

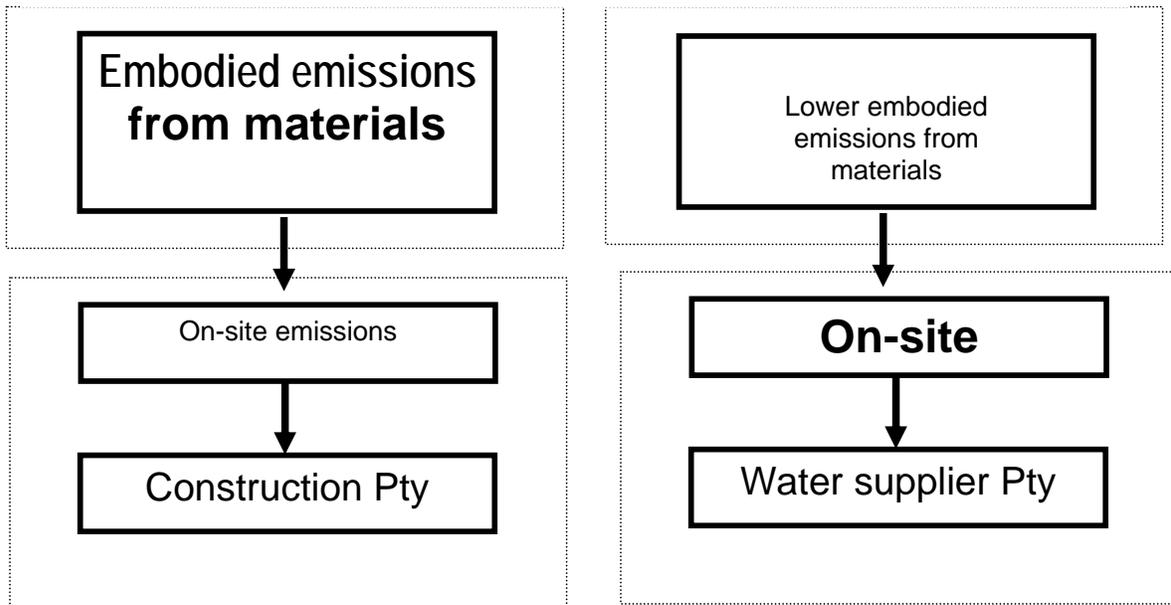


Supply chain thinking: the difference between making the right decision and the wrong one

Investors are entitled to a rigorous assessment of regulatory and financial risks related to climate change so they can evaluate which business plans are reckless and which are prudent in managing these risks. Ceres, Sept 2007 <http://www.ceres.org/NETCOMMUNITY/Page.aspx?pid=445&srcid=430>

Imagine you talked to a manager of an ethical investment portfolio. You hear that no urban water supplier is included in the portfolio. When companies were screened, water suppliers became ineligible because of their high greenhouse gas emissions stemming from water treatment processes. These emissions were seen as a financial risk under anticipated greenhouse taxes. You find that many construction companies are part of the portfolio, and that some of these use large amounts of aluminium. You look up how much electricity is needed to make aluminium, and estimate the greenhouse gases embodied in manufactured aluminium. To your surprise you find that some of the construction companies create a higher greenhouse burden than your own water company, and therefore are associated with a higher financial risk under future greenhouse taxes. The only difference is that the construction companies' risks are "hidden" in their upstream supply chains, which the investment manager overlooked (Fig. 1). Supply-chain accounting provides essential tools for good decision making.

Fig 1 Supply chain accounting reveals hidden risks



The supply-chain reporting challenge for Corporate Sustainability Reporting has been recognised for some time. Despite the current debate, however the issue has changed little since 2002 when it was reflected by the World Business Council:

“Current reporting practices are often performed within the boundaries of the reporting organization. In the coming years, it is likely that companies will increasingly report across the value chain. This will represent a new challenge in terms of reporting on the upstream (supplier related) issues linked to human rights, environmental and societal impacts, and also of coping with the wider downstream (consumer related) impact of products and services”. World Business Council on Sustainable Development (2002). Sustainable Development Reporting: Striking the Balance. Council on Sustainable Development, Conches-Geneva, Switzerland. P. 55. http://www.wbcsd.ch/DocRoot/GGFpsq8dGngT5K56sAur/20030106_sdreport.pdf, World Business



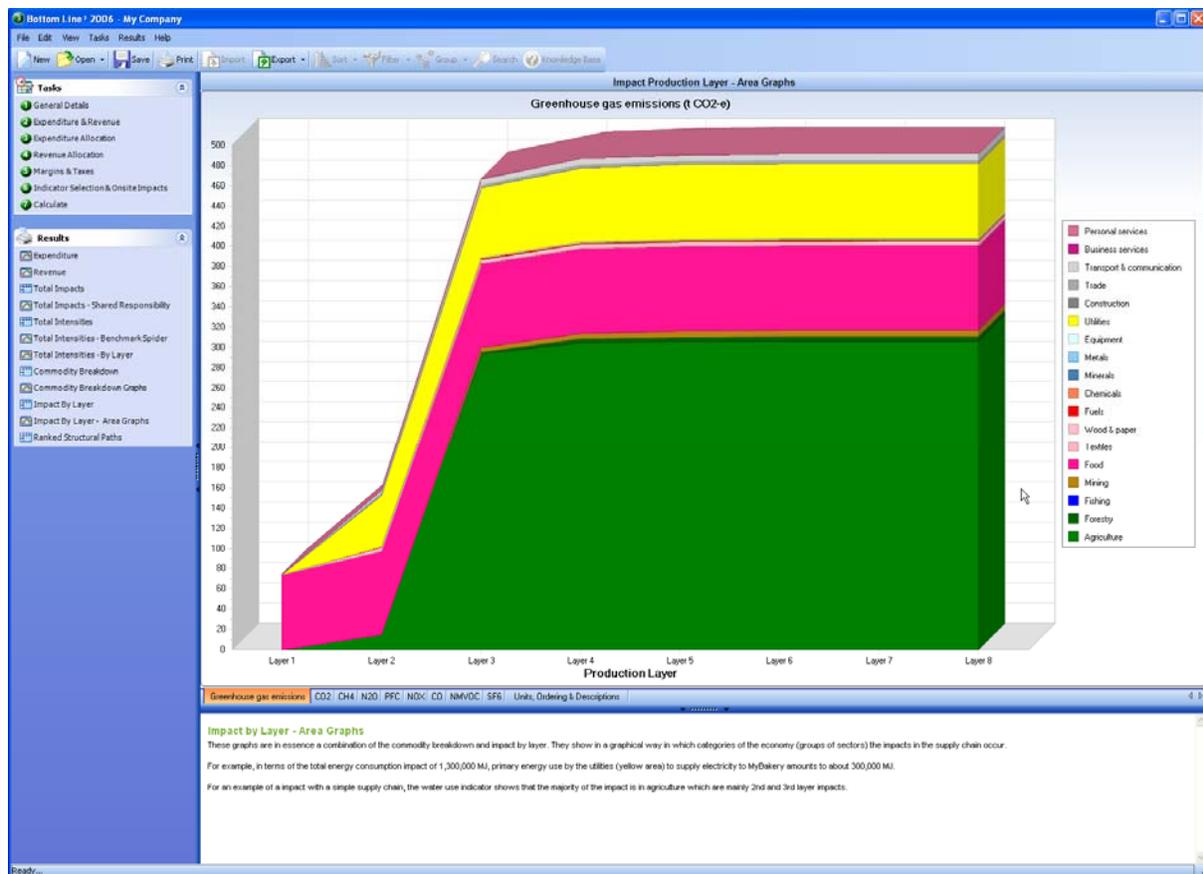
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Without supply chain thinking you run the risk of making not just a poor decision but the wrong decision. Just how crucial upstream disclosure is to the full picture of risk is evident in the graph below (Fig 2)¹. Along the x-axis are the production layers: layer 0 is the consumer; layer 1 is the company undertaking the Footprint analysis, in this case it is an organisation called *MyCompany*; layer 2 is *MyCompany*'s suppliers; layer 3 is the suppliers of the suppliers of *MyCompany*; and so on. The y-axis shows greenhouse gas emissions in tonnes (t CO₂-e).

The graph shows that *MyCompany* is directly responsible for about 70t of CO₂-e (layer 1). Approximately 85t of CO₂-e are contributed by *MyCompany*'s suppliers (layer 2). However a massive 305t of CO₂-e are contributed by the suppliers of *MyCompany*'s suppliers (layer 3).

This contribution could be missed in an analysis that only took in the first layer of suppliers. Depending on the organisation, major contributions can be hidden even further up the supply chain. Without this information you miss crucial opportunities to make decisions that will protect your company from flow on costs.

Fig 2 exposing the supply chain



According to the Australian Commonwealth Superannuation Scheme, the financial risks flowing from management of environmental impacts “have increased in line with the increasing number and severity of regulatory measures, and with changing market

¹ Example of graph generated by the BL³ Carbon Footprint software <http://www.bottomline3.com/documents/BL3CarbonBrochure.pdf>



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expectations. These risks are material to the financial position of many listed companies, or will become so in the near term.” The CSS goes on to say that disclosure of environmental risk is crucial to enabling assessment of financial risk and that in a “post Enron/HHW/Worldcom investment market climate, leading management thinking recognises transparency and disclosure as business assets”. Commonwealth Superannuation Scheme http://www.css.gov.au/news/2002/environmental_non-disclosure.html

Perhaps related to this is the suggestion that an increasing number of Australasian investors are choosing to invest their money in an environmentally and socially responsible manner. A survey conducted for the Australian Ethical Investment Association (EIA) found that at 30 June 2005 assets of socially responsible investment (SRI) managed funds in Australia had topped \$7.67 billion, an increase of almost 24 times since 2000²

The risk is well defined and understood. Investors, it seems, are aware of the issue and in many cases are willing to act on their understanding of the risk and their belief in environmental responsibility. What is still missing is a universally accepted standard of reporting that will expose the full upstream supply chain as well as providing a comprehensive onsite account of doing business. While some organisations continue in their belief that supply chain thinking is only about better numbers those that understand the issue know that it is fundamentally about making **the right** decisions.

With this understanding and the right tools organisations are not waiting for standards they are seeking out the best available methodologies and are confident that this will give them a strategic advantage in the market place. However unless you really know your supply chain it can backfire. Take the case of Tesco in the UK. In 2007 Tesco announced a £500m investment in a ‘carbon calorie counter’ to carbon label its produce. It pledged to deliver a ‘revolution in green consumption’³. In 2008 Tesco was facing attack over its carbon footprinting which some organisations said amounted to greenwash because it severely underestimated its true contribution to climate change⁴.

In Australia the Australian Competition and Consumer Commission⁵ has recently queried business claims about levels of greenhouse gas emissions. The ACCC has advised consumers to question claims about carbon emissions and ask producers if calculations take into account the whole life cycle of the product.

“Firms which make environmental or ‘green’ claims should ensure that their claims are scientifically sound and appropriately substantiated. Consumers are entitled to rely on any environmental claims you make and to expect these claims to be truthful. Not only is this good business practice; it is law. The Trade Practices Act 1974 (the Act) states that businesses must not mislead or deceive consumers in any way, and it carries serious penalties for businesses that fail to meet these requirements.”⁶

Supply chain thinking and the tools that support it underscore today’s sound decision making. They will ensure that your efforts to account openly for your ghg emissions do not backfire. Other organisations seeking advantage in the market place will never be able to accuse you of greenwash. In fact supply chain thinking will always give *you* the advantage.

² Sustainable Responsible Investment in Australia – 2005 Benchmarking Survey, EIA, October 2005).

http://www.epa.vic.gov.au/bus/unep/finance_sector.asp#investment

³ <http://www.independent.co.uk/news/business/news/tesco-invests-163500m-to-create-green-consumer-revolution-432797.html>

⁴ <http://www.planet2025news.net/ntext.rxml?id=4943&photo=>

⁵ <http://www.accc.gov.au/content/index.phtml/itemId/142>

<http://www.accc.gov.au/content/item.phtml?itemId=810050&nodeId=69646a6d15e7958a41b40ab5848c6968&fn=Green marketing and the Trade Practices Act.pdf>

⁶ <http://www.accc.gov.au/content/item.phtml?itemId=810050&nodeId=69646a6d15e7958a41b40ab5848c6968&fn=Green marketing and the Trade Practices Act.pdf>