

SUSTAINABILITY AS CORPORATE STRATEGY : THE EMERGING DIMENSION

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Deforestation, East Kalimantan, Borneo

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Organisations can no longer operate in isolation. Leveraging sustainability is key to business growth, differentiation and business innovation.

Businesses across the world are increasingly acknowledging the importance of sustainable development as an integral component of their core operational strategy. With the emerging global sensitivity to the increasing risks associated with input and output price volatility, and resource scarcity, the need for innovative sustainable business models to ensure business continuity is prominent. Organisations can no longer operate in isolation as the environmental and social risks and opportunities linked to their value chain have far reaching impacts and consequences on their own bottom-line. To enable growth and tackle increasing competition, companies have also begun to leverage sustainability for brand differentiation and product/service innovation. This trend is more prominent in the developed world, but many businesses in the developing world are also catching up. Yet, large components of business enterprises, especially in the emerging markets, still remain ignorant of the significance of “sustainability” as a corporate strategy. In the interest of protecting their own bottom-lines, the question that looms large: Why should businesses bother about sustainability? Does it affect their profitability?

Despite the growing recognition of sustainability in some sectors of industry, the concept remains abstract and theoretical for many business executives. At a macro-policy level, the recognition of sustainability as a triad or trinity of economic, social, and environmental concerns that need to be reconciled (see Fig. 1) is more ubiquitous on paper than in practice. At the firm level, the Brundtland Commission definition of sustainable development as “development that meets the needs of the present without compromising the ability of future generations to meet their own needs”, is often treated as a as an “ethical”, “normative”, and a “value judgmental” concern. That is precisely why even today, a large number of organisations view sustainability as “social responsibility”.

At a micro-level, organisations accept that protecting their capital base is important for their own bottom-line. They rarely recognize the possibility of extending the notion to the world's natural and human resources. In fact, till a point in time, environmental and ecological concerns were perceived in most parts of the world as an ethical argument which might be anti-developmental. Organisations are yet to recognise sustainable development as an integral part of their growth strategy and are unable to effectively monetize the intangible benefits to justify the cost of the externalities. This entire notion made conservation initiatives move asymptotically with business operations, and was initially considered as something external to the fundamental human existence.

The Changing Perception

A few decades ago, “conservation as an anti-developmental force” was also the feeling in the developed world. At one point in time, therefore, the corporate sector felt that the conservation needs of the planet do not really concern them. The entire environmental concern was not intrinsic to its core business and business plan. Pollution, for example, is an externality, and often only government regulation forces them to internalise costs of pollution.

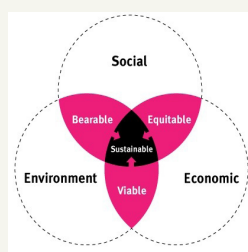


Fig 1. Tripple Bottom Line

But, the accrual of knowledge and scientific understanding at the interface of nature, economy, and society since the 1980s and 1990s started changing this perception in the developed world. The extensive development of science in this domain also made us understand that there is bidirectional causality between ecosystem and the economy. Ever since the Club of Rome's prediction of “apocalypse” in their *The Limits to Growth* thesis, the human response to the “approaching doomsday” has been characterized by extensive research, gradual knowledge accrual through global assessments, and conventions.

The Earth Summit of 1992 adopted the Brundtland Commission Report's definition of “sustainable development”, and opened the Convention of Biological Diversity (CBD) for signature which came into effect in December 1993. With CBD, for the first time, a framework of international law recognised conservation of biological diversity as an integral part of the development process. On the scientific front, the Millennium Ecosystem Assessment (MA) of 2005 enhanced human understanding of the fact that the ecosystem functions in its own inimitable ways to provide ecosystem services (benefits) to the human society in the form of provisioning services (e.g., food, raw materials, genetic resources, water, minerals, medicinal resources, energy, etc), regulating services (e.g., carbon sequestration, climate regulation, pest and disease control, etc), cultural services (tourism, religion, etc), and above all, supporting services that are necessary for production of all other ecosystem services (e.g. nutrient recycling, gene-pool protection, primary production, soil formation, etc).

The linkage seemed much clearer with the better delineation of ecosystem services. Referring to Fig. 2, social systems create economic forces and enforce economic actions due to the mismatch between needs and availability. “Actions” on the ecosystem are fundamentally meant to satisfy economic needs; hence “Actions” are “Economic Activities”. “Economic Activities” emerge as interventions on the ecosystem structure and functions, and provide ecosystem services to human society. The proper delineation of “ecosystem services” helped in understanding the direct linkage between human society and biodiversity: for every bit of existence of human society, there is a critical need for the biodiversity as a “stock” to exist, to ensure the “flow” of these ecosystem services. Recent scientific assessments at this interactive interface like *The Economics of Ecosystems and Biodiversity (TEEB)*, published in 2010, recognised that these ecosystem services are “GDP of the poor”, as the poor's incomes and survival are dependent on the ecosystem.

This was a major step, effectively recognising the need to ensure the integrity of the ecosystem structure and functions in order to maintain the flow of ecosystem services which manage the ecological balance of the food chain; and to this end, conservation



Air pollution and emissions from a steel factory

goals become important. For businesses to survive, the natural resources are needed. For businesses to survive, the natural resources are needed. For sustainable management of the natural resources like forests, wetlands, rivers, etc. one needs to set the right conservation goals for flora and fauna, which through their natural functioning, support and sustain these resources, and provide ecosystem services. Businesses therefore inextricably depend on biodiversity through a well-defined supply-chain, whose recognition is obscure in the public domain, especially in India and the developing world.

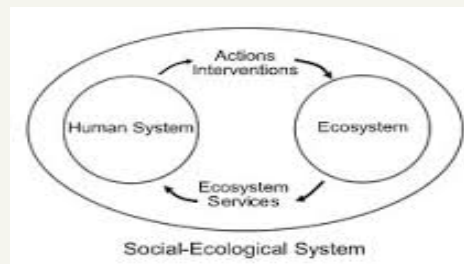


Fig 2. Social Ecological System

Most recently this received greater acknowledgment under the Sustainable Development Goals (SDGs) in 2015 with a 2030 Agenda for Sustainable Development through an intergovernmental set of 17 aspiration goals with 169 targets focusing on people, planet, prosperity, peace and partnership. There is clear evidence that SDGs are being adopted by many leading companies as a way to shape their sustainability strategies.

On the national front, India has also taken measures under the National Voluntary Guidelines (NVGs) on the Social, Environmental and Economic Responsibilities of Business, released by the Ministry of Corporate Affairs in 2009, to shift the business perception of sustainability from philanthropy to corporate responsibility. These voluntary frameworks have increased the awareness levels amongst business stakeholders and have initiated the incorporation of sustainability as a key element of corporate growth strategy across sectors. Though the level of adoption is at nascent levels in India, these trends show promise for widespread adoption of sustainability in mainstream businesses.

Importantly, this widening strategic horizon at the company level has brought the corporate sector into greater contact with a broader range of actors from civil society, includi

ing NGOs. Whereas once traditional approaches to business and conservation may not have overlapped, except in a dynamic of conflicting interests, there is now a greater realization on the part of companies to seek the expertise of NGOs in a collaborative manner required to engage with companies on areas of mutual interest and benefit. Similarly, NGOs have widened their traditional scope of operation at the field level, to build capacity.

Embracing Sustainability and Creating Shared Value

Although a majority of companies still focus on improving their bottom-line as their principal objective, some businesses are beginning to demonstrate increasing environmental/social awareness and accountability. The perception of the corporate sector changed with the notion of “sustainable business” and an understanding that: their longer term survival is contingent upon the resource base that is steadily getting depleted; their long-term costs will only increase as they impede on the working of the ecosystem thereby diminishing the capacity of the ecosystem to provide its services; those with a “sustainable” and “green” business model will generally have a competitive advantage, and will earn their local community’s goodwill and see their efforts reflected in the bottom line.

‘Green’ business models have competitive advantage, capacity to earn goodwill and aid in long-term benefits

In emerging markets, businesses continue to struggle to balance their need for making money for their survival and taking responsibility for the environmental and social implications of their operations. There are many who are completely oblivious to their ecological and social responsibilities, and constant reiterations through various forums fail to infuse that responsible business culture. In India, businesses have often been criticized as a major cause of social, environmental, and economic problems; companies are widely thought to be prospering at the expense of the local communities; at times trust in business falls to such nadir that governments’ corrective policies undermine competitiveness and sap economic growth.

Therefore, when viewed through the sustainability lens, the trade-off for the firm also arises between the choices of short-term rent-seeking behaviour, and long-term optimization. Porter and Kramer¹ have argued that firms’ focus on optimizing short-term financial performance leads them to overlook the greatest unmet needs in the market as well as broader influences on their long-term success. Why else would companies ignore the well-being of their customers, the depletion of natural resources vital to their businesses, the viability of suppliers, and the economic distress of the communities in which they produce and sell? It is in this context that Porter and Kramer bring in the notion of CSV or “creating shared value” – a process by which companies could bring business and society back together by generating economic value in a way that also produces value for society by addressing its challenges. A shared value approach reconnects company success with social progress.

According to Porter and Kramer, firms can create shared value in three distinct ways: by re-conceiving products and markets, redefining productivity in the value chain, and by building supportive industry clusters at the company’s locations. This can be exhibited in the case of IKEA, who being leading players in the global value chain through their various home furnishing products, attempted to redefine their supply chain in many areas including cotton and forest fibre. IKEA is actively involved in developing better cotton cultivation practices to increase the volume of cotton produced in an environmentally friendly way. They worked intensively with small-holder farmers to improve yield, quality, and address environmental impacts of cultivation. IKEA joined hands with the farmers by advising them better on farming practices and helped growers secure inputs at better under a certification known as the Better Cotton Initiative. This certification improved market linkages but also required extensive collaboration with NGO partners like WWF to define the scope of work and execute it on the ground. This entire initiative created shared value which was embedded in the firm’s strategic subscription to principles of sustainability.

¹Porter, M. and M.R. Kramer (2011): “Creating Shared Value”, Harvard Business Review, January–February 2011 Issue.

Case Study : The IKEA Group

PEOPLE & PLANET POSITIVE TARGETS
By August 2017, at least 50% of our wood will come from more sustainable sources. By August 2020, we aim to source 100% of our wood, paper and cardboard from more sustainable sources. ¹
By August 2015, all cotton used in IKEA products will be sourced from more sustainable sources, ² and we will continuously investigate complementary fibres with improved sustainability performance compared to cotton.
By December 2015, all palm oil, currently used in home furnishing products such as candles or as a food ingredient, will either come from certified segregated sustainable sources or be substituted with more sustainable alternatives.
By August 2017, all of the leather we use will have full chain of custody and be produced according to standards that help protect forests and respect human rights and animal welfare. ⁴
All seafood sourced for the IKEA Restaurants and Swedish Food Markets are certified by August 2015.

IKEA focuses on the efficient use of material resources through innovative product design and “sustainable” sourcing of key materials like wood and cotton. Their work in the area of sustainable production aims to contribute to the increased supply of sustainable materials across the industry, beyond the volumes required for their own business. They address waste management and resource availability by designing products that can be easily reused, repaired, and recycled. This facilitates their existing products to be a ‘bank of materials’ for the future thereby closing the loop through a circular economy approach. To ensure credibility and transparency in their sustainable sourcing commitments, IKEA is also adopting product sustainability standards which indirectly are also influencing the sustainable growth and development of the commodity markets as well. Due to the sheer size and volume of their business, this strategy has created large scale impact opportunities to contribute to the positive development of the raw material ecosystem, employee well-being and consumer lifestyles; while staying focused on the core business.

Fig 3. Creating Shared Value

The IKEA Group, one of the largest home furnishing companies in the world, adopted a sustainability strategy in 2012 which addressed the linkage between their sales expansion plans focusing on emerging markets and the raw material availability based on the nature of their business. They identified three change drivers that will transform their business influencing their entire value chain from its raw materials sourcing to the lifestyle of its end consumers. By striving to be ‘People & Planet Positive’, the organization has demonstrated the business case for creating shared value, which directly influences their long term growth plans.



Fig 4. Case study : The IKEA Group



Fig 5. IKEA and WWF partnership

WWF and IKEA work together in India and Pakistan to improve the livelihoods of cotton farmers while reducing the crop's negative environmental impact. The partnership implemented sustainable solutions in cooperation with the Better Cotton Initiative. Since August 2015, all cotton used in IKEA products come from sustainable sources including Better Cotton, cotton grown to other sustainability standards in the USA and cotton from farmers working towards the BCI standards. Source: WWF – Better Cotton (wwf.panda.org)

The way forward..

In the wake of globalization and shifts in market regulation, and competition, the Indian corporate sector needs to balance increased regulation, protecting the brand and ensuring stable supply chains with new opportunities to enhance performance.

Sustainability as a strategy and the reporting and disclosure of the same will be increasingly important. Increasing awareness levels among investors has resulted in an increase in the demand for disclosure on the non-financial performance of companies. Businesses are also under pressure from media, industry analysts, regulatory and non-regulatory government bodies, NGOs, customers and communities to divulge information about their sustainability strategy, program and performance. Sustainability Reports in accordance with international reporting frameworks like the GRI are an important first step for companies. These reports consist of various initiatives on water management, resource management, energy management, employee benefits, community development, etc by the organization and are disseminated through various modes of communication. These reports have become important strategic tools for positioning the organization by informing stakeholders about the sustainability performance, and progress made over time in terms of the various indicators.

As the IKEA case demonstrates, it is critical for companies to understand the important role of ecosystem services for the survival of their own business and the global community at large. It is important to understand the footprint created by their own operations; this entails understanding the ecosystem service losses created by their projects or initiatives. This can be done through natural resource accounting which essentially defines a monetary value to the ecosystem services. Firstly, this will help the community understand the importance of eco-system services to human society. Secondly, valuation offers a relatively objective instrument for decision making. Thirdly, it can raise the awareness levels of the market and the policy-makers on the importance of the ecosystem services under consideration. Fourthly, valuation of ecosystem services can help revise investment decisions: e.g. infrastructure development, that might otherwise ignore the related harm expected to be caused to the natural environment and consequent loss to the ecosystem services.

The new strategic vision entails developing and integrating a detailed sustainability vision into the long-term strategic plan in a way that creates lasting value whilst also building public trust is a common challenge for all types of organisations. What is becoming increasingly clear is that a sound sustainability strategy not only protects but also rebuilds a company's reputation, drives innovation and employee engagement, it satisfies consumers and attracts and retains top talent. At a different level, it demonstrates compliance and leads to market differentiation, thereby helping positioning of the organization with a unique reputation in the market. Therefore, as argued, embracing sustainability in the corporate strategy is not merely about creating sustainable bottom-lines, but also about creating shared value.