

Is sustainability incompatible with business growth?

A summary of the Atradius white paper
November 2009



Sustainability. Meeting the needs of the present without undermining the ability of future generations to meet their own needs.¹

¹This is the classic definition of sustainability that first appeared in the Brundtland Commission report *Our Common Future* 1987

Sustainability in business is not just an ethical question, but a crucial factor in future commercial success. The Atradius white paper looks at a range of factors that can help – or hinder - a sustainable business process: governmental encouragement or penalty; a shift in consumer demand; and an increasing awareness of the implications of either adopting or rejecting sustainability. It shows that sustainability can pay dividends at a time when businesses are seeking ways to improve their bottom line.

Sustainability as a commercial necessity

In a recent speech on the Global Green Economy, UN Under-Secretary General Achim Steiner pointed to the fact that, often, commercial enterprises are slow to understand the commercial possibilities of technologies designed to improve our living conditions, and those of future generations.

In its 2004 report ‘The Materiality of Social, Environmental and Corporate Governance Issues to Equity Pricing’, the UN (through its Environmental Programme Finance Initiative) demonstrated how some leading industrial players integrate sustainability considerations into their equity valuations. The overall finding of the report was that environmental and social criteria are important to investors with a long term focus.

The commercial potential of ‘The Green Economy’ is also apparent in the far-sightedness of Japanese car makers in producing high-tech fuel efficient cars like the Toyota Prius.

The cost and potential savings of adopting a sustainability policy

In any industry, where processes are changed, there will be an initial ‘set up’ cost: the cost of investment in adapting equipment, retraining, rebranding, and redesign. Many businesses have been deterred from changing to a sustainable policy for fear of incurring major costs. But lack of clarity can itself be a deterrent to meaningful change.

The role of governments

Governments can both encourage businesses to introduce sustainable processes and penalise those who don't. But for change to be lasting it has to be consensual, not forced. Penalties do not themselves provide a solution, and may be viewed as an acceptable 'fee' for continuing to act in a certain manner, rather than as a way to change behaviour. It is tax breaks, government investment and subsidy in the development of sustainable technologies that achieve long term goals.

Governments can play an important role in taking the development of sustainable technologies and renewable energy out of the competitive arena, so that all nations can gain from those developments.

An example of how governments can stimulate the industry to the benefit of all those involved is that of Germany's support for its solar power industry, by setting above-market prices for electricity produced through renewable means and stipulating that utilities must buy it. Similar arrangements across Europe have ensured that technologies can compete with fossil fuels. The aim is to increase renewable market share to meet the goal of 20% of European energy produced from renewable sources by 2020.

Total Quality Management

The link between Total Quality Management (TQM) and sustainability was described by Professor Mohamed Zairi, chair in TQM at the University of Bradford School of Management, UK, in his 2005 paper 'TQM Sustainability: how to Maintain its Gains Through Transformational Change'. He defines sustainability as 'the ability of an organisation to adapt to change in the business environment to capture contemporary best practice methods and to achieve and maintain superior competitive performance. The reasons for pursuing sustainability are: morality, intergenerational equity, survival, and organizational benefits and risks'.

The opportunities afforded by sustainability

In its research document 'Innovative environmental growth markets from a company perspective' (November 2007), strategy consultants Roland Berger looked at the extent to which the European environmental technology industry contributes - and has the potential to contribute further - towards European economic growth. Berger recommended a range of measures that could enable the industry to flourish even more, including:

- Ambitious targets set by governments to push businesses to become innovative.
- Pan-European harmonization of conditions and regulations.
- Stimulation of demand through public procurement of environmental products.
- More financial stimuli, simplification of requirements for obtaining research and development funding, easier access to loans and long term subsidy programmes.

The obstacles to progress

China is still the world's largest producer of CO₂ from power generation: it overtook the US in the second half of 2008, although per capita the US's emissions still far outweigh those of China. Despite its ratification of the Kyoto treaty, the

rise in China's emission of green house gases – up 120% since the beginning of the decade – calls into question the real effectiveness of Kyoto. There is however an argument that emerging economies, even of the magnitude of China and India, have a right to develop their economies in the same way that Western industrialised nations have in the past.

Challenging China over its pollution record would be futile at a time when it can simply point to the lack of action on sustainability by the USA (in failing to ratify the Kyoto Protocol): far better to concentrate efforts on convincing the USA, under its new regime, and thus remove the central pillar of China's justification of its actions.

These economic giants aside, globally, we consume renewable capital such as forests far faster than they can be regenerated, and pump out green house gases faster than they can be absorbed and neutralised.

Education – and people power

What strengthens the case for change, in whatever context, is education and transparency, enabling the public to make informed decisions. Individuals within businesses, as well as their customers, can influence the way that those businesses operate.

Judah Schiller, Executive Vice President of the PR and Marketing firm Saatchi & Saatchi S, was instrumental in introducing a Personal Sustainability Project (PSP) to multi-national corporation Walmart. As he put it in a recent interview: *'The natural inclination for most companies is toward a traditional, top-down program, but we've found that top-down approaches don't tend to work for sustainability. The much more effective approach is to educate and inspire and to provide people with the resources and channels to take action. Employees ... are the ones who ultimately change the way operations are run, materials are sourced, and products are manufactured and distributed'*.

That underlines that 'people power' requires the foundation of independent and unbiased education on the issue of sustainability to create an understanding of the outcomes of either ignoring or redressing the warning signs.

Adult education in any field is naturally more complex than for those in full time education, and needs to be present everywhere to be effective: combining government policy, and a wide range of channels for information and advertising.

The process of education can also come from clear leadership on sustainability from within industries. Where that leadership is lacking it is difficult if not impossible to engage a whole industry within a country in a drive to reduce carbon emissions and achieve cost savings.

The obligation on business to change

In March 2009 Atradius published its report 'Saving the planet: risk and opportunities in climate protection'. The introduction states: *'Environmental protection is a cause that is easy to embrace. No one wants to leave a damaged planet for future generations, and by now everyone is aware of scientific evidence pointing to a warming trend in the atmosphere. Business has a particularly important role to play in ensuring a cleaner future – by both reversing past practices that may contribute to the problem, and by devising innovative alternatives'*.

Most people have a social conscience and a tendency to do what they consider to be right. Hence more and more businesses are setting out a sustainability policy, and ensuring that sustainability is a boardroom issue that helps drive costs down and quality up, and increases both customer and employee satisfaction. They are adopting what has become known as the ‘triple bottom line’ approach: people, profits, planet.

The Triple Bottom Line

In his book ‘The Triple Bottom Line’, Andrew W Savitz points to both the underlying misunderstanding that many businesses have of sustainability, and to the tipping point when businesses realise that there is a better way of operating.

First, the misunderstanding:

‘Business leaders with a superficial understanding of sustainability think of it as a distraction from their main purpose, a chore they hope can be discharged quickly and easily. "We're responsible corporate citizens, so let's write a check to the United Way or allow employees to volunteer for the local cleanup drive or food kitchen and get back to work."

This approach reveals a fundamental misunderstanding. Sustainability is not about philanthropy. There's nothing wrong with corporate charity, but the sustainable company conducts its business so that benefits flow naturally to all stakeholders, including employees, customers, business partners, the communities in which it operates, and, of course, shareholders.’

And the tipping point...

‘It could be said that the truly sustainable company would have no need to write checks to charity or "give back" to the local community, because the company's daily operations wouldn't deprive the community, but would enrich it. Sustainable companies find areas of mutual interest and ways to make "doing good" and "doing well" synonymous, thus avoiding the implied conflict between society and shareholders.’

Once a business has understood the benefits of a sustainable approach, its attitude to the role of governments and other regulatory bodies can change: the targets set by those bodies become a helpful yardstick to measure progress rather than an imposition.

The practical cost benefits of a sustainable approach also take on a new dimension, as the business’s economic values are augmented naturally by a set of ethical values.

The following excerpt from the Dow Jones Sustainability Indexes (DJSI) –which tracks the financial performance of leading sustainability-driven companies worldwide – shows the all-round benefits that this holistic view of sustainability can achieve:

‘With 3M's Pollution Prevention Pays (3P) program being in its fourth decade, the high visibility regarding environmental management systems and eco-efficiency comes as no surprise. Emission data point toward consistent improvement in eco-efficiency. Eco-design and life-cycle assessment techniques are systematically used during new product development thereby responding to customer demand for environmentally lean products and reducing exposure to future liabilities. Recent examples from the innovation stream include fire protection fluids with minimal

environmental impact and low emission solvent as well as solventless technologies for adhesive applications. The stream of product innovations is grounded in the company's approach to human capital development and talent attraction and retention, criteria in which the company outperforms its industry peers.'

Beware of Greenwash

There will still be those who see being 'green' as a marketing ploy rather than a genuine corporate philosophy: as a way to position themselves in a more favourable light and thereby gain a competitive advantage. The Atradius report 'Saving the Planet: risks and opportunities in climate protection' refers to the 2008 survey by corporate brand identity and image consultants Lippincott that showed a direct correlation between consumers' loyalty to particular brands and those companies' stated ambitions to act on climate change.

However, consumers are increasingly sceptical of corporate claims to be 'green'. The UK Advertising Standards Authority for one has reported a sharp rise in consumer complaints about so-called 'green wash': dubious claims to environmental purity.

Conclusions and recommendations

Sustainability and business growth are not at odds with each other. There is much to be gained in terms of cost savings, increased market share, improved service, customer satisfaction, brand value, and increased profitability, from adopting a sustainable policy.

Cost savings - As a natural extension of total quality management, a business that concentrates on the economic and effective use of all its finite resources will, by definition, save costs.

Increased market share - As informed consumers express their preference for products and services produced using sustainable processes, those businesses that have foreseen this trend and adapted products and processes accordingly will be the suppliers of choice.

Improved service - A business that has an ethical dimension to its business model that encompasses the three Ps – People, Profits, Planet – will engage its own employees fully in its vision.

Customer satisfaction – Most people want to feel that they are contributing, through their choices and actions, to a healthier environment. A sustainability ethic within a business leads to greater overall satisfaction for its customers.

Brand value - The genuinely eco-responsible business will gain kudos for its brand simply by living up to its stated standards.

Increased profitability - The bottom line. And the end result that accrues from the combination of each of the other benefits listed above: cost savings, market share, service, satisfaction and value.

The role of government

Governments have a vital part to play in creating a sustainable business environment. While the will to change must come from within business itself, the environment in which this can be fostered is to a large degree created by governments. Governments can and should encourage sustainable business through incentives and subsidies, and

punish transgressors through taxation or fines. However, penalties should be used with caution as they in themselves may be viewed as an acceptable price to pay for continuing a polluting process.

Governments can and should encourage the development of new environmental technologies, through subsidies and by actions designed to create a market for those technologies and their end-products. This will generate the revenue to offset at least some of the initial costs of developing sustainable industries.

People power and education

As people become more informed, through the many and varied channels of education and awareness, they become more discerning and more demanding. People aren't simply prepared unquestioningly to accept what is offered to them:

Our investigation has found that businesses have much to gain from adopting a sustainability philosophy.

- We would recommend therefore that governments develop a model for supporting and funding the development of sustainable industry and technology – as the German government has. Initiatives such as the Kyoto Protocol and the forthcoming Copenhagen gathering should continue to seek the commitment of all participants to regulate and encourage their respective industries to develop sustainable processes. However, the long term aim of all governments must be to enable sustainable industries to become self sufficient.
- We would recommend that the development of sustainable technologies and renewable energy sources be taken out of the competitive arena. By sharing knowledge, governments and those involved in the development of those technologies can accelerate that development to the benefit of all nations.
- We endorse the use of positive incentives, such as tax breaks that encourage businesses to adopt sustainable processes. However we warn against penalties for nations and businesses that continue to pollute if those penalties are being perceived to be, and used as, an acceptable 'fee' for maintaining the status quo.
- We would recommend that all businesses investigate the positive profitable benefits of adopting a sustainability policy – in the holistic sense described as 'The Triple Bottom Line': People, Profits, Planet.
- We see education and transparency as the real key to creating long term sustainable benefits in business. We therefore urge governments to:
 - provide clear and unbiased information on the benefits of sustainability,
 - set measurable standards of sustainability and timelines for businesses to meet those standards - coupled with guidance on how they should do so,
 - publicise clear information about which businesses are complying, or taking action to comply, with those standards. Based upon that knowledge, this will enable consumers to make informed choices.