# CORPORATE INTERNALIZATION OF SUSTAINABILITY REQUIREMENTS

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## CONCLUSIONS

**Sustainability has become the boiling point of theoretical business discussions. At first it was only a concept everybody was talking about but no one knew how it should be materialized. Now we can understand how and why companies are inclined to follow the principle. This gives the policy makers and other stakeholders the tools to alter market conditions in ways that more and more companies accept the requirements of sustainability. Several levels of sustainability have been identified and now the discussion is shifting towards achieving a common ground how to measure sustainability. Since sustainability is such a broad concept and it is very dependant on the factors of the given industry the analyzed company is operating in, two major ways to measure the companies' performance were identified:**

- **One way, which is propagated by Barrett, is to look at the values the company internalized.**
- **The other way is to try to define a commonly accepted framework of requirements and then apply this framework to measure the performance of the specific company.**

**The future will tell which method will be embraced but my bet is on the one which offers clear-cut, easy-to-understand, and easy-to-implement solutions to companies.**


## ABSTRACT

The world's troubles are increasing both in numbers and in extent. The majority of the globe's population lives in poverty and environmental disasters with droughts or floods follow one another while the overall population is increasing. The concept of sustainable development was created and accepted as an adequate tool to deal with these problems. It refers to a „development which meets the needs of the present without compromising the ability of future generations to meet their own needs." (*World Commission on Environment and Development, 1987, p. 54.*) However, this definition is too broad and evasive; it has to be broken down to the „to-do-level" of societal participants like consumers or companies. This paper will focus on the corporate perspective. We will look into the following questions

– What is the connection between sustainability and corporate activity?

– How could the concept of sustainability be internalized into corporate values?

– Why and when are corporations strategically motivated to adopt a socially important but, at first sight, economically not feasible value?

## INTRODUCTION

At the moment we are experiencing a change in societal values. The problems in the world are getting more numerous, the majority of the globe's population lives in poverty, there are more and more environmental catastrophes like drought, floods, hurricanes while the population is increasing and this increased population has to be catered for under worsening environmental circumstances. The discontent of the masses and their exclusion from the resources of the world cry out for a solution. Sustainable development which stands for meeting the needs of the present without compromising the ability of future generations to meet their own needs, was accepted commonly by the policymakers and scientists. In order to achieve sustainability, the issues should be looked upon in a holistic way, i.e. from the economic, environmental, and social points of view, also known as the triple bottom line. The concept of sustainability is a global and evasive notion about issues which should be addressed with down to earth and concrete solutions. That is why it is necessary to look at what has to be done by the different actors of society in everyday life. The corporate aspect is analyzed below because as data shows most of the earth's pollution is caused by the activities of the corporations. Their trade and industrial strategies drive globalization which is the main reason behind social and environmental troubles. If we understand corporate behavior, we can also find a way to tackle the majority of sustainability issues.

## INTERNALIZATION OF THE SUSTAINABILITY CONCEPT INTO CORPORATE VALUES

Corporations do not exist in a vacuum, they are part of a broader social setting and this social scene influences their operations. The environment of a company can be broken up into several groups, into the so called stakeholders. These stakeholders relay their values, that is what is desirable in their view, to the given company. There are three main groups of stakeholders:

1. *Market-related (primary) stakeholders:* this is the group of stakeholders which is the most directly in contact with the company and has the shortest influential route and the biggest influence. The following actors belong to the stakeholders of the market:

- Financial institutions, investors: they want to have a high return on investment. They value the sustainability of corporations as a means to avoid capital loss - caused by high state imposed penalties or lost turnover resulting from public boycott.
- Customers: they want to purchase goods which fulfill their needs whether functional or emotional such as feeling good about their purchase decision, or feeling accepted by the opinion leaders around them. They might avoid buying products that are not made according to the sustainability principle because these products might not satisfy their emotional needs.
- Competitors: through their better adaptation to sustainability requirements of a certain consumer group, competitors might gain a considerable advantage over a company which lags behind in meeting sustainability requirements.
- Suppliers: through the products or services they deliver they influence the companies' accordance with sustainability requirements as it is their services or products the company builds on. Companies might experience problems in terms of their image if they partner up with a supplier which lacks conformity with sustainability.
- Partners: they can decide not to partner up with a company whose lack of accordance with sustainability principles might risk damaging their reputation.

2. *Political (secondary) stakeholders* constitute the second group and they influence primarily the market, rather than single corporations. Among these one can find:

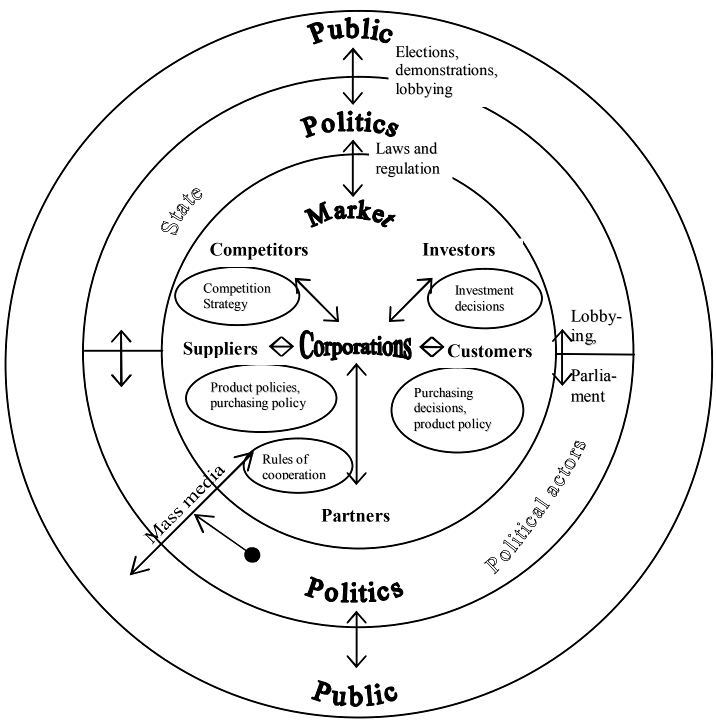
- Government: that passes sustainability driven laws and impose penalties on companies which do not adhere to them.
- Non-governmental organizations, public interest groups: some of these devote their activities to promote sustainability and to achieve their goals they organize demonstrations, mass media campaigns, boycotts against those businesses which fail or refuse to address the sustainability issue.

3. Finally, the third (*tertiary*) stakeholder group is the *public*. It consists of the same people customers or non-governmental organizations do but in this category they are considered in their other role as voters and facilitators of politics. They express their opinions through their political decisions which can convince governments (states) to pass laws that influence companies' environmental or societal behavior.

The interactions between the company and the stakeholders are not one way but rather reciprocal. Companies influence and transmit their internal values towards the stakeholders, too. This is especially visible when companies shape public values, instead of waiting for public values to shape them. Below Figure 1. summarizes how and through which mechanism this value-transmission takes place.

**Figure 1**

**Stakeholder relations and value transmission**




*Source*: own depiction, (based on Fichter, 1998, cited by Bolli, 1999, p. 40)

Based on the figure two conclusions can be drawn:

1. Market is the most important influential factor. If a company does not fulfill market needs, it will not survive. The political group follows the market-related stakeholders in terms of influential power. The least influence is created by the public, as political actor. The reason behind this rather light influence of public is that first political stakeholders have to be convinced. The market conditions can only be changed afterwards.

2. Companies are not doing less or more than what their stakeholder environment influences them to do. If stakeholders force a company to meet sustainability, it will. If they do not force it, the company has to be an extreme visionary to want to anticipate stakeholders' requirements.

## THE BENEFITS OF ACTING IN ACCORDANCE WITH THE STAKEHOLDERS' VALUES

Companies are „selfish" and are following their own interests which are basically the interests of their owners/investors. Regarding interests pursued by companies, three types of businesses can be distinguished:

1. *Companies operating outside the model of market economy*: these are the businesses that were created to enhance and *serve a certain public aim*; they get their funding through subsidies and are less pressured by profitability issues.

2. *Companies which are on the borderline of market economy*: they are created for *furthering a value but are also driven by profitability issues*. The first bio-producers used to belong to this group. They were not competitive in the beginning. They targeted a niche market which was just big enough to provide for a small company's survival.

3. *Companies operating inside market economy*: they make their decisions based on feasibility; consider *profit* as their primary but not necessarily only aim.

In a lot of cases this classification indicates also a development route. First a company is created by the state as a pilot project and it is subsidized and nurtured. Then, if it proves to be a good idea, and the value the company stands for is accepted, new small businesses are created by private capital to promote that value. Finally, when public acceptance is high, the value is incorporated into the values of the majority of the stakeholders, it starts to spread and an increasing number of profit driven companies internalize it. We can experience this latter stage today in terms of sustainability. To be sustainable is starting to be feasible and not so visionary corporations begin to deal with the concept as well. In my view there is, however, nothing wrong with the selfishness of the companies because it is this selfishness that makes even profit driven companies want to follow sustainability requirements, as they can insure them some of the following benefits:

- Better financial performance: higher turnover, higher attraction of investment, less penalties, higher share price.
- Better competitiveness: if fulfilling sustainability requirements is a necessary minimum on a particular market, the business will not prevail without it. In some other markets competitiveness is rather an opportunity to grow or attract new customers.
- Better reputation: even if sustainability is not a necessary minimum, a corporation that is innovative enough to internalize this value and is able to get the word out will have a better reputation. Not to mention the contrary scenario when a lack of accordance can ruin the image of the company.

## WAYS OF BEING SUSTAINABLE

Since sustainability is still developing and because there are no commonly accepted and defined minimum performance indicators which would inform companies from which point onwards and how sustainable they are, there are several ways of being in accordance with the sustainability requirements. Dylick et al. (cited by *Bieker, 2003*) defined five strategies how companies approach sustainability.

- Strategy „*safe*”: primary aim of such a company is to reduce risks deriving from the financial, managerial or reputational sphere, in other words the non-accordance with sustainability might result in financial or reputational losses. These companies want to ensure that their images prevail and with these images their market shares are secured, too.
- Strategy „*credible*”: these businesses are focused on looking good. Credibility is one of the non-tangible assets; it ensures low conflicts with authorities and stakeholders. This strategy is often followed by corporations in industries where credibility is highly important, such as food, pharmaceutics, cosmetics, etc.
- Strategy „*efficient*”: it focuses on enhancing productivity and efficiency and, thereby, reducing cost and increasing cost competitiveness. Cost competitiveness means not only price competitiveness but product operating cost advantage as well. Strategy „efficient” is a wide spread strategy and is used for instance in the printing industry, in the white goods market, in the automobile sector, etc.
- Strategy „*innovative*”: it aims at differentiation of the company's products in the market by being a front runner and providing added value through sustainability to the customer. The strategy is very much dependant on finding the right innovation, an innovation, that answers customers' needs and can be communicated widely.
- Strategy „*transformative*”: it is trying to create new markets by changing needs, politics, and the institutions. This is a proactive strategy which incorporated a vision and requires a very long term focus from the companies, that is why this strategy is rather for big and innovative corporations than for smaller start-up firms.

The different strategies can also be understood as different levels. Strategy „safe” is the basic one. Strategy „credible” represents an already more active level. Strategy „efficient” is more developed and more innovative (within the company) than „credible”. Strategy „innovative” and „transformative” are proactive ones where „innovative” is dealing with existing value constellations while „transformative” tries to change values.

### Drivers of changes from one level to another

Changes in companies' values happen when any of the following three changes:

- The *environment* of the company changes – external change: the surrounding of the company is changing, the stakeholders convey a different desired behavior so the company is forced as well to change its behavior and values.
- Substantial *learning* takes place within the organization that changes commonly shared values – internal change: Environmental catastrophes caused by the company itself and resulting in huge losses can initiate such a learning process.
- The company gets into a *different stage of its life cycle* – automatic change.

With companies' growth priorities their competitive situation changes and this inflicts an automatic change in the behavior of companies.

A company changes from being safe to being credible when either its market changes, the organization learns newer ways of operation, or because it gets into a lifecycle stage where being more long-term focused gains importance.

## MEASURING THE INTERNALIZATION OF SUSTAINABILITY

In order to persuade companies to integrate sustainability into their business philosophy, they need models which tell them from which point on they have integrated sustainability principles so that they can see how to proceed to fully internalize the concept. Barrett's „Full Spectrum Sustainability" concept (*Barrett, 2001*) describes one of the ways to understand how sustainable a company is. It is a notion to measure corporate performance through values that are internalized and followed by the company. It takes account both of internal factors like organizational effectiveness, employee fulfillment, and customer satisfaction and external factors like social and environmental responsibility. The model originates in Maslow's theory of hierarchy of needs. Barrett consequently argues that not only human beings but also companies have a hierarchy of needs and only the most developed companies reach full spectrum sustainability. Barrett defined seven levels:

- Level 1: Survival − these companies are solely focused on survival; they do not care about anything else but doing the necessary minimum.
- Level 2: Relationship − these companies already try to develop strong relationships with employees, try to achieve employee and customer loyalty.
- Level 3: Self-Esteem − building on the previous levels these companies constantly try to improve productivity, quality and organizational effectiveness.
- Level 4: Transformation − besides fulfilling all previous levels, these businesses, constantly adapt their products to the changing market place. These organizations are focused on learning, knowledge management, and innovation.
- Level 5: Internal Cohesion − this corporations focus on aligning the employees with their vision and values.
- Level 6: Inclusion − the companies at this stage try to develop mutual and strategic alliance with partners and the local community.
- Level 7: Unity − these are the full spectrum organizations because they are good global citizens and through this they protect their long term interest.

Another way of measuring accordance with sustainability could be to define a commonly accepted framework of requirements. This framework can have statements like:

The company is operating on the basis of sustainability if

- it uses the best available technology in that industry and/or
- it invests a certain percentage of its profits into environmental research or social benefits to its employees.

After the definition of these requirements the performance of the given company can be analyzed.

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