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Growing with 'Green Models'

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Growth is the only way to create value in the long-term. It is difficult to grow economically without CO_2 emissions. The environment is becoming a critical issue for companies. Companies need to develop new competitive business models that reduce the environmental footprint through 'green models'. Which ones and how?

Traditional approaches to reducing our environmental footprint are no longer sufficient

In 50 years, atmospheric CO_2 concentration has risen from 320 parts per million to over 400 parts per million. It has increased by almost 30 %, and temperatures have risen by 1,5 °C. There is an urgent need to reduce this environmental footprint, and in especially CO_2 emissions, to limit the temperature rise. This is the ambition of the Paris COP 21 signed in 2015.

In addition to good corporate citizenship, there are four main economic reasons for companies to reduce their environmental footprint:

A strong value for employees, especially the younger generation. This dimension is becoming a factor in attracting and retaining employees. It is no longer simply a secondary factor, but a primary one.

Increased value for customers. They are beginning to make their own consumption choices, by avoiding products and companies that have not embarked on an environmental transition. They are willing to pay more for ecologically designed products that limit their environmental impact. The trend is recent, still emerging, and particularly segmented across product categories, geographies, and price points.

Added value for investors. Investors increasingly value companies that have initiated environmental transitions, whether for reasons of corporate citizenship, opportunism or because they are convinced that fiscal mechanisms will be put in place quickly. Green financing conditions are more advantageous than others. This trend is expected to continue.

Increased taxation. Taxes already exist to penalize activities with a high environmental impact. These taxes will increase, as in Europe, for example, with the 'Carbon Border Adjustment Mechanism' (CBAM).

Companies must therefore combine their ambition to create economic value with reducing their environmental impact.

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Two necessary directions in the environmental strategy

1 Reducing the environmental footprint

- Development of eco-design (sustainable materials, recycled materials, alternative technologies, minimum use of materials, durability, etc.)
- Development of renewable energies in production and distribution
- Improvement of energy efficiency in production and distribution
- Reduction of upstream and downstream transport footprints
- ...

2 Developing Green Models on the right scale and at the right speed

- Circularity model
- Second-life model
- Repair model
- Usage economy models (rental)

There are no alternatives anymore, it is a necessity. All three dimensions (together with human performance) must be integrated and pursued simultaneously.

Large companies have taken steps to reduce their environmental footprint: development of eco-design (sustainable materials, recycled materials, alternative technologies, minimum use of materials, sustainability, etc.), development of renewable energies in production and distribution, improvement of energy efficiency in production and distribution, reduction of upstream and downstream transport footprints, etc.

While these actions are necessary, they are no longer sufficient. Traditional transnational product sales models will not reconcile economic and environmental performance. Sacrificing economic performance would not be desirable either for the company's shareholders or for the environment. In this case, the least virtuous models will gain market share (in the short and medium term) and the overall environmental objective will not be achieved. Alternatively, environmental performance is sacrificed, with emissions volumes continuing to rise. In this case, long-term competitiveness will be compromised

The four main business models

Four major 'green models' are emerging that can be a source of profitable growth, while reducing CO_2 emissions.

Circularity models. In many industries, a significant portion of CO_2 emissions come from raw materials. Developing circular models can reduce the environmental footprint while creating significant entry barriers. The high demand for sustainable polyester in the textile industry has led to a supply-demand imbalance and price pressure. In all industries where upstream resources become scarce, value migrates upstream.

For a company using polyester, strategic investment in recycling infrastructure is critical to secure supply and control purchase prices. It's a matter of defining the appropriate model in terms of positioning in the value chain (raw material sourcing, sorting and primary transformation, secondary transformation, and supply chain organization) and modalities (in-house; co-investment; partnership; strategic agreements).

This is the move made by thermoformed food packaging manufacturer Faerch, which has invested in Cirrec, a recycler of PET from food packaging.

Second-life models. The second-life market has experienced strong growth in recent years driven by several strong and long-lasting trends: an eco-responsibility wave (citizen/ecological motivations), a generational wave with the transition from an ultra-niche market to a mass market, an economic wave allowing middle-income populations to access branded goods, a regulatory wave with, for example, Extended Producer Responsibility (EPR) in France or Erweiterte Herstellerverantwortung (EHV) in Germany, and a technological wave facilitating and segmenting the relationship between sellers and buyers.

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‘Green models’ require ambition, focus, speed and operational excellence

KEY TAKEAWAYS

- Growth is the only way to create value in the long term. A company that does not grow by more than 7.5% per year (i.e., a doubling of revenue every 10 years) loses its attractiveness and independence in the long term.
- It is difficult to grow economically without CO_2 emissions.
- However, there is a consensus on the impact of CO_2 emissions on global warming, and therefore on the urgent need to reduce CO_2 emissions.
- Traditional approaches to CO_2 reduction are necessary, but not sufficient:
  - Development of eco-design (sustainable materials, recycled materials, alternative technologies, minimum use of materials, durability, etc.);
  - Development of renewable energies in production and distribution;
  - Improvement of energy efficiency in production and distribution;
  - Reduction of upstream and downstream transport footprints...
- We need to develop new business models that are sources of competitiveness, profitability and growth:
  - Circularity models
  - Second life models
  - Repair models
  - Usage economy models (rental)
- These ‘green models’ require ambition, focus, speed and operational excellence, and must be driven and steered by the President.

With so many solutions on the market, the challenge is to define the right model in terms of value chain positioning (collection, refurbishment, marketing and customer management) and level of specialization (niche vs. mass markets). Fast-growing players such as Vinted (CtoC second-hand clothing marketplace), Thredup (BtoC refurbishment and sale of fashion clothing), Backmarket (BtoC refurbished electronics marketplace), or Trove (white-label turnkey technological and logistical solution for brands wishing to develop a second-hand offering) offer different positioning and levels of specialization, resulting in different barriers to entry and potential for value creation.

Repair and maintenance models. Many companies have significant growth potential in repair and maintenance responding to a long-term growth trend: the logic of product repairability. The era of disposable products with no circularity and/or reparability is over.

The development of these models affects on the entire value chain: in product design, by developing products with stronger, more easily replaceable components; in the development of centralized or decentralized maintenance points; and in logistics operations. In certain industries, such as elevators or aircraft engines, much of the value creation is in repair and maintenance models. This logic is expected to extend to many other industries.

Use economy (rental) models. Historically, rental models have focused on the durable goods industry (housing, automobiles, etc.), with short, medium or long-term leasing options. Today, usage economy models are expanding into new applications. In the cycling sector, particularly in densely populated areas, there are now various rental options: hourly or half-day rentals, weekly rentals, long-term rentals or rentals with no fixed term. Swapfiets, part of the Pon Holdings Group (8 Bn€ in revenue), provides its customers with a bike for a monthly fee, and promises to repair or exchange it within 48 hours if an issue arises. It is rolling out this model across Europe, and this activity now contributes over 20% of the Group's value creation.

Success factors for new “green” business models

The development of these new business models is necessary, and represents a major opportunity for value creation. They require an approach based on five key principles.

Define an ambition and scope commensurate with the challenges. Ambition must be set at the right level, so that it is consistent with environmental (and CO_2 emission reduction) and strategic (leadership positions for competitiveness and industry consolidation) challenges. Ambition tends to be too modest compared to the scale of the challenge.

Significant speed to make an impact. It is crucial to invest at the right pace to strike a balance between investment and achieving leadership positions, and to make strategic logic (leadership positions), financial logic (development financing), and operational logic (organizing for growth) coherent. The speed and level of investment are generally insufficient to match ambition.

Focused approach and concentrated resources. There is a need to focus investments and resources on relevantand differenciated approaches. Dilution of resources and endless POC developments are detrimental. Concentration of resources, skills, and expertise is critial to increase impact and speed.

Business model prioritization and precision. Business models must to be fine-tuned before deployment. They need to integrate the different dimensions of the model and be fine-tuned and adjusted by leveraging on different experiences through a feedback mechanism.

Operational excellence and continuous model evolution. The simplicity of the model facilitates its deployment at the right pace. Consistent skill development avoids bottlenecks. Consideration of different stages accelerates progress at the right time.

What to conclude?

The environmental transition is a fundamental structural movement for companies, which will have a significant impact on their strategy, finance, organization and operating methods over the next 10 to 20 years.

It will lead to the development of new business models: green models. Companies that rise to this challenge will be able to develop sustainable competitive advantages. New players will emerge. Historical players will need to leverage their positions. As with any breakthrough, a structured approach, led at the highest corporate level, is needed to ensure consistency between ambition and resources, and to create the conditions for deployment at the right speed and on the right scale.

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