Building Investor-Proof Sustainability Strategies

By Jan Van der Kaaij, Managing Partner and Co-Founder of Between-us

Investors are increasingly looking for companies that report transparently on sustainability opportunities. But organisations remain stuck in reporting activities, failing to capture potential value from environmental, social and governance issues.

In 2014, it emerged that more than 71% of investors were dissatisfied with how U.S.-listed companies disclosed the relevance and implications of sustainability risks and issues. Moreover 80% were dissatisfied with how risks and opportunities were identified and quantified in financial terms. At the same time large investors such as BlackRock and Apax Partners expressed their concern with the difficulty companies have in describing the real business return of their sustainability activities.

While increased stakeholder demands and industry-level standardisation of environmental, social and governance (ESG) issues have made non-financial reporting more professional over the past decade, reporting has become more and more elaborate and time-consuming. This increases the risk of making the corporate sustainability report the end objective, particularly for listed companies, throwing them into the so-called “reporting trap”. These

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companies predominantly use their capacity and their materiality analysis for reporting purposes. This shifts focus and limits the potential of sustainability activities.

In line with the frustrations of investors, **a recent study** by MIT Sloan School of Management demonstrated the difficult position for sustainability in the C-suite. The study showed that only 26% of CEO's trust they have a clear business case for sustainability. At the same time, 65% of CEO's mention sustainability as a priority on the senior management's agenda. This leaves roughly 40% of companies that perceive sustainability as a "necessary evil" rather than an integral part of the company strategy.

What frontrunners are doing differently

In a recent study, **Avoiding the Reporting Trap**, conducted by Between-us in collaboration with Dow Jones Sustainability Index (DJSI) composer RobecoSAM, we analysed four major industries; chemicals, pharmaceuticals, food and telecommunications to investigate how frontrunner companies are meeting investor expectations by having a much stronger focus on value creation.

Obviously, around the globe, most listed companies have developed their own materiality analysis to determine and report on relevant ESG issues and their business impact. But when compared to the DJSI sector average of their peers, the top 5 frontrunners in their respective sectors are taking things much further. To avoid the reporting trap, these companies are truly sweating their ESG issues. Typically they do this by:

- Regarding materialities (industry speak for the social and environmental issues most important to the business and stakeholders) as new business opportunities

- Creating a strong business case for sustainability, avoiding philanthropy solutions

- Building partnering capabilities to team up with strategic partners in the value chain

In the study, in each of the four sectors researched, the smallest differences between frontrunners and the industry's average are noticeable for compliance-driven criteria, such as codes of conduct and corporate governance. The largest gaps are to be found in value creation criteria, such

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as climate strategy, operational eco-efficiency and human capital development.

Where sustainability is business development

The Danish biotech company Novozymes for instance has been extremely successful in studying materialities more closely to reveal their true potential. As the world leader in the industrial enzymes business with 48% market share, Novozymes' sustainability department is constantly on the lookout for opportunities. Being part of the business development team, the team researches materialities in its day-to-day practice and in its specific environment for which the support of value chain partners is indispensable.

Source: RobecoSAM, DJSI 2014 results

The most familiar Novozymes enzyme development is in the laundry detergents that enable consumers to wash at lower temperatures. Novozymes forged a partnership with Procter & Gamble as P&G was looking to revitalise its Ariel Brand, and a Life-Cycle-Analysis (LCA) showed that most energy was used in the home when heating the washing machine. The joint

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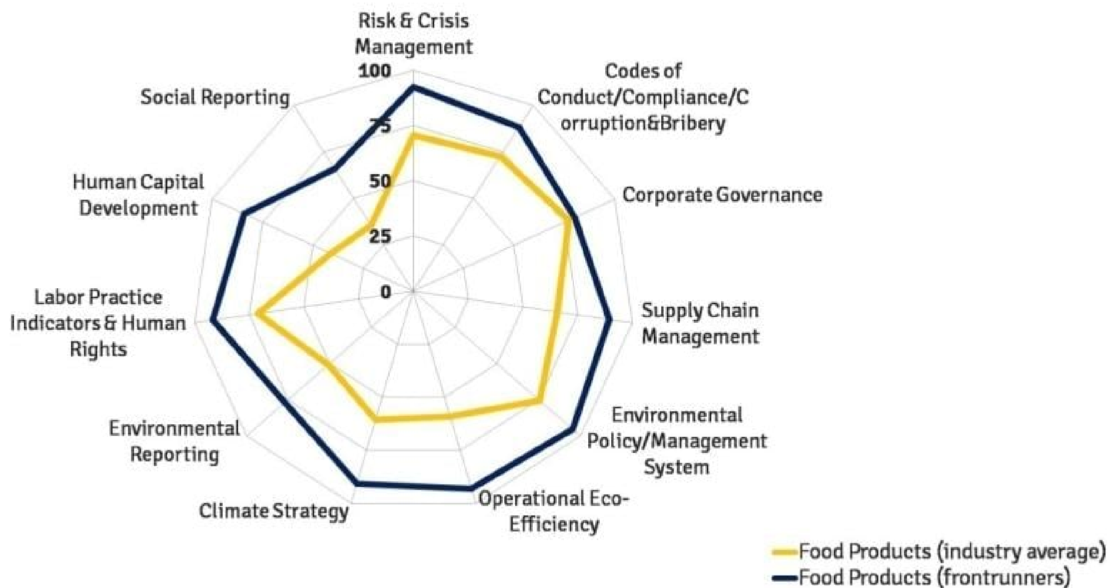
efforts of P&G and Novozymes resulted in the launch of the Ariel "Turn to 30" campaign in 2006, which made Ariel being the first global brand to promote doing laundry at 30°C.

Eight years on, by the end of 2014, the market share of detergents with enzymes was 95% in Europe, 70% in the Americas and around 60% in the rest of the world. The significance was obvious; customers in the household care division represented 36% of its 2013 sales.

Does more efficient product use impede sales?

Like the chemical sector, the food industry has very high industry average scores on DJSI criteria, which indicates well-established industry standards and a mature level of sustainability. Therefore it is no surprise that food companies such as Unilever and Nestlé, are consistently named among overall global sustainability leaders.



Source: RobecoSAM, DJSI 2014 results

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A great example is set by Unilever with its Hellmann’s mayonnaise brand. True to their slogan “bring out the best” the company brand came up with a product innovation that grew sales and reduced its environmental impact. To address the increasingly important issue of food and packaging waste, Unilever developed the “Easy Out” technology together with key suppliers. This was a squeezy bottle enabling customers to get more mayo out of the bottle. The result is less waste, less mess and more sales. The innovative new packaging has taken the average amount of leftover mayo in a bottle down from 13 percent to 3 percent, saving 5,000 tonnes of landfill per year in the process. Furthermore the novelty contributed to sales growth of 9.2 percent for Hellmann’s in the U.K. proving that a positive business case could be made by innovation of a material issue.

How to sweat the issues and put the materialities to work

Unfortunately, sparking sustainable innovation from materialities in a way that investors appreciate is not always plain sailing. Material issues as formulated in the corporate annual sustainability report need to be “decoded” to make them usable in practice. To put the corporate materiality matrix to work, three extra design criteria are to be considered:

1. **Terminology:** morph the legal and accountancy lingo into language that can be straightforwardly linked to the business. Life cycle analysis data is often a useful instrument when locating the right “hotspots”.

2. **Easily scalable:** include solutions for local or emerging markets with different cultures or in the early stages of their sustainability journey.

3. **Clear measurement of progress:** not merely on internal KPI’s, but also on external perception.

Companies such as Novozymes and Unilever light the way for avoiding the reporting trap by embedding their sustainability activities company-wide. They view materialities not just as risks but also as opportunities for value creation in terms of cost reduction, revenue generation and/or gross margin protection. In addition they work hard on developing the capabilities to collaborate with value chain partners, which more often leads to breakthrough ideas that have potential. And last but not least, they focus on creating a strong business case for sustainability, which makes convincing investors of the real business value of sustainability a lot easier.

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__Jan Van Der Kaaij__ is the Managing Partner of __Between-us__ a strategy and sustainability consultancy and a partner in INSEAD's __Leading the Business of Sustainability__ executive development programme. He is also a member of the __INSEAD Sustainability Roundtable__ Advisory Board.

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