Sustainability: Water as a Business Risk

Mazars Global Water Risk Survey Results

2018 GLOBAL WATER DAY EDITION
A growing number of stakeholders are sensitive to water risks, largely as a result of media coverage of some of the water related events that have affected millions of lives in the last few years or simply because of concerns that demand for this critical resource is under tremendous pressure due to an ever increasing population.

The corporate world is a water stakeholder exposed to the same risks, and yet you rarely hear or read about this risk being assessed and managed by corporations, with the exceptions of leading fortune 500 organizations. We are herein contributing to the discussion of water as a business risk, its assessment, materiality, and reporting.

We conducted, with the support of YouGov, a global survey of c-level executives across all sectors, all company sizes, and across seven countries that represent some of the major economies and countries with important water challenges: France, United Kingdom, China, Spain, Germany, India, and United States of America. The survey contains 61% of business with revenue less than $50 million, qualified as small business; 21% of business with revenue ranging from $50 Million to $1 Billion, as mid-size; and 11% of business with revenue more than $1 billion, as large business.
For a large majority of the 665 respondents, more than two out of three assess water risk as more critical than average. Most countries surveyed present similar profiles with less than 5% of respondents considering this risk as below average. The United Kingdom stands out as an outlier with risk being considered the less critical compared to other countries (only 33% responded above average) and with the biggest population (16%) assessing this risk below average. On the other end of the spectrum, China and India were the two countries where the risk was deemed the most critical. For 69% of the respondents, water related events will significantly affect global business either now or in the next 10 years. In terms of the long-term perspective of planning and potential capital projects required, this is an important issue for companies that needs immediate attention.

Key risk types

Business risk refers to the possibility that a company will experience lower profits or lose value as a result of events, circumstances, actions, or inactions. As the world become ever more sophisticated, we benefit from technology advances, and externalities evolve, we include an ever growing number of factors to the list of those impacting business risks. Water has emerged as one of these factors and it affects all commonly accepted risks: strategy, compliance, financial, operational, and reputational. The top risks when it comes to water are:

Environmental impacts:
For decades, water has been a critical resource for industrial processes as cleaning material, for the energy industry as a cooling fluid, for any agricultural operations as a nutrient, and in many other industries. At the end of all these processes there are discharges in natural water ways, i.e. rivers, aquifers, or oceans. The chemical make-up, temperature, and density of these discharges affect the environment daily, and potentially create liabilities.

Supply chain dependence:
Without a proper understanding of a company’s operational dependance on water, or of their suppliers to water sources that might be stressed, a company should plan for capital projects in areas that will be impacted by the effect of changes in water, or find its operations at a full stop due to unprecedented climate conditions. In both cases, the lack of consideration for the dependence on water will ultimately destroy value for shareholders.

Social responsibility:
There is mounting market pressures (investors, regulators, customers, etc.) for corporates to be focused on the greater good for our planet and society. In the water sector, the need to produce more with less water in order to reduce corporates’ pressure on global demand and therefore price of water is a prime example. Businesses that neglect this call for greater water efficiency are exposed to major reputational risks.

When do you think global water related events will significantly impact global business, if ever?

87% Will impact
25% Immediate impact

How do you evaluate today’s global water risk?
69% Critical
6% Low risk

Currently, to what extent do you think that shareholders and financial markets are properly valuing and/or rewarding good water management and stewardship?

All shareholders and financial markers do so
17%
Some of the shareholders and financial markers do so
29%
Not enough shareholders and financial markers do so
33%
None of shareholders and financial markers do so
12%
I don’t know
10%

Business with less than $50 Million revenue
All shareholders and financial markers do so
9%
Some of the shareholders and financial markers do so
22%
Not enough shareholders and financial markers do so
40%
None of shareholders and financial markers do so
16%
I don’t know
13%

Business with More than $1 Billion revenue
All shareholders and financial markers do so
36%
Some of the shareholders and financial markers do so
43%
Not enough shareholders and financial markers do so
14%
None of shareholders and financial markers do so
7%
I don’t know
0%

Almost half of respondents to our survey consider that financial markets and shareholders properly value and reward good water management and stewardship. However, we note that the results are consistent with our expectations and that mid-size and larger companies (with more than $50 million revenue and beyond), which have embraced earlier sustainability practices and reporting, perceive value in these processes and procedures. The smaller and very small companies (with less than $50 million revenue) are significantly less convinced by the value of implementing water management best practices.
The majority of respondents across countries find water risks and impacts reporting insufficient at best. We note that interestingly enough the results for China and India were much more geared toward a positive appreciation of practices in these reporting areas in today’s global corporate reporting & communication. It is further interesting to note that these same two countries, when asked what should be driving reporting on water risks and impacts, selected that it should be ‘a must have’.

Otherwise the larger majority across all countries considers that this reporting and communication should be “required by law”. These two choices topped the third one, which calls for standardization as the most important. This is a very important argument in the financial reporting arena that the most critical is for end users of corporate reporting to be able to compare peers in similar sector or across sectors.

We are seeing that institutional investors are looking for quoted companies to report more meaningfully on the non-financial aspects of their business; in particular on ESG issues including water. This is not only for compliance purposes; they have seen that those companies that properly address these issues are more profitable over the longer term.

Richard KARMEL, Mazars Partner, London

How do you think that water risks & impacts reporting should be in corporate reporting & communication?

- A must have: 27%
- Something to be required (by law, by public opinion, company annual reports etc.): 37%
- Something to be standardized: 24%
- Something optional: 6%
- Unnecessary: 1%
- I don’t know: 5%

From all the results to most of the questions, we understand that there is a real call for action in the area of measuring impacts and assessing risks. The actions might differ between the large corporates and the smaller ones, with the later ones looking for further guidance and directions. Through a number of questions, we tried to assess who should be driving better water engagement practices. The first two choices are clearly corporate leaders just as much as regulators, followed very closely by international organizations. This confirms our views that how well these water risks will be managed will differentiate good from greater leaders.

Which three roles are most effective in pushing forward better water engagement practices?

- Corporate leaders
- Regulators
- International & local organizations

What could be the top most significant drivers towards proper water risks management practices?

- Regulation
- Practice benchmark
- Reporting standard

It is equally interesting but somewhat surprising to see that investors are not expected to play a major role. As the ultimate users of the non-financial information, we would expect them to drive and require adoption of water risks and impacts reporting practices. International Organizations ranking in third place illustrate an important level of sophistication and understanding of where some of the concepts around sustainability have been bourgeoning for the last 10 to 20 years, specifically with the role of the United Nations.
Despite clear recognition that water is an important risk not only for survival and society, but almost just as significant for the corporate world, financial executives and professional investors. The latter does not seem to be equipped with the proper tools to include this risk in evaluating companies or projects.

Jerome DEVILLERS
Mazars Partner, New York

Tools to Filter Risks

What will be the most helpful tool to price or assess water risks?

<table>
<thead>
<tr>
<th>Tool</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>Standard water risk index</td>
<td>36%</td>
</tr>
<tr>
<td>Custom made risk model</td>
<td>20%</td>
</tr>
<tr>
<td>Financial market data (Stock price, water index, etc.)</td>
<td>14%</td>
</tr>
<tr>
<td>Insurance premium data</td>
<td>10%</td>
</tr>
<tr>
<td>Other</td>
<td>1%</td>
</tr>
<tr>
<td>None of these</td>
<td>4%</td>
</tr>
<tr>
<td>I don’t know</td>
<td>16%</td>
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</tbody>
</table>

If on every other topic the results of our survey provided very clear trends for the entire population and highlighted geographical differences, the responses to our question as to what tool would be the most helpful, responses were all over, including an important number of “I don’t know.”

Water is a critical yet an under-managed resource for most businesses. This is probably because of the cost of water, which varies from none to minimal today. The insignificance of this cost shades many executives and boards from the real value of water to their businesses. Leaders of tomorrow have to consider water as a business risk, and include water in risk management practices, sustainability programs, and discussions and communications with stakeholders. This will be a key factor in the judgment of their leadership and legacy.

Jerome DEVILLERS
Mazars Partner, New York

Stay Tuned for Our Next Edition

We are excited to share with you these key results on the 2018 World Water Day. There are more exciting and insightful discoveries, that we will be very happy to share with you in the coming months, including detailed results and analysis by countries, sectors, and business sizes among any other interesting perspectives.

So stay tuned to our Mazars water experts, or Mazars Business For Good™ on www.mazars.com
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