



The Value of Social Purpose

How to Receive Value for Your Values

Now, for tomorrow



Corporate Finance

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About Us

Baker Tilly Canada Corporate Finance is a national advisory firm focused on serving small- to mid-market entrepreneurial clients. We recognize that these clients are not adequately served by business brokers or larger investment firms but still require – and deserve – sophisticated, experienced professionals to get the job done right.

We are often shocked that simple tax issues and planning are ignored in business transitions. These issues can materially impact the value realized from a sale, and frequently not for the better.

Our team boasts an impressive combined resumé of academic credentials and decades of specific experience in accounting, taxation, corporate finance, valuation, business structuring and family transitions. Clients are often surprised at our breadth of expertise, across a wide range of complex topics – expertise that is essential when executing a successful sale, merger or acquisition.

We pay attention to the small details, ensure our clients maximize their after-tax proceeds upon exit and consistently exceed expectations. We fill a void in the marketplace, serving small- to mid-sized businesses, and look forward to the opportunity to serve you.

What We Do



Mergers & Acquisitions

- Sell-side
- Buy-side
- Go private
- Management buy out (MBO)



Advisory

- Valuations
- Fairness opinions
- Quality of Earnings (QoE)
- Financial Analysis



Capital Sourcing

- Acquisition financing
- Refinancing
- Debt recapitalizations



Executive Summary

In the past, brands thrived or died based on the functional benefits of its products and services. Today, consumers – among other stakeholders – are exerting extreme social and financial pressure on brands to have a social purpose beyond those mere functional benefits. As a result, businesses are taking social stands in very visible ways (Ex. Patagonia, TOMS, etc.) on previously taboo issues including the environment, politics, and social injustices. Large established brands who have grown just fine without a well-defined social purpose are at a pivotal junction in their journey in deciding how to respond to the very real challenge of developing an authentic social purpose fitting for their organization.

As businesses continue their rebuild and they bounce back from this pandemic, they are faced with a huge opportunity. They could carry on conducting business purely to generate profit; or they could make a change and use their business as a force for good.

Baker Tilly Canada Corporate Finance (“Baker Tilly”) believes that we are experiencing the beginning of a major business and cultural transformation that will disseminate social purpose (aka grand purpose) to all levels of business. In this scenario, businesses must adopt a social purpose and implement it through their strategy, and organizations that don’t engage in a purposeful way will be held as suspect, resulting in a degraded brand with potentially tremendous financial consequences. As this happens, it will change the very nature of what it means to be a commercial entity in business.

We are in a time of discontinuous change, urbanization, mass migration, discrimination, environmental constraints, technological advances, globalization, and challenges to public health. These disruptions provide commercial opportunities, but they also create societal problems and expectations that businesses will collaborate with civil society and government. Realizing this opportunity will happen one company at a time, driven by leaders courageous enough to embrace the business possibility and wise enough to operate within a framework of inclusive growth, in which all stakeholders reap the benefits of change.

After an extensive review of data, Baker Tilly has identified six key drivers of corporate value creation when companies implement their social purpose through their pre-existing business strategy. These drivers are:

- I. Brand differentiation;
- II. Employee engagement and retention;
- III. Risk mitigation;
- IV. Access of capital;
- V. Long-term performance; and
- VI. Innovation generation.



Each key driver has a positive impact on a business’s enterprise value (EV). For example, consider the Gordon Growth Model, which is defined as:

$$P = D / (r - g)$$

It says that the common equity share price, **P**, is a function of three (3) factors:

- D = dividends (distribution of profits to shareholders)
- r = cost of equity (shareholders’ investment in the business)
- g = growth rate in profits and dividend distributions

Companies with an authentic social purpose integrated into their business models will experience a positive impact to the three underlying factors to enterprise valuation.

Brand Differentiation

The consumer landscape is undergoing a dramatic change in purchasing preference. As consumers increasingly embrace social causes and become more educated, they seek products and brands that align with their values. In a survey conducted by IBM, nearly 80% of respondents indicate sustainability is important for them. Of those who say it is very important, over 70% would pay a 35% premium, on average, for brands that are sustainable and environmentally friendly¹. This level of brand advocacy will have strong positive impacts on a company's cash flows (D) and could influence the trajectory of the company in the long term (g). A social purpose can also expose a company to new competencies and capabilities within new markets, further supporting growth opportunities. A 2021 study was conducted that illustrated 84% of surveyed individuals expect CEOs to publicly speak out on societal challenges, including but not limited to societal issues, local community issues, job automation, etc¹⁶. Therefore, companies that do not take a stand on societal issues run the risk of losing valuable customers. In tandem with these developments, a flip of the classic pyramid of influence is evident as peer-to-peer discussions overtake customer influence. It is believed that the mass population is relying less on news media and, instead, choosing self-affirming online communities. With this shift, consumers are more likely to recommend purpose-driven brands to their peers, amplifying the brand's message and reach.

Ben & Jerry's, a long-standing supporter of social causes, had this to say on the topic. The company believes "the strongest, [and most sustainable] bond you can build with your consumers is over shared values"²³.

In the words of marketing guru, Seth Godin, "When price and availability are no longer sufficient advantages (because everything is available and the price is no longer news), then what we are drawn to is the vulnerability and transparency that bring us together...[the customers you serve] want your humanity, not your discounts".



Employee Engagement and Retention

Employees working for companies with strong social impact programs tend to find their jobs more meaningful and boost their day-to-day engagement and long-term commitment. Market research demonstrates that enthusiastic employees dedicated to a company's purpose and vision are the best proponents of a business's social purpose and brand quality. Teams who score in the top in engagement realize a 41% reduction in absenteeism and 59% less turnover. Engaged employees show up everyday with passion, purpose, presence, and energy^{2,3}. 60% of millennials want to work for companies with a purpose. A sense of purpose and impact on society are the second top criteria for young people when considering job opportunities (40.6% versus 49.3% for salary and financial compensation)⁴. In a survey of nearly 2,000 students and college-degreed workers across three generations, 45% of respondents said that they would take a 15% pay cut for a job that makes a social or environmental impact; and 51% said that a sense of social purpose is "essential" or "very important" for their ideal job⁵. Employers lacking a social purpose could limit their recruitment base by 50% or more of the future workforce and stunt future growth.

A social purpose also has the ability to elevate an organization's culture and, subsequently, attract top talent. Although the idea of culture can feel vague, the logic behind it is straightforward. According to Gallup, "strong cultures create employees who are brand ambassadors". A great culture increases engagement among employees, and engaged employees are more likely to recruit friends to their workplace. This is significant as 71% of workers claim to use referrals from current employees as a way to learn about the organization²⁴. Naturally, talented people want to work for an organization where their talents complement the company's mission and values.

Research shows that a work-life balance – having enough time and energy to enjoy life outside of work – is no longer enough. Millennials, who make up 50% of the Canadian labour force (and who will represent 75% of the labour force by 2025) are also looking for work-life integration, which means applying themselves to something that they feel passionate about, so that they can fulfill both an economic need and a need for a higher purpose. Thus, whether you want to recruit and retain millennials, or sell them a product, they will factor purpose into their decision-making process.

An example of employee engagement in action can be seen with mattress manufacturer and B Corporation ("B Corp") company, Leesa. In the midst of a pandemic, the company was able to design and deliver hospital beds for COVID patients in less than three weeks: the company's product launches typically take about nine months for completion. Leesa CEO, John Replogle credits some of the speed of their product launches with the barriers they removed in the decision-making process by flattening the company's hierarchy. The teams mandate to perform, both for impact and the profitability required to support the impact motivated everyone to step in as needed, regardless of whether the need fits their role or job title.

M&A Insight

High employee engagement and customer loyalty are synonymous with a strong company culture. According to an Accenture survey of C-suite executives, 75% agree that the cultural aspect of M&A is important in the merger/acquisition's success, especially following the COVID-19 pandemic. An estimated \$600 million is lost every year as a result of wide cultural disparity between acquirer and target company²⁷. The importance of employee consideration and support is especially felt in B2B companies, where employees represent the most powerful external communications channel.

Risk Mitigation

Risk mitigation serves to protect corporate value and the license to operate. Corporate value is perhaps more at risk now than ever before, as increasing public demands can translate into higher levels of immediate scrutiny. Social purpose companies that have translated their social purpose into their strategy and culture are less likely to face these reputation risks. According to a study done by the World Economic Forum, on average more than 25% of a company's market value is directly attributable to its reputation⁸. And in a highly connected world where reputations can be attacked with just a few keystrokes, that number is likely to grow moving forward. When a company's reputation spirals out of control, revenue and brand value are negatively impacted the most. In the same study, 41% of respondents who experienced a reputation risk event say a loss of revenue was the biggest impact; especially for companies in the consumer products and energy industries⁸. Social purpose companies executing on a purpose-driven business model are less prone to regulatory and consumer risks.

Additionally, purpose-led companies are proven to be more resilient in times of economic downturn. In a study conducted by the School of Management at SUNY Binghamton, researchers found that B Corps had a greater revenue growth rate (51%) than public companies of comparable size (11%) during the 2008 financial crisis²⁵. According to Chris Turner, a B Corp Executive, a company's road to recovery from the pandemic is going to depend on their ability to rebuild their business in a way that puts their people first and protects the communities and the environment on which they rely²⁶. The rate at which companies recover will vary across firms, however, three dimensions exist where resilient companies can enjoy better outcomes:

1. The immediate impact of an external shock on their performance can be lower than their peers.
2. The speed of their recovery can be higher than peers.
3. The extent of their recovery can be higher than peers.

Every company has social risks inherent to its business but in many cases this risk can often go undetected. As companies evaluate how they will interact in this changing world, assessing social risk will not only protect their bottom line, but it might also give them the ability to outpace their competition as they grow for the future, and ultimately make for a cleaner exit.

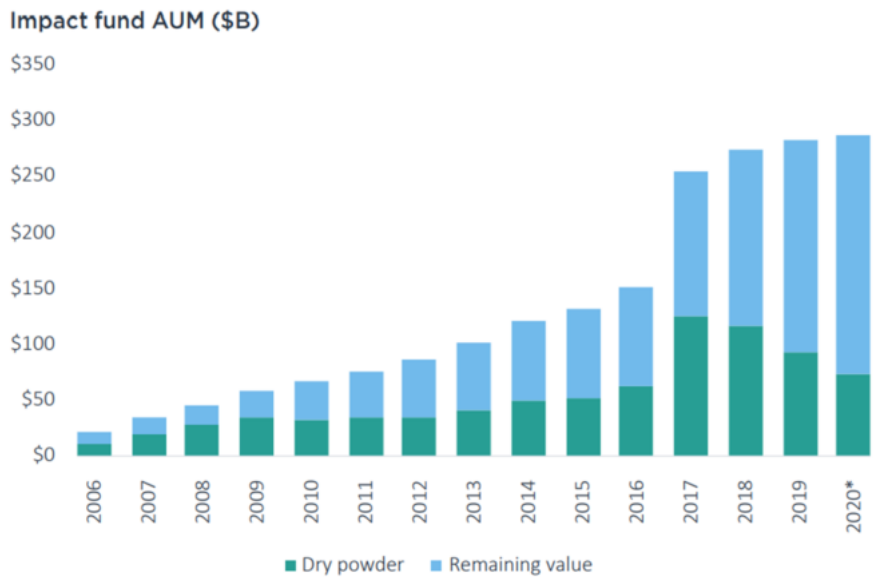
How did companies do during the pandemic?

Certified B Corps were 63% more likely to survive than other businesses of similar size during the 2008 recession, and they have a 90-99% survival rate compared to the 69% average among small businesses in the United States¹⁸. This resiliency may prove to be true for COVID, but still too early to tell.

Access to Capital

Baker Tilly is seeing more investors making hyper-critical decisions around capital allocation and the lack of a strong societal strategy – one that shows meaningful progress towards real sustainability and social impact – making for easy opt-outs for investors, regardless how attractive the business model is.

Moody’s, a large bond rating agency predicts that, following the pandemic, sustainability standards and disclosure requirements are expected to have more influence on investment decisions at all levels, from banks, to asset managers, to consumers⁹.



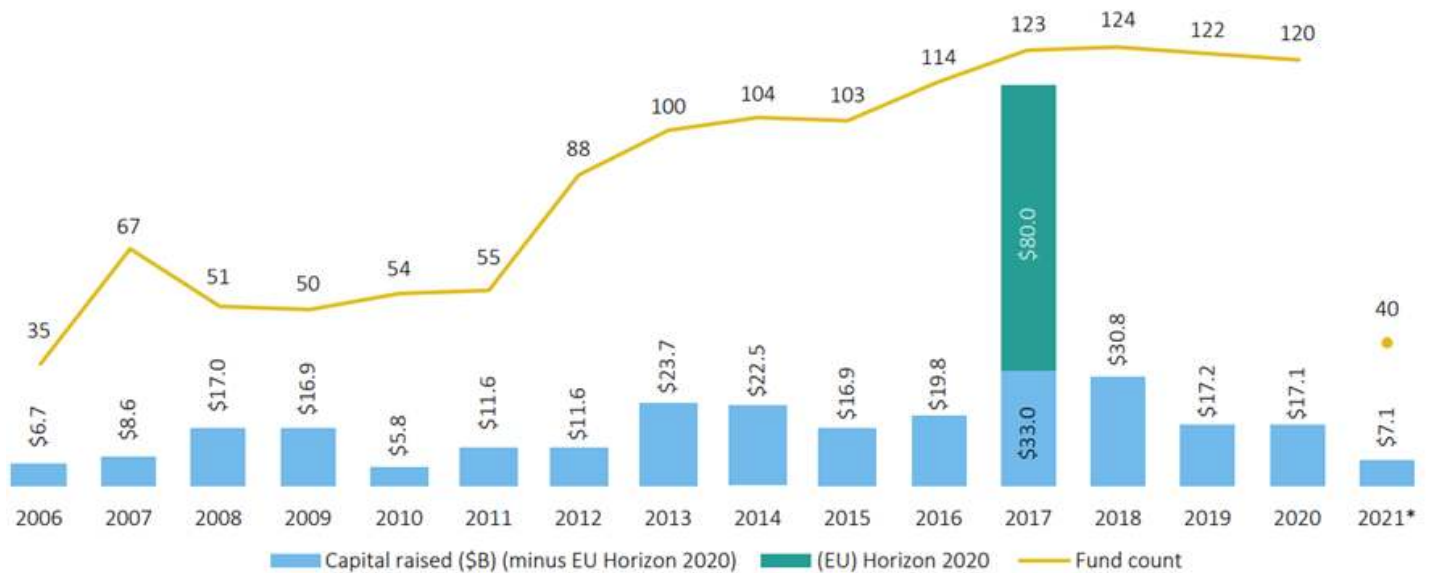
Source: PitchBook | Geography: Global
*As of December 31, 2020

Therefore, as a company without a social purpose and purpose-aligned strategy, you risk being left behind in terms of capital access. Without an established social purpose execution plan, a company’s growth trajectory and overall business valuation could be negatively affected. There is a strong demand for companies with a social purpose strategy: a report shows that the impact assets under management¹ (AUM) in Canada has grown from \$3.7B in 2012 to \$14.8B in 2017¹⁰. In the bigger picture, currently there is US\$73B in unallocated impact capital, with US\$212.9B invested, totaling US\$286B (above). Overall, there is an increasing trend globally in the number of impact funds that are closed each year (see graph on page 8).

There is also evidence that companies with certain purpose-led initiatives have greater access to capital in terms of lower borrowing costs. Companies that embrace an eco-friendly purpose have access to funds via green bonds or sustainability-linked bonds. The lower borrowing costs for the issuer is due to strong demand for sustainable bonds in general, and the term for this is known as the green premium (“greenium”).

¹Impact investing refers to investments "made into companies, organizations, and funds with the intention to generate a measurable, beneficial social or environmental impact alongside a financial return."

Impact fundraising activity from 2006 to March 2021



Source: PitchBook | Geography: Global
*As of June 21, 2021

Long-Term Performance

By choosing to align with social purpose, a company may lose out in the short-term due to initial costs such as purpose integration, extra training, opportunity cost, etc. In the long-term, the company stands to gain substantially. For example, US pharmacy company CVS Health has outperformed its industry in 88% of crisis quarters (quarters in which the industry relative shareholder return had a decline of at least 15% from the start of the quarter) by living up to their purpose of “helping people on their path to better health” by becoming the first drugstore to stop selling tobacco in 2014 and lose a \$2 billion revenue stream²⁰. Despite this high initial perceived loss, CVS Health grew in areas that aligned with their purpose, such as healthcare benefits management, which grew from US\$3.5B in 2017 to US\$74B in 2020^{20,21}. During the COVID-19 crisis, CVS has opened more than 1800 drive-through testing locations, which exhibits the robustness of their operations²⁰.

M&A Insight

As mentioned, above factors such as employee engagement, risk mitigation, brand differentiation, and capital access all contribute to operational efficiencies and potential for long-term cost savings/ revenue generation. For example, by implementing a social purpose strategy, a company can (a) increase the relative size of their investor base, thus lowering their cost of capital; (b) signal quality to consumers, leading to positive goodwill for the organization; and (c) foster innovation within the company, leading to more diverse revenue streams. According to Harvard Business Review, 58% of companies with a social purpose experienced revenue growth of 10% or more versus 42% of companies without a strong purpose¹⁷. A social purpose lens on business can help organizations set themselves up for a future business landscape and can make themselves more attractive to buyers.

Innovation Generation

Brands increasingly use social purpose to steer product innovation and uncover or access new market opportunities. Society’s needs are “innovation hot spots”. Trends that affect society can provide opportunities for social purpose companies to meet unmet needs. For example, consider chopsticks, a takeout food necessity, and how they are typically thrown away – not recycled. What most may consider as waste, others would consider it a valuable resource key to a circular economy. This is what ChopValue seeks to do – a B Corp that harvests used chopsticks from restaurants and upcycles them into various décor, table, or chairs. Since 2016, 38 million chopsticks have been recycled and upcycled, and ChopValue has been able to create a viable business and scale it nationally throughout Canada and Singapore through social purpose innovation²².

Executives who treat purpose as a core driver of strategy report greater ability to drive successful innovation and transformational change and deliver consistent revenue growth: 53% compared with 19% of the companies who have not put any thought into a social purpose strategy at all⁴.

In summary, the six main business benefits of Social Purpose have a direct and favorable impact on valuation. Their impact on each of the three underlying factors to valuation is summarized in the table on page 9:



	Customer Commitment	Employee Engagement	Risk Mitigation	Capital Access	Financial Performance	Innovation Generation
Cash Flow (D)	✓	✓	✓	✓	✓	✓
Cost of Equity (r)			✓	✓	✓	
Growth (g)	✓	✓	✓	✓	✓	✓

Whether it is attracting new talent, driving business growth, or increasing consumer trust, brands that identify a genuine social purpose and implement a strategy to support it, stand to benefit greatly with a stronger sense of mission and higher profits.

Social Purpose In Action

The Social Purpose Institute, which helps companies incubate, accelerate, and scale social purpose, has collaborated with companies such as Return-It, Hemlock Printers, and LGM Financial Services Inc to establish their social purpose. Return-It, a recycler, adopted their social purpose in that through collaboration and partnerships, coupled with their leadership and expertise, they will be able to create a world where nothing is waste¹¹. Hemlock Printers adopted their social purpose: to create connections, build community, and inspire actions that safeguard the health of the world’s forests¹³. LGM Financial Services Inc., an automotive finance firm, adopted their social purpose: to accelerate responsible mobility for all¹².

Telus has adopted a social purpose to connect all citizens for good, and a philosophy to give where we live¹⁵. It is quite clear that social purpose has impacted all these companies positively in terms of the six key drivers of corporate value creation:

1. Brand differentiation:

- Return-It strengthened existing partnerships and gained new ones such as Canada Plastics Pact, Ocean Wise and the Pacific Salmon Foundation¹¹.

2. Employee engagement and retention:

- Return-It increased employee commitment and engagement by identifying immediate and long-term initiatives to drive engagement via in-person employee consultation process to define social purpose¹¹.

3. Risk mitigation:

- Hemlock examined their supply chain more cautiously by asking their paper suppliers to provide forest of origin information to assess the risk to ancient and endangered forests¹³.

4. Access to Capital:

- Telus demonstrated their commitment to connect all citizens for good by linking financing to achieving net carbon neutrality by 2030. They raised C\$750M in bonds with an annual interest rate of 2.85% in 2021 through a sustainability-backed loan. They will pay that 2.85% interest rate if they can reduce their greenhouse gas emissions by 46% from 2019 to 2030, and an increase of 1% interest per annum if they are unable to¹⁴.

5. Financial Performance:

- LGM applied its social purpose to product development, and they were the first-to-market with a digital sales solution for their car dealers and OEM partners. The digital sales solution provides greater transparency and equity for consumers, which has allowed LGM to be industry-leading in digital finance and insurance solutions, ultimately enhancing revenue opportunities and creating efficiencies for their dealers and partners¹².

6. Innovation generation:

- Return-It invested in Canada's first compressed natural gas hybrid-electric compaction machine which replaces two diesel trucks, and increases the amount of beverage containers transported by six times¹¹.

As the landscape of business undergoes a rapid transformation, we are starting to see that traditional companies can only go so far. To the extent that society chooses to engage in social good, it has usually been through direct philanthropy, but philanthropy alone cannot create the impact on people and the planet with the scale and efficiency that focused market investments have the potential to do.

Embracing a social purpose can help companies engage and mobilize employees, attract customers, drive innovation and differentiation, and enhance profitability. The impact on shareholders and society that is created through social purpose will only be revealed through time in the long-run, and Baker Tilly is committed to the social purpose movement.

Change is an iterative process: this whitepaper marks the beginning of our journey, and it will not be the last. We believe that to drive change, it must be done collaboratively – we invite anyone that wishes to be a part of the social purpose movement to reach out as we tackle this matter together.



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Authors

Mike McIsaac, CPA, CA

Managing Director
Baker Tilly Canada Corporate Finance
mmcisaac@bakertilly.ca

Kevin Shaw, MBA

Managing Director
Baker Tilly Canada Corporate Finance
kshaw@bakertilly.ca

Howard Ma, CFA

Director
Baker Tilly Canada Corporate Finance
howardma@bakertilly.ca

Bongani Moyo

Senior Analyst
Baker Tilly Canada Corporate Finance
bwmoyo@bakertilly.ca

Chris Lum

Analyst
Baker Tilly Canada Corporate Finance
chlum@bakertilly.ca

Baker Tilly Canada Corporate Finance

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