Drucker.

"The best way to predict the future is to invent it."

Quoted from Allan Kay, a prominent US computer scientist.

It is not possible to make predictions about the business environment in which companies operate: in addition to the accelerating development of technology, geopolitical instability is increasing, and uncertainty about the future is growing. Because of this uncertainty, we must create flexible and strong "resilient organisations". I believe that a resilient business organisation is a "future-proof" organisation that does not fear the future.

First, let us think about the definition of a resilient company.

Resilient companies are able to recover after facing a crisis, respond flexibly to changes in its business environment, find new opportunities amidst stress and uncertainty, and conducts business in a way that contributes to the wellbeing of society as a whole. (The Resilient Company [2015])

One could say that the ideal image of a company is portrayed here, but is there a realistic framework or method to even come close to achieving this state? In his books "Reinventing Organisations" (2018) by Fredric Laloux, which is currently gaining much attention in Japan, Laloux states that the properties of organisations can be categorised by colour. The spectrum ranges from "red", which represents organisations that are managed like a wolf pack ruled by fear to blue-green (Teal) organisations with several other categories in-between.

A Teal-type organisation has an intrinsic and deep *raison d'être*, and the members that make up the organisation are almost self-organising. There is no need for traditional "management" and they can be said to be similar to a living entity. This may sound good, however, for a large corporation with a pyramid-like structure in place, unfortunately this is an idealistic state that lacks realism and striving for this can lead to frustration and dissatisfaction within the company.

I would therefore like to bring forward a realistic option to achieving a resilient organisation which I call "management innovation" based on Triple-A management. I believe that continuous improvements of an organisation's Triple-A characteristics is the most solid way to achieve a flexible and strong people-oriented organisation.

As shown in figure 1, companies can strengthen "Triple-A" through 9 specific activities. Also, through these 9 aspects companies can analyse their current state to find out their strengths and weaknesses. The key point here is the "next step" after conducting such an analysis.

### Anchoring

In turbulent times, this becomes a base that unites the organisation. Corporate values, purpose (mission), and vision are important, but trust is the key to anchoring, especially among internal stakeholders. However, if trust is weakened, the MVV = Mission, Vision, Values set out by the company could in fact cause employees to lose motivation.

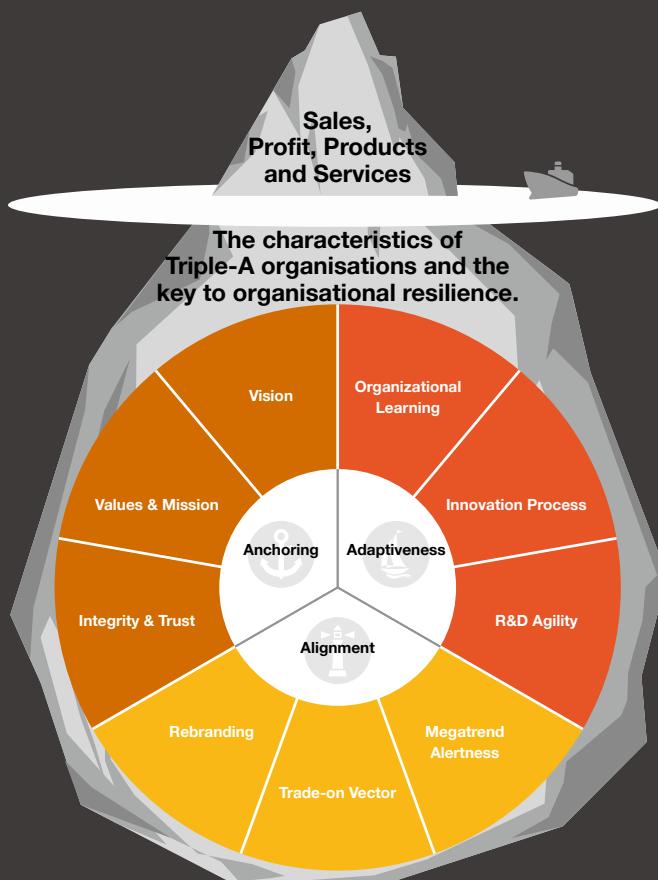
### Adaptiveness

This Refers to the organisation having structures and capabilities to continuously change itself. The key points here are to evolve into a stage of learning where innovation takes place in all levels of the organisation. For this to be possible the organisation must organise itself for innovation, and be agile in its approach to R&D and market expansion.

### Alignment

The most important factor and differentiator in the markets of the 21st century is to be able to align strategies with changing stakeholder expectations and demands as well as being able to understand and align oneself with society at large. It goes without saying that organised crime and anti-social forces is the very opposite of what society expects from companies, but alignment goes beyond this. It means having the vision and executing strategies to enable the elimination of negative trade-offs between a company's operations and society or the natural environment and instead creating positive "trade-ons", as well as well as embracing the concept of "brand identity".

Figure 1 An overview of Triple-A management





**Peter David Pedersen**

Director, TACL - The Academy for Corporate Leadership.  
Co-founder, NELIS (Next Leaders Initiative for Sustainability)

## The concept of management innovation

The term "innovation" is often translated into "technological innovation" in Japan, but it is necessary to be aware of the limitations of this way of looking at innovation. In 2005 the OECD published the "Oslo Manual" on innovation management which categorises innovation into four categories.

**Figure 2**

### The four categories of innovation according to OECD's "Oslo Manual"



I think this way of looking at innovation is very sound and useful, as bringing about innovation in one category means it is often necessary to connect with the other categories. I think this view often requires collaboration with other boxes in order to bring about innovation in one box. As an illustrative example, one leading French manufacturer set an innovative "business process" goal of reducing the carbon footprint of its factories by 30% in five years. To achieve this, innovations in the "management" box, such as the creation of new roles and responsibilities, updates in the evaluation criteria for variable compensation as well as extensions of payback periods for investments proved effective.

In my opinion, this type of "management innovation" is exactly what Triple-A management described above is about, and is also something that many Japanese corporations lack. In a rigid organisation employees lose track of their purpose, are unable to express their creativity and go about their work every day without any real sense of their "contribution to society", which should be a prerequisite for sales and profits. It is obvious that an organisation managed in this way has no chance of becoming a flexible and resilient organisation.

## Coming to grips with Management innovation

So, to actually bring about Management Innovation as seen through the lens of Triple-A management, what type of management approach should one take? I propose three specific steps as outlined below:

### Step 1

Do an unbiased analysis of your company based on the three concepts of Triple-A management. When doing this make sure to involve not only top management, but also get the opinions of mid-career employees in their 30's whose level of engagement tends to be low.

### Step 2

It is of course imperative to draw on the strengths of the company, but are the company's strengths really those as perceived by top management? As described in step 1 - the input from mid-management is therefore very important. For areas recognised as weaknesses - pinpoint their causes and severity through workshops and invest in time to come up with concrete ideas for improvement.

### Step 3

After discussions with management and senior management, tackle the issues where there is in-house capacity yourself and ask for external support where needed. Concentrate all your energy on solving these issues.

If your efforts with Triple-A management are half-hearted you will not see any results. Also, if you are not honest with your current status and pretend not to see any issues, problems will arise in the future as can be seen in many Japanese companies today.

Even if you work on management innovation through Triple-A, you will not see any effect. Also, if you do not look at the current situation of Triple A, and you "pretend not to see", future problems will occur, as seen in the below examples from Japan.

- The launch of new large business enterprises being delayed by 5-6 years.
- Sudden acquisition by a Taiwanese manufacturer.
- Neglecting taking measures against fraudulent behaviour and deficient products despite these issues becoming social issues over ten years ago with reoccurring incidents as a consequence.

On the other hand, if you take a whole-hearted approach towards Management Innovation it is possible to see the effects after just a year or two. I am certain that through an unbiased analysis at one's organisation, involvement of younger middle management, by facing sometimes inconvenient truths and by firmly sticking to these actions until they result in continuous transformation, it is possible to bring about transformation into a resilient organisation.

# Concluding Remarks

Japanese companies are currently seriously considering how to go forward in managing long-term value creation, and are going forward with a trial and error approach. However, the standard for evaluating short term and long term success is not necessarily the same, which sometimes causes contradictions to appear. Several executives still see sustainability initiatives as simply a cost and something that does not create value for the company.

However, our study of awareness and perception of sustainability among people working at large Japanese corporations has shown that awareness has been changing significantly over the past two years. In particular, the significant increase in the level of awareness of specific initiatives related to sustainability, such as the Sustainable Development Goals (SDGs) and ESG investment, is a major change in our opinion. And while management's leadership in showing the way for long-term management strategies is important, equally important is the long-term support for such activities by the companies' employees. We believe this increased level of awareness identified in our survey will have a major impact on the development of sustainability within Japanese companies going forward.

We at PwC believe that the transition from second-generation triple bottom-line CSR to third-generation Corporate Sustainability is indispensable for the development of management within Japanese companies going forward. We would therefore like to present three specific actions Japanese companies should consider taking when going forward on their sustainability journey. We strongly believe that the implementation of these actions will contribute to long-term value creation among Japanese companies.

## **Understand your position**

To understand your strengths and weaknesses, as much as possible, objectively analyse the needs of today, what other companies are doing and the needs and expectations of your stakeholders.

## **Implement strategic stakeholder management**

After identifying the influencers most relevant to your company, implement stakeholder management to establish active and collaborative relationships.

## **Establish strategies and make roadmaps towards third generation Corporate Sustainability**

Develop a corporate sustainability strategy that stimulates innovation, contributes to increasing corporate value, strengthens competitive advantages, and put the strategy into action through medium- to long-term roadmaps.

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## Survey methodology

To provide a more detailed analysis, the sample of our online survey was increased from 2,387 to 2,471 individuals. We also added questions to better understand the current state of Corporate Sustainability among Japanese companies compared to the previous survey.

Study area: Japan

Survey period: October 9 to October 11, 2018

Target population sample:

- Employees of listed Japanese companies (not including JASDAQ)
- 25-59 years old, both men and women.
- Full time employees (employees, section managers, department and division managers [executives excluded] )
- At least four years working for the current company.

	Employees & Assistant Managers	Section managers	Department managers	Total
Men	1,036	639	412	2,087
Women	338	37	9	384
Total	1,374	676	421	2,471

Source: 2017 Survey results taken from "Corporate Sustainability and the resilience of organizations: the road to new triple A management"(only available in Japanese)  
( <https://www.pwc.com/jp/ja/knowledge/thoughtleadership/2017/assets/pdf/corporate-sustainability1708.pdf> )



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