Embedded Sustainability: A strategy for market leaders

By Chris Laszlo and Nadya Zhexembayeva

Consumers, employees, and investors are beginning to demand socially and environmentally-savvy products without compromise, while radical transparency is putting every company under a microscope.

In recent years three big trends – declining resources, radical transparency, and increasing expectations – have redefined the way companies compete. The linear throw-away economy, in which products and services follow a one-way trajectory from extraction to use and disposal, can no longer be supported, as we are simply running out of things to unearth and place to landfill. Consumers, employees, and investors are beginning to demand socially and environmentally-savvy products without compromise, while radical transparency is putting every company under a microscope.

With a new set of pressures on hand, what is business to do? We are not talking about the Body Shops and Ethical Banks of this world but rather the Unilevers and HSBCs: industry leaders pursuing middle-of-the-road customers, who find themselves often blind-sided by ecological and social burdens. So, how are we as business unit and functional managers to treat social, health and environmental demands in the mainstream?

There are many managers who still go with familiar approaches, treating these new pressures as annoying obligations and merely tipping their hats to corporate social responsibility. While many more now recognize social and environmental performance as business opportunity, most continue to “bolt it on” to existing strategy and operations.

Only a handful are choosing to embed sustainability into the very DNA of what they do, incorporating environmental, health, and social value into core business activities with no trade-offs in price or quality. They are learning to leverage global challenges, such as climate stability, for enduring profit and growth. Through innovation – in product design, process and business model – these pioneers are creating even more value for their customers and investors than they would otherwise.

In a decade of working with companies in the US, Europe, South America and Asia – big and small, manufacturing and services – we have observed the following lessons learned.

The first is that managers need an awareness of the external competitive environment that MBA programs and on-the-job training typically do not provide. The second is that embedding sustainability creates business value at many levels – not just risk mitigation or cost efficiencies – that managers fail to fully leverage. The third is that the pursuit of sustainability involves hidden choices – whether to reduce negatives or provide positive solutions, and whether to pursue incremental change or heretical innovation – which are proving crucial to business strategy. The fourth and fifth lessons concern the nature of change management at the systems level.

While the five lessons form an integral whole for anyone embarking on the journey, it all starts with a better understanding of three megatrends and what they mean for value creation.

I. Awareness

You might have noticed that sushi restaur-
Bolt-On vs. Embedded Sustainability: Key Dimensions

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<tr>
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<th>Bolt-On Sustainability</th>
<th>Embedded Sustainability</th>
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<tbody>
<tr>
<td>goal</td>
<td>Pursue shareholder value</td>
<td>Pursue sustainable value</td>
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<tr>
<td>scope</td>
<td>Add symbolic wins at the margins</td>
<td>Transform core business activities</td>
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<td>customer</td>
<td>Offer ‘green’ and ‘socially responsible’ products at premium prices or with diminished quality</td>
<td>Offer ‘smarter’ solutions with no trade-off in quality and no social or green premium</td>
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<td>value chain</td>
<td>Manage company’s own activities</td>
<td>Manage across the product or service life cycle value chain</td>
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<td>organization</td>
<td>Create a ‘scapegoat’ department of sustainability</td>
<td>Make sustainability everyone’s job</td>
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II. Sustainable value creation

For those pursuing embedded sustainability, there are many ways to create business value. Companies in every sector have already made great strides in complying with and anticipating environmental and social regulations. They have learned operational best practices in eco-efficiency – the process cost reductions that come from conserving energy, eliminating waste and improving material throughput – in some case saving billions of dollars as DuPont and 3M are purported to have done. But relatively few have focused on top-line (gross revenues) growth based on product or brand differentiation. Even fewer have used stakeholder value creation as a way to drive new markets and business context change.

Market leaders in every sector are finding that a brand/culture based on creating stakeholder value is rapidly becoming a source of competitive advantage.

Mainstream players such as Unilever and Nissan are democratizing green products by redesigning their value chains to enable product prices in line with their traditional (non-green) counterparts. It is now possible to buy an organic cotton shirt at Walmart for about the same price as one made from conventionally grown cotton. In financial services, HSBC and Itau Unibanco (Brazil) are among those recognized for their leadership in integrating sustainability into banking operations. Market leaders in every sector are finding that a brand/culture based on creating stakeholder value is rapidly becoming a source of competitive advantage. Among other benefits, a sustainability image draws in higher-income consumers, attracts and retains talented people, and can ease negotiations with government regulators concerned about industry impacts.

Here is one way to visualize the range of available value creation opportunities, with radical innovation cutting across and enabling the other value-creating levels. Companies can use radical innovation to simultaneously lower costs, differentiate their products and enter entirely new markets. (See figure 1)

At each level of sustainable value creation, managers need to ask a different set of questions. Mitigating risk is about avoiding value destruction by managing potential costly liabilities, as BP discovered in 2010. At the efficiency level, the query is into operational excellence: how can embedded sustainability contribute to greater savings along the lifecycle value chain? At the product differentiation level, the inquiry concerns consumer expectations and how these are changing to incorporate ever greater environmental, health and social attributes. In terms of new market opportunities, the probe is into business models: how can businesses find profitable solutions to global problems? One such new market/business model example is that of meeting the unmet needs of poor consumers in emerging markets, as with Muhammad Yunus and his Grameen Bank model of unsecured micro-credit. At the level of image and reputation, the interrogation goes to the core identity of the company: to what extent are social and ecological goals parts of its mission or culture? At the
level of business context, it is about shaping government regulations or industry standards that favor the market leaders over the competition.

Whatever the sustainability project or company-wide initiative, managers can benefit from assessing, and acting on, its value creating potential at these multiple levels.

### Levels of sustainable value creation

1. **Mitigating risk**
2. **Reducing energy, waste, materials**
3. **Differentiating products**
4. **Entering new markets**
5. **Protecting & enhancing brand**
6. **Influencing industry standards**

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### III. Hidden choices

**Are you intent only on making your products less wasteful and more energy efficient?** If these are your sustainability goals, you are probably focused on doing less harm. On the other hand, if you are in the business of providing clean water or nutritional products to the poor – as do units within Unilever and DuPont – then you are helping to solve global problems. Of course many companies are doing both – witness General Electric’s efforts to clean up its impacts on the Hudson River while moving into eco-solutions such as wind turbines and water desalination. The point is only to be deliberate about the choice.

Once you know where you are and where you want to go, you also need to know what kind of change will get you from here to there. Is it incremental or disruptive? Both are needed – and baby steps can lead to more advanced ones – but unfortunately, too many companies set goals that amount at best to ‘rearranging the deck chairs on the Titanic’ and at worst to greenwashing. Setting future targets of reducing CO2 emissions by five percent may be wholly insufficient for an energy intensive manufacturing facility, given the stated objectives of the world’s scientific community to cut global CO2 emissions by 85 percent by 2050. A “mild hybrid” drivetrain is a poor ecological incentive of the world’s scientific community to cut global CO2 emissions for an energy intensive manufacturing facility, given the stated objectives of the world’s scientific community to cut global CO2 emissions by 85 percent by 2050. A “mild hybrid” drivetrain is a poor ecological alternative to rethink personal mobility from an environmental perspective, considering new technologies such as plug-in electric and even hydrogen fuel cell.

A good example of disruptive innovation comes from floor-cleaning equipment leader Tennant. While its competitors were busy working to reduce the harshness of their cleaning chemicals, Tennant simply eliminated the use of its chemicals altogether. The company’s flagship product, the ec-H2O, electrically converts plain tap water to perform like a powerful detergent, using 70 percent less water than traditional cleaning methods. Best of all, the ec-H2O gives its customers the lowest possible total cost of ownership. It took asking heretical questions and an unlikely source of inspiration – the observed practice in Japanese hospitals of using ionized water to clean wounds – for Tennant’s R&D team to produce the innovation.

### IV. A messy process

Embedding sustainability is a complex, multi-activity and multi-actor challenge; no simple recipes are possible. Unlike the streamlined and often linear steps taken for bolt-on sustainability efforts, the task of embedding social and environmental value into the DNA of a business is iterative, repetitive and chaotic. It demands new thinking and unorthodox solutions that can spring from unlikely sources and in improbably ways. Having said this, the experience of market leaders suggests four interdependent and interconnected lines of action to help guide the journey:

- **Getting the Right Start:** mobilizing, educating, and acting around specific low hanging fruits. Building momentum in the organization for sustainability projects that support existing business priorities and provide demonstrable pay-off.
- **Building the Buy-In:** aligning company, value chain, and all other stakeholders around the vision of embedded sustainability.
- **Moving from Incremental to Breakthrough:** developing clear but unorthodox goals, designing the strategy and capturing value through co-creation and innovation.
- **Staying with It:** managing learning and energy while making sustainability ubiquitous but largely invisible in the business practice.

Engagement of one business unit after another demands a ‘right’ start; new action calls for education and training, while building true buy-in remains a daily task. Many low hanging fruit are pursued and harvested before companies are even ready to play with – let alone design – a masterful embedded sustainability business strategy.

### V. New competencies

While traditional business skills remain vital when embedding sustainability into the DNA of your company, they must be complemented by new competencies. We have found the following four to be essential yet rarely valued in today’s corporate world: Design. Inquiry. Appreciation. Wholeness.

**Design** is first and foremost an attitude or mode of thinking. At its core is an assumption strikingly different from the one that underlies...
the typical business decision. If decision-making is all about making a hard choice between easy-to-identify alternatives, design attitude assumes an easy choice between difficult-to-create alternatives. Tim Brown, CEO and President of IDEO, ranked among the ten most innovative companies in the world, illustrates this point in the following way: “a management philosophy based only on selecting from existing strategies is likely to be overwhelmed by new developments at home and abroad. What we need are new choices – new products that balance the needs of individuals and of society as a whole; new ideas that tackle the global challenges of health, poverty and education; new strategies that result in differences that matter and a sense of purpose that engages everyone affected by them. What we need is an approach to innovation that is powerful, effective and broadly accessible. Design thinking…offers just such an approach.”

The next two competencies – Inquiry and Appreciation – build respectively on what is possible and on the existing strengths present in every business system. We have had the privilege of working closely with Professors David Cooperrider and Ron Fry, co-originators of Appreciative Inquiry, a change management methodology that, as its name implies, has these two competencies at its very core. Appreciative Inquiry has enabled managers at leading firms such as Hewlett-Packard, Walmart and McKinsey to discover the best of their shared experiences and tap into the larger system’s capacity for cooperation. Efforts to discover and elaborate the positive core – the past, present and future capacities of the whole system – lead to innovations that integrate societal stakeholder issues that are often excluded from consideration in conventional approaches to decision-making.

Wholeness is the final skill needed to master the complex challenge of embedding sustainability across entire business systems. It requires an ability not only to see the big picture, but also to understand the linkages within the system. Donella Meadows, the systems scientist, quotes an ancient Sufi teaching that captures this focus: “You think because you understand one you must understand two, because one and one makes two. But you must also understand and.” Learning systems tools such as feedback loops, lifecycle analyses and stakeholder value maps can help managers develop solutions that are less fragmentary and contradictory than bolt on sustainability measures developed in isolation.

From bolt-on to embedded: A growing competitive advantage

We know how to meet the demands of shareholder value – years of managerial excellence testify to this achievement. We know how to create stakeholder value: traditional approaches such as CSR and philanthropy that predictably lead to added costs. We also have a growing number of bolt-on sustainability efforts producing fragmentary and symbolic wins at the fringes of the company.

What we are still discovering is how to meet both shareholder and stakeholder requirements in the core business – without mediocrity and without compromise – creating value for the company that cannot be disentangled from the value it creates for society and the environment. Embedded sustainability is just such a strategy, one that will only grow as today’s global challenges continue to deepen.

About the authors


Chris is the author of Sustainable Value (2008) and The Sustainable Company (2003, paperback 2005). He is an Associate Professor at Case Western Reserve University’s Weatherhead School of Management, where he is the Faculty Research Director at the Fowler Center for Sustainable Value. A former executive with building materials leader Lafarge, Chris is co-founder and Managing Partner of Sustainable Value Partners, LLC, an advisory services firm specializing in sustainability for strategic advantage.

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Notes

1. “Fish Story: Big Tuna Sells for Record $396,000”, MSNBC news, January 5, 2011
4. HSBC and Itau Unibanco were among the mainstream winners of the 2010 FT Sustainable Banking Awards
5. The Intergovernmental Panel on Climate Change (IPCC) Fourth Assessment Report, 2007