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Sustainability

Can business do well by doing good?

By Bruno Berthon, David J. Abood and Peter Lacy

Yes, but not until basic sustainability practices are fully integrated into the way business is done, both strategically and operationally. For that to happen, five major obstacles must be overcome.

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Today, there probably isn't a company anywhere in the world that does not at least acknowledge the importance of sustainability—of doing business in an environmentally and socially responsible way.

Indeed, for many companies, sustainability is now as much of a strategic priority as such traditional business concerns as technology, talent and customers. The commitment to sustainability has weathered the storm of the downturn well; in some cases, it has even been strengthened by it. Meanwhile, an emerging body of research suggests that sustainable business practices correlate closely with high performance.

On an operational level, however, sustainability is not yet seamlessly woven into the fabric of business. Executives still must make, almost daily, difficult trade-offs between practices that meet short-term business needs and those that will contribute to sustaining the needs of future generations.

A new research study from Accenture, in partnership with the United Nations, captures the dilemma of the world's CEOs, who are caught between the long-term perspective of sustainability and the near-term pressures of the bottom line.*

This conflict can be seen on another level as well: Investments in sustainability today are seldom reflected in next quarter's earnings announcement. This misalignment, which is, of course, a function of basic financial performance analysis, must be reconciled before sustainability can be integrated and embedded in operations—that is,

before sustainability becomes a truly integral part of what it means to be a high-performance business.

According to the Accenture–UN research, 93 percent of CEOs surveyed globally see sustainability as important to their companies' future success. Across a number of parameters, corporate commitment to sustainability has increased since the last time a similar CEO survey was conducted in 2007.

Sustainability and performance

Such commitment is also being rewarded in terms of business performance. Accenture Sustainability Services, in conjunction with the company's Institute for High Performance, recently compared the business performance and sustainability performance data of a representative cross-industry group of 275 companies from the Fortune Global 1,000. The research found that the 50 companies ranked highest in sustainability leadership (based on external factors such as inclusion in commonly used sustainability indexes or adherence to voluntary sustainability agreements) also outperformed their peers in terms of shareholder returns.

Specifically, the 50 sustainability leaders:

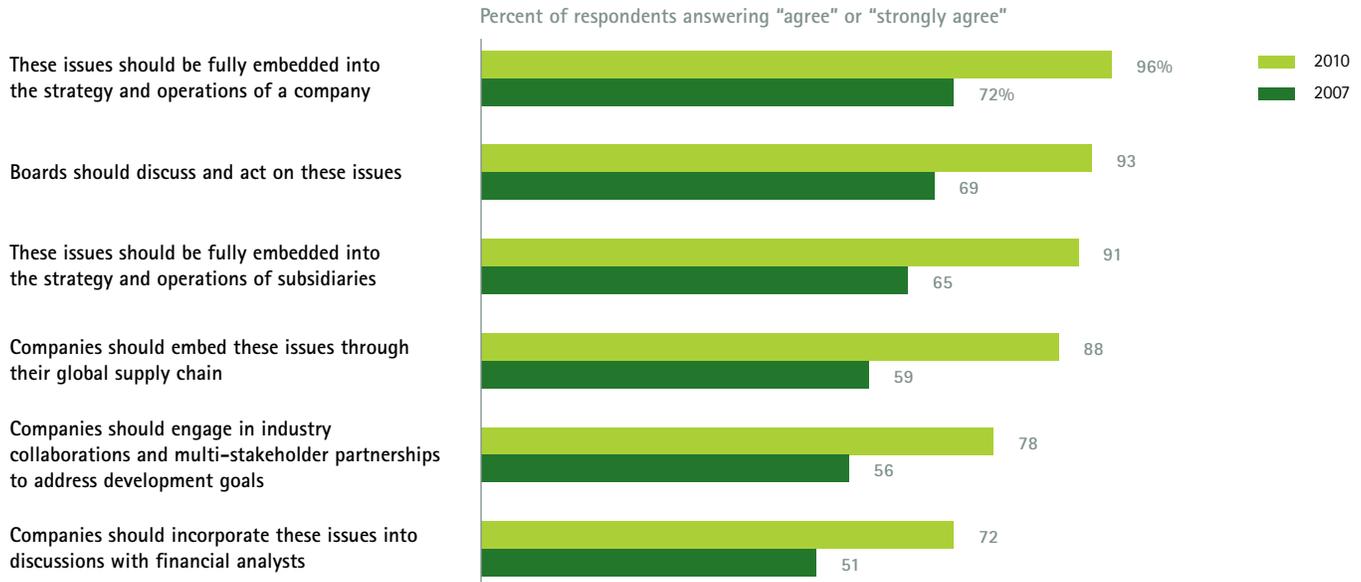
- Outperformed the bottom-performing 50 companies in three-year total return to shareholders by 16 percentage points, and outperformed the middle group of 50 average sustainability peers by 6 percentage points.
- Exceeded their bottom- and middle-50 peers in five-year share-

* "A New Era of Sustainability: UN Global Compact–Accenture CEO Study 2010." The United Nations Global Compact—a policy platform and a practical framework for companies that are committed to sustainability and responsible business practices—administers a survey of its CEO members every two years. The latest report, conducted in collaboration with Accenture, was based on an online survey of 766 Global Compact CEOs and more than 100 in-depth interviews with member executives, civil society leaders, external experts and UN Global Compact board members.

New mindset

A significant shift in mindset has occurred among CEOs since 2007, with the vast majority now believing that sustainability issues should be embedded in core business.

To what extent do you agree with each of the following statements about environmental, social and corporate governance issues?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

holder returns by an even more impressive margin—38 and 21 percentage points, respectively.

To be sure, these are correlations rather than clear evidence of causality. In other words, the link between sustainability and high performance has not yet been solidly established.

This may be due to another fact highlighted by the Accenture–UN research: Businesses and financial analysts have not yet figured out a standardized way of valuing, in today’s terms, a company’s sustainability investments since those returns may not be evident for years. Nor are there agreed-to methods for valuing products and services in such fast-growing sustainability-related areas as clean energy, water conservation or waste management.

Still, the correlation between sustainability investments and performance is promising, and it shows that some companies committed to sustainable business practices are thriving in the marketplace.

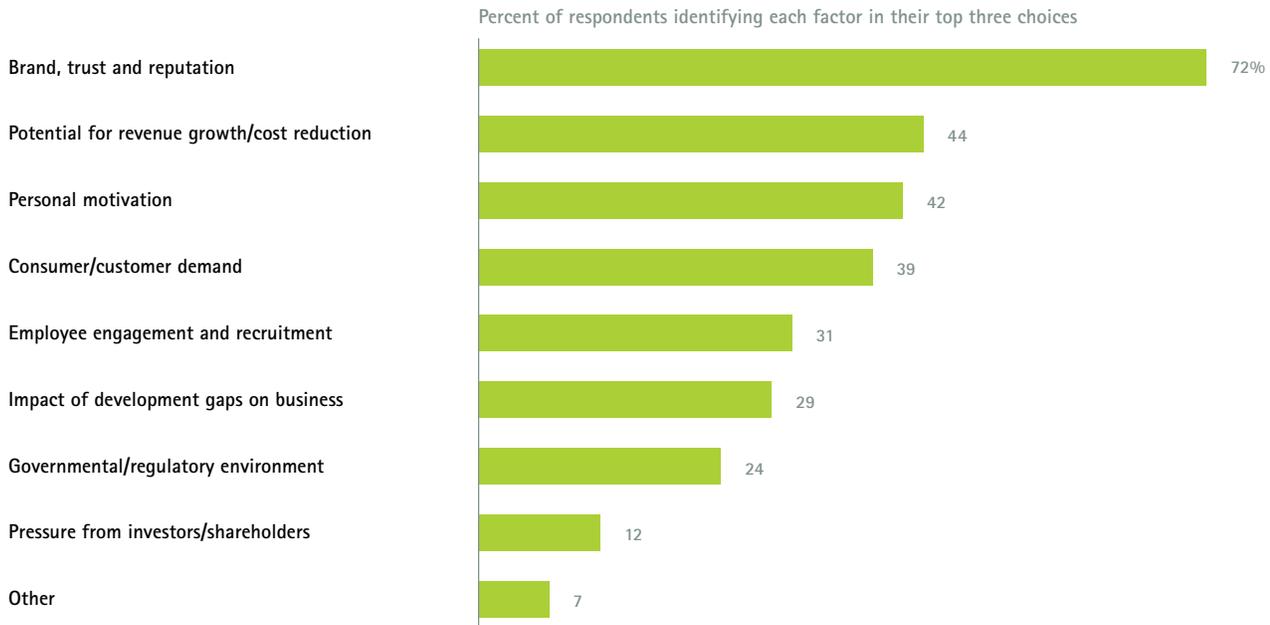
The global economic downturn has had a variety of effects on sustainable business practices. On the positive side, financial duress has actually focused companies more intensely on the business value of sustainability: 74 percent of executives in the Accenture–UN survey said that the downturn has led their company to align sustainability more closely with core business goals, such as cost reduction and revenue growth.

At the same time, however, companies must confront the public perception that business itself is

The motivation

CEOs cite brand, trust and reputation as the primary motivation in taking action on sustainability issues.

Which factors have driven you, as a CEO, to take action on sustainability issues?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

partly to blame for the economic crisis—a perception that has damaged companies' relationships with consumers and stakeholders alike. Being a more responsible corporate citizen is a big part of regaining society's trust—"regaining it with a culture of good behavior," in the words of Kaspar Villiger, chairman of UBS.

Pursuing a sustainability agenda can be one aspect of that good behavior—as seen by the fact that "brand, trust and reputation" was named as one of three top motivators for sustainable business practices by 72 percent of CEOs in the Accenture-UN survey.

But building real trust means tackling the issues that genuinely matter to consumers rather than making token gestures intended to

move the public relations dial. For example, global pharmaceuticals company GlaxoSmithKline has put significant emphasis on building trust. As CEO Andrew Witty told us, "To be a successful and sustainable business, we must fulfill our social responsibilities and build trust with our stakeholders."

At GSK, this has meant rethinking the approach to intellectual property as well as the company's pricing strategy for drugs in emerging and least-developed countries, with the goal of providing better access to more affordable medicines.

Struggling to execute

Although impressive success stories exist, businesses are struggling to integrate sustainability fully into both strategy and operations. Forty-nine percent of CEOs identified "complexity

of implementing strategy across functions” as the most significant challenge when adopting a companywide approach to sustainability issues. Competing strategic priorities was second, with 48 percent.

The Accenture–UN research revealed five key dilemmas that, in many

cases, are preventing executives from integrating sustainability further across their operations and supply chains. However, for each dilemma, business leaders also have an opportunity to take action that can help them drive competitive advantage from a sustainability strategy.

Dilemma No. 1

Can I afford to invest in sustainability-oriented product and service lines when I'm getting mixed signals from consumers and enterprise customers?

Many CEOs in our research expressed skepticism and uncertainty about the extent to which social and environmental concerns influence the buying habits of consumers as well as business and government customers.

For example, some of the CEOs surveyed were unsure whether the perceived concerns of Generation Y (the twentysomething age group that is often most vocal about environmental issues) would last or whether their interest would turn out to be short-lived. As the CEO of one consumer-goods multinational told us, “Consumer engagement may be soft. The apparent concern with environmental and sustainability issues may be explained by Generation Y’s longer period of carefree living. But their values may not follow through into middle age.”

The skepticism is perhaps best summed up by one business leader who noted, “The holy grail is to be able to say that the impact on purchasing behavior of consumers for sustainable brands is clear. It is not.”

The picture is somewhat clearer with business customers, who

are looking for services that help them address their own sustainability needs—for carbon reduction or energy efficiency, for example. Governments are also driving demand; globally, national stimulus packages focused on sustainable practices in areas such as clean energy, water use and waste reduction total \$521 billion. However, there was widespread admission from CEOs that they need to do more to align their offerings more closely with the emerging needs of these enterprise customers.

Shaping consumer behaviors

Currently, most companies have shifted the burden of “sustainability choice” onto consumers. For example, a shopper at a grocery store who wants to support a fair-trade product, or one whose environmental impact is lower than competing brands, often has to pay a premium for that choice.

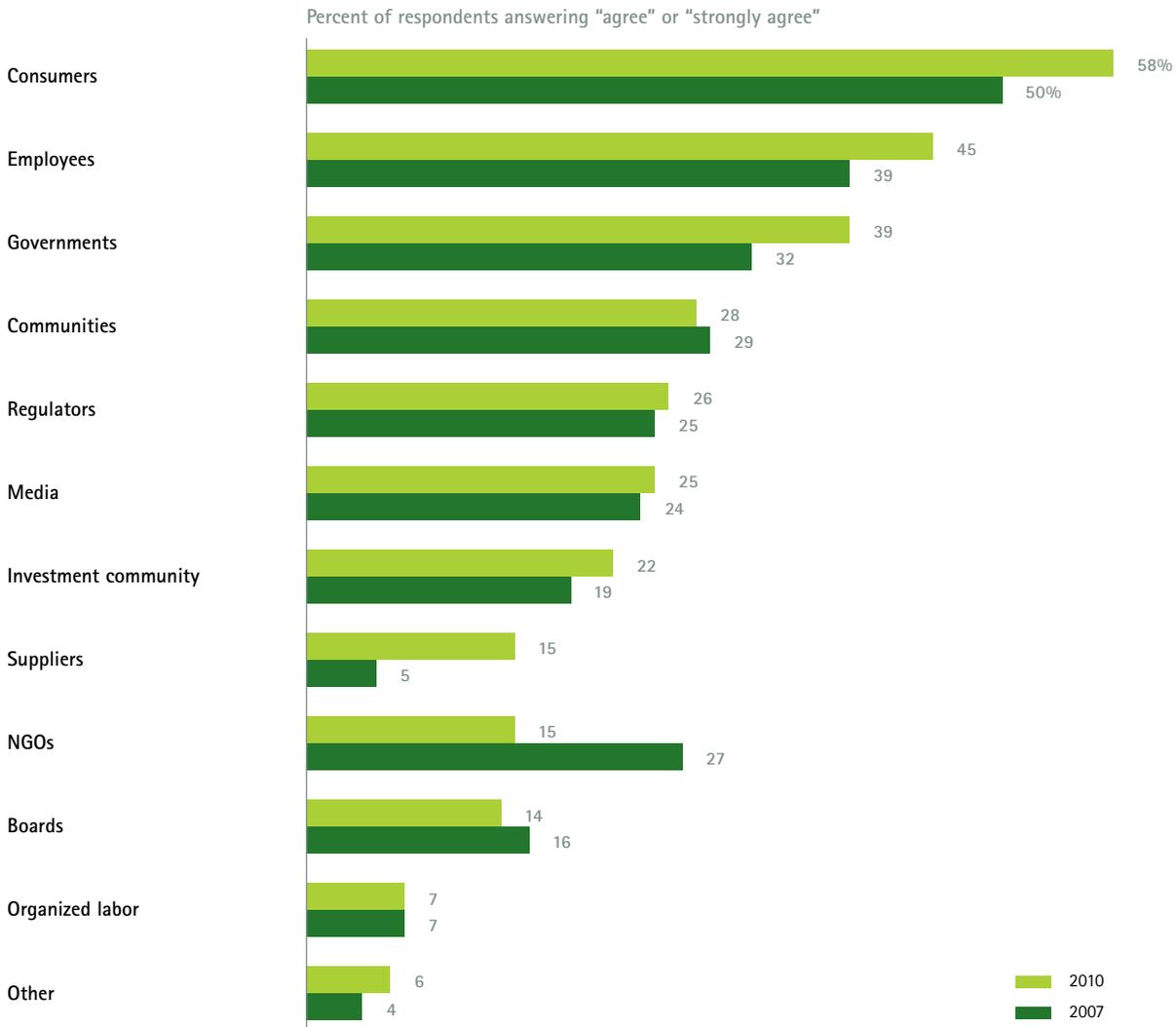
This is not a viable approach to embedding sustainability into consumers’ behaviors. To bring sustainability to the mainstream, the environmentally sound choice must also be the easiest choice.

The first step in overcoming this dilemma lies in product development

The stakeholders

Consumers are increasingly driving businesses' approach to sustainability.

Over the next five years, which stakeholder groups do you believe will have the greatest impact on the way you manage societal expectations?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

and innovation that lead to goods and services that genuinely tackle sustainability issues. For example, Siemens generated revenues of \$28 billion in 2009 from its environmental portfolio of energy-efficient products and services, about an 11 percent increase from 2008 and nearly one-third of Siemens's total annual revenues. Last year alone, Siemens helped customers

cut approximately 210 million tons of CO₂ emissions—the equivalent of the annual emissions of Berlin, London, Munich, New York and Tokyo combined.

Second, educating consumers so that they can make the right choice is a key step for businesses to take, often in collaboration with governments. Some businesses are

already starting to shape emerging tastes and preferences for sustainable products and services. For example, PepsiCo has partnered with the Carbon Trust to certify the carbon footprint of several PepsiCo products.

Third, incentives—financial and psychological—can also orient or shape consumer behavior. And one

aspect of this is providing consumers with the right information. For example, in the utilities sector, smart meters enable consumers to compare their energy consumption with other homeowners in the neighborhood. More directly related to the consumer pocketbook are government subsidies that promote the take-up of environmentally friendly products and services.

Dilemma No. 2

How do I develop the right talent capabilities to manage sustainability as a core business, given the many things that I'm already asking my employees to do?

One of the more surprising findings from the Accenture–UN survey was that executives identified “education” as the most important development challenge to the future success of their business—even ahead of climate change.

In the context of day-to-day business, education means training a new generation of managers about how to integrate sustainability into strategy and operations as well as ensuring a steadier supply of workers with the requisite skills in such key areas as science, technology and engineering. These are difficult challenges, especially since companies already place a high number of skill demands on their employees.

The first step for businesses to take is to define the competencies that will enable them to effectively manage the challenges of sustainability.

Once that is done, delivering the requisite skills will require a mix of both internal training and external education. When

sustainable leadership principles are a prerequisite for all business schools, and sustainable design principles are a prerequisite for all engineering schools—embedded across the curriculum rather than in standalone environment modules—we will know we have reached a new era of sustainability.

Businesses must also take an active role in lobbying policy makers and education administrators to identify their emerging needs and to make the case for sustainable skills development that will support those needs. Businesses can also take a more active role in shaping educational curriculums related to sustainability leadership skills.

For example, in collaboration with top university engineering programs, the Renault Foundation has created specific courses for MBA programs around mobility, electric vehicles and sustainable transport. The foundation contributes \$3.4 million to its mission every year and, since its creation, has welcomed more than 370 students from nine countries.

Dilemma No. 3

How can I move my business toward a new way of assessing corporate value that takes into account sustainability practices when the metrics are so elusive?

The hope of many CEOs is that we are moving toward an era in which businesses will no longer focus purely on near-term profit and loss as the primary means of valuation, but rather also take into account the positive and negative effects on society and the environment.

According to the CEO of a global telecommunications company, “It is not only a company’s economic performance that determines its success, but rather successfully combining economic performance with active management of how the business impacts on social and environmental factors.” This would entail a significant shift on the part of business that would in turn involve meeting at least three significant challenges.

First, it would require companies to measure their sustainability performance in terms of the positive and negative impacts on society. Second, businesses would need to link their performance on sustainability to traditional business metrics and value creation, such as revenue growth, cost reduction, risk management and brand/reputation. Third, it would necessitate the embedding of sustainability outcomes within employee performance frameworks and remuneration packages. These changes would require new kinds of information systems and analytics to support a company’s sustainability performance management.

Where to begin?

Businesses must take a more active role, at both the organizational and individual levels, in creating a commercial and social environment in which the positive and negative impacts of a business on society

are as important as traditional performance metrics.

There are already signs that some businesses are taking the lead here. For example, Danish healthcare company Novo Nordisk has integrated the measurement of its sustainability performance across the organization into a balanced scorecard.

Brewing giant Heineken International recently released a report that documents the company’s positive impact on society and the economy in the 19 European countries in which it operates. Heineken calculates that in 2009, it directly and indirectly employed 495,000 people and contributed \$13.9 billion through value creation—defined as value added and created by supplying the retail and hospitality sectors.

Embedding sustainability into operations to deliver measurable business improvements requires embedding metrics as well. In many of our conversations with CEOs, we encountered businesses that are struggling with software-based performance management tools that require considerable manual intervention.

“We’re getting better and better at tracking the benefits [of sustainability],” said one European business leader, “but there’s still a lot of work to be done. If you’re looking at the cost of materials, or energy costs, then it’s very easy. But brand value is more difficult to assess.”

Using sustainability as a factor in the performance and remuneration packages of top executives and management was seen by many CEOs as one of the most effective means of ensuring more active

management and monitoring of sustainability impacts. As one executive put it, “People have a habit of doing what you pay them to do.”

We found several innovative approaches to embedding metrics programs. In 2009, National Grid launched a remuneration scheme in

the United Kingdom that builds carbon targets into the pay packages of senior leaders and management. The plan has given the company a way to differentiate itself from its competitors by underscoring its willingness to take action and put individual rewards on the line in the interests of better environmental outcomes.

Dilemma No. 4

How can I make long-term sustainability investments when the regulatory environment is not clear or consistent within or across different countries?

The Accenture–UN survey revealed that across the board, executives believe that regulatory uncertainty is a top inhibitor to creating a new era of sustainability and thus potentially a major detriment to business. As Ignacio Galán, chairman and CEO of Spanish energy company Iberdrola, told us: “We want regulation to be stable and predictable.” Another CEO, one from the financial sector, told us: “Uncertainty can lead to paralysis.”

Consider how regulatory inconsistency in carbon reduction and pricing is hindering companies’ progress. One CEO in the electronics sector told us, “The biggest inhibitor is carbon trading....You can’t create a level playing field, and if you look at the fluctuations in the price, how can anyone make an economic decision based on that market?”

The clamor for regulatory clarity is so strong that 60 percent of CEOs told us they would welcome clearer and more consistent government involvement to drive sustainability. This is surprising, given the concerns some CEOs have that government efforts to regulate the financial sector will spill over into other industries.

Clearing the air

To avoid any unintended consequences of regulation as they work

to build trust and provide a more informed basis for sustainability policy making, however, businesses must adopt a more proactive and collaborative approach with governments.

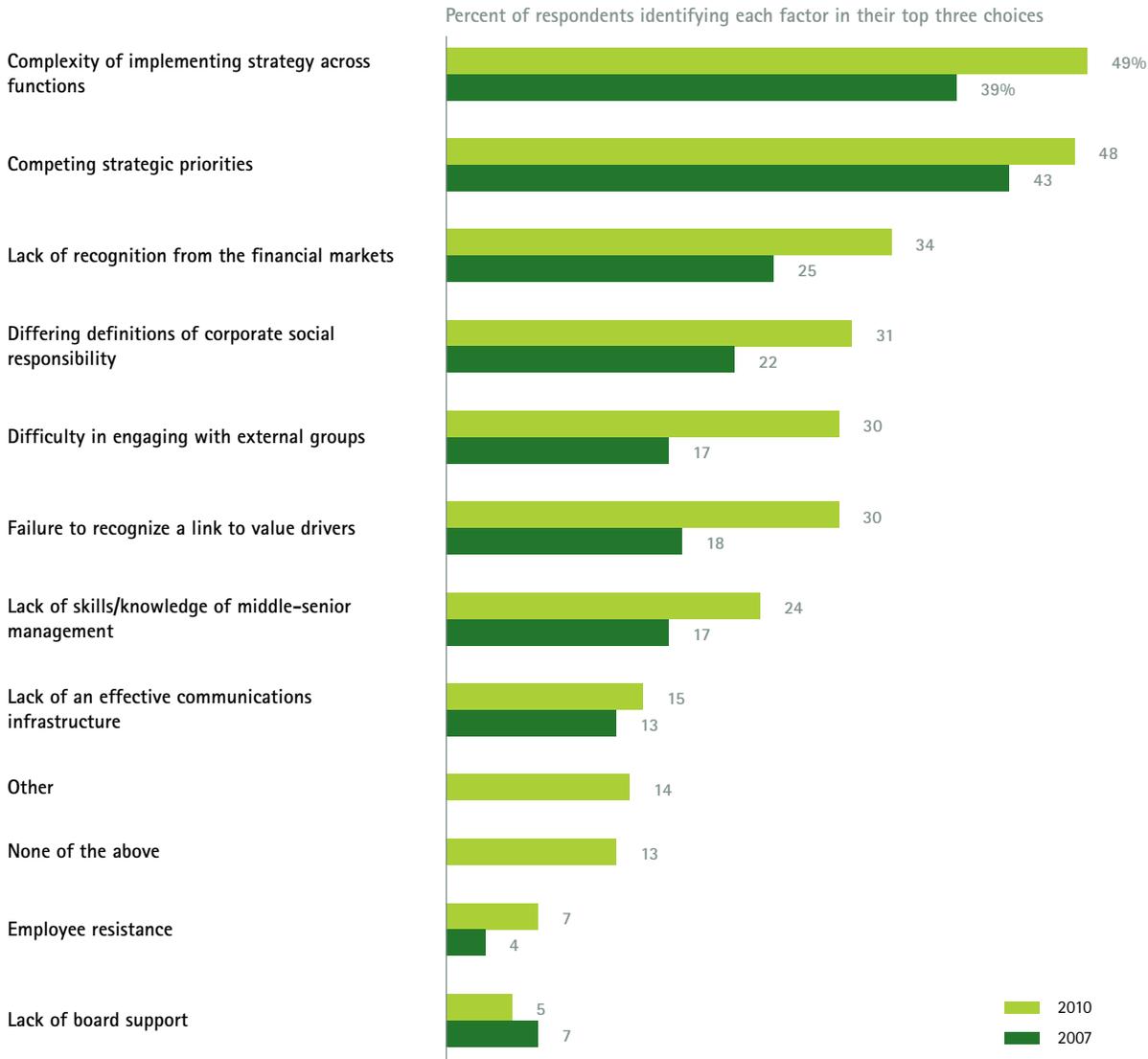
One example of creating more direct cooperation between business and government comes from Banco de España, Spain’s bank regulator. The organization has co-located some of its members at the offices of Banco Santander, the country’s largest bank, to promote greater understanding, openness and collaboration as a means of safeguarding the stability of the financial sector. Similarly, members of the Sekem Group—an Egyptian organization that promotes sustainable development—sit on government working groups to help promote environmental stewardship and biodynamic agriculture and to improve educational and health conditions in North Africa.

Alternatively, cooperative efforts can involve more complex undertakings to raise standards and social awareness across a large and diverse industry. For example, industry leader De Beers played a key role in engaging with multiple stakeholders to develop the Kimberley Process, a certification program aimed at preventing revenues from the sale of diamonds from being used to fund conflict.

The barriers

CEOs report that the complexity of implementation and competing strategic priorities are the key barriers to embedding sustainability issues.

Which barriers keep you, as a CEO, from implementing an integrated and strategic companywide approach to environmental, social and corporate governance issues?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

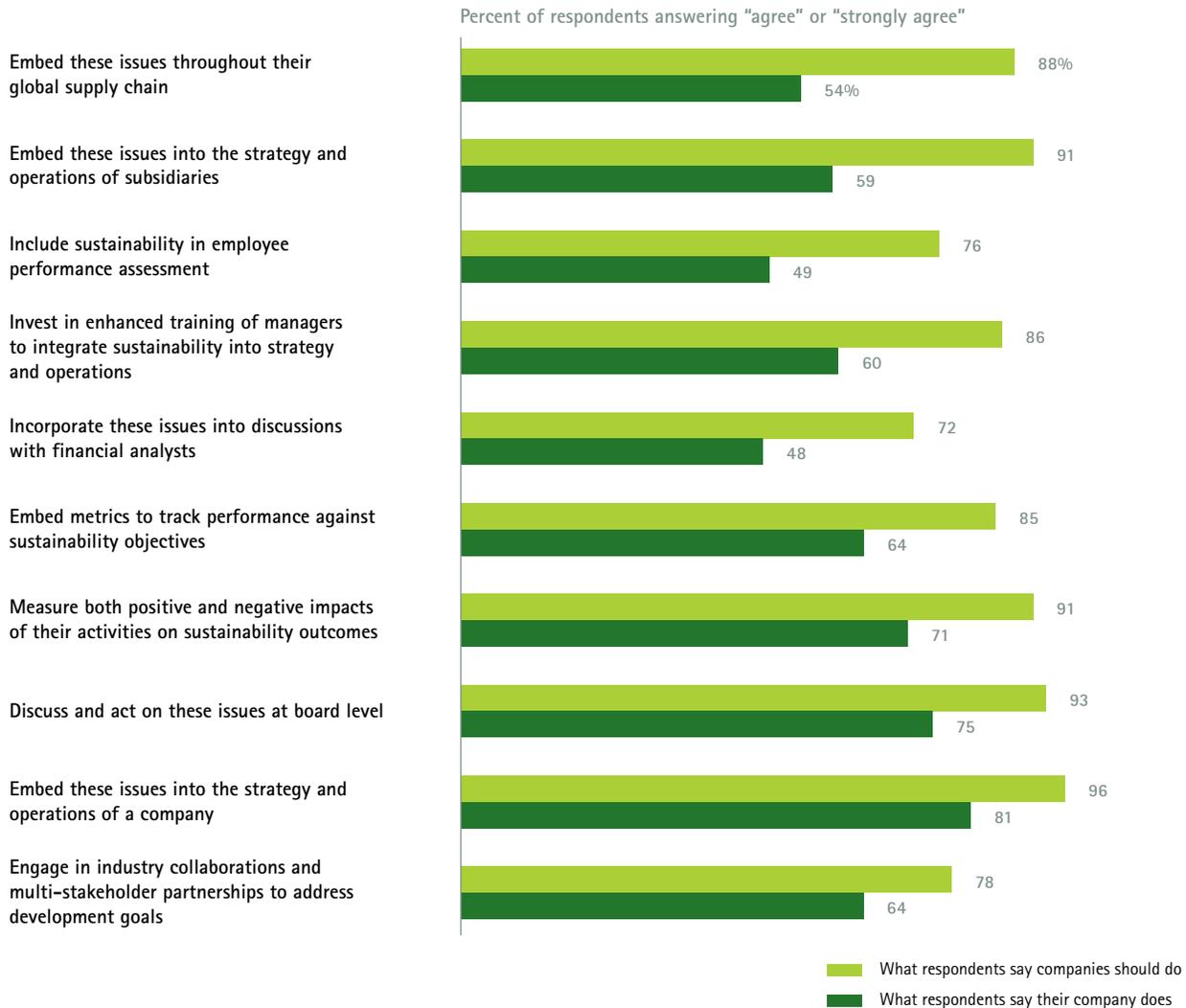
These kinds of public-private joint efforts can pay big dividends by driving a more evidence-based approach to collaboration and to demonstrating its impact on sustainability issues. In this way, companies can help ensure that the potential business and societal

benefits of such collaboration are realized. In the process, they can help reassert the role of business in society and shift further toward an alignment of market and sustainable development outcomes that has thus far proved elusive.

Intentions and reality

Our survey shows a significant gap between what respondents say companies should do and what their company actually does.

To what extent do you agree with each of the following statements about environmental, social and corporate governance issues?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

Dilemma No. 5

Why should I invest in sustainability initiatives when there is no evidence that the investor community will reward me for it?

CEOs are concerned that sustainability investments will not be valued appropriately by the financial community. There are two reasons for this concern. First, given the longer-term nature of the impact of sus-

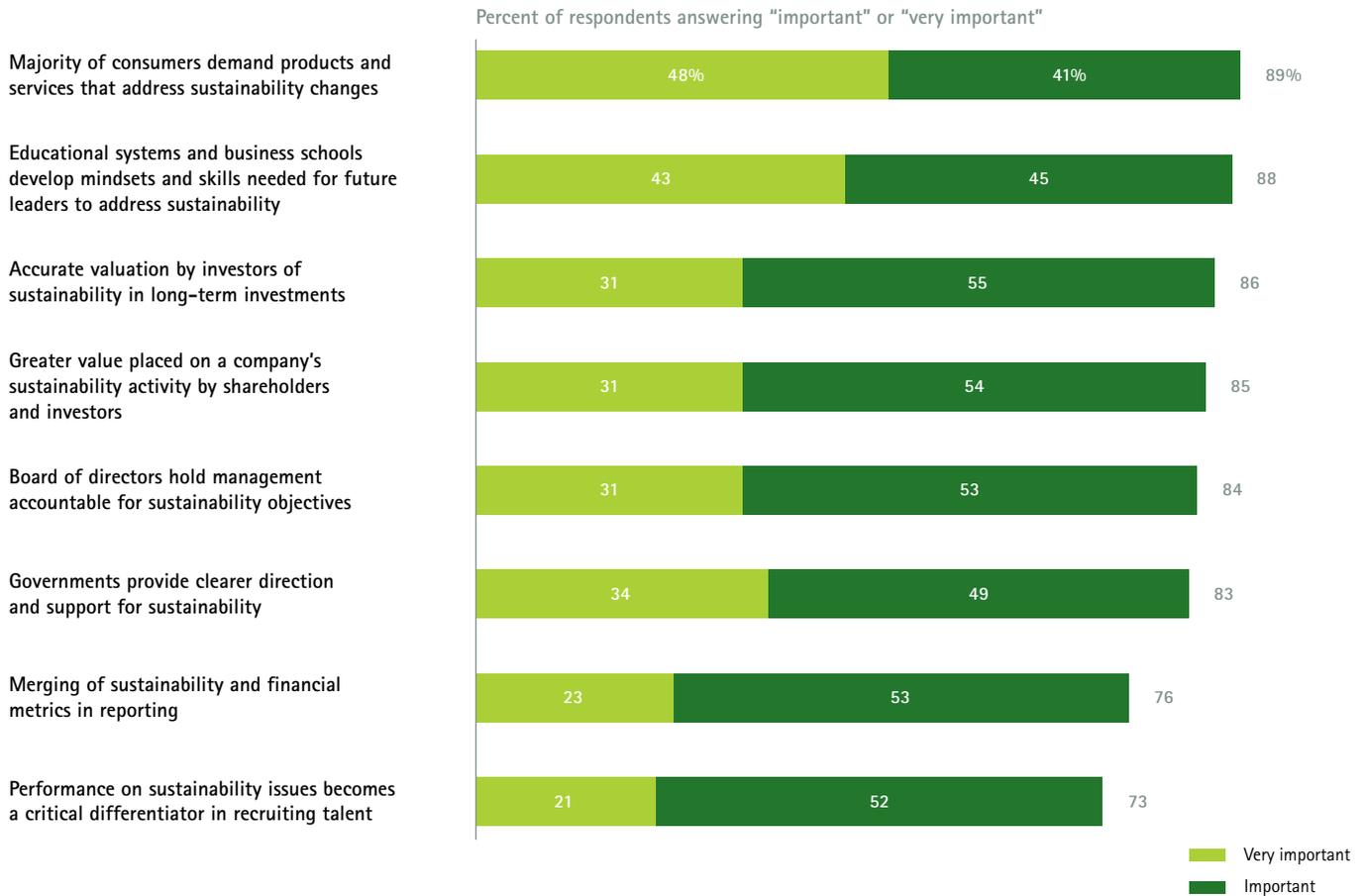
tainability investments, they seldom affect the short-term financial results analysts and investors focus on.

Second, mainstream investors are, for the most part, conspicuously absent

The tipping point

CEOs see that to reach a tipping point in sustainability, a number of conditions are important.

How important will the following changes be in order to reach a "tipping point" where sustainability is embedded within the core business strategies of the majority of companies globally?



Source: United Nations Global Compact CEO Survey 2010 (based on 766 completed responses)

from the sustainability debate. In our conversations with CEOs, they frequently referred to the lack of interest in sustainability activities among investors and analysts, beyond very occasional requests from the socially responsible investment community. As one business leader put it, "Investors talk a good game about investing in sustainable business, but that potential has yet to be realized."

Perhaps reflecting this attitude, only 22 percent of CEOs identified the investor community as one of their

most influential stakeholders over the next five years. As one European business leader told us, "The real pressure, which isn't there at all, is investor pressure." Most executives believed that even if sustainability performance were tracked and measured at a corporate level, the investor community would not be interested or prepared to factor these metrics into their valuation models.

Common ground

Only when sustainable business practices are factored accurately into valuations, through widely

accepted metrics, will capital begin to flow to those companies that are most sustainable. Why? Because the investor's decision is driven primarily by core business concerns rather than a sense of philanthropic zeal or social obligation.

To help bring about this new approach to valuation, business leaders need to be much more proactive with the investor community and engage with them in terms they understand. "We need to realize that analysts bring with them an education rooted within the green borders of Excel," one executive told us. "But we are talking about externalities that very often are not linked directly to line items. CEOs need to be able to link these to cash flow and the balance sheet."

Better communication on a more regular basis is also vital. According

to Edemir Pinto, CEO of Bovespa, the São Paulo stock exchange, "CEOs may complain that investors do not value their sustainability activities properly, but they need to tell investors what they are doing. If they don't communicate regularly, investors cannot incorporate these issues into their models."

So rather than waiting for the investor community to take more of an interest in sustainability investments and their impact on the bottom line, business leaders need to first track and understand that impact, and then communicate it in terms understood by investors. Furthermore, by engaging with policy makers and building the case for better incentives for sustainable products and services, business leaders can help ensure an environment that will reward their endeavor.

As with many new strategic priorities, you know you've succeeded when you no longer have to refer to the idea as a discrete or separate element. Consider by analogy what has happened to the concept of "e-commerce." The word is now dead, but only because e-commerce is simply an essential and integral part of the way all commerce is conducted. If a new era of sustainability is to be reached, it must follow a similar path.

New business models

If this new era is reached, it will drive new business models. Witness the Timberland Co., whose focus on sustainability is embedded across all elements of its value chain, from product design and innovation to manufacturing, distribution, marketing and disposal. Environmental metrics have been integrated into the company's main design platform, encouraging designers to consider the whole-life impact of the materials they select and enabling them to engage consumers on the basis of enhanced environmental performance. Timberland's new "Earthkeepers 2.0" footwear was conceived with "cradle-to-cradle" principles in mind, and designed to be disassembled for life. Recognizing the implications of a new era, Timberland's CEO Jeffrey Swartz told us, "In 2020, the consumer will care and he'll penalize you.... He can inspect the environmental and social impacts of your business."

Central to this transition to a new era is a paradigm shift in the concept of value and corporate valuation: from the short term to the long term, and from a purely business focus to a broader understanding of a business's impact on society. Reaching this new era will require businesses and investors to understand better and account for the value that can be derived from a host of such factors as resource efficiency, investments in R&D and engagement with local communities.

While these challenges may appear daunting, businesses have an opportunity to shape a future in which they will “do well by doing good.” By doing so, they will not only understand the opportunities available from integrated sustainability; they will also take important steps toward achieving high performance in a new era of sustainability.

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