

# How an Australian resources company makes ESG a priority

**Karen Wood, chair of South32, talks about what makes the company's purpose and strategy resilient in unpredictable times.**

**The consequences of risk**, from pandemics to climate change, dominate the business agenda. They also underscore the importance for business leaders to strengthen their companies' environmental, social, and governance (ESG) propositions, says Karen Wood, chair of the board of South32, a diversified resources company headquartered in Australia that does business in around 60 countries. Before assuming the role of chair, Wood served as independent nonexecutive director and part of the remuneration, sustainability, and nomination and governance committees for South32. Prior to that, she was part of the executive leadership team at BHP from 2001 to 2014.

While the resources industry has long made ESG a priority, industry veteran Wood believes the COVID-19 pandemic has led broader industry to become more focused on the importance of the social element too. "We need to be focused on the economic and the social cost that comes from addressing this issue," she says of the pandemic's unequal impact on different segments of society. In August, Wood spoke with McKinsey's Michael Ellis on how her role as chair of the board has been affected by the pandemic, the steps South32 is taking to prepare for a low-carbon world, and the opportunities for multistakeholder collaboration to tackle some of the world's pressing challenges.

**The Quarterly:** *How has COVID-19 affected your views on the role South32 can play in the world?*

**Karen Wood:** There is a real opportunity for us to think about how we approach our work and open up a different conversation about some of the issues that we need to confront, both as a business and as a society. From a South32 perspective, we're taking this as an opportunity to have that different conversation and use this as a catalyst to take that forward.

We've seen real collaboration across forces including employee groups, unions, businesses. That's given us all an enormous amount of confidence about what might be achieved when we can align behind a common goal. It's an opportunity that I'd hate to see squandered.

**The Quarterly:** *What's changing?*

**Karen Wood:** The ESG agenda has come to the fore, with the social aspect being critically important. I think about the countries where South32 does business, such as South Africa and Mozambique, where the COVID-19 pandemic presented a significant challenge and has required a collaborative approach between government, business, and civil society. We all have a role to play in addressing the crisis.

An obvious example for us is the fact that we operate on land that is owned by other people. And, very often, by traditional owners who have a deep and abiding connection with the land that goes back, in some cases, millennia. Those people need to be better off for us being there than not.

We believe we can make a genuine difference in [four areas]: first, education and leadership, empowering young people to take leadership roles in their community; second, supporting participation in the [local] economy; third, [helping with] mental-health issues, which have been a concern for a long time in some of the remote communities where South32 operates; and fourth, in natural-resource resilience.

**The Quarterly:** *How have the purpose and values of South32 been tested during this period?*

**Karen Wood:** A clear purpose statement is a unifying statement and a benchmark to test decisions. Ours is built off of three planks. First, to make a difference by developing natural resources to improve people's lives. The second plank is to [consider the impact on] future generations. Third, to earn the trust of our owners and our partners so they know that we realize the value of their resources. That purpose is underpinned by our values—care, excellence, togetherness, and trust. They have been the foundation for our decision making through the pandemic and are the foundation we will rely on to confront the challenges that emerge postpandemic.

During the pandemic, keeping our people safe and well has been the primary objective; second, maintaining safe and reliable operations; third, supporting our communities. Those three things fit so neatly into the purpose of South32. We haven't had to go back and say, "Gee, you know, what is our reason for being?"

**The Quarterly:** *What are your investors' responses to South32's ESG focus?*

**Karen Wood:** Even before COVID, discussions with shareholders had been much more centered around the ESG risks we confront as a company. People are actively looking for a dialogue on what part companies are playing in that space. The days of separating shareholder interests from broader social interests are gone.

There was a time [in this industry] when we talked about a trade-off between production outcomes and safe outcomes. That hasn't been the case for a very long time, as we've recognized that you can't have a productive asset unless you've got a safe asset. [In the same way,] you can't have a productive company unless you've got one eye on your impact.

**The Quarterly:** *What does this mean, in practice, for the board?*

**Karen Wood:** We're in an industry that is used to making decisions where we're talking about deploying large amounts of capital with a long-term impact. We often have the luxury of a decision-making process that can go on for months or years. In this scenario, that wasn't the case. We thought about our work in three phases: What do we need to do immediately to address the health crisis to keep our people safe and support local communities? What do we need to do in the medium term to make sure that our business is protected? And what does the long term look like?

The board is thinking about it in those three phases, because, as I said, right at the outset we do not want to lose the opportunity for a different conversation, a different way of thinking to come to grips with what the world is going to look like when we emerge on the other side of this.

**The Quarterly:** *What are the implications for company strategy?*

**Karen Wood:** The strategy has not changed. Clearly, we've had to make some short-term decisions. We've had to suspend some work that wasn't business critical, and we've had to free up teams to address the health crisis.

But the strategy has not changed. One plank is to optimize the operations that we have, the second is to unlock the value in those operations, and the third, to identify opportunities for growth. In that third plank, we have a bias to base metals because we [favor] commodities that will have a long-term future in a low-carbon world.

You see it in a number of recent initiatives: the planned divestment of the energy coal business in South Africa; the investment in the Hermosa Project in Arizona, a silver, lead, and zinc deposit; and our participation in the joint venture with Ambler Metals in Alaska for copper, silver, lead, and zinc.

**The Quarterly:** *How does that affect your capital allocation?*

**Karen Wood:** Our capital-management strategy, which underpins the broader strategy of optimize, unlock, identify, is also unchanged and has shown the flexibility needed to react in these unprecedented times. It's also focused on three things: maintaining safe and reliable operations and retaining our investment credit-grade rating; second, returning 40 percent of our underlining earnings to shareholders through ordinary dividends; and third, setting up competition for the capital that is left.

Within the third plank sits opportunities of the M&A kind that might emerge through this crisis, but they have to compete for remaining capital. We've also had the flexibility inside

our capital-management strategy to respond—by suspending the buyback, for instance—until we get more certainty about what the long-term ramifications of the pandemic might be. As you know, our business is conducted in developed and developing countries around the world, the latter of which may not come through quite as quickly as some of the more developed nations. So we feel very confident that both our business and capital-allocation strategies are robust and will see us through this period.

**The Quarterly:** *How is South32 dealing with increased unpredictability and instability in global trading relationships?*

**Karen Wood:** Global free trade is an absolutely critical part of our business. As a society, we cannot address global challenges without global free trade. Look at China, where millions of people have been lifted out of poverty as a result of industrialization—fueled, in part, by resources that come from Australia.

So the global tensions are concerning, not least because they have an impact on commodity markets. We need to watch closely and run our business as efficiently as possible. But we also need to make sure that we have open and constructive relationships with our customers around the world. That is absolutely critical. South32 has a very diverse customer base. We have relationships with customers around the world that go back decades. We need to focus on the interdependencies between companies, which are the platform for constructive relationships.

It's not a particularly secret ingredient, is it, that trust-based relationships are the basis upon which all strong business relationships are built? But it does really underpin the success of South32's model.

**The Quarterly:** *One final question: Where do you see the mining industry and South32 20 years from now?*

**Karen Wood:** From a South32 perspective, I feel very confident that the strategy of optimize, unlock, and identify will lead us to a simpler commodity portfolio with a bias toward base metals. It will be a portfolio with the sort of commodities that are necessary in a low-carbon future. South32 has made a commitment to carbon neutrality by 2050, and our broader capital-management strategy is consistent with that.

By 2050, we will all be well beyond this debate about shareholder interest versus broader stakeholder interest. That debate will be well and truly settled—these are shared interests that can both be met simultaneously. The world cannot possibly address the critical challenges it faces unless corporations take a broader perspective that looks at impact and how corporations can make a fundamental difference. Q

**Karen Wood** is chair of South32. This interview was conducted by **Michael Ellis**, a senior partner in McKinsey's Sydney office.