Where's the Real Value?

Searching for environmental value that matters to executives

By Richard MacLean

In these tough economic times, environmental managers are struggling to prove that their efforts are adding value to their companies. It's a hot issue, but one that appears to be eliciting the "same-old, same-old" responses that focus on justifying individual projects and staff resources. This article explores techniques for identifying value — methods centered on models of business competition.

ADP, a provider of payroll and human resource administration services, ran an ad in *Fortune* last year that was as amusing as it was sobering. It contained a picture of an office worker fumbling while trying to make his own paper-clips. The caption read, "Make your own paper clips? No? So why would you do HR administration in-house?" The text went on to state, "Performing tasks that don't generate profits can get you bent out of shape."

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Human resources (HR) administration is necessary; it is important and there are regulations to follow, but is it strategic? I don't think so. Substitute "environmental" for HR and ask yourself the same question. Feeling uncomfortable or getting defensive? Environmental managers are not making paper clips, but some business executives view them as spending a lot of time on administrative (read staff overhead) tasks that add about as much value to the business as HR administration. You and I both know that there are many essential and strategic dimensions to environment management; do not assume your business executives have the same understanding.

This harsh reality was brought home to a corporate environmental manager when we conducted interviews of top executives to evaluate priorities and review her group's mission. As she later confessed, "I have been to the top and it is ugly!" Without a doubt, her business executives could eloquently communicate the company's devotion to sustainable development in front of an audience. Behind the scenes, they did not have even a rudimentary understanding of what was really going on and how her department added value beyond keeping the company in compliance.

"Not in my company!," you may be saying to yourself. Indeed, there are companies where the business executives have a good grasp of how environmental resources add value. But, unless you have directly explored this question with your executives, do not assume anything. Environmental managers rarely have frank, open discussions with business executives on this topic. When I ask for information on business management's understanding of specific issues, the environmental managers that I have worked with often do not have the answers (thus, the need for the revealing interviews as mentioned earlier).

Executive communication is typically focused on the crisis du jour, the project underway or the few standard (typically lagging) metrics that business managers track. The subject of "environmental value," if it does come up, is usually framed in the narrow context of justifying a specific new project by using standard costing techniques, such as those summarized in the Global Environmental Management Initiative (GEMI) report, *Environment: Value to Business*.[1] This may win the battle (i.e., project approval), but sheds little light on the war (i.e., how the environmental group adds value in a broader context).

Calls to reduce staff headcount inevitably trigger evaluations of the value added by the environmental group. Benchmarking is the favored technique, using a combination of industry sector (are we leaner than everyone else?) and outside service provider (do we cost less than consultants?) benchmarks. Both benchmarks offer little clarity on the real business value of environmental resources, only on the relative cost of services. Big difference.

Management will continue to wonder if it is getting the lowest cost paperclip (i.e., administrative service) and re-visit this question again and again. Environmental staffs almost always represent a small fraction of the total workforce. Even if the environmental manager can prove that internal resources are cost effective vs. outsourcing, business executives may see the difference as trivial in the grand scheme of things and not worth the hassle of keeping the resources in-house.

In-house environmental staffs (especially those that are fully integrated within shared service organizations) may have an increasingly difficult time justifying their existence; in the future, they will have to compete with external service providers who are moving to network internationally for the lowest cost technical support.[2]

What Value Can Be Brought to the Table?

The business textbook definition of "value creation" centers on the amount that buyers are willing to pay for a product or service. A business is profitable (and thus competitive) if the value it creates exceeds the cost of performing these "value activities."

Yes, saving some money by competitively performing tasks in-house will contribute value, but these cost savings may not be significant enough to justify the headcount for the reasons previously cited. There needs to be much more justification. Similarly, an environmental project may not go forward, even if it has a substantial positive return, if there are other business projects that have even greater returns.

The strategic value environmental matters can add to (or remove from) the table is related to four factors.

Environmental managers love to use the risk and liability angle to pump up their value (i.e., if there is a problem, the liabilities and bad press will be enormous!), but this approach is beginning to fall on deaf ears, just as the traditional "You will go to jail!" will more than likely alienate management today. The larger consulting firms have also been swaying business management over with contractual provisions to limit company liability or make good on any problems created by substandard service delivery.

The reality is that environmental staff resources can bring the full spectrum of value, from low-value mundane administrative tasks to high-value strategic positioning upon which the company's future may hinge. Asbestos, genetically altered foods, CFCs and so on serve as constant reminders of this fact.

Just how much strategic value environmental matters can add to (or remove from) the table is primarily related to four factors. Every company has its own unique profile. First, where does the company sit in the supply chain? Resource companies (at the very beginning of the chain) and companies interfacing with the consumers (at the end of the chain) typically have the greatest potential for environmental value creation or loss.

Second, what is the company size? Large, deep-pocket companies are more likely to reap environmental value creation or loss. Third, what are the legacy issues and the environmental footprint? Companies with significant exposure face the greatest strategic value challenges. Finally, what is the brand image of the company? Companies making pharmaceuticals are typically far more concerned about their environmental image than a company making widgets for the military.

So, how do you map the location of your company along these value dimensions for your business executives? Volumes have been written on how to identify environmental value, but much of it has been authored by environmental health and safety (EHS) specialists instead of well-known business leaders and researchers. Often steeped in environmental buzzwords, these methods of identifying and quantifying environmental value may be suspected as being biased and immediately dismissed by business executives.

Changing the Perception of Environmental Value

The essential first task is to differentiate, for business management, the distinction between environmental administrative services and those activities that have the potential for high value. In the minds of many business executives, the activities that the environmental groups perform have been co-mingled into one category, namely services. Just as executives do not look toward HR administration for the future competitive success of the company, executives may believe that environmental issues are strictly an administrative cost of doing business.

How does one go about changing this perception? Although it is worthwhile to review published environmental resources for possible ideas, environmental managers should rely on methodologies that are familiar to their executives. Since adding value is all about improving a company's competitive position (beyond just providing the lowest cost services), start with business models of profitability and competitive forces and work backwards. The writings by Michael Porter, professor of business administration at Harvard Business School, are particularly good.[3]

The objective is to identify the key areas that represent competitive advantage for your company, based on emerging dynamics (both business and environmental) and your company's strategic business plan. For example, **Table 1** contains a list of potential areas where companies may identify their competitive advantages. This list was adapted from Michael Porter's work. Similar lists exist in environmental writings but, again you are much better off using business sources. Similarly, refer to these business references to turn the list in **Table 1** into possible candidates for further evaluation.

Identifying possibilities is relatively easy. Translating these into something that has the power to shift management thinking on environmental value is much more difficult. In the past, significant environmental value was associated with reducing the cost impact of multi-million dollar pollution control infrastructures required by emerging regulations. While this could easily be translated into dollars and cents, it reinforced the narrow view that environmental value was regulatory driven.

Today, the most significant potential environmental value is related to the strategic use of resources, both human (the essence of social responsibility) and material (at the heart of sustainable development). Environmental specialists have been talking about this shift for more than a decade, but with little impact. Within the past few years, there are growing signs that some traditional "business types" are beginning to take note.

For example, Sharon Begley, science journal editor of the *Wall Street Journal,* ran an article discussing the dynamics of global warming, what that means to the Gulf Stream and how business and the military may respond.[4] This is in direct contrast with a decade of *Wall Street Journal* editorials espousing how environmental issues are overblown. The message until now has been "Things are fine, indeed improving and in spite of what the alarmists say, there is little real concern to the public."

Table 1. Areas of Competitor Strengths and Weaknesses**

Products
- Standing of products, from the user's point of view
- Breadth and depth of the product line

Dealer/Distribution
- Supply chain coverage and quality
- Strength of supply chain relationships
- Ability to service the supply chain

Marketing and Selling
- Skills in each aspect of the marketing mix
- Skills in market research and new product development

Operations
- Manufacturing cost position
- Technological sophistication of facilities and equipment
- Flexibility of facilities and equipment
- Proprietary know-how and unique patent or cost advantages
- Skills in capacity addition, quality control, tooling, etc.
- Location, including labor and transportation costs
- Labor force climate; unionization situation
- Access to and cost of raw materials
- Degree of vertical integration

Research and Engineering
- In-house capability in the research and development process
- Access to outside sources of research and engineering

Overall Costs
- Overall relative costs
- Shared costs or activities with other business units
- Where the competitor is generating the scale or other factors

Financial Strength
- Short- and long-term borrowing capacity (relative debt/equity ratio)
- New equity capacity over the foreseeable future
- Financial management ability, including negotiation, raising capital

Corporate Portfolio
- Ability of corporation to support planned changes
- Ability of corporation to supplement or reinforce business unit strengths

Other
- Special treatment by or access to government bodies
- Personnel turnover

** Adapted from Michael Porter, *Competitive Strategy — Techniques for Analyzing Industries and Competitors,* The Free Press, 1980, Pages 64-65.

Focus on the broader concepts of what environmental resources can bring to the company.

There is a recent ground swell in material that can be used by environmental managers to position their staffs to demonstrate added value. Much of this is found in unfamiliar resources not tracked by environmental managers. For example, there is emerging information by researchers, such as Marc Epstein at Rice University's Jones Graduate School of Management; investigations by The Conference Board; studies by Ernst & Young and the Center for Business Innovation; research by Innovest Strategic Value Advisors; emerging research on intangible assets by McKinsey; and so on.

Identifying and interpreting this material should receive high priority, more so than dealing with the (comfortable) crisis of the moment. Changing management's perception of environmental value offers the greatest chance to break free from the current situation of endlessly trying to preserve staff resources.

Conclusions

The chief financial officer (CFO) and the HR director that oversee organizations have mundane (but important) administrative duties, as well as strategic functions. To boards and the CEOs, there is no confusion over the separation of the important stuff from the strategic stuff that these individuals manage. No such clear distinction exists, however, with environmental managers in most companies.

In many respects it is our own fault, because we have historically touted everything we do as important, as we breathlessly declare the disastrous consequences of even a minor error on some waste manifest. Listening to this over the years, management has indeed decided that everything is important (just as HR administration is important), but very little is of competitive value. It is time to change this approach and, to quote the old cliché, become more business-like.

Don't try to justify the current state; push for a new state and a new understanding of what the environmental group does (or should be doing). Focus on the broader concepts of what environmental resources can bring to the company, based on emerging business research. Evaluate each of the current environmental activities in light of how these enhance profitability and competitive position. If an activity does nothing more than accomplish a required administrative task, ask yourself the "paperclip question" that appeared in the opening paragraph of this article. Consider getting rid of all these "important" but non-strategic activities and shift resources to value-added activities. EP

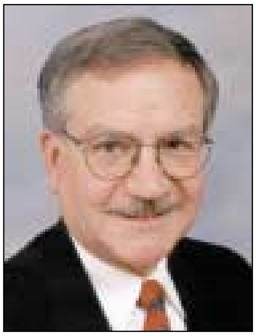
References

1 GEMI, Global Environmental Management Initiative, Environment: Value to Business, 1998, *www.gemi.org.*

2 For a discussion of this emerging dynamic, see R. MacLean, "Sustainable Careers — Preserving Your Career Options While Protecting the Environment," *Environmental Protection,* January/February 2003, Pages 14-15.

3 Three of the best by Michael Porter are *Competitive Strategy — Techniques for Analyzing Industries and Competitors* (Free Press, 1998), *Competitive Advantage — Creating and Sustaining Superior Performance* (Free Press, 1998) and *On Competition* (Harvard Business School Press, 1998).

4 Sharon Begley, "Global Warming Means a Possible Big Chill for Northern Regions," *Wall Street Journal,* March 7, 2003, Page B1.



Richard MacLean is president of Competitive Environment Inc., a management consulting firm established in 1995 in Scottsdale, Ariz.; a principal at Independent Perspectives, a virtual consulting network supporting business management; and the executive director of the Center for Environmental Innovation (CEI), a university-based nonprofit research organization. He can be reached via e-mail at maclean@competitive-e.com.

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