# Trends in sustainability

## PART 1: MACRO TRENDS AND DRIVERS

The roots of the term, "sustainability," date back to debates in the 1970s about environmental heath and economic development. In 1987, the World Commission on Environment and Development (Brundtland Commission) published a report, Our Common Future, which introduced the concept of "sustainable development." This concept offers the most widely accepted definition of "sustainability" today:

"Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs. ...

... In essence, sustainable development is a process of change in which the exploitation of resources, the direction of investments, the orientation of technological development; and institutional change are all in harmony and enhance both current and future potential to meet human needs and aspirations."

Below are the key macro trends driving the international agenda on and attitudes toward sustainable environmental, social and economic development.

### Population growth and urbanization with a power shift to emerging markets

→ The United Nations' (UN) World Population Prospects: 2010 Revision forecasts an increasingly urban global population of 9.3 billion by 2050 and 10.1 billion by 2100. About two-thirds will reside in cities by 2050.

→ Much of this increase is projected to come from high-fertility countries in developing and emerging regions.

→ By contrast, fertility is lower in the majority of developed countries, where population growth will peak before the end of the century and then decline.

→ Life expectancy is projected to increase from 68 years in 2005-2010 to 81 in 2095-2100, with low-fertility countries tending to have higher life expectancies than high-fertility countries.

→ In the lowest-fertility countries, declining fertility and increasing longevity lead to faster population aging and a shrinking base of experienced, skilled workers, with a projected increase from 11 percent aged 65 or over in 2010 to 26 percent in 2050.

→ In contrast, population aging and the decline in potential active workers are slowest among high-fertility countries, with a projected increase from 3 percent aged 65 or older in 2010 to just 6 percent in 2050 and 16 percent in 2100.

### Global consumption, resource depletion and ecosystem destruction

→ Growing populations and urbanization increase consumption, compounding the challenge of meeting the food, water, energy and material needs of nine billion by 2050.

→ The UN predicts that two-thirds of the world's population will live under water-stressed conditions in 2025. Climate change due to greenhouse gas emissions will exacerbate water scarcity, destabilize supporting ecosystems and disrupt global food chains.

→ Two UN Trends in Sustainable Development reports find that increased globalization, urbanization and rising prosperity are taking a greater toll on the world's ecosystems. Economic growth and ecological deterioration are coupled.

- Steep growth in resource extraction and use over the past several decades has overwhelmed technological and structural progress to mitigate the impact.
- Developed countries' ecological footprints continue to expand, mostly as a result of rising greenhouse gas emissions. In 2005, industrialized countries used 50 percent of fossil energy, industrial minerals and metallic ores while accounting for only one-sixth of the word's population.
- Developing countries are rapidly expanding their footprint with increased resource production, extraction and consumption, automobile ownership, e-waste generation, and transport demand.
- Countries exceeding their biocapacity went from none in 1960 to 24 countries at present.

→ The World Wildlife Fund's (WWF) 2010 Living Planet Report on the planet's health and impact of human activity finds a consistent trend of ecological overshoot.

- Humanity's ecological footprint has doubled since 1966, largely because of the carbon footprint, which has increased 11-fold since 1961.
- Global biodiversity is down 30 percent since 1970, due mostly to habitat loss in tropical regions, where biodiversity has declined by 60 percent.
- The majority of species have experienced population, habitat and genetic diversity declines. The Millennium Ecosystem Assessment (MA) estimates that over the past few hundred years, humans have increased species' extinction rates by as much as 1,000 times more than recorded in the fossil record.
- Natural resources are being consumed faster than the Earth is replenishing them—at the rate of 1.5 planets. By 2030, humanity will need the capacity of two planets to meet consumption needs and absorb $CO_2$ waste.
- Ending ecological overshoot is essential to sustain human health, wealth and wellbeing.

→ In economic terms, declining resources, soil degradation, water shortages and biodiversity loss will result in higher commodity prices, while the threat of climate change means:

- 2-3°C temperature rise = 3 percent annual global GDP loss
- 5°C temperature rise = 10 percent annual global GDP loss
- Sea levels rising 18-59 mm by 2100 with almost half of the world's population living within 200 km of a coastline will have an unprecedented and potentially devastating impact on all aspects of the supply chain and on how people live and work.

## Social response to a decade of turmoil and rising threats

→ The past decade has seen economic and socio-political upheaval and the declining credibility and financial capacity of society's institutions. The Harvard Business Review article, "Leadership in an Age of Transparency," describes unavoidable trends:

- Stakeholders demand greater transparency about companies' externalities—their direct and indirect environmental, social and economic impacts on the broader world.
- Businesses must recognize and be accountable for their externalities.

→ The HBR article attributes this move toward transparency and accountability to:

- Growing scale and volume of external impacts globally, now too large to ignore
- Improvements in sensors (data sources) that collect, measure and analyze these impacts
- Technologies and social media that open up information access, deepen conversations with stakeholders and transform the reporting environment into demand-pull rather than supply-push: "Blogs, twitters and the new media environment…have turned the brick walls of our offices into glass."
- Heightened stakeholder awareness of corporate impacts: "Consumers know everything about your company, not just its carbon emissions but its countless other 'invisible' effects on the globe. That has changed the rules forever."
- Higher stakeholder expectations for better sustainability information and performance, and more say on issues that interest and affect them

→ It is now incontrovertible that socio-economic trends, such as demographic shifts, urbanization and consumption patterns, and environmental trends are interlinked. The turmoil of the past decade has fueled a sense of urgency to address them.

- Climate change, biodiversity loss and ecological disruption impact and are impacted by such issues as poverty, income inequalities, human rights, conflict and public health.
- The net threatens socio-political stability and human wellbeing, pressuring society's institutions to intervene.

→ The findings from the 2011 Edelman Trust Barometer study of 5,075 people in 23 countries underpin people's views toward and expectations for institutions worldwide.

**Demand for greater transparency and trust**

- Globally, trust improves across all institutions, with emerging markets driving the increase: NGOs at 61 percent (+4 points); business at 56 percent (+2 points); government at 52 percent (+5 points); and media at 49 percent (+4 points).
- The stark exception is the U.S., which sees a decline across the board, dropping from fourth from the top in 2008 to the bottom three in 2011 (-11 points).
- Trust in banks plummets in the West and in the U.S. most steeply (-46 points), while technology remains at the top worldwide, and automotive climbs globally.
- Quality (69 percent), transparency and honesty (65 percent), trustworthiness (65 percent) and employee welfare (63 percent) rank as the most important for corporate reputation. Admired leadership and financial returns tie for last place (39 percent).

**Belief that business should align profit and purpose for social benefit**

- Business should create shareholder value in a way that aligns with society's interests, even if that means sacrificing shareholder value (85 percent the U.S.).
- Government should regulate corporations' activities to ensure business behaves responsibly (61 percent in the U.S.).

**Desire for authority, accountability and credibility amidst increased skepticism and noise**

- Trust in experts and the CEO rises: academic/expert (70 percent), technical expert in a company (64 percent), financial/industry analyst (53 percent), CEO (50 percent).
- While trust in media inched up globally, it declined significantly in the U.S. (-11 points to 27 percent) and the U.K. (-9 points to 22 percent).
- The majority need to hear something three to five times to believe it. One-quarter in the U.S. and U.K. need to hear it six to nine times—twice as many as two years ago.
- Search engines are the "go-to" information source (29 percent), followed by online news sources (19 percent), print (15 percent), broadcast media (12 percent), company website (11 percent), friends and family (7 percent) and social media (5 percent).
- In the face of information ubiquity and savvy information seekers, corporate communications should encompass mainstream, new, social and owned media.

**Trust as a protective agent for reputation; lack of trust as a barrier and liability**

- When a company is trusted, 51 percent believe positive news after hearing it once or twice; only 25 percent believe negative news after hearing it once or twice.
- When a company is distrusted, only 15 percent believe positive news after hearing it once or twice; 57 percent believe negative news after hearing it once or twice.
- Distrusted companies have a harder time overcoming negative news and changing opinion than they would if they were trusted at the outset. Nor do they get as much credit for good news as do trusted companies.

**Profound, far-reaching economic impact of business externalities**

→ The interlinked economic, environmental and social trends over the next 50 years will have a significant impact on the operating context and long-term viability of businesses.

→ Companies in all sectors both impact and depend on biodiversity and ecosystems. Businesses that fail to assess their impacts and dependence carry undefined risks and may neglect profitable opportunities.

→ The Economics of Ecosystems and Biodiversity (TEEB), a global study initiated by the G8 and five major developing economies, illustrates some examples of the economic value of biodiversity and the direct and indirect contributions of ecosystems to human well-being:

- Avoiding greenhouse gas (GHG) emissions by conserving forests: ~$3.7 trillion (NPV)
- Loss due to deforestation in China over the entire period 1950-98: ~$12 billion
- Contribution of insect pollinators to agricultural output: ~$190 billion/year
- Loss due to the 2007 collapse of honey bee colonies: ~$15 billion
- Intellectual property derived from genetic resources: ~25-50 percent of the $640 billion global pharmaceutical market

→ A Trucost study commissioned by The Principles for Responsible Investment (PRI) and the United Nations Environment Programme Finance Initiative (UNEP FI) calculates the current and future estimated cost of global environmental damage.

- The estimated annual environmental costs from global human activity are $6.6 trillion, equivalent to 11 percent of global GDP in 2008.
- The 3,000 largest publicly listed companies caused 35 percent of all environmental damage in 2008—valued at $2.15 trillion or 7 percent of combined revenues.
- Of the 3,000 companies, five sectors—electricity, gas and oil producers, industrial metals and mining, food producers, and construction and materials—account for 60 percent of all environmental damage costs.
- Over 50 percent of company earnings could be at risk from environmental costs in an equity portfolio weighted according to the MSCI All Country World Index.
- By 2050, the cost of global environmental damage from water and air pollution, GHG emissions, waste and depleted resources could reach $28 trillion or 18 percent of GDP.
- These costs could lower the value of portfolios broadly invested in capital markets via:
  - Higher insurance premiums, taxes, inflated input prices and physical cost of disasters
  - Reduced cash flows and dividends in the future
  - Damage to the profitability of other portfolio companies, adversely affecting other investments and reducing overall market return
- Beneficiaries—workers and retirees—could see lower pension payments from funds invested companies exposed to environmental costs.

**2010-2020—a new era of economic transformation rising from the ashes**

→ After the decade from hell, a new economy with a sustainability agenda is assembling, one that strives for balance across environmental, social and economic performance targets.

→ This agenda seeks to dismantle the economic and business order of the 19th and 20th centuries that has been both socially inequitable and environmentally unsustainable.

→ This destruction of old models paves the way for constructing new ones fit for a human population reaching nine billion by 2050 and sharing a small planet in ecological peril.

→ The Global Reporting Initiative (GRI) 2010 report, The Transparent Economy, identifies six trends—TIGERS—over the next decade that will shape this transformation.

- "Traceability" of products through complex global supply chains
- "Integrated reporting" across the triple bottom line—environmental, social and economic
- "Government leadership" in terms of regulation, disclosure rules, data aggregation and modeling transparency
- "Environmental boundaries" describing the links to planetary limits associated with climate, biodiversity and nutrient cycles
- "Rating and ranking" schemes that help spur and inform competition between companies and countries
- "Shadow economies" involving drug or sex trafficking, the weapons trade, illegal waste dumping and corruption

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# Trends in sustainability

## PART 2: BUSINESS RESPONSE TO SUSTAINABILITY

### Growing business commitment to sustainability, but not a top near-term priority

According to a 2011 global study of 4,700 executives, managers and thought leaders by the MIT Sloan Management Review and Boston Consulting Group, sustainability continues to gain ground in business; however, in the short run, other pressing issues often eclipse it.

→ The majority of respondents (70 percent) agree that sustainability is important to top management. A substantial number say it's changing the business model.

- For 28 percent, sustainability is now a permanent fixture and core consideration.
- For 42 percent, it's not a core strategic consideration, but it's on the agenda to stay.
- A total of 29 percent view it as either a temporary, non-core agenda item (19 percent); excluded as a passing fad (2 percent); or never considered at all (8 percent).
- For 40 percent, sustainability has changed their organization's business model.

→ Sustainability is becoming more important to prospective and existing employees.

- Nearly half (49 percent) say a company's degree of sustainability commitment could affect their choice to choose or change an employer.
- Far fewer people (35 percent) say it wouldn't.

→ Commitment to sustainability in terms of management attention and investment has dramatically increased since 2009.

- In 2011, 68 percent have increased their commitment from the previous year, and 74 percent expect it to grow in the year ahead.
- In 2010. 59 percent increased their commitment from the previous year.
- In 2009, 25 percent increased their commitment from the previous year.

→ Two-thirds (67 percent) say that sustainability strategies are necessary to be competitive—a 12 percent increase from 2010, when only 55 percent thought so.

- An additional 22 percent say that although sustainability strategies are not needed today to be competitive, they will be in the future.
- Only 7 percent disagree that they're needed at all, down a percent from 2010.

→ Despite the growth in commitment and importance, most don't consider sustainability issues to be the primary business challenges over the next two years.

- The top three are innovating to achieve competitive differentiation (46 percent), growing revenue (45 percent), and reducing costs and efficiencies (41 percent).
- Responding effectively to sustainability threats and opportunities is second to last, declining from 16 percent in 2010 to 14 percent in 2011.
- Responding effectively to globalization threats and opportunities (closely linked to sustainability issues) is at the bottom, declining from 14 percent to 12 percent.

### A sizeable minority—about a third—still skeptical about the value of sustainability

A 2011 Accenture survey of 247 C-suite decision makers in the U.S., UK and China confirms that a growing number of businesses see sustainability as a key strategic investment; however, a substantial percentage consider it peripheral and a cost to their business.

→ The majority of companies have implemented and benefited from sustainability initiatives.

- More than half (55 percent) have at least a few sustainability programs, and over a third (38 percent) have many.
- Most (72 percent) say the benefits have exceeded expectations, with the top four being improved reputation and trust (49 percent), perception as a responsible company (47 percent), lower costs (42 percent) and improved brand (41 percent.)

→ Among those with initiatives, the top five reasons for implementing programs are:

- Genuine concern for environment/society (53 percent)
- Reducing energy and materials costs (50 percent)
- Consumer/customer expectation (47 percent)
- Opportunities for business growth and higher margins (45 percent)
- Reputation/brand/trust (44 percent)

→ One-third of businesses, however, remain unconvinced of the value of sustainability.

- While 68 percent of senior business decision makers consider sustainability an integral part of their business, one in three (32 percent) still views it as peripheral.
- Similarly, 66 percent see sustainability as an investment and 34 percent see it as a cost.
- Although 60 percent believe their companies are investing the right level in sustainability initiatives, 28 percent say their businesses invest too much or far too much—more than those saying they spend too little or far too little (12 percent).
- The same percentage (28 percent) feel that businesses in general are doing too much to make sure their working practices are more sustainable.
- The good news is that two-thirds (67 percent) of these holdouts are likely to introduce initiatives in the next year, although a hardcore third (33 percent) aren't likely to do so.

→ The top five barriers are:

- Cost of sustainability initiatives (43 percent)
- Inability to measure sustainability initiatives (31 percent)
- Lack of government/local authority incentives (30 percent)
- Belief that one company can't make a difference to global warming (29 percent)
- Lack of consumer interest and senior leadership commitment (24 percent)

→ Moving forward, most believe that three external factors will push businesses to adopt sustainability practices (listed in priority order):

- Investment pressure
- Regulatory requirements
- Consumer/customer expectations and opportunities for growth and higher margins

### Finance, measurement and inconsistent regulation—persistent challenges

Like the 2011 Accenture study, KPMG's Corporate Sustainability: A progress report finds a slow uptake of sustainability by a third of businesses (those without a working sustainability strategy) worldwide. Additionally, KPMG's survey of 378 executives worldwide aligns with Accenture's findings on the top barriers to sustainability and offers additional insights.

→ Company size and ownership type

- Larger public companies are more likely to have corporate sustainability strategies (79 percent) than smaller private companies (49 percent).
- The 2010 annual review of over 1,200 companies participating in the United Nation Global Compact's corporate responsibility initiative confirms that larger and publically-traded companies far outperform small and medium-sized enterprises on all issues: human rights, labor, environment and anti-corruption.
- The capital investments for sustainability programs are often too large for small or medium-sized firms with limited access to credit and financing.
- Larger companies have more human resources to support sustainability programs.
- Public companies face greater scrutiny and pressures to disclose their external impacts.

→ Negative global economic environment

- Nearly half (45 percent) say business survival and short-term financial pressures are bigger priorities—a trend reinforced in the 2011 MIT Sloan Management Review study.
- The ROI for sustainability initiatives take longer to manifest, leading many to focus on other activities that retain customers, protect revenues and offer a faster return.
- Other cost concerns include beliefs that implementing sustainability may lead to more expensive products and services (36 percent) and reduced profitability (23 percent).

→ Lack of reliable data and relevant benchmarks to measure sustainability progress

- Over a third (36 percent) have issued at least one public report on sustainability performance. Another 19 percent will do so soon, but 38 percent have no plans to do so.
- Small private companies are least likely to report, while two-thirds of public companies with revenues over $5 billion do. Another12 percent plan to report within two years.
- The majority of respondents struggle with creating or finding reliable internal data (78 percent) and with finding meaningful benchmarks (76 percent).
- About two-thirds (65 percent) have difficulty determining what to report.

→ Lack of a clear, rigorous international framework of regulation

- Slow progress in establishing new international laws and guidelines on sustainability has created a high degree of uncertainty impacting companies' ability to plan effectively.
- In part because they know that regulation is inevitable, businesses generally agree that government should do more in terms of setting clear rules and targets.
- Two-thirds of executives (67 percent) are in favor of a successor to the Kyoto Protocol, the first phase of which is ending in 2012.
- One in five companies are lobbying on domestic legislation dealing with climate change. Of those lobbying, twice as many want tougher domestic regulations than those looking for weaker ones. Nearly four times as many want tougher international regulations.

### Despite challenges, sustainability leaders positioned to outperform laggards

A 2010 MIT Sloan Management Review and Boston Consulting Group study of over 3,000 executives and managers, Sustainability: The "Embracers" Seize the Advantage, concludes that embracers who place sustainability high on their strategic agenda have a competitive advantage over cautious adopters who have yet to focus on more than energy cost savings, material efficiency and risk mitigation.

→ Among those surveyed, embracers comprise 24 percent of business leaders who say:
  - Their company has a business case for sustainability.
  - Sustainability is necessary to be competitive.
  - Sustainability is a permanent management agenda.

→ Embracers tend to represent large global or regional companies from resource-intensive (i.e., product) and heavy industries with larger environmental footprints.

→ Embracers are bold, early movers, undeterred by ambiguity or lack of information.
  - They are prepared to act before they necessarily have all the answers.
  - They see action as a way to generate data, uncover opportunities and develop evidence iteratively that makes decision making increasingly effective.

→ Embracers are top performers, confident in their competitive position and successful balancers of vision and execution.
  - Embracers balance ambitious, long-term sustainability aims with projects that produce positive, bottom-line results in the near-term.
  - The majority of embracers (70 percent) say they outperform their competitors compared with just over half (53 percent) of cautious adopters.
  - Cautious adopters are twice as likely as embracers to admit they lag behind their peers (14 percent versus 6 percent).
  - Embracers are three times more likely than cautious adopters to believe their sustainability decisions have added to profits, such as increased sales from new, innovative products or sharpened focus on areas in which sustainability can deliver a competitive edge (66 percent versus 23 percent).

→ While both embracers and cautious adopters see brand reputation as a top benefit, embracers view sustainability advantages more broadly overall.
  - Embracers focus on the potential for growth, profitability and competitiveness: 1) brand reputation; 2) competitive advantage; 3) access to new markets; and 4) increased margins or market share.
  - Cautious adopters focus on reduced costs and risks: 1) brand reputation; 2) reduced costs due to energy efficiency; 3) reduced costs due to materials or waste efficiencies; and 4) reduced risk.

→ Embracers drive sustainability top-down and bottom-up.
  - At embracer companies, senior leadership sets the strategy and priorities, talking openly about sustainability challenges and opportunities for the business.
  - Embracer companies also enlist the involvement of employees at all levels, creating financial and managerial incentives to contribute.

→ Embracers aggressively "de-silo" and integrate sustainability throughout their operations.

- They don't treat sustainability as a separate function, but rather embed it in all business processes and practices to create a culture of sustainability.
- That includes integrating sustainability opportunities and material risks, along with traditional financial standards, into investment and other business decisions.

→ Embracers value and measure both the tangible and intangible impacts of sustainability.

- Embracers are more likely than cautious adopters to value and factor in the intangible benefits of sustainability, such as brand reputation, productivity, attracting and retaining top talent, and innovation of business models, processes, products and services.
- Embracers establish baselines and develop assessment methods to measure both tangible, physical impacts (waste and energy efficiency, water conservation, etc.) and intangible, qualitative ones—and if methods don't exist, they invent them.

→ Embracers strive for transparency and authenticity—internally and externally.

- They recognize the need to look toward long-term horizons, even if that means less impressive short-term profit margins.
- They are more likely to communicate challenges along with successes, although more embracers could adopt a "warts and all" approach to reporting and communications.

### Sustainable growth—five areas of focus for CEOs through 2014

In its 14th Annual Global CEO Survey conducted in the last quarter of 2010, PwC presents how over 1,200 CEOs in 69 countries intend to pursue "good growth"—one that is financially, socially and environmentally sustainable over the next three years.

→ Tap into growing customer sentiment about environmental and corporate responsibility practices.

- Nearly half of CEOs (48 percent) say the economic crisis has changed purchasing behaviors permanently, particularly in emerging markets where recovery is more rapid.
- CEOs expect customers to factor in environmental and corporate responsibility practices into purchasing decisions.
- About half say they'll change strategy to make their companies more responsive to societal expectations: 53 percent who rely on businesses as a significant source of revenue; 51 percent who rely on governments; and 49 percent who rely on consumers
- Plans include adapting or developing new offerings and answering questions not only about their practices, but also about their suppliers'.

→ Develop more ecofriendly products and services as part of an innovation strategy.

- Four out of five CEOs see operational efficiencies that provide competitive advantage (79 percent) and significant new revenue opportunities (78 percent) coming from their innovation pipeline.
- Nearly two-thirds (64 percent) say environmentally friendly products and services are an important part of that pipeline.
- About the same number (62 percent) plan to look more to their suppliers for help in developing ad carrying out a shared innovation agenda.

→ Work more effectively with governments on global risk issues, including climate change.

- Over half (55 percent) of global CEOs are optimistic that a shared agenda between the public and private sector would be more effective than it has been in the past—particularly around issues like developing talent, generating innovations, improving infrastructure and securing critical natural resources.
- In contrast, U.S. CEOs signal significant joint responsibility only for innovation, intellectual property protection and health of workers. Addressing climate change, securing natural resources and reducing poverty are lower priorities for U.S. CEOs than for their global peers.
- Most global CEOs (72 percent) would support policies promoting good growth, but 59 percent worry that overregulation could harm their company's growth prospects.
- CEOs are thinking win-win—meaning they want policy makers to balance their objectives against concerns about overregulation that could harm economic recovery.
- With the right framework for collaboration, CEOs are willing to join with governments in a sustained effort toward mitigating global risks and achieving financial sector stability, infrastructure improvement, workforce training and other positive outcomes.

→ Protect against natural resource depletion that threaten near-term growth prospects.

- One out of three CEOs has fundamentally changed strategies due to the worldwide recession and the global risks it exposed.
- CEOs across sectors view political instability and natural resource scarcity as the top two global risks over the next three years, followed by climate change and natural disasters.
- CEOs recognize that many global risks are interlinked in a complex web. Political instability, climate change and natural disasters—along with other health and environmental issues—can impact the availability of natural resources.
- Through 2014 and beyond, CEOs will need strategic discipline and foresight to untangle the web of risks and close the gap between strategic planning and operational reality.

→ Attract the right people capable of driving strategies for sustainable growth.

- Talent is at the top of the CEO agenda, with 83 percent anticipating changes to their talent management strategies over the next 12 months.
- Talent management strategies are likely to reflect CEOs' growth plans: navigating emerging market growth opportunities (76 percent) and developing more ecofriendly products and services (64 percent).
- Risk management (77 percent) and corporate reputation and rebuilding trust (63 percent) are other CEO focus areas that help attract and retain skilled employees.

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