Breaking Through

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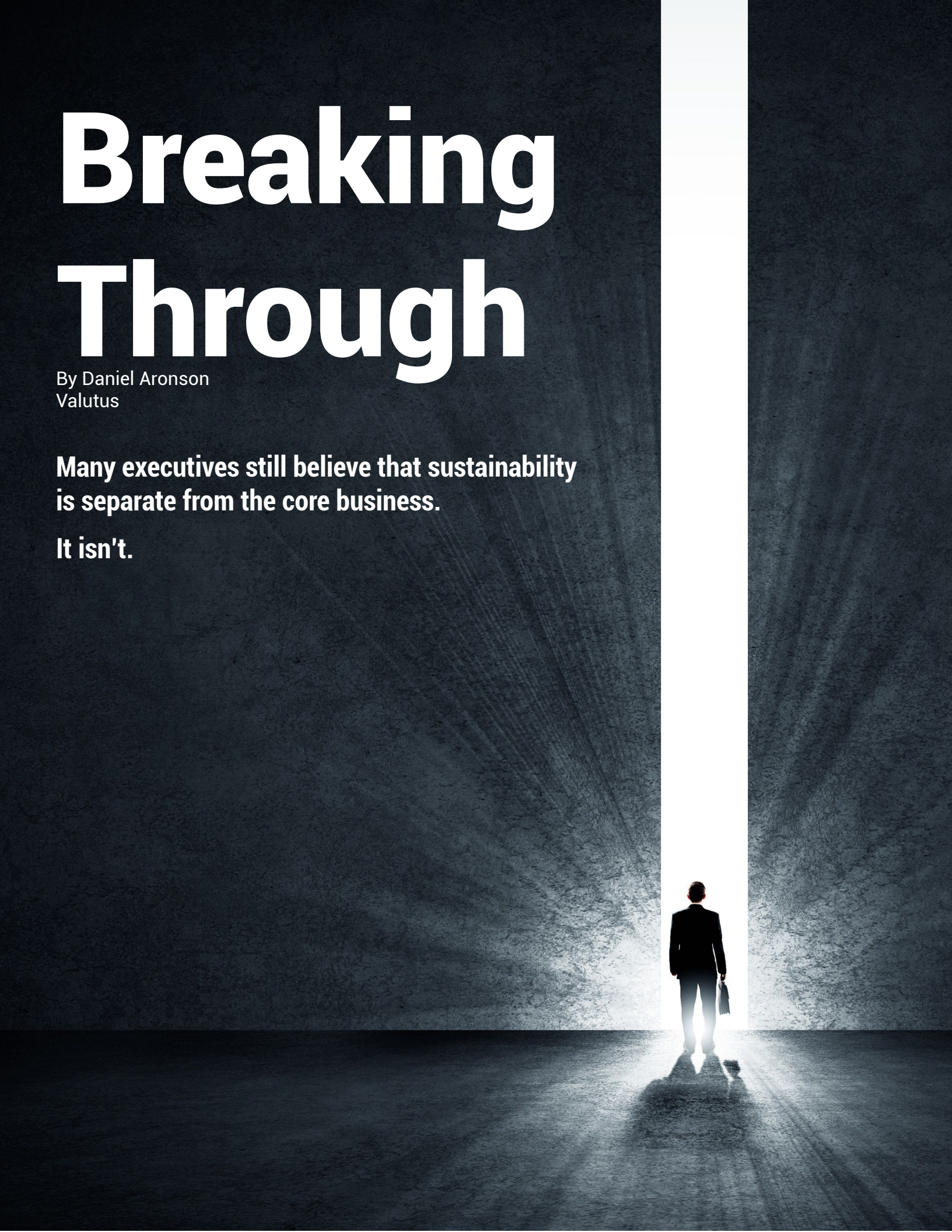
Many executives still believe that sustainability is separate from the core business.

It isn't.



Two years ago, the Weinreb Group's most up-to-date count had the number of publicly traded U.S. companies with a Chief Sustainability Officer at 44. In 2021, with Siberia reaching temperatures of 110 degrees or more, droughts, global health crises, and everything else, the number reached 95 — which is still only around 2% of such firms.

Moreover, what one sustainability expert told us at the time is likely still true: "If you ask how many of those have the real authority of a C-level position, the true answer is: Zero." Why? One reason: numbers and money.

Sustainability professionals are not seen as true business partners who speak the language of profits and tie their efforts directly to the company's financial success.

As the CFO of a multi-billion-dollar corporation told me, "There are only two departments that come into my office asking for money without numbers: HR and sustainability."

And even when the ROI is present, and presented to executives, the connection to the core business is often missed. Execs often think: 'The ROI numbers are nice, but we don't compete on energy use or waste. We compete on our core business offerings.'

Many executives are so well trained on maximizing shareholder value, they simply don't see beyond it easily. That doesn't mean other things – like doing the right thing – don't matter. They do. But ROI matters a lot too.

The ROI Barrier

There are three big walls that sustainability execs run into when trying to demonstrate the value of their work:

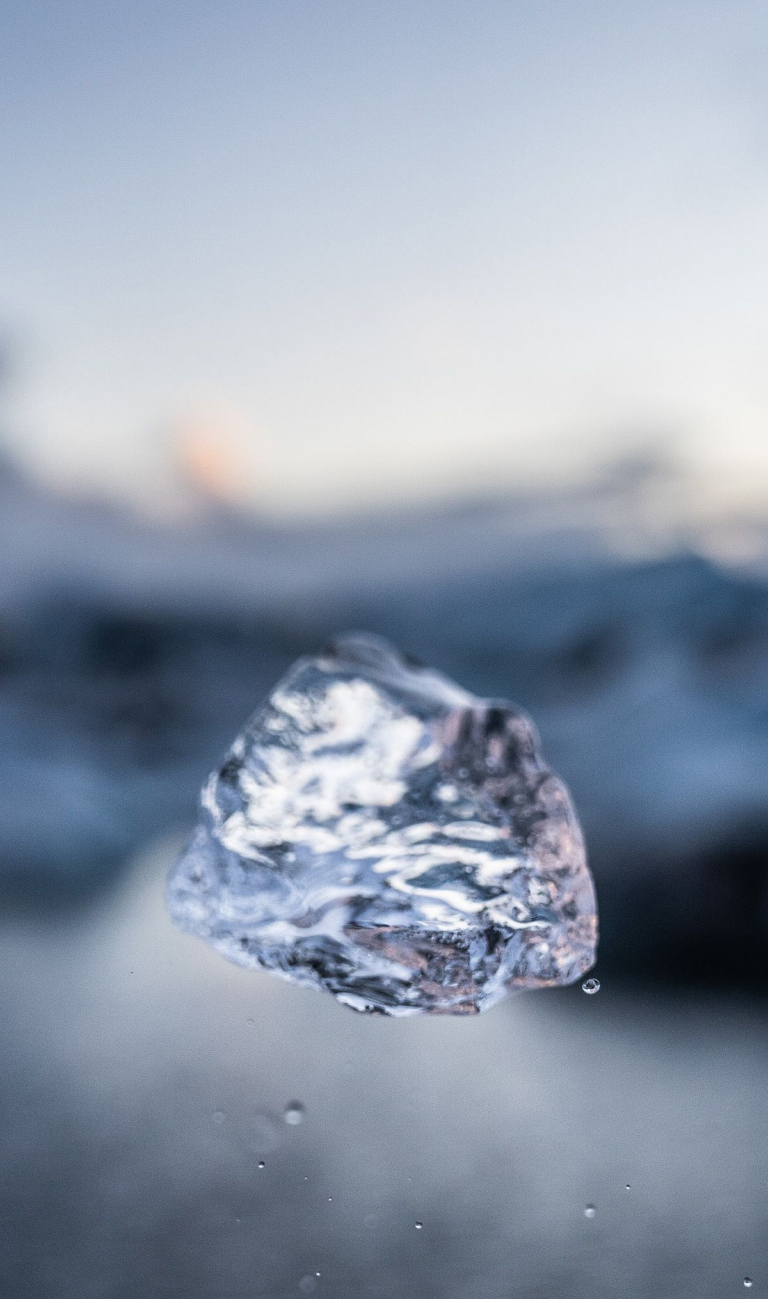
- The difficulty of seeing how sustainability creates value
- The challenge of quantifying submerged value
- The hurdles to credibly communicating sustainability's value

The first wall: The difficulty of seeing the ways sustainability creates value

The value created by sustainability falls into four categories, represented by the acronym CORE. The four areas are:

- Customers
- Operations
- Risks
- Employees

If you don't examine all these areas, you'll miss value, and you'll underestimate the benefits of sustainability. Maybe (as will be covered shortly) some customers prefer to buy from a more sustainable company (the Customers category), or possibly more efficient aircraft would reduce the amount spent hedging fuel prices (Operations). Conceivably, new onsite solar with battery storage lowers the chance production will be affected by a blackout (Risk) or being known as a sustainability leader helps acquire and retain the best talent (Employees). If you don't look at each category, you'll overlook benefits that sustainability provides.



The second wall: Submerged value

Seeing Submerged Value

Even if you know where to look for sustainability's value, you are very likely to miss a lot of it, because so much of it is **submerged** (hidden). It **is** obvious in hindsight, if you know where to look, but knowing where to look is rare. As a result, it is unseen and, therefore, unvalued.

Submerged value exists in each of the CORE areas, and it comes in many forms. Once understood, it begins to show up everywhere.

One company we worked with wanted to quantify the value of reducing waste. They were including (correctly) the benefits of lowering their waste disposal costs, but that was a tiny savings at under ten cents a pound. They also recognized that if they wasted less material, they could buy less, thus lowering purchasing costs. This benefit was larger but still not enough to financially justify the waste-reduction investment.

But these two areas just scratched the surface; we found about two dozen additional submerged benefits they had overlooked. Purchasing less means:

- No need to process the additional purchase orders
- Or put the resulting invoices through the accounts payable system
- Or put the additional material in the inventory system
- Or take it off the boat and put it in the truck
- Or take it off the truck and put it on the forklift and then into the warehouse
- There's no need for as much warehouse space
- Which lowers heating, cooling, and insurance expense
- There are fewer injuries, since no one ever got hurt moving material that was never bought to begin with
- Material that doesn't get purchased doesn't have to be tracked and rotated
- And it also doesn't require compliance with handling and storage requirements or certification that you did so
- Wasting less also means there's less waste material to take out of the inventory system, put back on the forklift, put back on a truck, and pay someone to take away

- And, during this whole process, unpurchased material doesn't consume working capital
- Plus, the more material isn't raising inventory levels, and that prevents many other potential problems that Lean identifies (such as reduced flexibility, lower productivity, etc.)

Note that **none of these submerged elements is intangible.** Submerged doesn't mean intangible; it only means unseen.

Quantifying Submerged Value

After it's identified and surfaced, submerged value must be quantified. For example, how much does it affect customer choice, for which customers, and under what circumstances? What is the impact in talent-related areas such as recruiting, retention, and productivity?

Answering questions like these is difficult, but it **is** possible. Earlier this year, we had tens of thousands of people choose between two products, varying whether one had an environmental or social attribute. As a result, we were able to quantify the change in preference for each sustainability attribute, based on data from over **50,000 consumer choices.**

Did it change the effect when the sustainable product was already preferred? What if people had originally preferred the competition's product? Did the effect on preference vary when the products were visibly different versus when they were almost identical? Our research was able to answer those questions and many more such as if the effect changed when the products were different prices versus when the price was the same for both. We were, in fact, able to show that sustainability **did** affect customers choices, enough to have a substantial financial impact.

You don't have to conduct original research involving tens of thousands of customers, however, to benefit from thinking about the customer-related value of sustainability. Whether it's hearing from select customers, using publicly available data, or talking to your sales force, what matters is to find a way to **identify how sustainability affects customer behavior.**

The customer-related effect of sustainability isn't always on preference: sometimes it shows up in other areas. For one European B2B company, we analyzed over 10,000 customer records covering multiple years and found that – when compared to a control group of similar companies – customers who were involved with the firm's sustainability efforts bought more frequently, were more likely to purchase higher-margin products, and remained customers longer. Even without considering any changes to preference, these other shifts drove a much higher customer lifetime value (CLV) than the companies in the control group.

Submerged value is just as prevalent in operations. We showed a telecommunications company how more energy-efficient data centers didn't just reduce energy expenses today, but also lowered future capital expenditures. We helped them see that the continued growth in servers, and thus electricity demand, would require upgrading the power infrastructure coming into the data center in the near future.

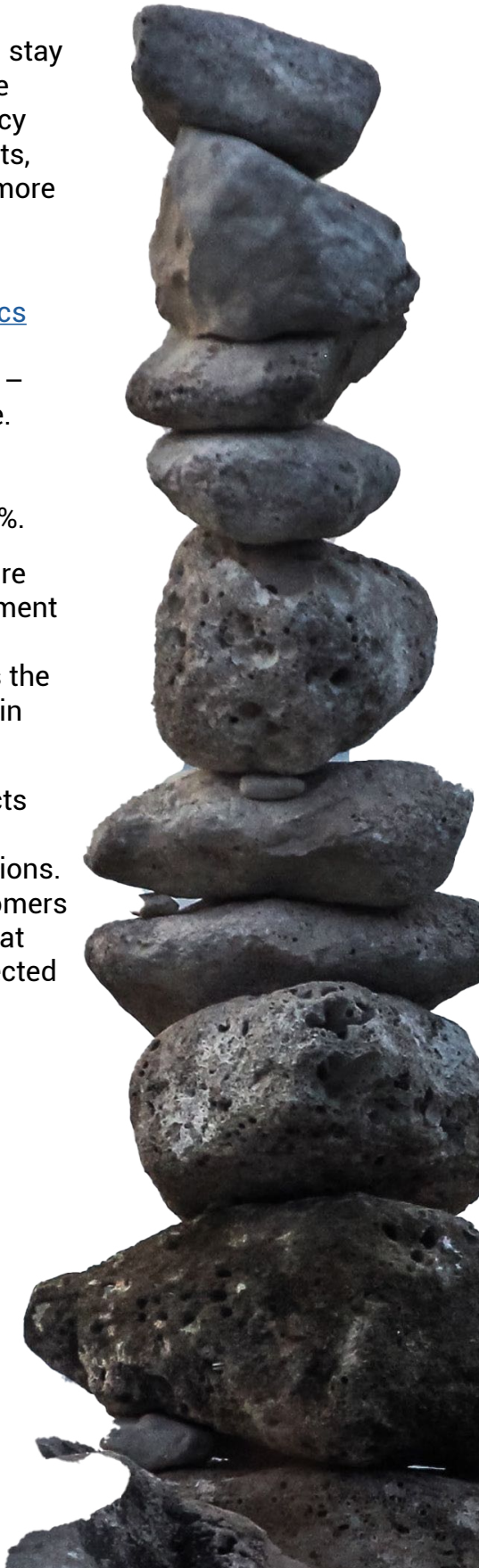
Since more energy-efficient servers would mean such upgrades could stay on hold for several years, translating into about 30% savings, using the company's preferred discount rate. In fact, since many energy efficiency techniques, such as virtualization, also reduce floor space requirements, there is also significant additional value in avoiding the need to build more – very expensive – data center space.

The sustainability aspects of risk have recently become more visible, after flying below the radar for decades. The advent of climate forensics and the increasing number of lawsuits (recently topping 1,500, and climbing) for changing the climate – and perhaps hiding climate risks – have made some sustainability-related risks dramatically more visible. But others, such as supply chain risks, are still largely submerged. For one manufacturer with thousands of Asian suppliers, supply chain responsibility actions lowered labor risks, resulting in an ROI over 100%.

Employee-related benefits can be either visible or submerged. Some are apparent – though rarely quantified financially – such as the improvement in recruitment and retention that occurs when employees feel their company reflects their values. And some are fully submerged, such as the changes in the way employees speak to customers and the reduction in errors they make.

Studies have shown that the way employees relate to customers affects client satisfaction and loyalty, which means the changes in employee behavior due to sustainability can have significant financial repercussions. At one $100 billion company, we found that employees talked to customers differently when they were part of a corporate responsibility initiative; at another multi-billion-dollar firm, we quantified how such changes affected customer satisfaction and buying behavior.

If you're starting to get the sense that submerged value can really add up, you're right. On average, we find the submerged value of sustainability initiatives is between four and ten times as much as the visible value. And it can be more.



A conversation I had with the head of CSR at one 50,000-person corporation illustrates the difference it makes when the real value of sustainability – including submerged value – is fully explored and quantified. I asked her how much talent-related financial value – attraction, retention, engagement, etc. – she thought the company's CSR programs created.

The most common response, by far, to this question is: "No idea. I'm not even sure how to answer that question." To her credit, this exec didn't throw up her hands and say, "I don't know." Instead, she estimated the value at about $3 million per year while making it clear the company's C-Suite would value it at perhaps $300K, just ten percent of her own appraisal.

Using very conservative assumptions (our standard practice) we quantified the value they knew was present but hadn't quantified – such as improved recruitment – as well as submerged value they hadn't seen at all. In both cases these things were assigned no value since people simply leave out any element they're not sure how to quantify. As MIT Professor John Sterman says, however, this is a mistake: when you don't value something you know matters, you're giving it the only value it **can't possibly have:** zero.

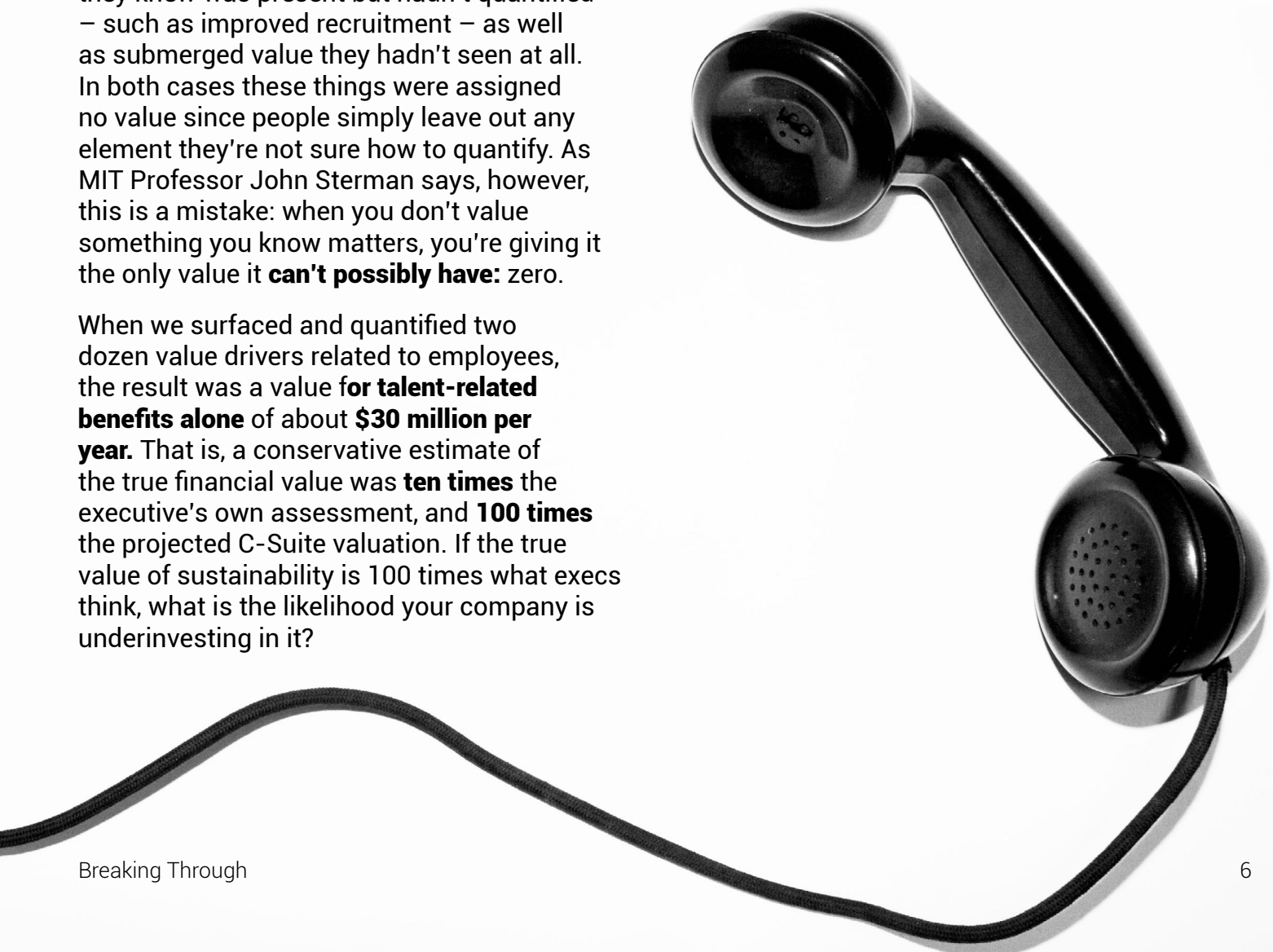
When we surfaced and quantified two dozen value drivers related to employees, the result was a value f**or talent-related benefits alone** of about **$30 million per year.** That is, a conservative estimate of the true financial value was **ten times** the executive's own assessment, and **100 times** the projected C-Suite valuation. If the true value of sustainability is 100 times what execs think, what is the likelihood your company is underinvesting in it?

The Third Wall: Communicating Value Credibly

Begin with the Audiences

It's difficult to identify, surface, and quantify submerged value. It's also not enough. Unless the value is credibly communicated, and **believed,** nothing changes.

Although this is the third wall, dealing with one critical piece of it should be among the first actions you take: you need to identify and analyze the key audiences of the business case exercise. **Begin with the audiences** and make sure they are reflected in everything you do.



At Valutus, we call this process AIM – Audiences, Information, Metrics – and it lays the groundwork for everything that follows.

- Who are the key audiences?
- What information do they have, and what do they need to find the results credible?
- What metrics do they focus on?

You don't have to do it the way we do, and you don't have to use the same questions. But you need to address the same issues. You don't want to get to the end of the effort, having worked hard to surface and quantify the key elements of value, and then have people disbelieve the result.

Explore the Results Together

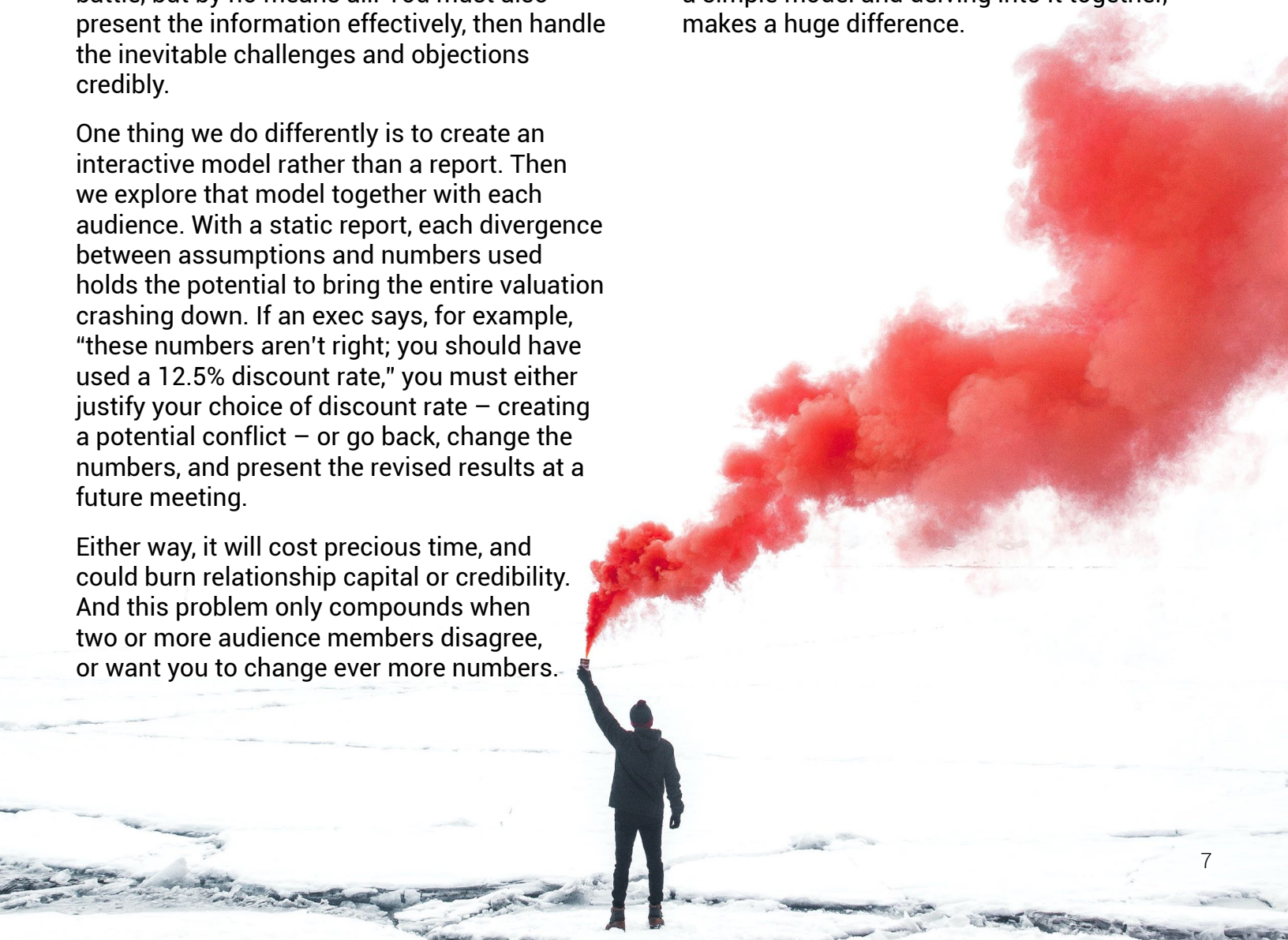
Getting the audiences right is most of the battle, but by no means all. You must also present the information effectively, then handle the inevitable challenges and objections credibly.

One thing we do differently is to create an interactive model rather than a report. Then we explore that model together with each audience. With a static report, each divergence between assumptions and numbers used holds the potential to bring the entire valuation crashing down. If an exec says, for example, "these numbers aren't right; you should have used a 12.5% discount rate," you must either justify your choice of discount rate – creating a potential conflict – or go back, change the numbers, and present the revised results at a future meeting.

Either way, it will cost precious time, and could burn relationship capital or credibility. And this problem only compounds when two or more audience members disagree, or want you to change ever more numbers.

If instead you are exploring an interactive model together you can say, "sure, let's change the discount rate to 12.5% right now, and see the difference." That shifts your relationship from adversarial positions on opposite sides of the table to a collaborative exchange wherein you're discovering and learning together.

This can be difficult – we've spent over half a decade building the web-based model we call InVEST™ (Interactive Valuation of Environmental and Social Transformation) – so that we can respond to the needs and thought patterns of various types of audiences, such as operations versus finance execs. But even without the time or expertise to build such a sophisticated, detailed model, you can still reap great benefit from a relatively simple one. The simple act of creating even a simple model and delving into it together, makes a huge difference.



Challenges and Objections

Interactive models are also useful for addressing objections around precision. Sometimes an audience member will say, “how do you know that the correct number is 10.5% and not 11.1% or 9.7%? If your number is wrong, it throws off your entire calculation, and we can't trust your result."

With an interactive approach, managing this is simple. First, change the number and together observe what happens. Does it make a significant or negligible difference in the result?

Second, re-focus on the **decision being made** rather than the precise **number.** Even if changing the figure makes a significant difference in final value, it may not matter to the decision. If the question is: “should the company invest more in its sustainability program or in communicating its values to customers?" then the difference between ROI of 112% or 134%, though significant, probably shouldn't impact the decision to invest. If the company's hurdle rate is 15%, then it makes sense to make the investment either way.

Many people have found this reframing – focusing on the decision rather than the exact number – very helpful, and I believe you will too. No model, regardless of how sophisticated, can fully capture everything that goes into creating the final return. This is true of any area with significant uncertainty – new products not only rarely pan out exactly as projected, up to 95% of them fail. But it's especially true for sustainability given its more difficult challenges and shorter track record than other areas of business. (I have been valuing sustainability for a quarter century, much longer than most in the field; yet that's a fraction of the 100+ years of valuation history in other areas of business.)

Moving Forward

The business case for sustainability matters. It's not the only thing that matters – there's real power in deciding to do the right thing **because** it's the right thing, and we should tell people that's why we want to do it.

Yet all too often companies desire to be more sustainable but believe they can't afford it. That's why you shouldn't neglect to mention that doing the right thing brings business benefits too.

The truth is that you **can** afford to be more sustainable. The fact is that, when submerged value is included, sustainability is a powerful driver of financial and business value. It's also becoming an increasingly powerful force, not just to customers, investors, governments, employees, and other stakeholders, but to the world at large.

When we looked at dozens of assessments of the top megatrends driving this decade (90% from businesses, governments, and other organizations that **don't** focus on sustainability), the **number one issue** across all of them was the climate crisis – and several other sustainability issues made the top 10. Soon, any company aspiring to be a top performer will need to be more sustainable: it won't be affordable **not to** be.