

The Future of Sustainability Leadership

Why you must act **TODAY** to achieve sustainability leadership **TOMORROW**

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In this white paper, we describe what will define sustainability leadership in the future and contrast it with what has defined it previously. We then outline what companies should do to position themselves to compete successfully in the Sustainability Age and gain unprecedented competitive advantage.

The case for change

We are living beyond our means – not just in the financial sense but in the environmental sense as well. Today, we are depleting the resources of the planet at a rate 50% greater than can be sustained¹. To make things worse, the next few decades of population growth combined with the increase in developing countries' standards-of-living will result in a consumption boom that will further endanger the planet's life support systems (clean water, clean air, stable climate, etc.). For example, scientists now predict that in the next 50 years we will have to grow more food than in the entire history of mankind² to keep up with growing demand in a world constrained in fresh water and healthy soil. The social and environmental challenges we face have never been more daunting.

Perhaps surprisingly, many companies have found real and positive opportunities amidst this crisis. By being Sustainability Leaders – doing business in a way that has a positive social, environmental and financial impact – leading companies have gained

competitive advantage³ in the form of reduced costs, process improvement, product innovation and employee and customer engagement. **In short, Sustainability Leaders are growing stronger by helping to solve the world's most pressing problems.**

Initially, Sustainability Leaders found success by focusing on brand image and internal cost savings but today's leaders are taking sustainability one step further to transform their products and processes. In the future, companies will need to evolve once more and rewrite the rules of the game to leap ahead of their competitors. Those companies that have the foresight to become the leaders of tomorrow will be rewarded by record business opportunities.

How can a company become (or remain) a Sustainability Leader? In the rest of this article, we describe **what will define leadership in the future** and most importantly **how to mobilize your company to get there.**

¹ Based on Ecological Footprint Index, 2010 Living Planet Report, WWF

² CSIRO (Commonwealth Scientific and Industrial Research Organisation of Australia)

³ 2nd greatest benefit from sustainability after improved brand reputation in survey of more than 3,000 business executives and managers from organizations located around the world, "Sustainability: The 'Embracers' Seize Advantage", BCG/MIT Research Report, Winter 2011

Sustainability Leadership: Past, Present, and Future

In order to define future sustainability leadership, we must first describe what characterized sustainability leadership in the past and in the present.

Yesterday: the early days of sustainability

Leaders in corporate sustainability in the past were mostly focused on regulatory compliance and risk mitigation.

The companies that first embraced sustainability were generally those whose businesses were most significantly impacted by social and environmental risk. For example, reinsurance companies such as Swiss Re integrated the potential cost of climate change into their economic models in 1994 and others followed suit soon after Hurricane Katrina. Similarly, Nike's sustainability journey was prompted by the public outrage when it was revealed that the company employed children to manufacture its products.

The focus of these leaders was primarily on operations within the four walls of the company. Initiatives were typically led by a Director of Sustainability who was equipped with rough metrics to understand the company's impacts in areas such as carbon, water, and waste. The focus was on eco-efficiencies: incremental actions with quick return on investment such as using less energy, water, etc. SC Johnson became a leader by eliminating over 420 million pounds of waste from its products and processes over the course of a decade, and saving over \$125 million in the process⁴. Similarly, Coca Cola started improving its water efficiency when it was criticized for over-drawing local aquifers and depriving the local communities of drinking water. As a result, the company improved its water efficiency by 13% between 2004 and 2010⁵.

Consumer communication about sustainability was nascent. The brand image of companies improved based on green claims that were well-meaning but rarely verified by third parties (with the notable exception of the organic label). An early example of leadership in communication was the Marine Stewardship Council (MSC) label, which was created to guide consumers towards more sustainable seafood purchases. The label is based on transparent standards and certification is verified by a third party: two essential features for any credible customer-facing communication today.

Today: leaders have made sustainability core to their business

Today, leadership is dramatically different. Compliance and eco-efficiency have been overtaken by business transformation. Companies are now finding new sources of value from sustainability,

Past: Compliance and Integration

Leading companies thought:

- Sustainability is primarily an internal benefit but with tangible PR value
- Green products are a small but growing niche

Their priorities were:

- Risk mitigation
- Eco-efficiency
- Brand image

⁴ <http://www.environmental-expert.com/resultteacharticle.aspx?codi=1481>

⁵ liters of water used / liters of product produced, 2009/2010 Coca Cola Sustainability Review

ranging from new revenue (via product innovation, expansion in new markets) and intangible benefits such as employee engagement and brand loyalty.

Perhaps the most visible shift has been how sustainability efforts are now targeting the entire supply chain, beyond the company's internal operations. Leaders often use external help by collaborating deeply with suppliers and forging partnerships that once seemed unlikely with non-profit organizations and academics. Decisions are informed by a more complete understanding of impacts, often based on life cycle assessments (LCA). This allows efforts to focus on hot spots in the supply chain and transform the business in the few areas that matter. For example, Unilever recently announced the ambitious goal to halve the environmental impact of its products which will require the participation of its entire supply chain.

Today's leaders are initiating a "race to the top" in their supply chain where better products with smaller footprints are rewarded. This virtuous cycle of innovation is displacing the old mentality of "race to the bottom", where the cheapest (and often lowest quality) product used to win out. For example, concentrated laundry detergent, which takes less energy to make and transport, is slowly becoming the norm in supermarket aisles. Procter & Gamble has taken steps to create a race to the top by creating a scorecard to evaluate the sustainability performance of its top suppliers. Similarly, Walmart, recognizing that the vast majority of its footprint resides in its supply chain has made a series of announcements – ranging from evaluating product packaging to conducting supplier sustainability assessments – which have put its 100,000 suppliers on notice. Such initiatives are almost always being championed by senior executives in the business, not just a sustainability officer, leading to greater synergy between sustainability and business decisions.

Leaders today also use sustainability as a tool for innovation and new product development. By integrating new objectives and taking new constraints into consideration for their design, product developers have created new products that are better for people, better for the world and better for the bottom line. For example, General Electric's Ecomagination portfolio exceeded \$18 billion in sales in 2009⁶. Its German-based competitor Siemens has embraced sustainability as well and generated €28 billion in sales from its environmental portfolio in 2010⁷ which includes renewable energy, smart building controls, energy-efficient lighting and more.

Success stories are being told to consumers online and offline, creating a new world of radical transparency in which a curious consumer can see the auditable truth behind any green product claim. Although the amount of eco-labels, some of them dubious, has continued to grow, there are now tools such as GoodGuide that can help consumers sort through the green claims bombarding them.

Present: Business Transformation

Leading companies think:

- Sustainability is key to competitive advantage and innovation
- Mainstream products have gone green

Their priorities are:

- Engage supply chain and external experts
- Grow revenue (new products, new markets,...)
- Intangible benefits (employee motivation, customer loyalty,...)

⁶ www.ecomagination.com/about/fact-sheet

⁷ www.siemens.com/sustainability/en/environmental-portfolio/Facts-figures/index.htm

Sustainability leadership in the future: a whole new game

In the near future, massive change in the way businesses operate will create game-changing opportunities unseen since the Industrial Revolution.

Sustainability Leaders in the future will derive value from entirely new business models, new forms of innovation, and system optimization across a fully transparent supply chain. New winners and losers will emerge who will transform the competitive landscape.

In this new future, consumers will have at their finger-tips a complete life cycle view of the products they buy. They will be equipped with sustainability indices, sophisticated yet intuitive rating systems that provide true apples-to-apples comparisons so they can choose the most sustainable product both online and in the stores.

In leading companies, sustainability will be a priority for the CEO and Board of Directors as well as for every employee, who will be accountable for how his or her job makes a difference on the social and environmental impact of the company.

Perhaps most ground-breaking, a company's sustainability performance will start influencing investment decisions. Sophisticated investors, relying on the emerging valuation of nature's services (the products and services that nature provides today, but are not yet accounted for), will start investing and rewarding companies who are positioned to thrive in a resource constrained world.

The "How": Winning strategies for becoming a leader

The destination is clear, but the path to get there is tricky. What lessons can be learned from the companies on the leading edge? We looked at some game-changing efforts that are establishing the foundation for a new way to compete and win and identified a handful of critical elements to becoming a Sustainability Leader in the future:

- 1. Work with your competitors:** Shape a new playing field and then compete hard to win
- 2. Drive change across the system:** Engage the entire economic value chain
- 3. Measure and disclose like never before:** Embrace the radical transparency movement
- 4. Change your accounting system:** Learn how valuing nature changes the answer
- 5. Make it personal:** Build courage and create momentum to tackle tough problems

Future: System Change

Leading companies will think:

- Companies have fiduciary responsibility to drive long term benefit to shareholders and stakeholders
- Products with the best environmental and social footprint are also the least expensive

Their priorities will be:

- Redefine industry rules
- New business models
- Process innovation
- Transparent, lean supply chain

1. Work with your competitors

In late 2009, two very unlikely partners met to discuss the future of apparel. Patagonia and Walmart, a proverbial David and Goliath, were an odd but compelling couple. What has resulted is the Sustainable Apparel Coalition, a partnership with many other forward thinking apparel retailers (Nike, Levi's, Gap, and Timberland just to name a few of the 30 or so organizations). Publicly announced in March 2011, the vision of the organization is to produce "no unnecessary environmental harm" and have a "positive impact on the people and communities associated with its activities."

By building on the foundation of the Outdoor Industry Association's Eco-Index and Nike's work in creation of its "Considered" design tools, the Sustainable Apparel Coalition was able to develop an index prototype in less than a year. This prototype is undergoing a thorough vetting with internal experts and external stakeholders, and will be piloted in the fall of this year. While it is still early days, this effort is noteworthy for a simple fact: they believe **working together to address problems no individual company can solve alone is the necessary foundational step to creating a new playing field on which they can then compete (hard) to win.** This pre-competitive collaboration is helping to define new rules of the game, which provides the Coalition members with a competitive advantage over any company not involved in the effort.

2. Drive change across the system

A significant source of greenhouse gas (GHG) emissions is the cattle and dairy industries. Annual emissions from the US dairy industry contribute as much carbon dioxide equivalent as 23 million cars. To tackle this problem, Dairy Management Inc. and the Innovation Center for US Dairy convened two "system-in-the-room" summits. These events, which gathered participants from "grass to glass," were designed to find common ground between the sometimes antagonistic members of the milk value chain. After two summits, the entire value chain quickly identified the few things that drive the most greenhouse gas emissions in the milk value chain and launched projects that will reduce emissions by 25% by 2020.

Specifically, the Dairy Power 2009 summit held in New York identified 17 specific initiatives to move forward the technology of methane digesters, which is an innovative way to turn manure into energy while dramatically reducing greenhouse gas emissions. This was accomplished with 200 cross-industry participants, including state and local government representatives. **This type of rapid breakthrough is only possible when you convene and effectively coordinate the actions of the entire system to find solutions that are beneficial to everyone involved.** It can be a powerful approach for companies that have decided to collaborate with their competitors pre-competitively.

3. Measure and disclose like never before

In 2009, Walmart announced it was supporting the creation of a Sustainability Index. The vision: encourage all consumer packaged goods companies to create more sustainable products. Today, over 70 companies (representing over \$1 trillion in purchasing power) such as Coca-Cola, Cargill, McDonalds, Intel, 3M, and Unilever have joined the Sustainability Consortium to create the underlying science and standards needed for the Index to become a reality.

Many companies - ranging from major players like SAP to LCA specialists - are investing millions to build solutions that will enable companies to collect and use data like never before. In the meantime, companies collecting and analyzing data with rough tools based on industry averages are already finding that it provides new and welcome insights into their business.

The trend is unmistakable and unstoppable. **Radical transparency, in this age of WikiLeaks, is here to stay.** Those who aspire to lead must be ready to share data which they have never before been asked to share. The information will drive change in B2B at first as companies encourage their supply chain partners to disclose more information about their sustainability performance. The companies who choose to share information more broadly, more transparently will be rewarded by enhanced customer trust and loyalty.



4. *Change your accounting system*

How much is nature worth? The estimate for the value of the free goods and services nature provides – clean air and water, climate regulation, soil erosion protection, pollination, and pest control and more – ranges between \$16-54 trillion⁸ (that's one to four times the GDP of the United States). Yet today most of the value of these "ecosystem services" is not priced into cost of goods and services we buy. How would it affect the decisions businesses make today if the true cost of our industrial system were readily apparent in the cost we pay?

This question is not as theoretical or far-fetched as it might seem. In February 2011, Dow Chemical and The Nature Conservancy announced that they are embarking on a 5 year, \$10 million joint effort to calculate the ecosystem costs and benefits at three of their manufacturing plants⁹. Recently, the apparel company Puma announced a similarly intentioned effort to produce an environmental profit-and-loss statement. The World Business Council for Sustainable Development (an organization whose members total \$7 trillion in annual revenues) in April just released their Guide to Corporate Ecosystem Valuation. This guide has already been tested by 14 global companies including AkzoNobel, Hitachi, Syngenta, Rio Tinto, and Veolia Environment¹⁰.

Leading companies are realizing that a new accounting system is emerging, **GAAP (Generally Accepted Accounting Principles) for the Sustainability Age**. The companies that understand how valuing nature changes the answer will be better positioned to compete and win when investors start integrating the value of ecosystems into their decisions.

5. *Make it personal*

A final element is essential for future leadership: people. Often, when companies focus on the rationale for sustainability, the human component is overlooked. **In many instances that we have seen, personal courage and passion of individuals is required for companies to become Sustainability Leaders, especially in the CEO role.**

Without seeing, tasting and experiencing it firsthand, the world's environmental and social challenges are sometimes too remote to fathom and too daunting to tackle. At Blu Skye, we take some of the world's most powerful executives on immersive journeys so they can experience sustainability challenges and understand how the decisions in their control can create meaningful change. For example, we recently took the leadership team of a \$50 billion company to witness the impact of beef production (via pollution from water run-off) on the marine ecosystem of the Chesapeake Bay and met

Putting a Price on Nature

The value that ecosystems contribute to human well-being is referred to as **ecosystem services**, and there have been increasing efforts to measure, in dollar terms, the value of the myriad benefits of ecosystem services such as erosion control, fresh water supply, carbon sequestration, clean air, raw materials, plant diversity to support new discoveries in drugs and pollinating insects to support global agriculture.



⁸ The Value of the World's Ecosystem Services and Natural Capital, Nature, May 1997

⁹ www.dow.com/news/multimedia/media_kits/2011_01_24a/pdfs/dow-tnc_joint_press_release.pdf

¹⁰ World Business Council for Sustainable Development, press release, April 7 2011

the people who have designed some groundbreaking solutions to tackle this challenge. This allowed the executives to viscerally understand the results their purchasing decisions had on the livelihoods of fishermen and build courage to expand the scope of their sustainability efforts.

Establishing a personal connection with sustainability is part of a larger trend. The alignment of personal goals along with company goals, combining both emotion and reason, will enable companies to tap into their employees' sense of purpose and unleash a tremendous force for change. This is exactly what is required to overcome the immense challenges we face.

In this inevitable and urgent future that is unfolding, all the world's key decision makers: producers, distributors, consumers, governments, investors, and employees are integrating sustainability into their decisions. The flow of money in our global economy will become increasingly consistent with the laws of nature.

For those business leaders who have the foresight to see the trends unfolding before our eyes, they will understand that existing business models are not simply being modified, they are being replaced. There will be new strategies for how to compete, how to innovate across entire systems, how to work with suppliers and customers, how to account for hidden assets (e.g. nature) in decision making, and how to inspire and find the courage to do the right thing.

They will also realize that although this type of system change is difficult, it is required. For those that act now, it will open up tremendous business opportunities. These prescient business leaders will not only create and win on the new playing field, they will shape and improve the world that we all live in.

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Blu Skye is a strategy consulting firm dedicated to helping companies create competitive advantage from sustainability. Find out more at bluskye.com.

Evolution of Sustainability Leadership: Summary

	Past: Compliance and Integration	Present: Business Transformation	Future: System Change
Tagline (Company)	"Sustainability is primarily an internal benefit but with tangible PR value"	"Sustainability is key to competitive advantage and innovation"	"Companies have fiduciary responsibility to drive long-term benefit to shareholders and stakeholders"
Tagline (Products)	"Green products are small and growing niche"	"Mainstream products have gone green"	"Products with the best environmental and social footprint are also the least expensive"
Business Value	Moderate value <ul style="list-style-type: none"> Eco-efficiencies (costs) PR/brand Risk mitigation (license to operate, security of supply) 	High value to the company <ul style="list-style-type: none"> Product Innovation New markets Intangibles (brand, employees,...) 	Highest value to the company and the broader system <ul style="list-style-type: none"> Process innovation New business models Transparent, lean supply chain
Scope	Internal, within 4 walls	External, including supply chains & external help (NGOs, academics, government)	Economic system, including competitors (pre-competitive)
Strategy focused on:	Quick wins	Innovation	Game changers
...and led by:	Head of sustainability	Senior executive in the business	CEO and Board of Directors
Employee engagement	Encourage after work activities (volunteer, donation matching, etc.)	Sustainability is a tool for employee engagement (green teams)	Sustainability is part of the job description for every employee
Metrics	Basic footprint	Life Cycle Assessment based	All impacts, using a new "accounting system"
Impacts measured	Carbon, maybe water/waste	All impacts, often spanning life cycle	All impacts, full ecosystem impacts (including externalities)
Regulation	Compliance	Voluntary corporate actions	Redefined industry rules
Consumer facing	Tower of "eco-babel", no transparency	Select sustainability ratings (e.g. GoodGuide), some transparency	Sustainability Index, full transparency, nearly all products