Sustainability and its impact on brand value

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by Paula Oliveira and Andrea Sullivan

One of the latest buzz words found in management journals, websites, and corporate documents is "sustainability." Some people even want to recognize it in a company's balance sheet as an asset. Okay, let's not go that far.

It is undeniable that sustainability is a new way of doing business, in the same way "re-engineering" or "just in time" were in the late 1980s. Sustainability is not an asset that can be bought or sold, rather it's becoming an integral part of many a company's philosophy. Just as company management practices influence business value, so do sustainability initiatives. Therefore, the question is: How does it create value?

Moral motivations to invest in sustainability are not in dispute: climate change, poverty, you name it. But what companies don't know yet is what level of investment they should make and what is the measurable benefit of investing. When the benefit is not clear enough to justify investments on economical grounds, managers easily turn to initiatives that guarantee short-term results and everyone's jobs, especially with recession knocking on the door.

There are some direct benefits, such as: compliance with an increasingly rigorous legislation; cost savings derived from optimization of production lines and supply chains to reduce energy consumption; reduction in CO_2 emissions; desire for more ethical products; and simply satisfying an emerging and cynical green consumer. But most importantly, incorporating sustainability as a business practice will not only increase companies' brand value, but guarantee a long life for the business.

Relationship between sustainability and brand value

Although it's hard to find consistency among definitions of sustainability it is common sense that it incorporates companies' relationships with the natural environment, social causes, and corporate governance. In boardrooms, this translates to the "triple bottom line," i.e., a company's initiatives must consider environmental, social, and financial impacts. Yes, financial impacts. That means companies must make investment decisions that will benefit the environment and society, and guarantee the sustainability of the project itself. We are not talking about charitable causes – but ethical products and services that will change consumers' behavior and help them to live a more "sustainable" life.

Brands enter the debate right about here. A leading brand translates to customers what is relevant in today's world, influencing buying behavior. It also develops a strong relationship with customers because of its distinct offerings, leading to repeated purchasing. In other words, a brand creates value in two ways: generating demand, and reducing risk and securing future earnings for the business. A sustainability program that is consistent with a brand's positioning will create value for companies by creating more value for its brands.

Generating demand for products and services

A study from Carbon Trust, a UK-based consultancy that helps businesses to reduce their carbon emissions, shows that social and environmental concerns can result in changes in consumer behavior. Among several factors that provoke this shift are "issues of immediate personal impact" and "realistic available choices." That's where brands can make a difference.

Let's take a sector for which sustainability is a big issue: automotive. Companies such as Honda recognized that mineral fuels are limited and prices of petroleum are rising. This motivated it to adapt its product range to fuel-efficient cars. Honda was one of the first movers in this direction and this is paying dividends today. It was the only car manufacturer to report better US sales in June 2008 than in June 2007, credited to fuel-efficient Civics and Fits. While reducing dependence of gas-guzzling cars and increasing the number of fuel efficient models became a "must do" in the automotive sector, Honda was first to differentiate and is ahead of the debate. This leading behavior contributed to an increase of 28 percent in Honda's brand value since 2004.

The same can be said about GE, which saw an increase in its brand value by more than US$ six billion since 2005, when Ecomagination was launched by then-CEO, Jeffrey Immelt. Among other goals, the program intended to increase spending on clean technologies, reduce greenhouse gas emissions, and generate US$ 20 billion in revenue from green products, including jet engines, locomotives, and wind turbines. This created a halo effect around other offers,

Figure 1 — Sustainability matrix, examples

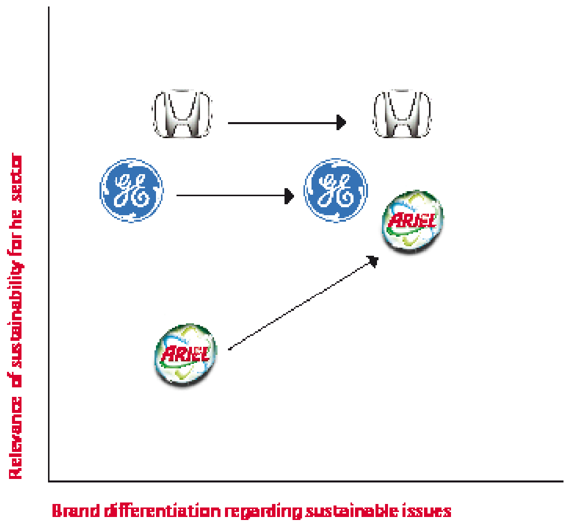
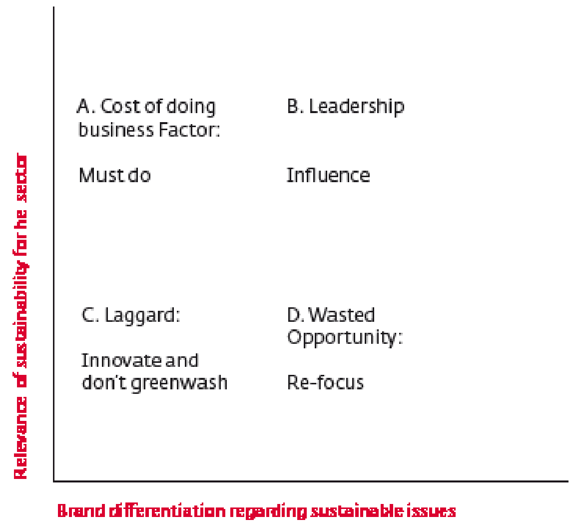


Figure 2 — Sustainability matrix, action points



improving perceptions about the company and making it top of mind in sustainability surveys. It moved ahead of competitors, such as Siemens and Phillips, which also have strong commitments to such initiatives. But GE led the debate and it is collecting the laurels – in the form of dividends – today.

P&G is another example, but in a different way. A few years ago, sustainability was not a relevant issue in the washing powder or detergent category. Through investments in R&D, P&G developed Tide Coldwater, which does not require hot water for usage and, as it is more concentrated, allows reduced packaging materials. Another example, also from P&G, is Ariel's "Turn to 30°" campaign. The campaign suggests consumers turn water temperature in washing machines from 40° to 30° when using Ariel with the same results guaranteed. These developments are beneficial for the customer, who can save energy from water heating. They are also beneficial for P&G, through revenues and positive opinion about both brands. P&G made sustainability relevant in an unexploited category and is now influencing consumer behavior – not only toward its brands, but toward a new and more "sustainable" way of washing clothes. P&G has similar initiatives in other product lines to save energy and replace chemicals with more suitable alternatives.

The first step in developing a "sustainable" strategy is to identify the relevance of the issue for the sector.

Honda and GE play in sectors in which sustainability is already a concern. Through portfolio management and innovation, they are now ahead of the sustainability debate and are influencing demand for their products and services. P&G went even further, raising awareness of sustainability issues in a category apparently unrelated. *See Figure 1*.

These examples suggest that the first step in developing a "sustainable" strategy is to identify the relevance of the issue for the sector and how differentiated the brand is regarding sustainability issues. *See Figure 2*.
Ann Hand, former SVP, Global Brand & Innovation at BP adds, "Brands need to have a point of view on the elements of sustainability that are relevant to their brand... they can't solve it all. For BP it's about a lower carbon world: alternative energy sources and lower emissions from traditional fuels. It also requires a clear, hard, baseline of where your firm is today; and commitment from the top in the CEO's agenda, backed with investment dollars that won't get cut off in six or twelve months if earnings slip."

For sectors such as energy and mining (*Figure 2A*), there is a massive impact on the environment and communities. As such, investments in sustainable initiatives are a "must do." But there is also an opportunity for differentiation. The same applies for automotive and diversified sectors. If the brand is perceived as differentiated, but sustainability is not relevant to the sector yet (*Figure 2C and 2D*), there is an opportunity to develop innovative products and services that will raise awareness and relevance of sustainability for the category (like P&G). The prize is not only leading the category, but positively influencing consumer behavior.

For brands that are not differentiated, and do not play in sectors in which sustainability is relevant (*Figure 2C*), there is an enormous risk of greenwashing, i.e., trying to differentiate through communication but not investing in sustainable development. A study published by TerraChoice, an environmental marketing firm, showed that 99 percent of 1,018 consumer products surveyed were guilty of greenwashing. These companies risk not only their reputation, but also future earnings for the business.

Reducing risk and securing future earnings for the business

Brands create value by generating demand and securing future earnings for the business. So how can investments in sustainability influence those future earnings and brand value?

A company's value is today's value of the earnings it will potentially generate in the future. It's a function of the magnitude of those earnings and the risk associated with them. Therefore, sustainability is strongly related to value: the more a company proves to the financial markets and other audiences that it is a sustainable business, the lower the risk associated with that company (and the lower the rate used to discount future earnings).

Similarly, brand value is today's value of the earnings a particular brand will generate in the future. Brand risk is a function of company's risk, adjusted by the strength of particular brands. This depends on many factors including the investments it receives (quantity and quality), brand image (brand's perceived personality and reputation) and customer franchise (relationship with customers).

Coca-Cola is the most valuable brand in the world. It consistently invests in its main brand and develops an emotional connection with consumers. So why did its brand value decline US$ 5.1 billion between 2003 and 2007?

Coca-Cola's decline is due to the fact that it is seen as one of the bad guys by many organizations. Increasing health concerns have been affecting brand earnings in developed markets, despite its light, diet and zero versions. Also, its image and reputation have been inconsistent around the world. On the upside, Coca-Cola has been investing in many initiatives, such as campaigns to improve community access to safe drinking water and adequate sanitation in India.
Is this only a form of CSR to boost the company's reputation after protests were held in the area? No. Investment in water supply in India is not only relevant to the population, but also to the sustainability of the business in the country. After all, how would Coca-Cola produce soft drinks without water? This and other initiatives positively influenced the company's share value at the end of 2007 and its brand value increased by two percent in 2008.

The same applies to oil and mining groups, both heavy users of natural resources. BP had been increasing its brand value since 1999 mainly due to its large investments in safety and renewable energy. However, its reputation suffered after an accident at a Texas City refinery in 2005, with shares dropping almost 10 percent in a month. The company's reputation has recovered, but the incident demonstrated the strong correlation between sustainable actions and value creation.

This correlation is also seen in the Best Global Brands 2008 ranking. Financial services institutions included in the 2007 and 2008 studies lost a total of US $10 billion in brand value. This reflects not only the financial impact from the US credit crunch but also the reputational damage caused by breach of trust between these companies and the investment community.

"The changing landscape of liability," a report published by the consultancy SustainAbility, suggests a rapid convergence between companies' risk management and sustainable development programs, as technical compliance "may no longer be an adequate defense against social and environment activists in the court of public opinion and even in the courts of law." This leads to a much more rigorous approach to risk assessment or, at best, an opportunity to develop winning strategies from multiple stakeholders' points of view – an opportunity that can help secure future earnings and the sustainability of the business in the long term.

Brands have the power to change the world

Sustainability is not a fad – it's a new way of doing business. We can determine the influence this business practice has on the overall business and brands, but there is no standard solution. Companies need to assess the relevance of sustainable issues to their business, as well as current perceptions about their brands on this matter, the potential upsides of investing in sustainability projects, and the reputational risk of not doing so. Brand value is a way to summarize all of this.

Most leading companies already understand of how sustainability issues can affect their businesses. The challenge is to embed a real sustainable behavior in everything a company does; not only to attract new customers, but to help define future behavior and shape the market. In other words, to be a leader. "The transformational challenge is to make "green" a part of the DNA of the enterprise, just the way companies had to make globalization and digital technology a part of nearly every business consideration," says Andrew L. Shapiro, founder and CEO of GreenOrder, a business strategy and management consulting firm that specializes in the field.

Brands can be the engine towards a more sustainable world. They should be ahead of the market and create products and services that will be relevant to consumers while, at the same time, helping them to live in a more sustainable manner. This will create a positive influence on the environment and communities, as well as generate dividends to shareholders through growing demand. A sustainable brand will also enhance a company's reputation and secure future earnings through stakeholder loyalty and advocacy, thus increasing brand value.

As the saying goes, "today's best practice is the best practice of tomorrow." Hopefully, today's successful sustainability strategies will soon become standard, promoting long-term benefits for businesses and generations to come. ■

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