
COURTESY GAP INC.

# UNLOCKING THE VALUE OF SASB STANDARDS

Gap Inc.

Gap Inc. is a leading global apparel retail company based in San Francisco, Calif. The company currently has more than 3,300 company-operated stores and more than 500 franchise stores and, during fiscal year 2018, the company generated $16.6 billion in revenues. In addition to its namesake brand, Gap Inc. also includes a variety of iconic apparel brands including Old Navy, Banana Republic, Athleta, Intermix, Janie and Jack, and Hill City. The company trades on the New York Stock Exchange (NYSE: GPS) and is a component company of the S&P 500.

> "WE WANT TO ENCOURAGE DIALOGUE WITH INVESTORS ABOUT HOW OUR PRODUCTS AND PRACTICES CAN CONTRIBUTE TO A MORE RESILIENT FUTURE FOR GAP INC., AS WELL AS FOR OUR CUSTOMERS AND THE COMMUNITIES IN WHICH WE OPERATE."
>
> – Victor Wong
> Director of Global Sustainability, Gap Inc.

Since Gap Inc. was founded in 1969, the competitive dynamics within the apparel industry have changed almost as much as the fashions on its shelves. Today, in addition to traditional value drivers such as economies of scale and brand recognition, the industry faces new and rapidly evolving demands related to a variety of emerging sustainability factors.

For example, apparel makers rely heavily on natural fibers such as cotton that are susceptible to volatile shifts in availability and pricing due to climate-related weather patterns, water scarcity, and the shifting economics of competing resources. Meanwhile, labor conditions in the apparel supply chain have come under increasing scrutiny as most apparel is manufactured in developing countries where economic growth is booming but safety laws and standards have not always kept pace—exposing companies not only to ethical dilemmas and reputational risks, but also the potential for increased cost or lost revenue from production disruptions.

For companies like Gap Inc., modern risk management means effectively addressing supply constraints, social and environmental externalities, and other sustainability factors through product and process innovations, engagement with business partners, and strategic planning with a long-term lens. Effectively managing these environmental, social, and governance (ESG) issues is particularly important for customer-facing companies whose brand value, market share, and revenues are often a function of customer perception.

For these and other reasons, Gap Inc. integrates key ESG issues into its core strategy, helping manage impacts to its business operations through initiatives such as responsible water stewardship, designing sustainable products, improving supply chain working conditions, and maintaining environmentally efficient operations. It's not just about being a "responsible" corporate citizen—although that's important to the company—it's also about optimizing business performance over the long run. As Chief Financial Officer Teri List-Stoll has said, "Integrating sustainability into our business benefits us in many ways. From building a talent pipeline through our This Way Ahead program's proven return on investment to optimizing costs as we address climate change and water risks within our sourcing strategy, we're seeing the benefit of building a more inclusive and resilient company."

## WHY SASB?

Gap Inc. issued its first corporate responsibility report in 2003, adopted the Global Reporting Initiative (GRI) framework in 2004, and today produces a robust, multi-faceted sustainability report each year. The company's 2017 Global Sustainability Report followed the GRI Standards (core option) and addressed the UN Global Compact's 10 principles, six relevant Sustainable Development Goals (SDGs), and—for the first time—included the SASB standards. The company also separately discloses to the CDP in alignment with the recommendations of the Task Force on Climate-Related Financial Disclosures (TCFD).

Given the maturity and sophistication of its sustainability reporting, Gap Inc. wasn't necessarily looking to add another reporting framework to the mix. However, the unique focus of the SASB standards, which address only the subset of ESG factors likely to have material financial impacts on a company, "seemed liked the right framework to support something that would be additive to what we were already doing," said Victor Wong, Director of Global Sustainability. Gap Inc. was drawn to SASB standards in part because it recognized that driving a fragmented, highly competitive industry toward more sustainable practices would require coordinated, industry-wide efforts on key issues with focused tracking of progress. For this and other reasons Gap Inc. engaged with SASB early and often—starting with participation in SASB's industry working groups in 2014—and chose to report in 2018 because of the credibility, investor backing and research that had gone into developing the standards.

The company also viewed the standards as a way to communicate more effectively with investors about its sustainability programs and performance. "We want to encourage dialogue with investors about how our products and practices can contribute to a more resilient future for Gap Inc., as well as for our customers and the communities in which we operate," Wong said, pointing to SASB's Investor Advisory Group (IAG) as a key indicator that the standards have strong support among the investment community. To help direct investors to this information, the company references its sustainability report in its most recent 10-K filing with the U.S. Securities and Exchange Commission.

## BUILDING ON A STRONG FOUNDATION

Gap Inc. has long been a data- and information-driven company, rooting its decision making in hard numbers, setting performance targets, and measuring progress against them. For example, as CEO Art Peck told CNBC last year, the company uses "big data" analytics to gain valuable consumer insights and more effectively direct advertising dollars. "Data is a huge asset for us," he said.

As a result, when Gap Inc. decided to move forward with the SASB standards, it found considerable overlap with its existing data tracking and disclosure efforts, which provided a relatively straightforward path to implementation. An initial gap analysis revealed only a couple of places where SASB-aligned information wasn't readily available. As an example, for Raw Material Sourcing, one of SASB's disclosure topics for the apparel sector, Gap Inc.'s sustainability team had already developed internal tracking by working with subject matter experts, business partners, and others to establish a process for collecting the necessary information. Reporting to the SASB standards required Gap Inc. to validate that it had built processes to report the data in a way that the company can stand by year over year.

> "WHAT'S HELPFUL IS THAT [THE SASB STANDARD IS] VERY PARED DOWN TO ESSENTIALS, SO WE'RE ABLE TO FOCUS ON THE MOST MATERIAL ISSUES FOR OUR INDUSTRY."
>
> – Ashita Soni
> Sustainability Data Insights Manager, Gap Inc.

The standards also helped Gap Inc. move existing programs forward. For example, "SASB also helped us have the conversation about Tier 2 suppliers and beyond," said Sustainability Reporting Manager Diana Rosenberg. "We are expanding our programs deeper in our supply chain beyond direct suppliers," she said, "but with an opaque and dynamic supply chain, how do we both measure and communicate that work?" Considering specific, rigorously defined performance metrics facilitated the process. "We needed to build a baseline there—that's an important step toward understanding how to make progress," Rosenberg said.

"What's helpful is that [the SASB standard is] very pared down to essentials," Sustainability Data Insights Manager Ashita Soni said, "so we're able to focus on the most material issues for our industry." In other words, the information yielded by the SASB standard is not just data—it's business intelligence.

## ENHANCING DATA QUALITY

Of course, for data to support effective decision making—either by management or investors—it must be reliable, comparable, and consistent. "If you think about it from the investor side, an investor gets data and builds financial models," Wong said. "If that data is not comparable, then those models have little value." In the absence of standards, Wong said, "every company can talk about things their own way—that's where having a consistent benchmark across the board helps." The same holds true for internal decision makers, he said, who also require reliable, comparable, and consistent data for managing progress.

To drive high-quality reporting on the SASB metrics, Gap Inc. leveraged its experience with other types of financial and non-financial data. The rigor of the process was driven—at least in part—by the nature of the SASB standards, which include detailed technical protocols to guide and support the collection investor-grade data. "Most frameworks are sustainability-driven," Rosenberg said. "This one builds a conversation with the controller, with the legal team and governance structure, in order to measure and disclose the right information in the right place." The resulting data is not only more reliable for investors, it also provides an enhanced level of confidence among internal decision makers.

To provide decision-useful information, "you need to have the system behind the scenes," Soni said. "If we have a certain percentage of fibers third-party certified, that means there's a process and strategy in place, there are goals set, and performance is being managed." This type of behind-the-scenes context—which is crucial to providing investors with a fuller picture—comes through in Gap Inc.'s public reporting related to SASB's qualitative, discussion-and-analysis metrics, which focus on the policies, processes, and management strategies the company has put in place to support performance. For example, with respect to materials sourcing, the company details its risk exposures and strategic responses related to cotton, synthetic materials, and other key inputs within its sustainability report.

## IMPROVEMENT THROUGH ITERATION

Although Gap Inc.'s runway to implement the Apparel, Accessories & Footwear industry standard was relatively short, it wasn't without twists and turns. For instance, the industry's SASB standard recommends disclosure related to labor conditions in the supply chain, including metrics aimed at measuring a company's engagement with and management of suppliers. All the nearly 800 supplier facilities producing for Gap Inc. are audited to a labor code of conduct. However, most apparel companies, even if they are sourcing from the same facility, have proprietary standards for vendor conduct; they measure and rank their suppliers in different ways. This can make comparable reporting a challenge.

For example, the industry standard is intended to measure the percent of supplier facilities that have been audited to a labor code of conduct, but Gap Inc.'s Code of Vendor Conduct may not match that of a competitor. Inconsistent approaches that require varying levels of management oversight of human rights and sustainability risks could result in numbers that suggest that Gap Inc. has worse (or better) performance, when, in fact, it's not a direct one-to-one comparison. Until the industry converges on labor performance standards, companies will need to explain the standards behind their approach to managing labor conditions in supplier facilities.

This type of convergence is what SASB hopes to facilitate within specific industries and the broader market through its Standards Advisory Group. The implementation challenges faced by Gap Inc. and other reporting companies will serve as important catalysts for discussions between companies and investors that should ultimately

> "CREDIBILITY IS AN IMPORTANT ISSUE FOR A LARGE COMPANY LIKE OURS BECAUSE PEOPLE TEND TO BE A BIT SKEPTICAL OF SUSTAINABILITY CLAIMS IF THEY AREN'T THOROUGHLY DOCUMENTED AND COMPARABLE."
>
> – **Diana Rosenberg**
> Sustainability Reporting Manager, Gap Inc.

help SASB better meet their needs with standardized, cost-effective, and decision-useful performance metrics.

However, companies don't have to wait for metrics to be flawless—or consistently applied—to make important progress on targets that internal and external audiences can easily understand. Gap Inc., for example, has already sharpened its focus on key issues reflected in SASB metrics, resulting in both realized and anticipated performance improvements among the company's suppliers. In 2015, about 18 percent of Gap Inc.'s suppliers were consistently low-performers on sustainability issues. After setting a goal in 2016 to only source from suppliers with an acceptable or high performance record, the rate was lowered to 2 percent within three years. Results like these illustrate the power of transparency and informed decision-making, Wong said. "That's a purely fact-based, metrics-driven outcome," he pointed out, noting that certain metrics—like non-conformance rates—are not only useful for investors but "to communicate with our business partners, because there's a goal—we need to get to zero—and tell them what their contribution needs to be to get there."

A key to achieving these outcomes was not letting the perfect be the enemy of the good. For example, Gap Inc.'s chemicals management program hasn't yet reached its full potential despite making significant strides. That didn't stop the company from reporting on the issue because transparency provides an important baseline for demonstrating the future progress Gap Inc. intends to make—both in terms of its performance and its reporting. "In the past, we would have probably waited a few years until we had a perfect program," he said. But, as the performance improvements cited above illustrate, there's value in being "more open and transparent about where we are in the process," Wong said.

## KEY TAKEAWAYS

The company's experience offers the following lessons:

- **Leverage what's already in place:** Although companies will be at different points along the adoption curve, all companies have systems, processes, and policies in place that can facilitate a speedier, less logistically daunting road to implementation. "We felt the SASB framework was an extension of what we're already doing," Wong said. In both Gap Inc.'s financial filings and sustainability reports, "We talk about things in a balanced, thoughtful, transparent way, and SASB naturally fit into that process." The company found value in taking one step at a time, starting with what they have and committing to incremental improvements. "It's a journey," Wong said, emphasizing that effective reporting doesn't happen overnight.
- **Own your narrative:** Gap Inc. reports a broad array of sustainability information to a variety of different stakeholders, which—like any communication—requires tailoring the message to the audience. Gap Inc. saw the SASB standards as a straightforward way to tell its sustainability story to a wide range of investors, whose unique areas of focus and data quality needs may not always be met by traditional approaches to sustainability reporting. This, in turn, enhances the narrative within the company's regular reporting process. As Rosenberg said, "Within our annual Global Sustainability Report, we can explain the nuances behind the numbers. That information can then be adapted for a broad set of purposes."
- **Collaborate across functions:** In implementing SASB standards, Gap Inc.'s global sustainability team engaged with a variety of departments and committees across the

organization, including finance, legal, supply chain management, and more. Getting buy-in from others in the organization may, in some cases, be easier than you think, Wong said. For example, Gap Inc.'s path forward was made smoother by the fact that SASB had already engaged with its investor relations and finance teams along the way to provide guidance from legal and financial perspectives. "Don't underestimate the amount of time involved in bringing the rest of the organization on board," Soni said, "but don't let it hinder progress, either."

- **Speak the same language:** Cross-functional collaboration necessarily means establishing a common vernacular around sustainability performance and reporting. SASB standards' focus on clearly defined performance indicators with rigorous underlying technical protocols can help prevent sustainability from getting "lost in translation" when jointly managed. Companies can "leverage the detailed SASB guidance to have conversations with internal stakeholders and business partners," Wong said. "The guidance is well-vetted so that it's straightforward for sustainability, investors, and business audiences to understand."

Although Gap Inc. had well-established sustainability programs and robust reporting practices, the SASB metrics have helped the company reinforce that its efforts are more than just feel-good stories. "Credibility is an important issue for a large company like ours," Rosenberg said, "because people tend to be a bit skeptical of sustainability claims if they aren't thoroughly documented and comparable." As a company with a portfolio of well recognized brands, "We can often face greater scrutiny, leading to a greater responsibility of proving our case," she said. By rigorously measuring and reporting its performance on key ESG issues, Gap Inc. demonstrates to markets its commitment to transparency and its pursuit of progress.