Four Strategies for Responding to Sustainability-Oriented Competitors

By Matthew Lee , INSEAD Assistant Professor of Strategy

Sustainability-focused startups are entering established companies' market space, bringing both new threats and new opportunities.

Employees want to work for them, customers are willing to pay more for their products and investors are eager to become shareholders. “Hybrid social ventures” like Whole Foods, Patagonia, and Honest Tea that combine commerce with sustainability missions are leading the movement for sustainability-oriented innovation in business.

For established companies that were not necessarily built with sustainability in mind, these new entrants are competing for their most attractive customers and talent. Customers that prefer sustainability-oriented products and services tend to be young and relatively wealthy. Talented employees who have a choice of where to work, particularly millennials, increasingly want to use their skills at companies that they perceive to be doing good in the world. A continued generational shift toward sustainability-oriented values threatens to shift the balance even further in favour of companies that have sustainability baked into their DNA.

Although these hybrid social ventures are still relatively small in many industries, forward-thinking executives have begun to take notice and create plans for responding to them.

The competitive dynamics of responding to hybrid social ventures differ from responding to a traditional entrant. Paradoxically, hybrid social ventures have an incentive to help established companies move toward more sustainable strategies. First, they benefit from the network effect of a larger business ecosystem of sustainability-oriented customers and suppliers that the involvement of a large, established company can help to create. Clothing company Patagonia, for example, facing short supply of organic cotton, shared information on its supply chain with Marks & Spencer and Nike, and joined forces with these companies through the Sustainable Apparel Coalition to create a stronger market for responsibly-grown cotton. Second, influencing established companies offers a large-scale channel to achieve their sustainability missions.

Established companies must thus balance impulses to compete with cooperation. To treat them like any other competitor would potentially miss an opportunity to capture some of the value of sustainability-oriented business.

How to respond?

So how can they respond to these rapidly growing upstarts and how might they benefit from their motivation to collaborate?

In a recently-published paper, **Strategic Responses to Hybrid Social Ventures** (co-authored with Jason Jay of MIT Sloan), we sought to answer these questions. We started by analysing eight established consumer-facing companies and how they responded to social ventures arriving on the scene. We then categorised these responses in terms of how they fit within the established companies’ overall strategies.

		Opportunities for Customer Value Creation through Sustainability	
		High	**Low**
Opportunities for Employee Value Creation through Sustainability	**High**	**Integrated Responses** *Acquire and integrate a hybrid social venture; actively diffuse practice and ethos across enterprise* Examples in our research: Unilever / Ben and Jerry's Danone / Stonyfield Farm	**Employee-Centered Responses** *Consult with hybrid social ventures to grow capabilities for sustainability innovation* Examples in our research: Panera Cares BJs / Whole Foods
	Low	**Customer-Centered Responses** *Create a brand OR acquire at arms length to explore and compete in the hybrid social ventures' market niche* Examples in our research: Skechers / Tom's Shoes Coke / Honest Tea	**Defensive Responses** *Monitor hybrids and defend mass-market position* Examples in our research: ConAgra Beverage Marketing (Arizona)

The acquisition approach

The first response method we studied was the "integrated response" that sought to collaborate with the hybrid social venture in order to create sustainability-oriented value with its own customers and employees. In these examples, the established company acquired the hybrid social venture and integrated its offerings and practices into its core businesses.

For example, Danone's acquisition of Stonyfield Farm was followed by long-term efforts to integrate sustainability-oriented offerings and practices of the hybrid social venture into the company's business. In 1998, Danone became one of the first companies to begin issuing annual reports combining economic and social performance and in 2001 acquired a majority stake in Stonyfield. Post-acquisition, Stonyfield's CEO gave Danone managers open access to study its climate action process. This informed Danone's move to measure its environmental footprint across product lines and business units.

In addition, Danone, Stonyfield and Cargill jointly invested in R&D for Polylactic Acid (PLA), to be used as an alternative to petroleum-based plastics in yogurt packaging and used Stonyfield's brand as the test market. By 2014, Danone began incorporating PLA into its own packaging. Danone then built on this by creating a new organic yogurt brand and went on to acquire a majority interest in an Irish organic dairy. By experimenting and knowledge sharing in its acquisition, Danone was able to more readily appeal to both customers and employees that value sustainability.

The customer-centric response

In the second category sits many established companies that have a niche of customers who might be willing to pay more for sustainable offerings, but their general position might be threatened by launching a company-wide sustainability strategy. This might be because their core businesses are highly price sensitive or sustainable values might cause internal disruption.

Coca Cola, for example, bought Honest Tea in 2011 as the company saw it “sitting at the intersection of…social responsibility, health and wellness and environmental consciousness”. The move gave Coke a short-term solution to satisfy its sustainability-oriented customers, while also providing a foothold for future expansion of its sustainability-oriented offerings through the Honest brand. For now, Honest Tea allows Coke to respond to growing customer demand for sustainable offerings while managing the brand at arm’s-length as part of its portfolio.

The employee-centred response

Some companies are caught between a strong employee desire to be more sustainable and a customer base unwilling to pay for more sustainable offerings. Panera Bread, a fast-casual restaurant chain with more than 1,700 outlets in 44 U.S. states and Canada, was one such case. The company had long operated philanthropy programmes such as in-kind donations of Panera products, but a coalition of Panera franchisees, along with the company’s founder and CEO Ron Shaich, wanted to develop a programme that did a better job of expressing its philanthropic goals and identity.

It consulted New Jersey-based Better World Café, a hybrid social venture operating a pay-as-you-can model that subsidises meals for the poor. Building on this model, Shaich and these key franchisees led the launch of Panera Cares, a pay-as-you-can concept featuring the Panera brand and product. Panera went on to open in five Panera Cares locations across the U.S. The programme has also received an unexpectedly high level of positive media attention.

Defence

Finally, companies can choose not to pursue sustainability-oriented innovations to protect their core businesses. Companies responding in this way, which often occupy low-cost positions, will typically continue to keep a close eye on hybrid social ventures, with responses typically focused on protecting the core business. ConAgra, for example, owner of several popular food brands including Orville Redenbacher and Peter Pan, was called out by sustainability activists for its perceived **failure to address sustainability issues**. While sustainability-oriented products are succeeding in ConAgra's product categories, they are inconsistent with ConAgra's low-cost position, which depends heavily on low prices and bulk retail channels. In addition, perceptions of ConAgra as non-environmentally conscious were so great that any move into the area might have come across as "green washing".

In the long-run, however, the choice to defend the core business without making moves toward sustainability may prove untenable. McDonald's had long adopted a "wait-and-see" approach on sustainable meat. But in recent years, under pressure from consumers and competitors like Chipotle who loudly promote their sustainability efforts (McDonald's, ironically, once held a majority stake in Chipotle), McDonald's has committed to begin sourcing beef from sustainable providers.

How deeply the sustainability movement affects other low-cost players, whose customers and employees tend to be very price-sensitive, remains to be seen.

Choosing the right approach

The sustainability movement is still unfolding, and companies must make decisions with limited information and adjust strategy over time. Managers can begin to consider their options for responding to hybrid social ventures in two ways. First, evaluate the sustainability orientation of your customers and employees. Do your employees express interest in sustainability in their outside activities? Are your customers willing to pay more? Are there trends in this direction, and if so, how quickly or slowly are they moving?

The second step is to gauge the willingness of hybrid social ventures to enter into a partnership. In conversations with potential partners, remember that the hybrid social venture benefits are related to leveraging your resources and scale. Some might be sceptical about losing their identity if an acquisition or other loss of control is on the table. Overcoming this scepticism is a key step in realising the potential value of such a partnership.

Hybrid social ventures and established corporations are often seen as operating in two separate worlds. But as the sustainability movement matures, they will find themselves in the same markets more and more – as competitors, but also as potential allies in a societal-level shift toward a more sustainable form of capitalism.

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