Time to act

Healthcare at a turning point on ESG

BARCLAYS

Contents

Time to act on ESG

Why healthcare needs to catch up

The healthcare industry has fallen behind its peers when it comes to sustainability. This report shares insights from some of the leaders in the field on how operators can make up lost ground in this increasingly critical area of business.

Climate change is arguably the biggest challenge facing the world today and is just one of a number of threats accelerating the focus on sustainability. Investing in sustainability is not just a moral imperative but a commercial opportunity.

- UK healthcare organisations, particularly those in social care, are lagging in the adoption of environmental, social and governance (ESG) strategies: more than half of care operators have no ESG strategy and no emissions reduction plan.[1]

- While this may be understandable in the light of huge challenges faced by the sector in recent years, delaying their ESG journey is not a viable option for operators over the longer term:

  Environmental: due to the sector's property footprint, carbon emissions are high, exposing businesses to higher operating costs and reputational damage.

  Social: the value of the sector to society is undeniable but needs to be measured and articulated – progressive operators are finding ways to do this.

  Governance: While care governance is highly regulated, businesses must still work to improve and demonstrate that they are responsibly run.

- Commissioners, investors, stakeholders, lenders and operators will increasingly demand evidence of ESG credentials to continue supporting healthcare operators.

- Perhaps most pressingly in the current employment context, credible ESG action supports recruitment and retention, particularly among younger talent – almost half of under 34s would switch employers for this reason.[2]

ESG defined

ESG – Environmental, Social and Governance – is a set of standards measuring a business's impact on society, the environment, and how transparent and accountable it is. For the purpose of this report, we see ESG as a means of measuring how a business integrates good practices into its operations, and the impact and sustainability of its business model.

Embracing change

Healthcare cannot imagine itself exempt from ESG

More than a third of the world's biggest publicly-traded companies now have net zero targets - although 65% of them do not yet meet minimum standards of robustness.[3] However, the response of health and social care to these imperatives has been muted, at best. Private hospitals have largely started to embrace the challenges, but social care operators have yet to do so. Barring some notable exceptions, most providers we speak to are either just embarking on their sustainability transition to a low carbon economy or have yet to start.

One reason may be the sector's reliance on its undeniably positive social impact. The social value of healthcare is plain in a way that does not apply to many corporates. However, this in itself does not exempt the sector from their need to track and demonstrate impact and to achieve genuine diversity and inclusion. Defining metrics to measure the social impact of health and social care is difficult, but – as our report reveals – progressive operators are finding a way.

Existential risks

Delaying the implementation of an ESG strategy has been possible to date, but will not be an option for much longer. There are multiple risks to inaction, some of them existential. Acting now is an investment in customer trust and commissioner confidence; in the ability to attract the best talent; and in the future valuation and long-term viability of any healthcare business.

22%

of 18 to 34 year olds now cite corporate values above salary in their priorities[2]

"Credible ESG action is a growing factor in the ability to attract and retain younger staff, in particular."

The carbon footprint of most health and social care businesses is high relative to businesses of comparable size in other sectors. This provides opportunities to begin reducing environmental impact. Operators who have made an early start in this area have told us they are already benefiting through mitigation of soaring energy costs in recent months.

Credible ESG action is also a growing factor in the ability to attract and retain younger staff, in particular. Recent UK research suggests 47% of 18 to 34 year olds would seek work elsewhere if they felt their employer was not committed to the cause; 22% in this age group now cite corporate values above salary in their job-seeking priorities.[2]

It is also instructive to note the extent to which investors have adopted ESG parameters. Many funds are now prepared to invest only in ESG-compliant assets. Failing to focus on ESG will likely, in the long term, severely limit access to capital, while reducing asset values.

Not just for corporates

To urge operators to embrace sustainability is not to underestimate the aftereffects of the pandemic and the acute impact of the recruitment crisis, which we have explored in previous reports. Compounding these challenges, the urgent requirement to manage the effects of soaring inflation is likely to divert attention from ESG progress.

The pressures are especially acute for the great number of smaller operators in social care, which may lack the time and resources of bigger players, but which face equal opportunities and risks through sustainability. They may find inspiration in the insights of the larger providers who have shared experiences of their ESG journeys for this report.

Support and guidance

Another challenge is the difficulty of finding external help. While nine in ten small businesses believe it is important for them to be sustainable, 42% say they struggle due to lack of guidance.[4] This is likely to be especially true for health and social care, which lack the independent, sector-specific guidance available to sectors such as retail and hospitality.

"The pressures are especially acute for the smaller operators, which may lack the time and resources of bigger players, but face equal opportunities and risks through sustainability."

Banks such as Barclays offer a growing range of financing for sustainability-linked projects, some of which offer reduced funding costs linked to progress against sustainability goals. It is true, however, that smaller businesses whose borrowing is already high can still find it hard to access these facilities: expansion of the help available from lenders and policymakers is required to bring sustainability within easier reach of more firms.

Despite all these challenges, several operators are making big strides on the ESG agenda. This report is designed to offer inspiration for others to begin taking positive steps towards sustainability.

Steve Fergus
Head of Healthcare,
Barclays Corporate Banking

The ESG gap

Why is healthcare trailing other sectors?

The term ESG increasingly trips off the tongues of people in all streams of life. Awareness of the need to act responsibly is being translated into firm commitments by businesses and investors, and – to varying degrees – into expectations on the part of consumers and the wider public.

Business benefits
Responsible action on the environment, social impact and governance are no longer side issues. They are moving to the heart of business strategy and purpose. Leaders are recognising that beyond being 'the right thing to do', an effective ESG strategy can bring tangible business benefits.

Sustainability can deliver cost savings. It attracts investment and talent. And it enables businesses to go beyond meeting regulatory requirements, positioning themselves as the preferred suppliers to their customers.

However, UK healthcare organisations – and social care in particular – have been slow to embrace ESG. A recent survey by the real estate consultancy CBRE suggests more than 50% of care operators have no ESG strategy, and no plan to cut carbon emissions.[1]

Pressures and priorities
There are plausible reasons for this, not least the sector's recent experiences. "No one can underestimate what care home operators and staff went through in the Covid-19 pandemic," says Emma Glynn, Head of Healthcare, Valuation Advisory at JLL. "They are now recovering in terms of occupancy and profitability, but still face significant challenges around staffing and rising inflation."

Despite the operational challenges faced by many operators, Glynn says, investors see attractive credentials in the sector. These include the inherently positive social impact of its core work, and the tight regulation of governance in the sector. The variance in stock across the market does, however, present challenges around the sector's environmental credentials, particularly since dated stock often has a high carbon footprint.

Only 39% of healthcare operators have a current ESG strategy, but 79% of investors in the market prioritise ESG in their decision-making.[1]

The cost of inaction

Investors, staff, regulators and consumers expect commitment

The sector's general lateness in tackling environmental issues is all the more worrying because its impact is relatively intense.

Big footprint
By the nature of their business, healthcare operators are big carbon emitters. Residential care demands round-the-clock heating, lighting and water use; food waste is often an issue too. Hospitals require ventilators, scanners and other powerful equipment. Road transport is generally the only viable mode for domiciliary care providers.

While legislation does not yet require all businesses to act, the UK government's legal commitment to achieve net zero by 2050 will see regulation evolve. Since April 2022, over 1,300 of the largest UK-registered companies and financial institutions have been required to disclose climate-related financial information.[5] Many are already seeking similar assurances from their smaller suppliers to prove that their entire supply chains are compliant. These relate to Scope 3 emissions (see next page).

Putting off engagement with this agenda is therefore likely to store up bigger headaches for the future – and there are several positive reasons to get ahead of the game.

Green payback
Cost is the most obvious driver. Businesses that made an early move to renewables – from solar panels to electric cars – have seen the benefits as energy prices soared.

Specialist care group CareTech identified its extensive estate and vehicle fleet as twin priorities for emissions reduction. Its move towards an all-electric transport fleet will entail significant investment, says Jonathan Freeman, the group's Sustainability Director – but the payback will be relatively swift.

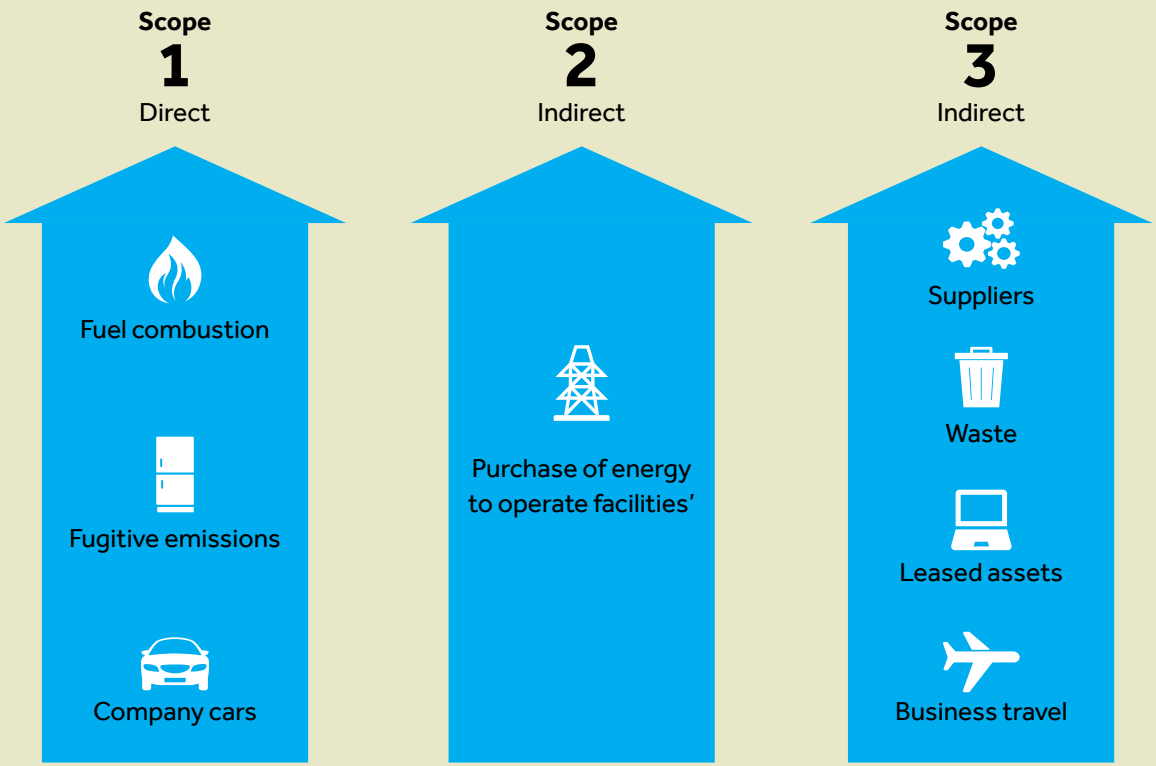
"If you look through a narrow lens, electric cars look a lot more expensive," he accepts. "But by analysing costs over three years, we showed electric car options could be funded at the same outlay as petrol ones. It was a no-brainer. And given rising fuel prices, the cost-benefit analysis is now even better than a year ago."

Investor demand
Another important reason to implement carbon reduction – and wider ESG measures – is to ensure a business is attractive to future owners or potential investors, from traditional banks to institutional funds.

The CBRE study mentioned in the previous section found that while only 39% of operators have a current ESG strategy, 79% of investors in the healthcare market prioritise ESG in their decision-making.

This mismatch is a concern, says JLL's Emma Glynn, who finds that healthcare investors now bring up ESG and sustainability "in every conversation". Failure to demonstrate a plan on the part of an operator suggests a future erosion of asset values.

"If you're looking for investment to grow or to facilitate financing – through ground rents or leasebacks, for example – then you need to be able to demonstrate that you have an ESG strategy and that you're delivering on it, so that those investors in turn can show they are investing in sustainable businesses," she says.



Defining emissions

Greenhouse gas (GHG) emissions are grouped in three main ways under the most widely-used international accounting tool, the GHG Protocol.

Scope 1 – Emissions over which a business has direct control, such as running its boiler

Scope 2 – Fewer direct emissions, such as the production of energy to fuel the business

Scope 3 - For many companies, the majority of their emissions lie outside their own operations. These are known as 'Scope 3' emissions. Many larger businesses are now assessing these emissions, by tracking their suppliers' carbon footprints and net zero plans alongside their own.

"Equally, if you plan to exit and sell to private equity or to another operator, you now need to demonstrate strong ESG credentials."

That is echoed by Matt Jolley, Head of ESG Origination at Barclays Corporate Banking. "The big private equity houses are setting net zero and ESG ambitions, and rolling them through to their portfolio companies," he notes. "So if you're attracting PE investors, or you have one already, you will feel the pressure very soon.

"But that is also an opportunity. For businesses trying to grapple with how to approach ESG, having the investors behind you can really help to give you direction and provide a framework for success."

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>
> **Emma Glynn**
> Head of Healthcare, Valuation Advisory, JLL

Stakeholder pressures

Even smaller businesses that are not yet legally required to have a transition plan for net zero can come under pressure from larger customers seeking to demonstrate that their entire supply chains are compliant. In future, commissioners are likely to expect providers to demonstrate ESG credentials. it seems reasonable to expect that insurance firms will follow suit, referring policyholders only to hospitals that can show they are responsible businesses.

Patients and residents, too, are increasingly aware of sustainability when selecting a service. While Glynn does not see ESG as a dealbreaker for most consumers at present, she says it is rising up the agenda as a factor, alongside fees, reputation and quality of care.

Perhaps most significantly in the current context, potential recruits are also drawn to companies with a clear commitment to sustainability, especially where they see they can have a personal influence on it. Given the recruitment crisis in the sector, a competitive edge here could be a significant factor in determining whether a healthcare business thrives or flounders.

A roadmap for success

Engaging, realistic, evidence-based: key principles for ESG action

Setting out on an ESG journey requires an analysis of the current state of the business, to inform priorities for action. Glynn suggests "measure, audit, communicate" as watchwords. The latter is critical to ensure staff feel they are part of the journey, and to make stakeholders aware of the company's ambitions and progress.

Jonathan Freeman was already CEO of CareTech's independent charity, the CareTech Foundation, when the Group appointed him as the UK care sector's first Group Sustainability Director. The move was a recognition that the charity alone was not sufficient to demonstrate CareTech's social purpose.

Involving teams

Freeman set about developing a clear ESG strategy. Dubbed CARE4, it focuses on CareTech's commitment to people, communities, the planet and innovation. Engaging the group's 11,000 staff was key: "We kept it as simple as possible," Freeman says, "so everyone could get a sense of what we're about."

Through a programme termed Runway, each CareTech service is encouraged to find its own ways to make an impact, using a model of 10 tried and tested principles.

For example, Hill House School in Lymington developed its own strategy in collaboration with students. One result is a revamp of the school's menu, to cut food waste. "Through quite simple changes, they saved £6,000 in the first six months, with no reduction in quality," says Freeman. "They got such a buzz out of that."

Scope for action

Most organisations embarking on their net zero journey focus first on emissions defined as Scope 1 (direct emissions, such as running a boiler) and Scope 2 (indirect emissions, such as the production of the energy used by a hospital or home), since these are the categories easiest to control.

CareTech sought external expertise to help set priorities for emissions reduction. It has reviewed energy performance certificates for each of its properties, to provide a baseline for action. This in turn will form part of a costed plan to reach net zero by 2050, to be considered by the board later this year.

Property dilemma

Environmental targets often revolve around energy use and waste reduction. On a more structural level, many operators have buildings that require work to bring them up to modern environmental standards, says Glynn: "We have a real breadth of quality of stock across the UK, a very high proportion of which is non-purpose built or pre-dates 2000."

The prospect of major investment in environmental estate upgrades can be a daunting one for operators. As well as the upfront costs, managers naturally want to be sure that the technology they install does not risk impairing residents' experience of their services, even as it reduces emissions.

Operators who do pursue improvements will find lenders offer an increasing number of green financing products. And, according to Glynn, many investors who have leased healthcare properties to operators are now open to collaboration on finding solutions.

"These leases have often been drawn up several years prior, before ESG became prominent. Investors now find that they have no control over a building until it comes back to them in the mid-2040s – and by 2050 it might need to be net zero carbon. Many investors that I speak to are now saying they will work with operators in a partnership approach, to ensure those buildings continue to deliver."

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>
> **Jonathan Freeman**
> Sustainability Director, CareTech

Barclays' Matt Jolley acknowledges the high cost of transition and appreciates why businesses may feel nervous about taking the first step. His key advice is to start with easy-to-measure yardsticks, such as carbon emissions, energy consumption and waste levels, before going on to broader business practices.

Most businesses have already made some achievements, he adds: these should be recorded alongside the targets, "so it's all easily accessible for colleagues when they're working on procurement or with customers and other stakeholders."

Defining social impact
While environmental action can have the most direct impact on costs, operators cannot afford to neglect the 'S' and 'G' elements of ESG, says Glynn.

On the face of it, the social impact of social care providers should be straightforward – it is, after all, the reason for the sector's existence. For CareTech's service users, impact can range from gaining a job or a qualification, to being able to dress independently or make a cup of tea.

"Lots of organisations measure their community giving or volunteering, but that's the easy bit," Freeman says. "None of them look at the core business. How do you put a social metric around our core work? That's going to be tough, but given outcomes-based commissioning, I think it's the way the sector has to go."

CareTech is developing its own metrics, based around four broad themes: independent living, learning, thriving and participation.

Freeman hopes technology will make recording as streamlined as possible, allowing staff to focus on care. The successful roll-out of the Mind of My Own app – which allows young service users to log their feelings around mental health – is already providing some valuable data.

Sustainable delivery
Technology of this kind also has a part to play in future service delivery. For CareTech, a vision of a sustainable future cannot be founded on business as usual.

In 2020 the company acquired Smartbox, an assistive technology firm that allows disabled people without speech to have a voice and live more independently. It's a symbol of CareTech's intention to be a digital leader in the sector – underlined by its identification of innovation as one of the four pillars of its strategy.

The business will continue to harness new innovations, says Freeman: "We can't keep on just delivering social care the way we always have – it's becoming exponentially more expensive, while not meeting people's needs. The way we provide care can change dramatically for the better."

True diversity
Measures to ensure staff wellbeing and development are also a key element of the social impact agenda. That includes an effective commitment to diversity, says Matt Jolley.

While the health and social care sector have highly diverse workforces, that is not always evident in the boardroom: "The important bit is making sure diversity flows right through to the top," Jolley says. "That's where you often get a disjoint, where executive management level doesn't match the diversity of the workforce and the community served by the organisation." This is an issue that funders of sustainability-linked financing often home in on, he observes.

While good governance in the sector is heavily monitored through regulation, some operators are finding ways to strengthen this further – for example, by recruiting non-executive directors to provide challenge.

"The important bit is making sure diversity flows right to the top. That's where you often get a disjoint - where executive management level doesn't match the diversity of the workforce"

Matt Jolley
Head of ESG Origination, Barclays Corporate Banking

Realistic attitude
Gathering these diverse elements into a coherent strategy – and putting it at the centre of the business – is key to success, according to Freeman at CareTech.

"If the sustainability agenda is just something nice on the side, it will fail," he says. "We're genuinely doing this because it's the right thing, but if it didn't directly support the business it would always be marginalised."

He is realistic about the company's progress towards its targets: "We're not going to do everything tomorrow, and we're not going to get it all right. I'm sure we will have a year where perhaps we go backwards or sideways, but that doesn't matter – it's a long-term agenda that we're embarking on. I'm blessed with a senior leadership team who understand this agenda and empower me to make it happen."

Bottom-line benefits

Strong ESG commitment helps Spire Healthcare drive success

As Interim Head of Investor Relations and ESG lead at Spire Healthcare, one of the country's leading private hospital and healthcare providers, Angus Prentice is witnessing first-hand "the rising importance of ESG within the sector", as well as the impact ESG can have on the bottom line for healthcare firms.

"I agree, generally, that many firms in this sector are lagging when it comes to ESG – and especially when it comes to being able to demonstrate their ESG credentials, even if they are actually doing some good things already," he explains. "It's a bit of a mixed bag. Some firms are certainly better than others. But the more sophisticated businesses are really embedding ESG into their business strategy now."

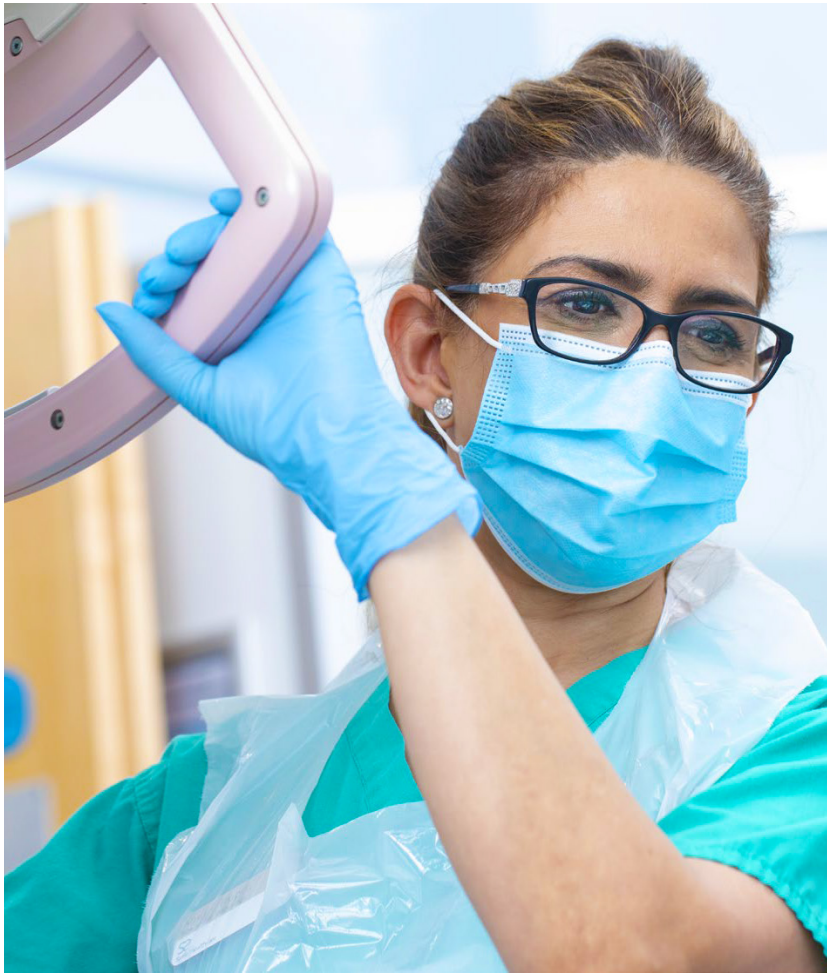
Reputational risks

In his frontline investor relations role at Spire – which operates 39 hospitals and eight clinics across the UK and has a market capitalisation of nearly £1bn – Prentice is clear on the risks facing healthcare firms that fail to grasp the importance of ESG today.

"Many of the risks are transparent and obvious," he says. "As a listed company, there is a real risk of falling out of favour with institutional investors and the lending banks. That is a real issue now because investors are absolutely scrutinising every aspect of where their money goes. Falling behind on ESG certainly has the potential to make it more challenging to raise finance.

"But there are more subtle risks, too – such as failing to attract and retain the right colleagues in an increasingly competitive talent market," he adds. "People coming into the healthcare sector are now quite cognizant of and keen to understand how an organisation deals with its people, how it relates to its people, how it relates to diversity.

"What's more, our hospitals and clinics sit at the heart of local communities – and those communities are also becoming increasingly aware of performance and reputation. So, it's also increasingly critical in terms of ensuring we are front of mind when they are choosing a provider."



Early stages
While Spire is clearly working hard to demonstrate its own ESG credentials, Prentice says that, like many other organisations, it's really only in the early stages of telling its full ESG story.

"I certainly put our hand up and say we're only just getting into this," he explains. "If I use the metaphor of a 100-metre race – we're probably still in the first 25 metres. It's not that we've not been conducting a number of ESG-related initiatives and actions for several years. It's actually about pulling that together into something that people would recognise as a sustainability report, whether that's a standalone report or a part of the annual report. We're really only just starting that."

Despite that, the firm has made some considerable strides in recent times.

"Sustainability is now very much part of our agenda and the way we operate," Prentice says. "We have a stated ambition to target net zero carbon emissions by 2030, which is part of our sustainability-linked funding via Barclays, and there is evidence of that in the work we have done to convert to steam boilers within our hospitals, the photovoltaic panels we now have on top of our buildings, and the electricity charging points we have installed.

"Outside of carbon, there is very clear evidence of our commitment through our waste disposal strategy, where we are working hard to reduce single-use plastics in order to reduce pollution. And we have a very strong social agenda within the business, which is now one of our core pillars."

Cost benefits
While those moves are helping demonstrate Spire's commitment to ESG, they are also delivering clear and tangible benefits to the balance sheet.

Among those, Prentice cites a reduction in energy costs as a result of the photovoltaic panels and LED lighting installed across sites; a reduction in recruitment costs and an ability to attract the best talent; and greater staff retention.

So, how can others in the sector advance their own ESG journey? Prentice points to three clear actions.

"The first thing is to just get on with it," he says. "Don't be put off by the complexity – just jump in and get started. The second thing is that it's OK to begin with incremental steps – you don't have to start with a with a fully-fledged end game, and that comes back to the 100-metre race analogy. And, finally, lead from the top. Only if it is led from the very top and endorsed at board level can ESG truly be embedded in the culture of the business."

"Only if it is led from the very top and endorsed at board level can ESG truly be embedded in the culture of the business."

Angus Prentice
Interim Head of Investor Relations and ESG lead, Spire Healthcare

Barclays ESG solutions

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Find out more: barclayscorporate.com/solutions/corporate-banking-solutions/green-solutions

Strategies for success

Key steps to a dynamic, credible ESG plan

Reach out

Don't work in isolation. Seek guidance from external partners, such as your bank; find out how your peers, customers and suppliers are tackling ESG.

Measure and plan

Set a baseline through audit. Work out which actions will have the most impact – perhaps in insulation, recycling, water efficiencies – so you can gain some quick wins. Record progress, including advances made before your plan came into action.

Involve staff

Share your plan with staff. Ensure that it's simple and engaging. Allow teams to devise and work on their own ESG projects, within set parameters. Ensure your commitments are prominent in your recruitment materials.

Don't forget the S...

Assess your social impact, from how you support local communities and ensure staff wellbeing to how you measure care quality. Consider ways you might develop the latter beyond regulatory metrics, perhaps involving clients and service users.

...and the G

Start by assessing your policies on diversity and inclusion, especially at more senior levels. Consider acquiring an external challenge at board level on these issues if not already in place.

About the author

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Steve joined Barclays in 2019 and was appointed Head of Healthcare in 2020. With more than 15 years' experience within Corporate Banking, he has undertaken roles ranging from leveraged finance to client coverage, with his focus being purely on healthcare over the past eight years.

The Barclays Corporate Healthcare team supports a wide-ranging client base with their dedicated specialist approach, industry knowledge, and sector-specific products and services.

For further information and to find out how our sector specialist team can help your business respond to the issues outlined in this report, please contact Steve Fergus

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