The drive for low carbon growth is reshaping the rules of supply, demand and regulation. Before long, an economically sustainable business will simply be a good business. While some have been quick to innovate, mistrust, delusion and disengagement still exist. In this article, Criticaleye asked Peter Lacy and Justin Keeble, of Accenture, how sustainability can become ingrained in the business agenda, how should leaders approach sustainability issues in terms of regulation and reporting, what are the challenges, which companies are succeeding and why businesses should view the move to a low-carbon economy as a business opportunity and a chance to secure a competitive advantage.
As we enter a new era of opportunity in sustainability and technology, the next decade will represent a disaggregation of carbon in the value chain. This shift towards sustainability will be the next disruptive trend and means that every leader will have to consider how to secure innovation and technological competitive advantage.

Sustainability changes a business’s inputs and the way leaders think about labour, talent management and employee engagement. There are changes to consumer demand too – increasingly NGOs and other stakeholders are influencing demand curves because they are changing their wants and needs. The ‘rules of the game’ are also changing; the increased prominence of environmental issues - driven by, for example, The Stern Report in 2006 and The Copenhagen Summit in 2009 - is changing the way that leading businesses approach their strategy and operations.

COMMUNITY COMMENT
Christine Farnish
Public Policy Director
Barclays

“With regard to regulation, the ‘something must be done’ mentality will often lead to actions being taken without fully thinking through the consequences. In the UK, especially, when you’ve got regulation set in primary, and sometimes secondary, legislation it is very difficult to go back and revisit it. We need to have that feedback loop. And the onus is on organisations to work with government to help them set workable frameworks. We’re not currently so good at doing it in this country. Does making formal demands on companies to report (whereby you get reams and reams of impenetrable data and teams of lawyers pouring over disclaimers) make the world a better place? Surely a better approach is to have continual pressure on businesses to be accountable and transparent about their practices, looking more carefully at how they operate, especially those difficult, crunch decisions, where they have to make judgements on whom not to do business with. I think it’s more about businesses saying no to certain things that are perfectly within the law, but where their ethics, culture or desire to protect their reputation says, ‘we don’t want to go there, these are the reasons why and we’re going to form a company policy on it’. It’s about being more willing to disclose that type of approach. I think that’s the way we’re going and I think that might deliver better outcomes.”

This shift in mindsets is informed by the recognition of an urgent need to reduce the carbon impact of the economy. Added to these pressures are increasing consumer and regulatory trends that will ultimately demand a new industrial revolution. In this new era, growth and innovation will be driven by technological advance.

As an integrated business challenge, sustainability needs to encompass social, environmental and governance pillars. And these pillars cannot be treated in isolation. Our UN Global Compact-Accenture CEO Study 2010 highlights increasing clarity on this issue at the highest level: most CEOs now recognise that sustainability is an integrated agenda.

How should leaders approach sustainability issues in terms of regulation and reporting?

In many areas we are going to see policy and regulatory measures drive incentives for good performance and create disincentives for poor performance. The UK government has pledged to meet a target of 80 per cent greenhouse gas emissions reductions by 2050 and has set legally binding emission reduction targets for 2020 (a reduction of 34 per cent in greenhouse gas emissions) so it is likely that by 2020, we will have some clear policy frameworks.

However, while science suggests that we need to move faster than this, our UN Global Compact-Accenture CEO Study has revealed that these regulatory drivers will not become mainstream for another decade. Eighty per cent of CEOs think it will take 10 to 15 years for sustainability to be fully integrated into the way that markets work and into the strategy and operations of the majority of global organisations.

Ultimately, carbon has a cost. The UK government has recently introduced five-yearly carbon budgets to help ensure the carbon targets are met. It runs in parallel to the financial budget and will eventually become an integrated part of the engine for growth. At the moment, we are playing around the edges with, for example, the Carbon Reduction Commitment. The plumbing is in; it’s just that the tap is not fully open. We must move beyond carbon to include other key metrics such as water, waste and biodiversity which will become part of the way we think about the balance sheet.

If you had asked the average FTSE CEO three years ago what their carbon footprint was, a third would have known exactly what it was, a third would have had some ideas...
about what it was, but little idea about what the underlying industry big themes were, and a third would have looked at you like some sort of ‘tree-hugging, sandal-wearing weirdo’. In 10 years, this will come full circle and sustainability will be part and parcel of the way businesses operate. It probably won’t be called ‘sustainability’ anymore, but will simply be embedded into the organisation’s working fabric.

We see more and more companies incorporating sustainability into their staff reward structure, although this currently takes place at a higher level. If you look at what it takes to transition a business towards competitive advantage in sustainability, there are three pillars: products and services, core capabilities and people. It’s about driving the right knowledge, skills and attitudes of managers and employees to be able to manage this, not as an isolated issue but as a lens for revenue growth, cost reduction, risk or brand intangibilities at their individual levels – whatever makes it real for them. This brings in the full HR mix of reward, training and development, leadership and learning. Indeed, we are seeing more and more CEOs integrating this into the executive board remuneration structure. Once that exists, the next challenge is to cascade it throughout the rest of the organisation.

What are the challenges in trying to engender trust on a business’s sustainability practices?

Based on our study, there appears to be plenty to be positive about when looking into the future of sustainable business practice: ninety-three per cent of CEOs believe that sustainability will be critical to the future success of their business; 80 per cent are doing more now than three years ago and 91 per cent plan to increase new technology in sustainability over the next decade.

However, the majority of leaders dramatically overestimate the progress that their business is making on sustainability: eighty per cent of CEOs think that they have fully integrated sustainability into their performance evaluations but, in reality, the figure is less than five per cent. And, of this fraction, none would actually admit it, because they would understand what ‘fully integrated’ really means and know that this is currently an unrealistic claim. Many leaders don’t appreciate what being fully sustainable really entails. They have misjudged the extent of the sustainability revolution and what it takes to create a successful business in this context.

There are delusions of stakeholder trust too. A huge delta has opened up between the levels of trust that the CEO believes he/she has and how people really perceive their company. For whatever reason, they are simply not grasping the reality.

As organisations, we need to be clearer and sharper about the way we measure and communicate the performance of products and services. We need to do this authentically and, in parallel, make this easier and simpler in order to engage the average consumer. As consumers, we want the simple ‘green, yellow, red’ approach; as business leaders, the adage, ‘don’t wait for demand, shape it yourself’ applies here.

For example, there’s an iPhone ‘app’, The Good Guide, which uses a compound index to rate various attributes for any given product that you scan into your iPhone. This is about using technology and
employing the full marketing mix to make things smoother at the point of purchase, to make complex messages simpler and transform consumer behaviour. The next 5 to 10 years will be all about articulating data in order to give the consumer greater ability to make their 'choice edits'.

From an employee perspective there is reliable data missing, but that’s largely because the data is not systematically formed into production processes. We must understand the sustainability key performance indicators (KPIs) across the products and services lifecycle, and how they play out across the different relationships between business measures. For this to happen, managers need metrics that will cascade KPIs down to performance incentives.

Fundamentally, there’s a huge difference between interpreting data and articulating it. When Boots did a study on the authenticity of products and services lifecycle, and how they play out across the different relationships between business measures. For this to happen, managers need metrics that will cascade KPIs down to performance incentives.

You never create competitive advantage by moving in step with the competition. GE’s attitude is “wait if you want, but we believe there’s real demand for this and we are positioning ourselves ahead of the curve”. It’s paid off too: the ‘ecomagination’ part of the business has developed a $20 billion revenue stream and has grown enormously in the last few years. Philips, too, is tapping into the demand for energy efficient products and services, particularly in their lighting business. In 2006, Philips set out to derive 30 per cent of its environmental portfolio related to sustainability by 2012. It achieved this target two years early and now, by 2015, wants half of its revenues to derive from energy efficiency, particularly in lighting. That’s already an eight billion dollar revenue stream.

You don’t create competitive advantage by moving in step with the competition

Sustainability is a huge factor in innovation. The ‘environment friendly’ shampoo that doesn’t need water, will therefore become more common.

**Which companies are leading the field in sustainable business practice?**

The companies that stand out are those that see sustainability as a lens for growth and innovation, not as a defensive risk and part of the reputational agenda. There are able to grasp the genuine business benefits, tapping into new markets and developing new products and services to tackle some of these business issues. Currently, this is most strikingly evident in the infrastructure and hi-tech space. GE, Siemens and Philips, for instance, represent a cluster of competing, yet differentiated companies that are making huge progress on this agenda.

Take Siemens. Nearly a third (30 per cent) of its business is now related to sustainable infrastructure - a $20 billion revenue stream of a $70 billion revenue company. Actually, it was the only part of the business that grew during the downturn - up 11 per cent in 2009.

Now take GE. Its growth focuses only on two things: affordable health care and clean energy. Under their R&D ‘ecomagination’ banner alone, they have essentially gambled $10 billion over the next five years that clean energy is the path to growth for the business. Despite the short-term uncertainty over regulation policy, GE believes the scientific play over the long-term will drive policy making.

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Think about the prevalence in usage of the term ‘e-commerce’ about a decade ago; now think about the last time you heard it used - you haven’t, because it’s been ingrained into the retailers’ and the consumers’ consciousness. And, if you understand that sustainability is a disruptive trend, it’s possible to see how having a ‘green’ or ‘eco’ prefix for your products and services will simply become irrelevant.

What are the key differences in how these issues are playing out in the emerging markets versus developed economies?

Sustainability is not just a preoccupation of industrialised countries. It is becoming more universally appreciated, too: ninety-eight per cent of CEOs in Asian-based businesses think sustainability will be important to the future growth of their business. The differences are down to, primarily, the lens of proximity: in the West, we’re worried about global emissions and the more macro preoccupations. But the reality for businesses in developing nations is concern over the local issues, such as air pollution, food scarcity, unclean water and the safety of the local workforce.

China is taking a big handful of clean technology spaghetti and throwing it against the wall to see what sticks

In other industries, M&S’s Plan A has thought very carefully about the impact of waste in its systems and has recognised that resource and energy efficiency is a positive market-value pay. As the supplier of choice for new materials, Bayer is also doing some exciting things.

Timberland, too, has recognised there is a growing expectation on price and product design for a premium lifestyle brand and has done some interesting work in the ‘cradle to cradle’ sphere – an idea first coined by global sustainability consultants MBDC where products are developed for closed-loop systems in which every ingredient is biodegradable or fully recyclable, and business operations are powered by renewable energy with a focus on respecting people and preserving ecosystems.

Up to 80 per cent of the materials from Timberland’s range of ‘Earthkeepers 2.0’ boots, for example, can be recycled or reused at the end of the boot’s first life. The Earthkeepers initiative has demanded a new approach from product designers, encouraging them to consider the whole-life

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 Camden Comment

Patrick Thomas, Chairman & CEO, Bayer MaterialScience AG

“We still need incentives to change. Indeed, many industries have the means to develop efficiencies, but are simply not encouraged to make use of it. In the automotive industry, for example, we know how to make cars lighter but the industry is traditionally conservative and there are capital barriers to innovation. Or take the chlorine industry. Bayer’s ‘ODC technology’ would mean 30 per cent less electricity is used in the production of chlorine which, for example, accounts for 4 per cent of total German electricity consumption. We know we can produce chlorine more efficiently, but there are no incentives to do this in the West. The Chinese do not appear to be similarly encumbered. By contrast, the Chinese are the fastest growing in this area. Bluestar, a Chinese/US private equity-backed joint venture, is building a pilot unit using the new technology. It fits with their values. They always ask ‘What’s that in terms of coal consumption?’ From Bayer’s perspective, our operation in Caojing, China, is now our largest manufacturing site in the world and the most energy efficient. It is a benchmark for all our facilities globally.

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thinking is also, if we drive this as fast as we can, there’s a tremendous opportunity to participate in a disruptive global trend and create a competitive advantage of nations.

In the same way that the US grew off the back of the IT explosion, this presents a strategic opportunity for emerging markets to have the same global domination. Tata Motors, for example, completely grasps the disruptive trend in automotive manufacturing. No one owns the leadership position for producing hybrid and electric cars and Tata understands where their strategy can impact dominance in local, and therefore global, markets.

China is positioning itself for global leadership in the transition to a sustainable, low-carbon global economy. The pace and scale of investment are staggering as it becomes the ‘clean tech laboratory’ of the world. In effect, China is taking a big handful of clean technology spaghetti and throwing it against the wall to see what sticks.

SUSTAINABILITY IS AT THE HEART OF BUSINESS OPPORTUNITY

To succeed along the sustainable path, businesses must align their sustainability practices with their core business strategy. They must understand how sustainability forces will impact their markets and view it not as a functional challenge, but as a way of thinking about business operations and strategy: how does this change my revenue structure, cost base, etc? For management, it’s undoubtedly a difficult conversation to have with business leaders, but it’s the only way to get real engagement, because they will be able to see how it can help the business grow market share.

The biggest challenge for CEOs is to translate this from strategy to execution across the business. CEOs often struggle to communicate this. It must be evidence-based, and it must be rigorously researched, as you would do on financial metrics for profit and loss. But, if you work backwards and infuse it into each part of the business, not as a standalone play, but as part of the overall HR mix, you can then articulate the correct incentives for all employees. That’s the next step to creating an organisation that genuinely engages on sustainability.

Based on our CEO survey, many leaders believe there are a number of must-have conditions that need to be put in place to encourage the integration of sustainability into core business practice:

1. Leaders need to increase the provision of consumer information and set clear standards
2. Governments need to increase incentives and investment in areas such as energy, transport and public infrastructure
3. CEOs need to increase their own efforts to engender the right skills and mindsets in their managers and future leaders
4. Leaders must better engage with investors to ensure that the value of sustainability activities can be demonstrated through traditional metrics such as cost reduction and revenue growth
5. Businesses need to measure the societal impacts of their business, manage sustainability’s impact on core business drivers and metrics and embed it in individual performance frameworks for managers across their organisations
6. Businesses need to take a leadership role in their collaboration with governments and NGOs to seek out genuine opportunities for business and societal benefit

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