C E

Center for
Effective
Organizations

Sustainability Initiatives are Not the Answer – A Management Reset is Needed

CEO Publication
G 11-04 (592)

Edward E. Lawler III

Director

Center for Effective Organizations

University of Southern California

Christopher Worley

Senior Research Scientist

Center for Effective Organizations

University of Southern California

July 2011

Center for Effective Organizations - Marshall School of Business - University of Southern California
Los Angeles CA 90089–0871 (213) 740-9814 Fax (213) 740-4354 http://ceo.usc.edu

Sustainability Initiatives are Not the Answer- A Management Reset is Needed

Edward E. Lawler III and Christopher Worley
Center for Effective Organizations
Marshall School of Business
University of Southern California

Sustainability has become a major issue for most organizations. Large corporations are under the most pressure. They are very much aware that they cannot continue to ignore their impact on the environment, the people they employ, and the societies they operate in. A recent global survey of CEOs found that 96% believe sustainability issues are critical to the future success of their firms. Sustainability's increasing importance has led to discussions in the board rooms of most major corporations about the programs and initiatives that are intended to reduce environmental or social harm or increase environmental and social health. However, they have not led to organizations that are designed and managed to perform well financially, socially and environmentally, that is to achieve sustainable effective organizations.

The world has changed its opinion concerning what corporations should be held accountable for and how they should be expected to perform. Successful financial performance is required of corporations, but it is not enough in the eyes of more and more individuals, governments, and societies. They believe that corporations must do more than produce satisfactory financial results; they must also have a positive impact on people and the environment.

At this point, most corporations have one or more sustainability initiatives as well as multiple social responsibility programs. Most sustainability initiatives focus on the environmental impact of business operations, including travel reductions, more environmentally sensitive product packaging and reducing the amount of energy products utilized once they are in the hands of customers. In many cases, these sustainability programs are win/win efforts: they have a positive environmental impact and they contribute to the financial performance of the corporation.

But what about sustainability and social initiatives that don't have a positive impact on the bottom line? More importantly, what about the ability of corporations to develop a comprehensive long term capability to operate with a triple bottom line commitment?

Failure of Change Efforts

A great deal of research on organizational change efforts and initiatives shows that they are often briefly successful, but quickly lose their effectiveness and disappear. This is particularly true when they require behaviors that are not supported by the management approach of the organization. The list of temporarily interesting and successful change initiatives that have been abandoned because they are counter to the management style of organizations is long.

Remember reengineering, quality circles, total quality management, and suggestion systems? All of these programs focused on improving an important element of an organization's performance, but lost their impact after an initial period of excitement and support. They never became part of the standard operating procedure of most organizations in large part because they required an organization to engage in unnatural acts, i.e. to behave in ways that were not supported by the management approach of most organizations.

Estimates of the failure rate of organizational change efforts range from 60 to 80 percent. In our view there is no reason to believe that today's sustainability and corporate social responsibility initiatives are doing or will do any better. The one exception may be those sustainability initiatives that have a clear and direct impact on the bottom line of corporations. They have a much higher probability of survival because they are clearly aligned with primary organizing and operating values of most corporations: maximizing financial results. This is hardly a new thought - Milton Friedman long ago argued that indeed these are the only type of initiatives that corporations should undertake. But, having a successful sustainability initiative is not the same thing as having an organization that is sustainable effective.

Sustainability initiatives and corporate social responsibility programs are a possible first step toward developing organizations that are able to perform well financially, socially, and environmentally, what we like to call sustainable effectiveness. However, organizations to survive in a global economy that demands high levels of financial, social, and environmental performance, it is not enough to simply launch a series of sustainability initiatives and social responsibility programs. Organizations must develop a comprehensive approach to management that fully integrates sustainable effectiveness into their strategy and operations.

The management approaches used by most corporations today fail to do what is required in order to achieve sustainable effectiveness. They were designed to operate in a relatively stable environment that holds most corporations responsible for primarily their financial performance. Both of these conditions no longer exist. We live in a world of increasingly rapid change and a world that requires organizations to perform in ways that go beyond simply generating a high return for their shareholders.

Many organizations are launching programs that focus on innovation, agility, and sustainability in the hope they will enable them to perform well in today's global environment. But, and it is a big but, there is little reason to believe that most organizations can perform adequately in a rapidly changing world that requires sustainable effectiveness even if they launch the right initiatives. All too often organizational change initiatives are too superficial; the change equivalent to putting "lipstick on a pig."

What is Needed

Fundamental change in how organizations are managed is needed in order for them to be sustainable effective. Traditional command and control hierarchical structures need to be abandoned and a new approach to management adopted that starts at the top of the corporation and changes how it operates from top to bottom. An approach to management is emerging that does just this. While the details are still being developed, some corporations, including DaVita and Patagonia, already are practicing a management approach that has many of the characteristics needed to create sustainable effectiveness in a rapidly changing world. Let's look at the key features of this management approach.

Defining a Value Creation Identity

Creating an identity - an integration of the organization's culture and brand/image/reputation - that pursues and creates three kinds of value is an important feature of the sustainable approach of management. Accomplishing it requires aligning the major features of an organization, its strategy, structure, leadership, governance, etc. with this identity.

Following the traditional principles of “maximizing shareholder wealth,” most organizations have identities oriented around the singular goal of profitability. Identities that embrace financial, social and environmental value creation reject that singular focus. They see balancing the three kinds of value they create as a core part of who they are. Their sustainability initiatives and corporate social responsibility programs are “in addition to” rather than central to their core identity and lead to decisions that integrate and/or balance profits, social outcomes, and environmental health. All too often, financial value creation simply trumps sustainability and social responsibility and the tough tradeoffs that need to be made are not made.

Nokia and Unilever are two organizations that have created identities – brands and cultures - that are concerned about balance. Their identities are manifest in terms of a portfolio of products that are financially successful, environmentally friendly, and socially beneficial. They don’t emphasize efforts to produce a particular “sustainable” product. Instead, and because sustainable effectiveness is rooted in their identities, they talk about creating a portfolio of products that are financially successful, environmentally friendly, and socially beneficial.

In sustainable organizations, decisions cannot be made that always favor any one of the three types of value they are committed to creating. Decisions need to be taken individually and collectively with an eye toward creating responsible financial results, social benefits, and positive environmental outcomes. This is only likely to happen in an organization when an organization has a clear identity that stresses all three types of value. Initiatives and change programs can not accomplish this. They come and go like other change programs and as a result fail to produce organizational decisions that integrate and balance the creation of the three types of value that sustainable organizations are committed to creating. Simply stated, the commitment to sustainable effectiveness needs to be fully integrated into the "DNA" of an organization so that it is part of an organization's identity.

Putting the emphasis on sustainable effectiveness – on achieving all three types of value - does not mean performing poorly in the financial area. It does mean however, that an organization that emphasizes sustainable effectiveness may never be the very best performer in its industry. The best performer at any particular time is likely to be one that is managed to maximize its financial performance in the existing environment. However, its outstanding financial performance often is unlikely to be sustainable because its focus on present performance prevents it from developing the adaptive capability needed to respond to changes in the environment and to switch to a new source of competitive advantage. Sustainable organizations develop the capability to adapt but recognize that the cost of this adaptability is a reduction in current financial performance to support innovation and long term financial performance.

Strategizing for Competitive Advantage

"Find a sustainable competitive advantage" is a common piece of advice that has been given to companies for years by business strategy experts and consulting firms. It is hard to argue against organizations basing their strategy on a sustainable competitive advantage if they can find one. Unfortunately, it is virtually impossible in today's rapidly changing business environment to find sustainable competitive advantages. Advantages are quickly wiped out by competitor actions, new technologies, government regulations, and rapidly changing business environments.

The alternative – and the one pursued by organizations pursuing sustainable effectiveness – is to think in terms of a series of momentary advantages. What sustainable organizations must do better than traditional command and control organizations is possess and leverage the ability to effectively move from one source of competitive advantage to another as the world changes. Building a change capability to support this requires having some slack in the organization's operations. Because they are focused on optimizing value in three areas and on agility, sustainable organizations are designed to be solid long-term financial performers.

During the 1990s and 2000s, Starbucks strung together a series of economic and social advantages as they created coffee experiences, social experiences facilitated by comfortable surroundings, technical experiences with T-Mobile hotspots, musical experiences, and food experiences (although to be fair, they did struggle with their food experience). At the same time, they delivered on environmental intentions that include supporting fair labor agreements with their coffee growers, using recycled components and promoting recycling at a local level, and more recently supporting clean water initiatives. All of these environmental initiatives complemented and extended the coffee and social experiences in the store as well as their reputation for being a good employer.

In order to create a series of competitive advantages, the strategizing process needs to include more than just executives and the board of directors; other stakeholders need to be active participants in it. Because of the focus on three areas of value creation, individuals throughout the organization and other stakeholders have valuable data about what is happening in the firm as well as in the environment. Thus, it is important to create an ongoing strategizing process that captures data from the environment and key stakeholders. Making this happen calls for a particular type of board of directors and an approach to organization design and structure that supports individuals throughout the organization understanding what is occurring in the external environment.

Governing at the Board Level

The boards of most corporations in the United States and Europe are designed and staffed to serve one stakeholder group – investors. Not surprisingly, this leads them to focus on the economic performance of their company. Boards need to be aware of and concerned about the impact of their organizations on multiple stakeholders. In order to do this, they must change their composition and focus.

First, it requires an independent chair and members that represent the most important organizational stakeholders. Investors yes, but also members who represent key community and environmental stakeholders. Diverse board membership better enables decisions that balance financial, social and environmental outcomes. It is unrealistic to expect a board that represents only owners to focus on sustainable effectiveness and to make balanced decisions. Steelcase is an example of an organization that has created a board with an independent chair and a membership dominated by outsiders, some of whom represent environmental and community groups. The Global Reporting Initiative is one effort to develop environmental impact measures. Its measures are being used by the boards of Shell, Kimberly-Clark and Cemex.

Second, boards need to receive different kinds of information. It is not enough for them simply to receive financial and operational information. They need to receive information about how the organization is impacting its employees, the communities that it operates in, and the environment. Further, boards need to be capable of thinking in terms of balancing the corporation's impact on multiple stakeholders.

Structuring to Support Sustainability

Sustainable effectiveness requires externally focused organization structures with "maximum surface area," dynamic decision making and resource allocation processes, and flexible work systems. An externally focused, maximum surface area structure puts the maximum number of people in contact with the environment. It is a critical feature because it is basic to individuals making meaningful inputs to strategy and operations. With a maximum surface area structure, employees more readily understand the kind of activities and behaviors required to meet financial, social, and environmental objectives. It also is the best way to make them aware of how the environment is changing and why the organization must change to achieve sustainable effectiveness.

IBM and Cisco have created externally focused, maximum surface area structures. In IBM's case, a "front-back" organization design puts cross-functional solutions teams into direct contact with customers, and the back office groups must stay current in their technical expertise to support the requested solutions. Both the front and back of the organization work to support IBM's "smarter planet" strategy.

Cisco's "council and board" structure has cross-functional teams that are responsible for particular segments of their environment, including enterprise customers, emerging markets, and emerging technologies. Their "eco-board" has the accountability for achieving the "if it can be connected, it can be green" objective across the organization.

The second design feature an organization needs to support sustainable effectiveness is a flexible decision making and resource allocation process. DaVita, the Fortune 500 kidney care and dialysis company, doesn't waste time and resources trying to communicate, coordinate resources and make decisions through structural boss-subordinate channels. Rather, they focus management attention and resources on the key projects and initiatives that will drive future success. For any activity that warrants attention, they ensure that there are people, finances, and clear objectives, and decision authority to support the effort. At any given time, those activities might include finding better ways to deliver dialysis treatment, connecting the local communities they serve, performing due diligence activities in support of a potential acquisition, and supporting the workforce. This allows the organization to gather and charter resources quickly, and when a project is over, the resources are available for other projects.

The third design feature is a flexible work system. At one level of flexibility, agile and sustainable organizations have structures that support traditional, reliable work, such as manufacturing existing products, as well as work that is designed to generate new projects, services, or other disruptive innovations. At the second level, agile and sustainable organizations are good at establishing and supporting work systems with characteristics that are very different from traditional work designs. This kind of work is characterized by shared goals, transparent information, and temporary and iterative work cycles.

Flexible work design can be seen in DaVita. In addition to ensuring that the core dialysis treatment continually improves and becomes more effective and reliable, the temporary project groups can also focus on creating new business opportunities. These groups report frequently on their progress and are controlled differently. For example, there are no job descriptions, a broad variety of information is shared openly, the groups are encouraged to “fail fast” or iterate on successful ideas quickly, and are measured according to metrics unique to the project.

Leadership

It is all too obvious that many of the executives and managers in today's organizations are not the type of leaders who can successfully manage an organization toward sustainable effectiveness. Hierarchical and power centralizing leadership approaches simply do not motivate individuals to change or support the behavior necessary to achieve sustainable effectiveness. As a result, their organizations are unable to adapt to the rapidly changing environment and are incapable of driving the necessary financial, social and environmental value tradeoffs.

Sustainable effectiveness requires that organizations have more leaders and different kinds of leaders than traditional organizations. This does not mean that they need more individuals in management jobs. Quite the contrary, to achieve sustainable effectiveness, organizations need fewer managers but more leaders. Individuals throughout the organization must have the willingness and skills to take leadership roles when it is appropriate. Paul Polman, soon after taking the top spot at Unilever, made the point clearly: My definition of leadership is simple. If you have a positive influence on someone, you are a leader.

When moments arise where the right thing to do is uncertain or when something needs to be challenged, sustainable organizations need individuals to come forward and provide leadership. They need to be effective in resolving issues, making tradeoffs, and getting the right things done to optimize a combination of economic, social, and environmental outcomes. This will only happen if the organization develops a leadership capability that comes from an identity and culture that supports shared responsibility and shared leadership. It requires a culture that says leadership doesn't rest with jobs and isn't restricted to executives. Leadership must be something that anyone in an organization who has a sense of what is right, what the customer requires, or what is necessary to meet environmental and social demands is not only welcomed, but encouraged to exercise. In short, leadership should be a shared responsibility that doesn't respect titles or hierarchy.

It is particularly important that leadership behaviors include supporting change. Since sustainable effectiveness very much depends on organizational change, managers need to be very cognizant of successfully introducing and supporting change. Without effective leadership it is impossible for an organization to change at the rate that is required in today's environment. Leaders need to be skilled at identifying the new behaviors that are necessary to support a new source of competitive advantage and at interfacing effectively with a rapidly changing external environment. Simply stated, there is no substitute for the leaders who direct, support, and role model the behaviors that are needed to successfully implement change.

Talent Management

Many organizations say that "talent is our most important asset", but they do not act as if it is. Because sustainable management organizations rely on a workforce that understands change and the requirements of achieving sustainable effectiveness, is able to accept and implement complex changes, and can assume leadership roles when it is appropriate, talent is their most valuable asset. To acquire the right talent, sustainable management organizations need to do a number of things that are not typical talent management practices.

Sustainable management organizations focus on skills and capabilities that individuals have and pay them based on those skills. This means developing accurate and comprehensive data on what skills individuals have, how they are being utilized, and how the individuals feel about working for their organization. Among the skill sets required, employees must have competencies associated with social and environmental issues as well as the traditional technical and financial ones. Creating these conditions is not easy, but there are some HR systems that when put in place can help. Let's look at a few practices that support the kind of talent management that is needed in sustainable management organizations.

Rewarding sustainable behaviors financially and non-financially is one key to attracting, retaining and motivating the right talent for sustainable management organizations. Exactly how this is done, what kinds of rewards are given needs to vary based on what business the organization is in and what rewards are available to it. In some cases, financial rewards should be given based on the individual's performance. But in most cases, it makes sense to stress group or team performance because of the interdependencies that exist in organizations that are committed to sustainable effectiveness.

Sustainable management organizations need to be particularly skillful at employee development because people are their most important asset. This includes making good decisions about career moves, development moves, and the nature of the employment relationship. IBM has developed a corporate wide talent information system that helps make this possible. It provides information on open positions, career paths, and on the skills and competencies of employees.

To attract the right kind of individuals for the right period of time, multiple employment deals and a wide diversity of work arrangements are required. Using contract labor, outsourcing, as well as making a commitment to developing key individuals are typically required.

Sustainable effectiveness requires a diverse workforce and this means creating a diversity of work relationships. It does not mean that everyone in the organization is expected to be a career employee, has job security, and can expect the organization to provide them with stable employment. Career employment might seem like a reasonable practice in terms of treating people who work for a sustainable management organization responsibly, but often it is not cost effective or even desired by everyone

Aligning reward systems to support sustainable effectiveness is critical. Employees, especially executives, need to be rewarded and recognized for achieving reasonable profit levels, corporate social responsibility targets, lower carbon footprints, and healthy relationships with the cultures and countries they operate in.

When organizations operate in diverse countries and cultures, it is particularly important that they develop the capability to treat employees as individuals. Individual treatment is necessary to match the skills, motives, and lifestyles of individuals with the work that needs to be done. A one size fits all employment deal or performance management system will not attract the right individuals, and is not the most responsible way to treat people. Accenture and Deloitte, with their career customization programs, have developed effective programs that allow their employees to choose and shape their careers. They make possible multiple career tracks, lifestyles, work hours and locations.

Creating Sustainable Management Organizations

Creating organizations that perform well in terms of the environment, profit, and people is a complex process. It requires much more than initiatives that focus on sustainability and social responsibility in isolation. It requires more than an organization that can adapt to change; it requires a new approach to management. It is because it requires a new management approach that so many sustainability and social responsibility efforts fail. They often have wonderful objectives, but they do not become permanent features of an organization's design. Most organizations are not designed to address social performance, environmental performance, and financial performance in an integrated and ongoing way. The only way to achieve sustainable effectiveness is to design organizations with this in mind. It is not easy to do, particularly in a rapidly changing environment that demands change, but it can be done by looking at all the key features of an organization and positioning them so that they support sustainable performance.

A note on methodology

Our article draws from a program of research at USC's Center for Effective Organizations that has involved a series of studies on large-scale organization change and organization development. Our understanding of sustainable management rests firmly on surveying and interviewing more than 40 large businesses. Our hypothesis was that agile firms were much more likely to be leaders in sustainability, and that has turned out to be true. Many of the companies highlighted in our new book, Management Reset, score very high on our agility profile, including Nokia, Cisco, Starbucks, Netflix, Davita, and others.

Our analysis of firm profitability in 14 industries over 30 years shows that a few firms are able to sustain above average levels of performance. Not surprisingly, consistently high financial performers are not only more likely to score high on agility; they are also likely to lead in environmental and social performance. To be fair, the correlation between financial sustainability and agility is stronger than the correlation between financial sustainability and social/environmental performance, but the link is there. Finally, we have done a number of interviews with firms having strong environmental and social reputations, including Patagonia, Nokia, and Alegent Health Care. Their insights into how to build business models that integrate financial and sustainability thinking were an important input to our thinking.