

Interviews and Findings from Industry Leaders

Sustainability—Problem or Opportunity?

An Australian Perspective



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Foreword

Sustainability is today's "big issue". You only have to read the newspapers, watch the news or look at the latest advertising to see that it is everywhere. But what does it mean for business leaders? What are the challenges they are facing? How are they meeting those challenges? Who is doing it well and gaining competitive advantage?

Recently in Melbourne and Sydney, Circ Consulting and Russell Reynolds Associates hosted a discussion with 20 leading senior marketers, representing some of Australia's largest and best-known businesses and brands. Facilitated by Chris Bulford, Managing Director of Circ Consulting, the group discussed what sustainability means to them and how they are responding to the challenges.

What Does Sustainability Mean?

Definition

Discussion began with an agreement on how "sustainability" is defined. It is now generally accepted there are three forms of sustainability: **economic, social and environmental**.

- **Economic sustainability:** is a measure of a business's ability to continue to generate value from its product or service. This has long been the measure of business success—the ability to generate long-term profitable growth.
- **Social sustainability:** came to the fore in the 1990s, reflecting a demand from the community at large that businesses have a responsibility to put something back into the community. This saw the emergence of community sponsorship programs, staff paid leave to work on community projects and consumer backlash against companies judged to be exploiting labour in developing countries.
- **Environmental sustainability:** has sprung to prominence in recent years, particularly since 2006, when the British economist Sir Nicholas Stern published a report which overtly linked climate change to economic costs. This is now the form of sustainability which dominates political and regulatory discussion.

The most widely used definition of sustainability is from the United Nations World Commission on Environment and Development, namely: "*Development that meets the needs of the present without compromising the ability of future generations to meet their own needs.*"

The Issues

While there was agreement that different industries are affected differently by changes in climate, legislation and stakeholder behaviour/attitude, there were some clear general themes from our discussion which appear to be having widespread impact on the way we do business and develop brands for the future.

- **Science:** There is now general acceptance that the predictions of the scientists have to be taken seriously. Forecasts for 2100 include:
 - Temperatures will increase by anywhere up to 6°C.

- Sea levels are likely to increase between 50 cm and 100 cm.
- Rainfalls will decline, with recent research from the CSIRO/BoM predicting that once-in-20-year droughts will occur every second year.

These changes in turn are predicted to destroy the Great Barrier Reef, eliminate snow from Australia and reduce agricultural yields by between 15 percent and 20 percent.

This will clearly have primary impact on certain industries (such as tourism and insurance), but it is recognised that with significant impact on food production, it will ultimately affect the global community and the global economy.

- **Regulation:** Most participants are still absorbing the likely impact of recent moves in legislation. The Federal government's green paper, released in July of this year, will precipitate a heavy period of lobbying by industry. However, it was widely recognised that the ensuing white paper (due at the end of 2009) will mark a permanent change in the way we do business.

Carbon trading, with its implications for more expensive products and services, is a reality. Most attendees were unsure about the implications of carbon trading but were keenly awaiting further releases from the government.

Of more familiarity is the The Australian Competition and Consumer Commission's (ACCC) recent activity around green marketing, and in particular its publications "Green Marketing and the TPA" and "Carbon Claims and the TPA", demonstrating the importance of justifying any claims. Marketers understand this area will be under close scrutiny and so-called "greenwashing" is dangerous. Interestingly, it was observed that the Canadian authorities have banned the use of such terms as "green", describing it as vague and misleading.

- **Consumer:** Within this context, there was considerable discussion about the consumer and his/her likely response. In particular, attendees were divided over whether people would be prepared to pay more for products they perceive to be more environmentally friendly. This may vary by category and by consumer segment. However, there are some indications of change in the traditional reluctance for consumers to translate what they say in research about their propensity to spend into actual behaviour at the check-out. For example:
 - In the United States, researchers now identify a large and growing segment as the "lifestyle of health and sustainability" segment. It is worth US\$300 billion in the U.S. market.
 - In Australia, the organic market continues to grow in excess of 20 percent per annum. It is now worth over A\$300 million and covers categories as diverse as chocolate and soap.

The concept of food miles was also discussed. U.K. retailer Tesco announced its intention to have all products declare on their labels the distance the food has travelled. Currently, implementation is proving difficult, but the concept is still being pursued.

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- **Competition:** Many of the marketers spoke of competitive moves in the environmental area, with a feeling of competitive urgency tempered by “doing it right”. In fact, Choice magazine recently conducted a survey of “non-food supermarket items” (such as detergents, tissues and toilet paper) and found that 185 products carried a total of 630 “green claims”.

There are some observations of potential pitfalls, just as there are examples of success stories. On the one hand, some have fallen foul of the ACCC through erroneous claims of carbon neutrality or misleading sourcing of raw materials; on the other, the makers of hybrid cars, “green energy” and water tanks have all realised both commercial and reputational benefit from environmental initiatives.

- **Organisation:** The sustainability debate is having a significant impact on organisational structure and the employment value proposition (EVP). Attendees were divided from those organisations that regard sustainability as part of the way every employee does his/her business, through to those who have ascribed accountability for sustainability to one area (often Corporate Affairs), through to those who have now created new roles, such as Sustainability Director or Carbon Manager.

In the EVP area, recent research from the United States showed that more than one-third of MBA graduates regard a firm’s environmental policy as “extremely” or “very” important when deciding on a job. It was widely recognised that a firm’s environmental policy is particularly important for recruiting and retaining Generation Y employees.

There was little discussion of measurement, and few attendees seem to have yet incorporated environmental measurement into their balanced scorecards for either their businesses or their brands or to have considered it as part of their remuneration plans.

- **Shareholder:** It is increasingly observed that “green business is good business”. Many case studies are now coming to prominence of businesses who have achieved substantial commercial advantage, often through cost savings, by adopting environmental initiatives.

There was widespread interest in the Goldman Sachs 2007 study that shows that companies with environmental and social policies outperform the stockmarkets by 25 percent.

The emergence of the Dow Jones Sustainability Index makes it clear that the focus on this area of a company’s performance is only going to increase in the next few years.

Building Sustainability Strategy

The discussions amplified the themes Circ Consulting hears from many of its clients, particularly when they start out on the process of developing a sustainability strategy.

The debate is no longer about whether a strategic response to sustainability is required—but about what the most appropriate response is and how it should be implemented. There is universal recognition that this must be on the business agenda now.

Often, clients are somewhat overwhelmed by the complexity of the issue, as it potentially involves all stakeholders and new information occurring every day (new scientific opinion, new regulation, changing consumer opinion, etc.).

Circ Consulting's advice to clients is presented as a simplified five-step process.

Step 1 - Understand all Stakeholders

The business needs to develop a good understanding of all the issues, through the eyes of all stakeholders. The broad issues mentioned above need to be understood in a specific way for an individual business. For example, what are the implications of the government white paper for your business? What is the consumer attitude to your product/service—is it changing? How do your employees feel about it?

Part of this process of understanding must also involve a total understanding of your own environmental footprint. Importantly, this must cover the whole value chain of the product and service you offer—from “cradle to grave”. Do you know where all the raw materials originate? Do you know how your customers consume your product(s)/service(s) and how they dispose of any residual(s)?

As an example of the danger of not understanding the changing marketplace—in 2004, General Motors did not believe the hybrid car would be commercially viable, when the price of petrol in the United States was \$1.50 per gallon. Within a year, the price of petrol was \$2.50 per gallon, and the car market in the United States was changing fundamentally. General Motors has been struggling to adapt—it recently announced a US\$15.5 billion quarterly loss, with North American sales down 20 percent.

Step 2 - Align to Business Strategy

It is clear that there is no “one size fits all” green strategy. Different businesses in different industries require different strategic responses. It is vital to ensure that the green strategy is aligned to the business's overall business strategy. The business needs to understand its own strategy and core values and develop a sustainability strategy that fits.

In fact, there are many shades of green strategy. To illustrate, the strategic response of The Body Shop, whose proposition has been built on a social and environmental platform, will differ markedly from the response of a company based on, for example, a low-price platform.

Step 3 - Articulate the Sustainability Strategy

The next stage is to bring all the external and internal analyses together to develop the succinct and clear expression of strategy. This often comes from facilitated workshop(s). This expression of the sustainability strategy will then inform the implementation plan.

Part of the process will involve working through trade-offs. For example, there is currently a debate in the United Kingdom about the relative merits of continuing to import flowers from Kenya, compared with growing them locally. How do you decide between the current social benefit to the Kenyans of the employment, versus the potential environmental benefit of reduced carbon miles?

Step 4 - Develop the Plan

The sustainability plan must again be multidimensional. There are risks and opportunities, and they are both external (i.e., market) and internal (i.e., organisational). The leading companies work through the process to come up with the activities that will both mitigate risk and realise commercial and reputational benefit.

Step 5 - Implement and Measure

Implementation of the sustainability strategy must follow standard processes for project implementation. There must be clear accountability, clear deliverables and clear time frames.

Measurement is critical. The measures of success may include the following:

- Environmental (carbon equivalent emissions, energy consumption and fuel use)
- Commercial (cost savings and revenue)
- Reputational (brand and reputation)
- Stockmarket (share price)

Building Sustainability into Corporate DNA

While different sectors are at diverse points in the sustainability journey, Russell Reynolds Associates has observed, in Australia and around the world, a heightened focus on sustainability in matters of culture, accountability and recruitment.

1. Role of the CEO

The involvement of the CEO is vital. We have observed that where the CEO is the champion of sustainability, a company-wide approach is embraced and the integration of sustainability practices is adopted. On-going articulation of the company's sustainability strategy ensures a consistent message. However, sustainability cannot be a single-person issue. Tying down the concept of sustainability must involve designing an effective organisational structure based on the company strategy.

2. Governance

There is an emerging trend of companies linking their board and senior management remuneration to their sustainability strategies and performance. From a governance perspective, we have seen a number of organisations develop subcommittees of their boards focused on corporate responsibility and sustainability. Established like the traditional audit committee, these subcommittees are focused on ensuring that the organisation operates in an ethically responsible and sustainable way.

3. The Sustainability Executive

We have seen the emergence of senior executives now holding significant roles, reporting directly to the CEO. The shift to elevate sustainability roles in an organisation reflects recognition by a lot of companies that this is not an issue they can afford to ignore—for the reasons of risk mitigation and commercial opportunity mentioned above. As a result, companies are now recruiting individuals to champion and embed best practices in their policies, procedures and corporate culture.

In the past, the issue sat loosely within the corporate and social responsibility function, public affairs, and corporate communications. Now, we see specific executives overseeing specific functions such as Global Head of Sustainability, Chief Sustainability Officer, Sustainability Director, Climate Change Director, Corporate Environment Manager, and Director of Emissions and Environment.

In the past five years, Russell Reynolds Associates has recruited a significant number of corporate sustainability executives in the power and industrial/natural resources sectors as well as in paper and packaging. In 2008, we have seen a broadening out from these sectors to other areas such as consumer products, property, banking, fast food and insurance.

4. Accountability

Assigning accountability for sustainability will have a significant impact on where the emphasis is placed. In businesses that roll the issue into Corporate Affairs, there is an inclination for an “issue management” approach, focusing more on compliance and risk mitigation; in businesses that assign leadership in this area to Marketing, there is more chance of a “commercial opportunity” outlook, looking at ways to turn the environmental agenda into commercial and reputational advantage. It is therefore vital to formulate business strategy before assigning accountability.

5. The Candidate

Candidates for these roles that we have recruited appear to sit in several experience “buckets” and cannot be easily categorised. We have discovered there are not many totally “ready-made” solutions for these roles, particularly given that they span across the strategic/external and practical/internal dimensions of a business. In our experience, candidate categories are typically:

- Environment
- Health and Safety
- Operations/Engineering
- Economics
- Government and Regulatory
- Consultancy
- Academia

Conclusion

Sustainable value:

- The issue is large, complex and evolving rapidly.
- There is no one answer—it is business specific.
- There is a process that can enable a business to develop robust strategy.
- Sustainability must be embraced by all CEOs.
- It is too important and complex an issue to be left to “shared accountability”. A specific resource needs to be assigned to drive the sustainability agenda through an organisation.
- As always, structure must follow strategy. You need to understand your sustainability strategy before you can determine the skills you require.
- As more companies wake up to the need to resource this area, it will become an increasingly competitive field. You are advised to move quickly to secure the best candidates.
- The benefit may take some time to materialise, but the risk of delay is huge.
- It is vital to get going now!

About Russell Reynolds Associates

Russell Reynolds Associates is a leading global executive search and assessment firm. We have more than 300 consultants based in 39 wholly owned offices across the Americas, Asia/Pacific and Europe. Our consultants conduct senior-level search and assessment assignments in a range of sectors for both commercial and non-profit public and private organizations of all sizes. With our deep knowledge of major industries and our commitment to outstanding client service, we ensure that our clients find and develop the best leadership teams for the ongoing success of their businesses. For more information, please visit www.russellreynolds.com.

About Circ Consulting

Circ Consulting is a strategy consultancy that specialises in helping its clients to develop "sustainable value" in today's complex business world. We have worked extensively in developing sustainability strategy by applying the rigorous process of understanding the needs of all stakeholders (analysts, customers, retailers, communities, employees and the environment); then developing compelling strategy that maximises strategic synergies and minimises trade-offs; and finally implementing and ensuring measurement and continuous improvement. We work across many industries, from agribusiness to the arts, from consumer products to financial services, from pharmaceuticals to industrials. For more information, please visit www.circconsulting.com.au

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