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Bringing discipline to your sustainability initiatives

Many companies have more sustainability initiatives than they can possibly manage. Here's how to get them under control.

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Sustainability has become a part of life for many companies. For some, it's a matter of meeting demands from customers seeking socially responsible goods and services. For others, it's about addressing pressure from stakeholders—including investors—or pursuing their own corporate values. For still others, especially those in a resource-constrained environment, it's a strategic imperative. Whatever the impetus, sustainability has become sufficiently pervasive that defining it and executing business programs, products, and practices with an eye to their environmental and social implications has become a demanding managerial exercise.

For some, sustainability has proved to be a valuable lens through which they have identified opportunities that they might have otherwise missed—to cut costs, reduce risk, and generate revenues. Consider the multinational consumer-goods company Unilever, for example, which changed the shape of a deodorant to use less plastic in packaging and created a concentrated laundry product that sharply reduces its use of water. German pharmaceutical company Bayer expects to save more than $10 million a year with a resource-efficiency check it developed to improve operations by using by-products and reducing wastewater. Global chemical company DuPont has recorded $2 billion in annual revenue from products that reduce greenhouse-gas emissions and another $11.8 billion in revenue from nondepletable resources.

Others, though, have struggled. To better understand the challenges they face at creating value from sustainability, we worked with several sustainability membership groups[1] to identify managers at 40 companies to volunteer to collaborate on analyzing their programs. What we found is that companies often have more initiatives under way than they can effectively manage. The sustainability movement is quite malleable, often including everything from environmentalism and resource management to corporate governance and human rights, and different managers in different regions can get quite enthusiastic about their own efforts without taking a company-wide perspective. In the most benign of such cases, the efforts are too fragmented to create much value—either for the company or for society.

Fortunately, the solution to that kind of problem is well known. In fact, we found that most companies would benefit from bringing more discipline to their sustainability initiatives by applying principles commonly associated with performance management: to keep their programs focused, set specific concrete goals, create accountability for performance, and communicate the financial impact.

Agree on where to focus

One of the biggest challenges companies face in sustainability is getting top-leadership attention. In a recent report for the United Nations Global Compact, 84 percent of the 1,000 global CEOs surveyed agreed that business "should lead efforts to define and deliver new goals on global priority issues," but only a third said that "business is doing enough to address global sustainability challenges."[2]

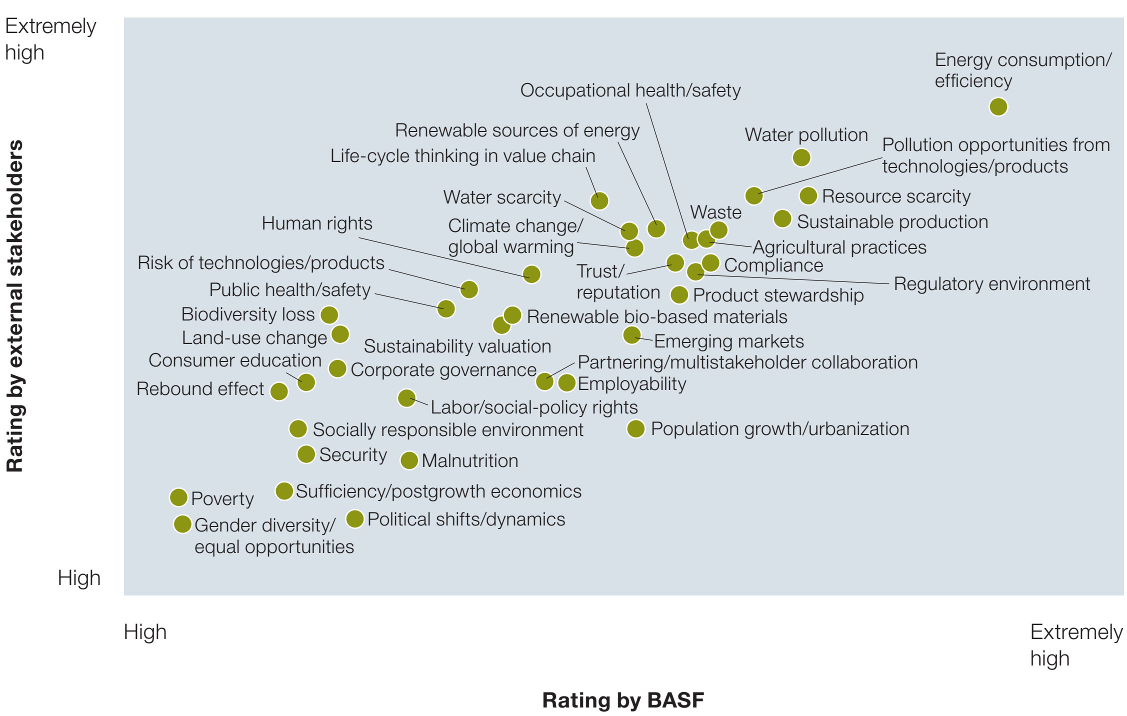
In our observation, the problem at many companies is often one of focus; two-thirds of companies in a representative sample from the S&P 500 have more than 10 different sustainability focus topics; some have more than 30. That's too many: it's hard to imagine how a sustainability agenda with more than 10 focus areas can break through and get the necessary buy-in to be successful. And if top management doesn't prioritize, then individual business units won't either, and the result is fragmented, decentralized, and not necessarily aligned with one another or with overall top-level goals. That diminishes not only the social and environmental impact but also the economic value. A recent McKinsey Global Survey found that companies with a unified strategy and no more than five strategic priorities were almost three times as likely to be among the strongest performers, both financially and on measures of sustainability.[3] Coca-Cola, for example, has set for itself a strategy it describes as "me, we, the world," which encompasses its approach to improving personal health and wellness, the communities in which it operates, and the environment. Within this strategy, the company reports making material, tangible progress on metrics related to three specific areas of focus: "well-being, women, and water." The company does not ignore other issues such as climate change and packaging, but it has made it clear that this is where it wants to lead.

To develop a clear set of priorities, it is important to start by analyzing what matters most along the entire value chain, through internal analysis and consultations with stakeholders, including customers, regulators, and nongovernmental organizations (NGOs). This process should enable companies to identify the sustainability issues with the greatest long-term potential and thus to create a systematic agenda—not a laundry list of vague desirables. After extensive consultations, for example, BASF, the global chemical company, put together a "materiality matrix" (exhibit). This chart ranked the importance of 38 sustainability-related issues, based on their importance to BASF and its stakeholders. (Other companies use similar matrixes.) Such exercises help companies to recognize the most important issues early and get internal stakeholders to agree on what will create the most value. Their focus needn't be mechanical but should instead reflect discussion on the strategic, reputational, and financial merits of different efforts.

Once the priorities are identified—in our experience, no more than three to five is best—the next step is to develop a fact base from which to create a detailed financial and sustainability analysis. This includes the same kind of valuation and financial analysis a company would do for any other business opportunity, including a detailed analysis of the market value or value at risk and implementation. Siemens, for example, used such an approach to sort through a range of potential priorities and home in on one—helping customers to reduce their carbon impact. As a result, it has created an environmental portfolio of green products and services, including energy efficiency, renewable energy, and environmental technology. In a 2013 interview, Siemens reported that this had generated revenues of €32.3 billion and saved 377 million metric tons of carbon emissions.

Exhibit

One company maps its sustainability priorities.



Source: Company website

Stronger goals seem to encourage innovation; people may feel more motivated to find ways to meet them.

Set specific, concrete goals

After completing the initial analysis, the next step is to translate this information into external goals that can be distilled into business metrics. These goals should be specific, ambitious, and measurable against an established baseline, such as greenhouse-gas emissions; they should have a long-term orientation (more than five years) and be integrated into business strategy. Finally, their intent should be unmistakable. One company stated as a goal: “Reduce the impact of our packaging on the environment.” From a different company came a sharper version: “Eliminate 20 million pounds of packaging by 2016.” Along the same lines, “reducing emissions” is a vague and almost meaningless phrase—it doesn’t say by how much the company should reduce emissions, by when, or compared with what benchmark. The approach taken by another sustainability leader is stronger and more specific: “Reduce 2005 CO_2 emissions by half by 2015.”

It is important to build internal support to meet these goals. Our analysis found that the companies that excelled at meeting sustainability goals made sure that they involved the business leaders responsible for implementing them from the start. One global manufacturer we interviewed announced in 2010 that it would reduce greenhouse-gas emissions and energy consumption by 20 percent by 2020. To do so, it has set up energy assessments and energy-management plans, established global programs to optimize procurement and building standards, trained and developed internal “champions” and coordinated best practices, and began to use renewable energy where possible—communicating early wins internally through a newsletter and regular conference calls. Four years into the ten-year effort, the project is already net present value positive.

Setting ambitious external goals motivates the organization, forces resources to be allocated, and promotes accountability. An analysis of companies that are part of the Carbon Disclosure Project found that those that set external goals did better when it came to cutting emissions—and also had better financial returns on such investments. Stronger goals, then, seem to encourage innovation; people may feel more motivated to find ways to meet them. Lack of goals is a sustainability killer: “What gets measured gets managed” is as true of sustainability as it is for any other business function. And yet it is not happening. McKinsey analysis of S&P 500 companies suggests that as of this writing only one in five S&P 500 companies sets quantified, long-term sustainability goals; half do not have any.

Communicate the financial impact

Despite the growing evidence of the value of investing in sustainability, many executives wrestle with lingering doubt. Senior leaders will give sustainability lip service but not capital if they do not see financial benefits. “Sustainability metrics can seem like random numbers and don’t do much,” one chemical-industry executive told us. “For our businesses, sustainability efforts have to compete directly with other demands, which means that financial impact is key.” Indeed, nearly half of the research participants reported that the pressure of short-term earnings performance is at odds with sustainability initiatives. A constructive response is to make the case that sustainability can pay for itself—and more. This needs to be done rigorously—even overcommunicated—reinforced with fully costed financial data and delivered in the language of business.

This is, of course, much easier said than done. At Intel, for example, although business leaders were interested in saving water, they saw little financial justification to do so: water was cheap. Advocates of the initiative were able to calculate that the full cost of water, including infrastructure and treatment, was much higher than the initial estimates. Saving water, they argued, could therefore create value in new and unexpected ways. On that basis, Intel went ahead with a major conservation effort. The company now has a finance analyst who concentrates on computing the financial value of sustainability efforts.

Making the business case for sustainability might sound like an obvious thing to do, but apparently it isn't. Only around a fifth of survey respondents reported that the financial benefits are clearly understood across the organization.

Sustainability initiatives can be challenging to measure because savings or returns may be divided across different parts of the business, and some benefits, such as an improved reputation, are indirect. It is important, then, not only to quantify what can be quantified but also to communicate other kinds of value. For example, an initiative might improve the perception important stakeholders—including consumer groups, NGOs, or regulators—have of the company, the better to build consumer loyalty, nurture relationships with like-minded nonprofits, and inform policy discussions.[4]

Create accountability

The top reason that respondents gave for their company's failure to capture the full value of sustainability is the lack of incentives to do so, whether positive or negative. According to the United Nations Global Compact, only 1 in 12 companies link executive remuneration to sustainability performance; 1 in 7 reward their suppliers for good sustainability performance. Among survey respondents, 1 in 3 named earnings pressure and lack of incentives as reasons for poor sustainability results; 1 in 4 named lack of key performance indicators and insufficient resources.

In this area, a number of companies exhibit good practices from which others learn. Some are strong when it comes to tracking data and reporting indicators, tracking carbon emissions and energy use, monitoring water use and waste, and recycling. Adidas demonstrates one useful approach. The sporting-goods company breaks down its long-term goals into shorter-term milestones. Its suppliers, for example, are given strategic targets three to five years ahead, as well as more immediate goals to encourage them to focus. The effort makes it very clear what is expected of suppliers for the current year. The beer company MillerCoors does something similar. It tracks and quantifies progress in ten areas, ranging from water to energy to packaging to human rights, using its own sustainability-assessment matrix. The idea is for MillerCoors to understand its performance, in quantitative terms, in areas that are often difficult to quantify.

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Becoming a sustainability leader can pay off, but it is not easy. "It's a perception issue," one executive told McKinsey. "We need to show that it makes good business sense to get over the hurdle." Fair enough—and the evidence is building that for the best companies, this standard is within reach.

[1] Corporate Eco Forum (corporateecoforum.com), The Sustainability Consortium (sustainabilityconsortium.org), and Sustainability Leadership Forum (onthecourtcoaching.net).

[2] *The UN Global Compact–Accenture CEO Study on Sustainability 2013: Architects of a Better World*, Accenture and United Nations Global Compact, 2013, unglobalcompact.org.

[3] In February 2014, McKinsey surveyed 3,344 executives about their companies' sustainability activities. The respondents represented the full range of regions, industries, company sizes, tenures, and functional specialties.

[4] Sheila Bonini, Timothy M. Koller, and Philip H. Mirvis, "Valuing social responsibility programs," *McKinsey Quarterly*, July 2009, mckinsey.com.

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