



# Corporate Social Responsibility in Spain

Sustainable companies, Competitive economy



# Report

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### Sustainable companies, Competitive economy



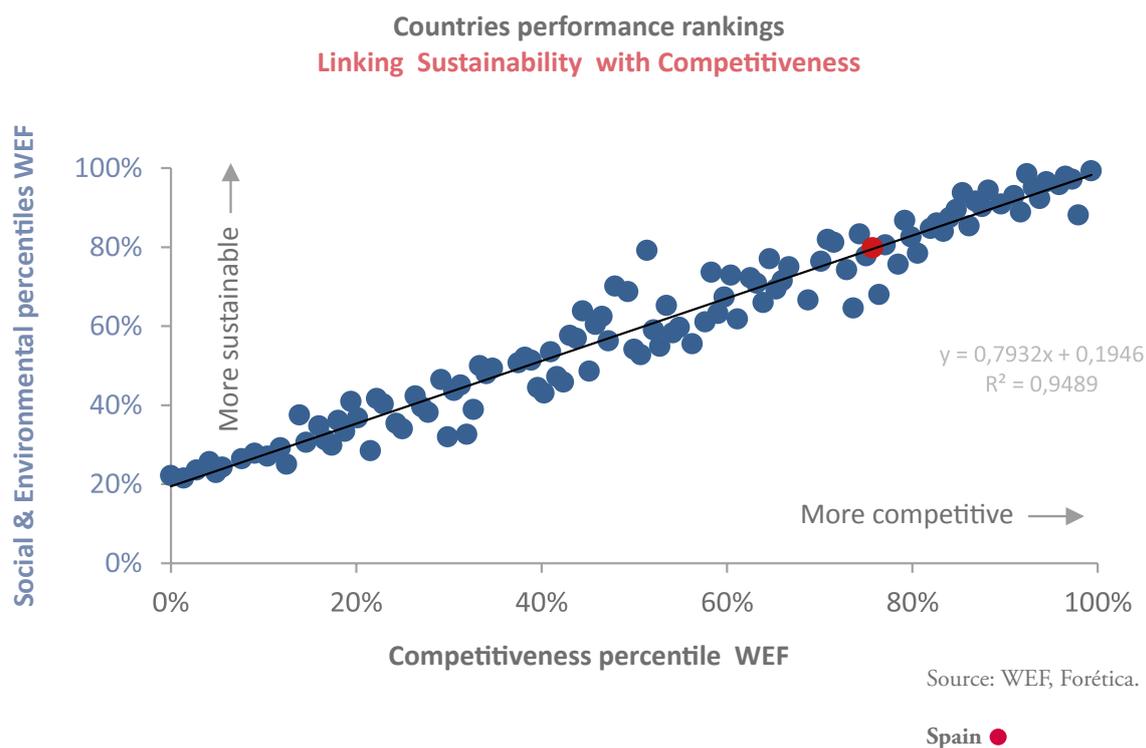
## EXECUTIVE SUMMARY

### About the Research

This executive summary contains the main findings of the research study carried out by Forética for Marca España about the state of the art of sustainability amongst Spanish companies. The report covers the cornerstones of value creation through CSR. It finds positive and direct correlations between sustainability and competitiveness at macro level. The study takes a close look at the penetration of CSR policies and management tools in medium and large Spanish companies. It measures the impact of CSR policies on key financial indicators, positively showing that sustainability acts as an enhancer of financial performance. A back-test of investment strategies focusing on optimizing ESG criteria within a 15 year period for Spanish listed companies would have outperformed the market with higher returns vis-à-vis a lower risk for across sustainable portfolios. Finally, the study takes a look at the potential of CSR with regards to international trade, revealing that Spanish trading partners tend to have high scores in sustainability, implying that CSR can play key role in improving the attractiveness of Spanish goods and investment opportunities.

## Sustainability, a driver for competitiveness

The extent to which countries embed Sustainability Policies can have a cross-cutting positive impact on competitiveness. When analyzing country competitiveness rankings against their sustainability scores, a highly positive and direct correlation emerges. This suggests that there is a deep link between the two<sup>1</sup>. Though the aim of this research is not to demonstrate causality with a statistical certainty, it can be asserted that the countries with highest scores in sustainability tend to be the most competitive and vice-versa. This supports the business case for sound sustainability policies at the country level.



## The three arrows of CSR made in Spain

Spain, at macro level, is positioned at the top quartile of sustainability performers yet shows a high potential for improvement. Spain's high performance on CSR is based on three pillars, which make sustainability a robust trend with an encouraging future. These three arrows appear in order of their contribution: (i) A set of large companies leading in the field of sustainability; (ii) Strong private and public institutional support and (iii) High exposure to sustainability-sensitive sectors across the economy.

### Arrow 1: High standards in Sustainability

Spanish companies show a high penetration rate of sustainability practices. 9 out of 10<sup>2</sup> large and medium sized businesses in Spain have adopted CSR policies and deployed advanced management practices for sustainability. Some objective measures illustrate the leading role of Spanish companies towards CSR practices:

<sup>1</sup> To test the consistency of these correlations, this exercise has been conducted using different ranking to avoid autocorrelation. For the calculations the authors have used the World Economic Forum benchmark for competitiveness. Sustainability scores have been extracted from the WEF Social and Environmental Rankings (shown in chart 1) and from RobecoSAM's ranking of sustainable countries.

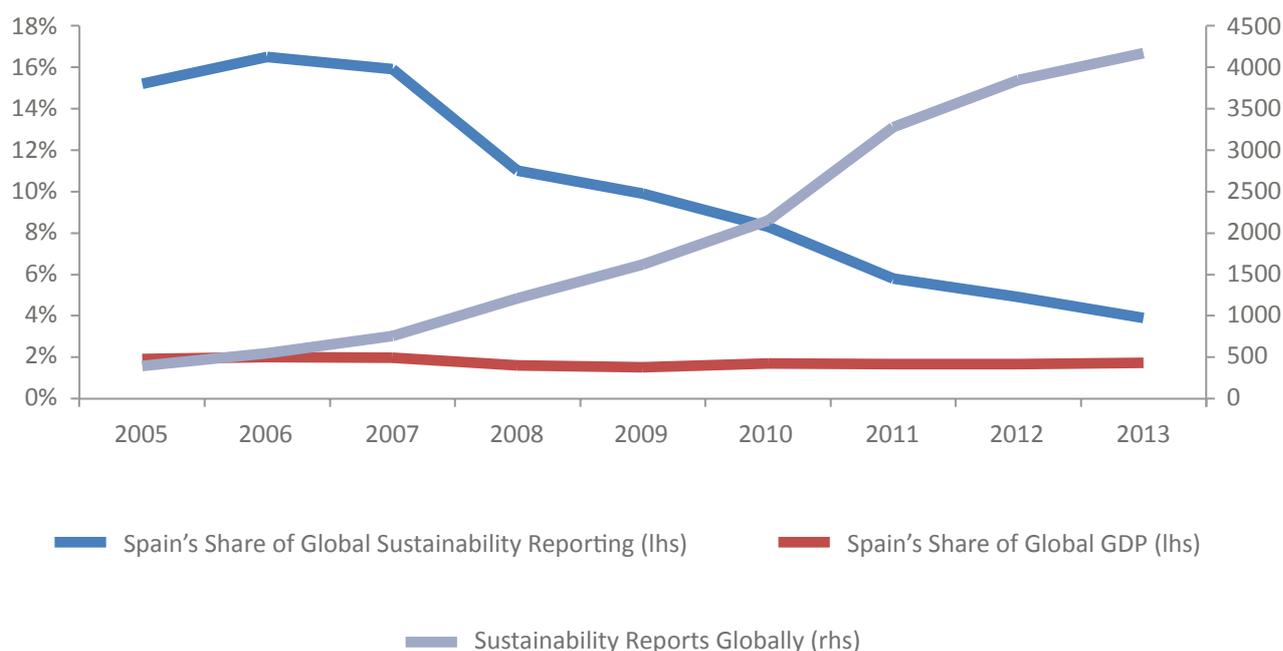
<sup>2</sup> Source: Forética Report 2011. Survey on the state of CSR in Spain. N= 1.037 respondent companies.

- **UN’s Global Compact support:** Spain is the global leader in terms of companies committed to the United Nation’s Global Compact initiative which has over 16 hundred organizations as signatories.

- **Sustainability Reporting, quantity plus quality:** Spain’s share of Sustainability Reporting is twice as large as its share of global GDP. This figure has diminished significantly as other countries have caught up to the trend. On the other hand, the quality of the reports issued by Spanish firms is 11% higher than the European average and 34% higher than the global score, according to KPMG’s survey<sup>3</sup>.

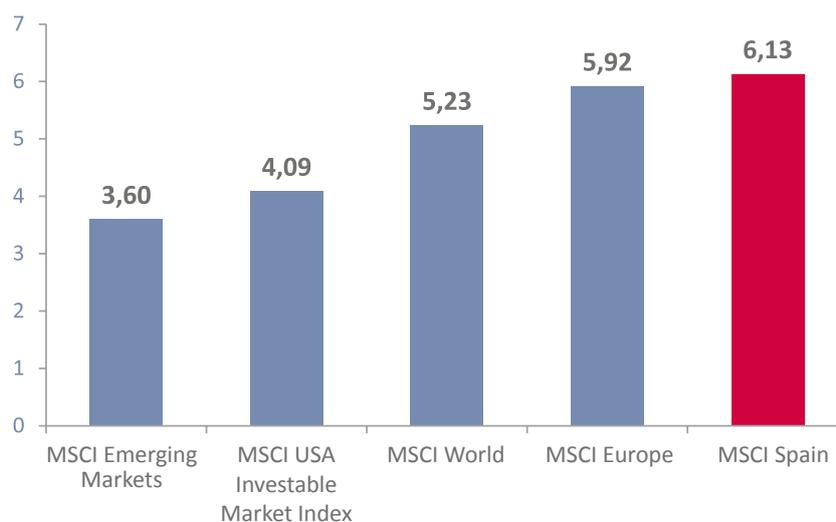
- **International ratings favorable to Spanish sustainability titans.** Spanish companies listed in the MSCI World ESG score 17% higher than the global average and 4% above its European peers on ESG. On the other hand, 20 companies are featured in RobecoSAM’s Sustainability Yearbook (2015), 13 of which are at the forefront of their respective sectors, falling into the gold, silver and bronze categories. In the last 5 years of this indices’ edition, 70% of Spanish companies were included in the top categories previously mentioned. The universe of Spanish listed companies represent the 8th most sustainable stock market according to Corporate Knights Capital, and has held the number one position for some time.

### Spain’s footprint on sustainability reporting



Source: GRI, World Bank, Forética.

<sup>3</sup>The KPMG Survey of Corporate Responsibility Reporting 2013. December 2013.

**Average sustainability rating per region**

Source: MSCI ESG Research.

**Arrow 2: Private and Public Institutional Support**

From the public institutions standpoint, CSR has been an ongoing theme since the creation of the first CSR Expert Panel in 2002. In 2008, Spain created the State Council on CSR to advise the government on policy and regulation regarding sustainability. This Council integrates national and regional administrations, employer federations, trade unions, and sustainability experts. Spain's CSR Strategy was approved in 2014. On the other hand, private institutions ranging from foundations to NGOs, have provided support and expertise to corporates in Spain accelerating the rate of adoption of CSR policies. Ten sustainability-themed outfits with an average of 10 years of experience have pioneered knowledge and tool development as well as acted as trend setters in regards to the integration of sustainability within companies' core competences. Finally, the media in Spain has been systematically covering CSR news for the last decade with six incumbent news providers specialized in sustainability issues.

**Arrow 3: Exposure to sustainability sensitive sectors**

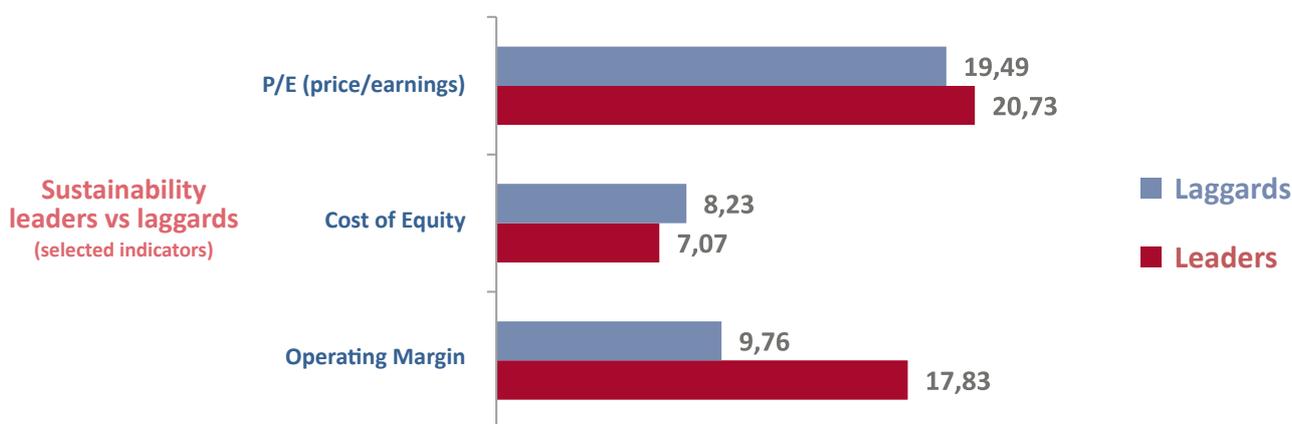
The composition of the business sector in Spain includes a large portion of companies in sustainability sensitive sectors. This creates the need to anticipate developments related to sustainability mega-trends, such as climate change, aging population, water scarcity, sustainable infrastructure or clean energy. Tourism, Food and Beverages, Healthcare, Renewable Energy and Infrastructures, are some of the leading industries where sustainability might have a significant impact on long-term prospects. Some of these sectors are at the same time a great source of exports, from Smart-city Solutions, to energy and water technology worldwide.

**CSR as a value enhancer for firms**

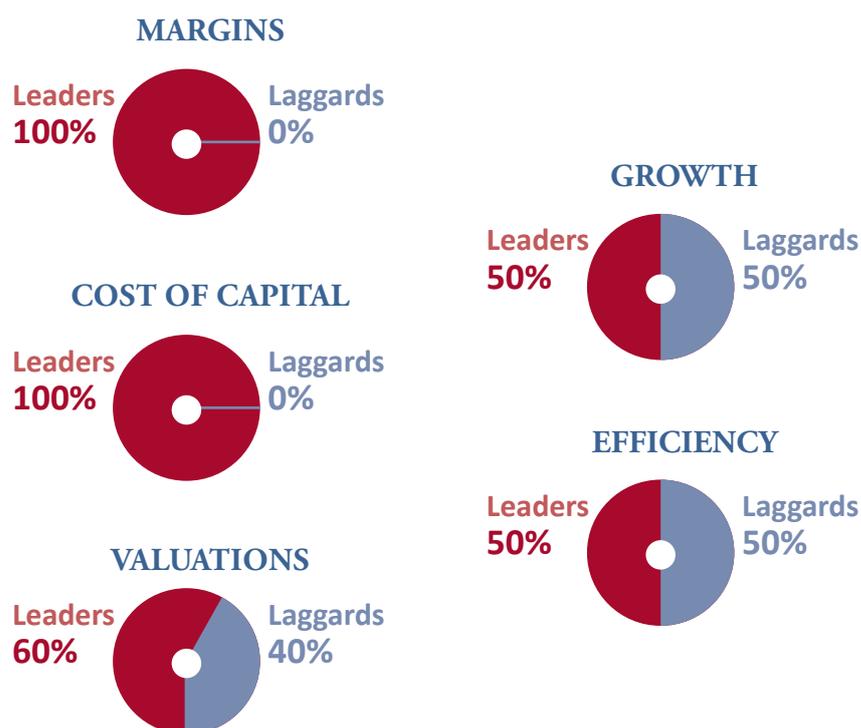
This report has looked at sustainability and enterprise value creation under two different- although related- perspectives: the relationship between high scores on sustainability performance and key financial indicators on one end and the impact of ESG scores on investment performance on the other. Not surprisingly, both analysis confirm each other highlighting that sustainability is in fact an enhancer of enterprise value.

### Sustainability passes the stress-tests with honors

Two control groups have been analyzed through a set of 16 long-term financial indicators –5-year averages have been used when appropriate. The *Sustainability leaders*, on the one hand, are the 15 Spanish listed companies which MSCI ESG has rated A or higher at the time of the analysis (June 2014). The *Sustainability laggards*, on the other hand, are the remaining 15 companies with a rating of BBB or below. The results strongly support the business case for sustainability. *Sustainability Leaders*, on average, outperform in all three profit margin dimensions (gross, operating and EBIT margins), as well as all four cost of capital dimensions (Unlevered Beta, Market Beta, Cost of Equity and Weighted Average Cost of Capital). They also beat their *less* sustainable peers on three out of five valuation metrics (beating on P/E, Price to Cash Flow and analyst’s recommendation, and underperforming on Price to Book Value and Price to intangible book value). A neutral relationship is seen on long term growth (beating on earnings per share growth and underperforming on sales growth rates) and Balance Sheet efficiency (higher Returns on Equity and lower Returns on Assets).



Source: MSCI ESG Research, Reuters, Bloomberg, Forética.

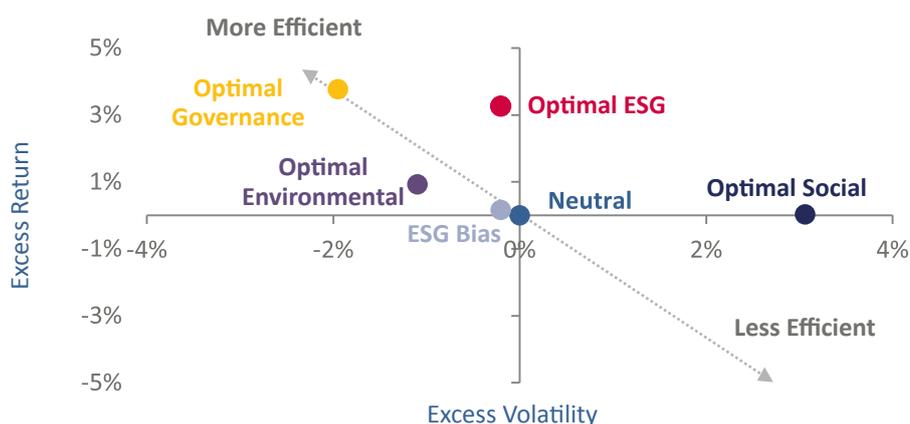


Source: MSCI ESG Research, Reuters, Bloomberg, Forética.

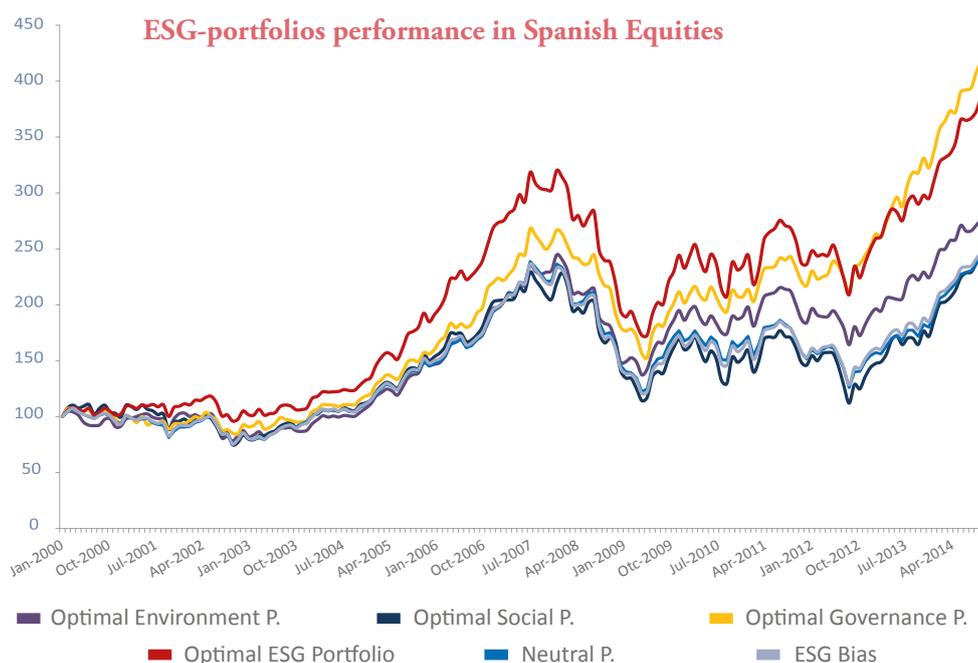
### Investment in Spain through ESG glasses. A “bigger bang for the buck”

A second analysis was conducted by back-testing the 14- years- performance of stock portfolios with different ESG profiles beginning in January 2000. Six investment strategies were applied- all subject to certain technical restrictions<sup>4</sup>. (1) *Neutral portfolio* –where no ESG is taken into account for portfolio construction- (2) *ESG-tilt portfolio* – where assets are weighted according to the individual contribution to the ESG score of the investable universe – (3) *Optimal Environment Portfolio* – where assets are weighted in order to maximize the environmental score of the portfolio- (4) *Optimal Social* - maximizing the social score of the portfolio- (5) *Optimal Governance Portfolio* – maximizing the governance score of the portfolio – (6) *Optimal ESG Portfolio* – where assets are weighted in order to maximize the total ESG score of the portfolio. The results not only confirm the findings of our analysis of key financial indicators but provide further support for the investment case of SRI. From a financial return standpoint, all ESG-driven portfolios outperform the *neutral* allocation. On the other hand, all but one (namely the *Optimal Social Portfolio*), experience equal or less volatility than the *Neutral portfolio* making them more efficient. Furthermore, two interesting findings emerge from the data. Optimizing ESG improves returns as much as 3.26% per annum and is the winning strategy 85% of the time span analyzed. When a rare event occurs –namely the restructuring of parts of the financial stocks as in the sample of 2012- the governance factor takes over outperforming all other strategies. This is an indication of the degree of sophistication when using ESG analysis among investors and the importance for companies to embed sound CSR practices.

#### ESG strategies efficiency versus benchmark



#### ESG-portfolios performance in Spanish Equities



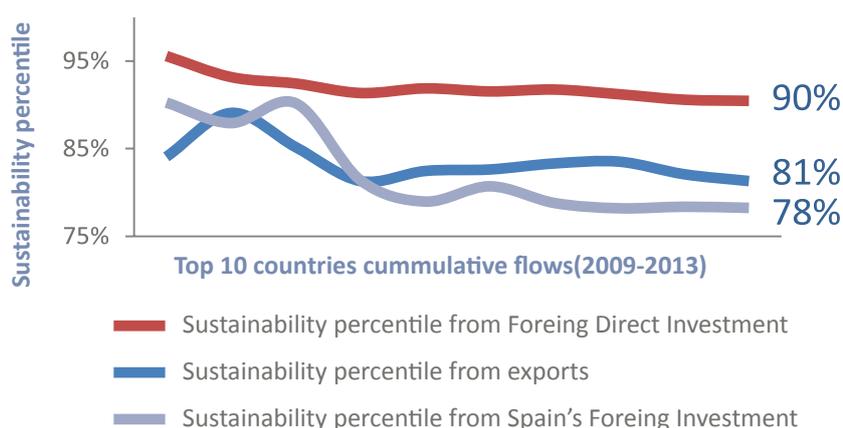
Source: Forética, MSCI ESG Research.

<sup>4</sup> Restrictions applied: All portfolios must hold all stocks listed at any given time. The maximum weight for a single asset must be less or equal to 4 the weight of a single stock as a simple not-capitalization –weighted average. The minimum weight of a single asset should be equal or higher to 0,5%.

## Sustainability and International Trade

One of the novelties brought out by this report is the analysis of the potential impact of *the sustainability factor* on international trade. To illustrate that possible outcome, the report analyzes the sustainability profile of the top 10 trading partners for Spain in the five year period between 2009 and 2013 on three dimensions: foreign direct investment, exports and Spanish investment outflows overseas. The weighted average percentile for the top ten countries that deploy investments in Spain is 90. This group of countries –that accounts for 86% of total foreign investment in Spain- represents the top-level of sustainability at the macro level. When analyzing Spanish exports overseas, these top-ten countries represent an average percentile of 81, still a very high score when it comes to sustainability. This gauge shows greater dispersion and accumulates only 64% of total exports. Finally, Spain's investments overseas score at a 78 percentile, gathering 73% of the bulk of capital deployed. Despite the fact that international transactions do not explicitly state a particular sustainability goal, linking this concept to international trade is valuable. The ability to generate sustainable investment opportunities for high performing countries in the field could improve Spain's attractiveness for international investors. The same logic works for the other two dimensions. Adding the sustainability factor to the export of goods can enhance the competitiveness especially in those sustainability demanding countries that, at the same time, tend to be the most competitive. Finally, commitment to CSR can help companies to improve Spanish companies' reputation and acceptance in foreign markets.

### Sustainability percentile of Spain's main trading partners



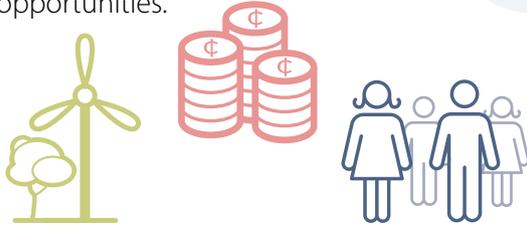
### Foreign Direct Investment in Spain 2009-2013 (thousand €)

Country	Volume	% Cummulative	# Sustainability
Netherlands	21.349.853	27%	5
Luxembourg	13.530.593	44%	12
United Kingdom	11.838.941	58%	11
France	6.937.970	67%	18
Germany	5.175.972	73%	3
United Arab Emirates	3.586.847	78%	16
Switzerland	1.793.379	80%	1
Portugal	1.759.521	82%	32
Brazil	1.633.599	84%	39
USA	1.618.618	86%	17

Source: Forética, ICEX.

## TRIPLE BOTTOM LINE

A balanced approach between economic prosperity, social welfare and environmental preservation, provide a solid anchor to face the world's prominent challenges and the competences to seize its opportunities.



## COMPETITIVENESS

There is a high direct correlation between countries competitive positions and their sustainability scores.



## ROI OF INVESTING IN SPAIN SUSTAINABLY

Applying ESG criteria when investing in Spain yielded a more efficient risk-reward since the beginning of the millennium.



CSR

Report  
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## CSR AND INTERNATIONAL TRADE

Sustainability as a differentiation factor toward trading partners:

-90: is the percentile in sustainability of the top-10 countries investing in Spain.

-80: is the percentile in sustainability of the top-10 countries as destination for Spanish exports.



**SUSTAINABILITY**



**COMPETITIVENESS**

**INSTITUTIONAL SUPPORT**

Spain has a favorable public and private institutional fabric creating capacity and incentives for a sound performance in sustainability.



Public



Private

- ✓ State Council for CSR
- ✓ Spain's National CSR strategy
- ✓ Business and Human Rights Plan
- ✓ Sustainable Economy Law
- ✓ CSR Law in the Extremadura region

More than 10 leading institutions promoting **CSR** across Spain.



**SUSTAINABILITY IN SPAIN:**  
Competitive economy



**SUSTAINABILITY TOP PERFORMERS**

Large companies are regarded as sustainability leaders:

- Outperforming the world average on ESG ratings by **17%** and quality of reporting by **34%**
- **8th** most sustainable stock market listing in the world.
- Global leader in terms of companies committed to the United Nation's Global Compact initiative.



# CSR Conclusions

This report finds strong evidence of a solid link between sustainability and CSR practices with competitiveness, both at the macro– through the enhancement of competitive drivers across the board with a potential to have a positive impact in the balance of payments – as well as the micro-level – having positive impact on financial performance, value creation and on the risk-reward relationship of investments. Spain is seen at the lower end of the top quartile in terms of sustainability, but shows very strong pillars to build upon. This includes a top notch group of large and medium companies leading in different parts of the sustainability spectrum, a supportive public and private institutional landscape, and the exposure to sustainability-sensitive sectors. All these elements can be encouraging, but a more-coordinated approach towards showcasing the quality of Spain’s CSR practice as a brand attribute of “CSR made in Spain” can yield greater benefits for the economy, its society and its environment as well as to the people of Spain.

## Workshop team

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