

Responding to global business critical issues

A source of innovation and transformation for FTSE 350 companies?

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Abstract

Purpose – *The main aim of this research was to review which FTSE 350 companies were responding to social, ethical and environmental business-critical global issues such as climate change, governance and technology. If they were, did this response result in innovation and transformation? The 14 issues were identified by a range of business practitioners and experts through a visioning exercise.*

Design/methodology/approach – *Independent data analysis of the companies, excluding around 50 investment trusts, by SERM Rating Agency provided a sector review of how companies were innovating or transforming their business as a response to the 14 issues. This review identified 40 companies as being most active in demonstrating their response. Of these 40, further analysis identified ten companies that showed signs of innovation or transformation.*

Findings – *The identified ten companies demonstrated evidence of pilot business transformation (or incremental innovation towards transformation) as a direct result of responding to the issues. For example, a mining company's HIV treatment program for its workers in South Africa. Most approaches were characterized by a wide-ranging series of incremental changes, with no convincing examples yet existing of transformation implemented across the entirety of the company's operations. Hints of this radical direction, however, are evident from the vision statements of several organizations.*

Research limitations/implications – *The research methodology is dependent on publicly available evidence. However, the implication of the research findings is that the 14 issues identified can be viewed as opportunities rather than obligations. Realizing the opportunity relies on integrating the issues in the core strategy of the organization.*

Practical implications – *This paper provides insight for business strategists and practitioners into potential new ways of working by companies. It illuminates an emerging source of innovation and ultimately business transformation driven by the growing significance of world issues to implementing corporate strategy and delivering sustainable profit.*

Originality/value – *The value of this paper is in the insight it provides on how companies are finding a source of innovation through responding to global issues.*

Keywords *Organizational restructuring, Innovation, Social responsibility*

Paper type *Research paper*

Introduction

Can you think beyond new products and new services to entirely new business concepts – ones that meet deep customer needs in unconventional ways? Can you think of unconventional ways of recharging an existing business concept? (Gary Hamel, 2000).

Changing environments

Companies face a complex and changing market and operating environment – from the impacts of global conflict to the technological leaps of the information age; from the

demographic challenges to world-wide health and education provision to the environmental impacts of climate change and water scarcity.

Multinational corporations and domestic business giants are increasingly expected by government and other elements of society to contribute to resolving these critical, yet apparently intractable, issues – a requirement recognized by parts of the business community in the 60 multi-sector partnerships announced during the Johannesburg Summit on Sustainable Development in 2002.

This business response is more than the responsive protection of corporate reputation. Leading companies recognize the importance of sophisticated (formal and informal) networks in the planning and delivery of appealing business solutions; and indeed, many multi-stakeholder partnerships may have unexpected and remarkable consequences, possessing the potential to transform the vision and strategy of the organization.

In this climate of complexity, innovative practice in relation to global issues – political, social, technological, environmental and governance-related – appears likely to become a central driver of competitive advantage in the coming decade.

Innovation

Peter Drucker's (1985) early contributions to the literature on business innovation assert that entrepreneurship lies in the careful analysis and exploitation of changes to a business and its external environment. Forget the "popular picture of innovators – half pop-psychology, half-Hollywood" that "makes them look like a cross between Superman and the Knights of the Round Table". Instead, Drucker suggests:

Successful innovators are conservative. They have to be. They are not "risk-focused"; they are "opportunity-focused".

In his book *Leading The Revolution* (Hamel, 2000) Gary Hamel confirmed that the basis of business innovation lies in a sensitivity to the radical changes of the business environment: that business concept innovation is "a capacity to create new wealth-generating strategies – strategies that are as revolutionary as the time we live in".

Article 13's research hypothesis was that a new model of innovation was emerging – that the concept was being "recharged" by the key challenges found within the social, environmental and ethical issues that form part of the CSR and sustainable development debates (see Table I). Enlightened business leaders are recognizing that commercial success requires them to address the current business-critical global issues, and in particular to understand and respond to the aspirations and expectations of a wide range of stakeholders – often groups that had traditionally been regarded as peripheral to the business.

Methodology

To test its hypothesis, Article 13 conducted a wide-ranging review into the history and prospects for the practice of sustainability-focused approaches to innovation. The first work phase reviewed the academic and business literature and press coverage for the major themes in innovation and social entrepreneurship.

This survey provided the basis for a round table visioning session with a number of business practitioners and specialists from the environmental, ethics, community-engagement and innovation fields to identify the key challenges facing the world – issues that provide a source of risk (and opportunity) for business in the next 20 years. The 14 issues business-critical global issues identified at the round-table are outlined in Table I.

Independent data from SERM Rating Agency was analyzed for the FTSE-350 companies (excluding the investment trusts) for evidence of management systems and business programs that sought to address a sample of eight of the 14 business-critical global issues that were identified at the round table: climate change; community; governance; health; sustainable production; technology; waste; and water.

Table I Business-critical world issues identified by Article 13

<i>Global issues</i>	<i>Role (and expectations) of business?</i>
<i>Political</i>	
Political agenda	Delivery of millennium development goals Public/private partnership
Conflict – and post-conflict	Responsible procurement and governance
<i>Social</i>	
Poverty – inequality	Generate secure employment Provision of food, shelter, health care, education and training Loans, micro credit
Education	Access to mentoring, capacity building and training
Health	Access, infrastructure for provision of health services Development and distribution of drugs Disease prevention Provide adequate health and safety program
Demographics	Family planning and education
<i>Technological</i>	
Technology – internet	Access to technology (computers) Use of technology/training/engagement
<i>Ethics</i>	
Governance – corruption, crime	Promote transparent governance Abide by the laws (but unfair and unjust laws) Reform of laws
Individual versus community versus global	Act local, think global, promote access of local services/products Staff involvement in the local community Partnership development Individuals working remotely Restructuring of board
<i>Environment</i>	
Climate change	Carbon neutral Energy efficiency and reduction, or switching to renewable energy
Water scarcity	Water recycling and reuse
Waste/reuse/recycle	Reduce waste, increase reuse and promote recycling – leadership Develop products with fewer materials, less energy
GMOs	Collect and communicate more information Implementation of precautionary principle
<i>Cross-over</i>	
Sustainable production and consumption (responsible consumerism)	Communicate benefits of sustainable production Improve labeling and communication of information of products Maximize efficiency of products and consider by-products Use components that have been produced in a socially and environmentally responsible manner

From the c. 300 companies (FTSE 350 less investment trusts), 40 leading organizations were then identified for an intensive case study review – a set of companies shown by the SERM Rating Agency research to be amongst the "most active" in demonstrating their response to the eight business-critical global issues.

Of the 40 companies, ten were featured in the final report, each of which demonstrated evidence of business transformation (or incremental innovation towards transformation) as a direct result of the companies' response to these global issues. The companies featured were: Anglo American; BP; BT; Centrica; GlaxoSmithKline; Kingfisher; Scottish Power; Tesco; Unilever; and Waste Recycling Group.

Results

Literature review and roundtable visioning

Through an extensive literature review and visioning exercise, Article 13 outlined the context for its research into business innovation. Key elements of this background – rooted in the challenges of (and changes to) business's operating environment – include:

- Organizations face a complex and changing market and operating environment – there is rapid and open movement of information and knowledge between societies; social and environmental catastrophes and inequalities persist; corporate boundaries are continually changing and companies are expected to contribute to resolving the critical issues facing society.
- In the 1990s, new tools and techniques in the measurement and reporting of social impact were led by overtly values-based businesses such as The Body Shop and Traidcraft. At the same time many mainstream companies also began to experiment, driven, for example, by public and campaigning organization pressure and in some cases subsequent regulation. A large proportion of these companies took a cautious approach to their activities and communication and sought to capture ad hoc benefits – reducing energy and raw material costs as well as environmental impact; reducing recruitment costs and improving productivity through higher levels of employee loyalty and commitment.
- Pressure for effective social responsibility management is slowly but surely becoming translated into standard commercial practice in the FTSE-350. Many of the quick wins – for example reducing costs from inefficient use of resources and improving employee loyalty – have been delivered and the on-going management processes have been mastered.

Data survey

Article 13's survey based on research from SERM Rating Agency (see Table II) demonstrates that corporate activity addressing the business-critical world issues is relatively consistent across all issues:

- Across ten industry sectors (FTSE Actuaries Industry Sectors), the average score per issue (on a scale of 1 to 10) ranges from 3.2 to 4.4.
- Health (4.4) and community issues (4.1) have the highest ratings.
- Companies performed more poorly on some long-standing environmental challenges (water – 3.2) as well as those issues that characterize the new environmental challenge (climate change and sustainable production – both 3.5). Scores on technology issues were also relatively poor (3.5).

The survey identified more significant differentials in performance on a cross-sectoral comparison, with performance strongest amongst utilities and non-cyclical consumer goods – industries facing regulatory and consumer pressure.

The utilities industry averaged a score of 8, performing strongly all issues including the environmental issues of waste and climate change.

Non-cyclical consumer goods businesses – including food, drink and healthcare companies – averaged 7 with strong scores on community (9) and health (8), The sector's scores were lower (6) for most environmental issues.

Table II Analysis of SERM Rating Agency research

Issues	Resources	Basic industries	General industries	Cyclical consumer goods	Non-cyclical consumer goods	Cyclical services	Non-cyclical services	Utilities	Information technology	Financials
Climate change	4	4	2	3	6	2	3	8	1	2
Water	4	2	2	2	6	2	2	7	1	2
Governance	5	3	2	3	7	3	3	6	2	4
Technology	4	4	2	3	6	2	3	7	1	3
Waste	4	5	2	3	6	2	3	9	1	2
Community	5	3	2	3	8	3	4	8	2	3
Health	6	4	2	3	9	3	4	9	1	3
Sustainable production	4	4	2	3	6	2	3	8	1	2
Average	5	4	2	3	7	2	4	8	1	3
		Chemicals	Aerospace and defense	Automobiles and parts	Beverages	General retailers	Food and drug retailers	Electricity	Hardware	Banks
		Construction and building materials	Electronic and electrical equipment	Household goods and textiles	Food producers and processors	Leisure and hotels	Food and drug retailers	Other utilities	Software	Insurance
		Forestry and paper	Engineering and machinery	Household goods and textiles	Health	Media and entertainment	Telecommunication services			Life assurance
		Mining			Personal care and household products	Support services				Real estate
		Oil and gas			Pharmaceuticals and biotech	Transport				Speciality and other finance

Note: Average FTSE 350 companies performance in demonstrating their commitment to addressing the Article 13 identified business critical world issues on a score of 10 (strong) to 1 (weak), categorized by FTSE Actuaries Industry sectors

The worst performing sector (averaging 1) was information technology. Other weak performers were cyclical services (2) and financial services (3).

Case studies

Article 13's subsequent case review of 40 companies took the analysis from the sector level to the practice of individual organizations.

Ten of the 40 businesses demonstrated evidence of significant innovation and potential transformation regarding the business-critical world issues (see Table III). As with the data analysis, community and health issues provided the most fertile area for business involvement. However, a number of programs addressing climate change and sustainable production were also identified.

Common aspects – relating to the companies' strategic positioning and operating environment – appear amongst the vanguard innovators. The “early adopter” companies of this new route to transformation frequently operate in consumer environments with supply chains and customer bases in volatile countries, with product and process issues that contain significant social, environmental and ethical risks, and where resolution of the issues requires high levels of collaborative problem-solving and high levels of current uncertainty (see Table IV).

Many approaches are currently cautious; pilot studies exploring the potential of new operating methods and alternative approaches to market. British Telecom, for example, decided in the autumn of 2003 to examine the potential of developing a wind-farm on its own land due to the absence of alternative “green” suppliers (see Table V).

This proposal was designed to break BT's historic methods of energy use and reduce costs – transforming the resourcing of the organization – as well as building its reputation by demonstrating the company's environmental awareness and responsibility.

Such apparently small-scale and piece-meal initiatives can represent part of a sustained and wide-ranging approach to the role of innovation in the delivery of competitive advantage – an incremental path to transformation. In the UK retail sector, Tesco, operating in a saturated market with limited opportunities to build new stores and a need for new and skilled staff, has piloted an approach to business development based on re-generation and social inclusion.

By developing what they term “regeneration partnership stores”, the company has been able to contribute to the regeneration of deprived areas, quantifying the new jobs provided and improvements in diet. The regeneration stores are the latest in a series of Tesco's apparently phased initiatives ranging from procurement and supply chain management to customer information and staff incentive programs – collectively working towards sector leadership and transformation of its business processes.

The Tesco example also illustrates the critical role of partnership in enabling the implementation of complex projects and demonstrating sensitivity to the expectations of a wide range of stakeholders. The key to the effective delivery of the regeneration stores was

Table III The ten innovators: areas of innovation

<i>Company</i>	<i>Sector</i>	<i>Area of innovation</i>
Anglo American	Mining	Health and community
BP	Oil	Climate change
BT	Telecommunications	Climate change
Centrica	Energy sales and other consumer services	Community
GlaxoSmithKline	Pharmaceuticals	Health
Kingfisher	Retailer – department	General (process)
Scottish Power	Electricity	Community
Tesco	Retailer – food	Community
Unilever	Food processor	Sustainable production
Waste Recycling Group	Environmental control	Waste

Table IV Analyzing the innovators: the characteristics of the vanguard

<i>Market and operating environment factors</i>	<i>Companies indicating innovation</i>
High income/information-rich consumers	BP BT Kingfisher Tesco Unilever
Supply chain in developing countries	Anglo American BP Kingfisher Tesco
Products/services with direct and significant impact on critical social issues	Centrica GlaxoSmithKline Scottish Power
Market access and growth in developing/volatile countries	BP GlaxoSmithKline
Strong tradition of NGO pressure	BP GlaxoSmithKline
Branded products/services	Centrica Kingfisher Scottish Power Tesco Unilever
Business to consumer	BP Centrica Kingfisher Scottish Power Tesco Unilever
New technology industries	BP Waste Recycling Group

Table V Approaches to innovation

	<i>Process innovations</i>	<i>Product/service and channels to market innovations</i>
Incremental change	Anglo American's HIV treatment programs BT's wind-farm energy self-supply BP's shift to renewables Centrica's customer education Scottish Power's community learning Unilever's sustainable production procurement guidelines	GlaxoSmithKline's alliance with generic drug manufacturer Tesco's regeneration partnership stores Waste Recycling Group's new products from recycled waste
Transformation	Kingfisher's sustainability management process	Evidence only in vision statements currently

the use of a phased pilot approach that generated learning through partnerships with local government and community groups.

A series of local partnerships are equally central to the delivery of Scottish Power Learning, the energy company's educational program for work-place and life-skills. The program was

launched in partnership with the trade unions, extending its remit beyond Scottish Power employees to their families, retirees and also selected groups in the wider community – so contributing to the company's networks with key employment groups as well as building human capital in its operating regions. The program now draws on the skills and networks of the unions, governmental bodies such as the Learning and Skills Council, NGOs such as The Prince's Trust, and small enterprises such as the Cumbernauld Theatre.

Operating in politically sensitive and economically deprived communities, the mining company Anglo American is another company paying careful attention to groups outside its primary stakeholders. Anglo American's subsidiaries have worked in partnership with local medical groups and NGOs to implement a series of initiatives to address serious community issues. For example, Anglo Coal's HIV initiative has increased condom usage and treated sex workers and their clients. Anglo American's managed operations have extended anti-retroviral therapy at company expense to HIV positive employees progressing to AIDS; and the company has now recognized publicly that the extension of interventions beyond the workplace into communities associated with its operations is vital for its sustainability.

Centrica's UK energy business, British Gas, received unfavorable media coverage in late 2003 following the death of an elderly couple whose power supply had been disconnected. This public pressure will be a key test of its long-standing relationship with Help the Aged, a partnership designed to make the lives of the elderly warmer and less isolated. Interestingly, BBC coverage of the case included comments from a Help the Aged spokesperson, who said: "I think the key issue here is that there is no system in place to flag up vulnerable people and though they [British Gas] knew there was vulnerability here they weren't able to tell social services," – her comments referring to the apparent implications of the Data Protection Act.

An innovative example of British Gas's partnership approach, looking beyond immediate delivery issues to the long-term health of its customer base, was its Benefits Advice scheme launched in December 2003. This pilot program is designed to address the confusion experienced by pensioners trying to understand the system of claiming benefits.

The formation of more unexpected relationships are also illustrated by the Article 13 review; the partnership may even be the critical innovation that creates a new market or transforms the costs and opportunity to access a new market, for examples the clinical trials alliance with a generic supplier announced by GlaxoSmithKline, the pharmaceuticals company.

Other case studies illustrate the creation of customer value through new products and services. An environmental services company, the Waste Recycling Group, has generated a series of environmentally beneficial production processes that create new green products. These include a green waste-composting alternative to peat-based products, and the recycling and recovery of organic content of household waste for use as soil conditioner.

The food processor, Unilever, has boldly embraced the sustainability agenda. As its corporate communications state:

We are committed to contribute to sustainable development. We see this as a hard-edged commercial imperative because we will only be able to maximise shareholder value and prosper in the long-term if we operate in a much more sustainable way.

The multinational Unilever faces extraordinary challenges in translating its vision into reality. Its first step was to structure its initiatives across three areas where it has direct control and believes it can make a substantial difference: agriculture, fish and water. The agricultural program seeks to ensure continued access "to the key agricultural raw materials, and ultimately to develop market mechanisms that allow consumers and customers to influence the sourcing of raw materials through their buying habits." Unilever's procurement innovation rests in the development of sustainability guidelines for its five key crops – palm oil, tea, peas, spinach and tomatoes – through a process of stakeholder engagement including a multi-stakeholder advisory board.

The global energy player, BP, has a similarly ambitious vision: "to do no damage to the environment" – a challenge that stimulates BP "to find innovative ways to manage our

environmental impact at local, regional and global levels." BP's approach is multi-pronged, addressing climate change (through combinations of energy efficiency, flaring reductions and lower carbon products), biodiversity, water usage, waste and air emissions.

BP believes that gas will be the transitional fuel for several decades; yet a critical activity for the business, leading the gradual transformation to a position "beyond petroleum", is driven by BP's challenge "to build a material and profitable renewables business" based on solar and wind. BP emphasizes the use of solar power to reach the "as much as one third of the world's population" which is currently without access to electricity. It also advocates the role of partnership in delivery, working with global funding agencies, NGOs and private sector organizations as well as managing the training of local people to install and maintain the solar products.

Underlying the majority of the ten cases of innovation are leadership commitments to the creation of social, environmental and economic value supported by effective measurement and management processes – the tools and measures that help organizations to implement and deliver business transformation. An outstanding example of business process innovation is demonstrated by the retailer Kingfisher, which has introduced a "ladder" management model structured around a set of business-critical issues – a global agenda translated into the specific strategic challenges in the European home retail market.

Kingfisher's approach, published in detail in its plan for corporate social responsibility, is explicitly designed to enable different businesses within the group to innovate independently (reflecting their own market conditions) around a commonly accepted vision of the future challenges facing the organization.

Kingfisher's shared vision and "ladder" approach is already delivering incremental changes to the group's activity. The results to date have enabled the organization to share and report on best practice, so encouraging employees' individual creativity to think (and realize) the unthinkable. The test for the organization is whether these immediate successes can generate a step change from a price-focused retail tradition to a responsible and sustainable competitive edge.

The ten examples illustrate the range of approaches to socially-focused innovation: from a series of incremental changes to the fundamental alteration of a business's historic direction; from the creation of new products and services, to the formation of new partnership networks to develop and deliver the products and services, and to the introduction of new management processes that underpin the partnerships and product offer.

Several of the cases are small scale, the innovations still at pilot stage; yet a more important note of caution comes from the notable absence of evidence regarding the skills base and competencies of their organizations in terms of delivering the stated strategic objectives. It is these capacities that will be central to the companies' ability to identify and exploit the sources for transformation in response to business-critical world issues.

The emerging model – summarizing the Article 13 review

The Article 13 review illuminates an emerging model of innovation – a source of business transformation driven by the growing significance of world issues to implementing corporate strategy and delivering sustainable profit.

Current corporate responses to these business-critical issues are frequently limited to complying with legal obligations and other immediate stakeholder pressures. But a vanguard of companies is demonstrating significant evidence of innovating towards business transformation.

These strategic breakthroughs encompass innovations in product and service, the creation of new routes to market through partnerships and informal networks, and innovations in technology and business process – all backed-up by new strategic tools and measures to support forward-planning and measure progress.

Most approaches are currently characterized by a wide-ranging series of incremental changes, with no convincing examples yet existing of transformation implemented across the entirety of the company's operations. Hints of this radical direction, however, are evident from the vision statements of several organizations.

Partnerships are significant in building the credibility of many innovations, and can also be essential in providing the skills and networks required to deliver the innovation effectively. Other success factors for implementation include new strategic tools and measures to support planning and calibrate progress in previously unmeasured issues and themes. A collective approach to the measurement of these intangibles can have the knock-on effect of fostering a shared vision of transformation and delivering a demonstrable approach to risk identification and management.

It is Article 13's belief that the 14 business-critical world issues identified in its visioning exercise tie in with a growing recognition across society that commercial operations have an effect upon the natural and social world that impacts us all – as customers, investors, employees and members of local and global communities.

These social and environmental impacts have economic implications – from rising insurance premiums due to the effects of climate change to the shortage and increasing price of key resources such as fossil fuels, fish and timber, and to the shortage of landfill sites in the UK leading to tax and waste disposal costs.

And the economic effects are sharpening the awareness and investigation of how companies can use innovation to rethink their business and transform it for future success.

The early agents of change identified in the Article 13 research are straining beyond the immediate concerns of their business operations, carefully and imaginatively assessing the possible routes to creating value over the next ten to 20 years.

They face serious limitations – distrust and skepticism extending from the boardroom to the shop floor, from the stock market to town halls and parliaments. Yet these companies are seeking to overcome skepticism with practical results – they are daring to think the unthinkable, work with the unexpected and create the unknown.

These pioneering companies (and the entrepreneurial individuals within them) have grasped the notion that the risk of staying the same is greater than the risk of changing – signs of innovation at work.

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