BEARS ON THE ROAD: [C] The Capabilities Route

THE CAPABILITIES ROUTE: is the common route organizations take when moving from level 2 (‘reactive’) to level 3 (‘active’) sustainable business approaches. Walking the capabilities route entails working towards higher degrees of both strategy integration and operational coordination. **Adaptive and managerial capabilities** are developed along the way (‘learning by doing’) whilst viable and more strategic sustainability approaches gradually take shape. **Integration into core operations** progresses in a step-by-step manner as the organization works towards overcoming key organizational tipping points.

Major internal barriers include the **recoupling** of varying practices, motivational drivers, values and interests (see Chapter 11 in *Principles of Sustainable Business*). Because resource, responsibility and budget allocations will change in accordance to new priorities and **adjustments in the organization’s value proposition** (see Chapter 9), internal power battles over vested interests and between ‘leading’ and ‘lagging’ departments are bound to appear. The focus along this route is on **developing greater levels of internal alignment**: more effective coordination and cooperation between and across functional areas of management, and a consistent uptake of the sustainability approach into systems, policies, processes and incentive mechanisms. External stakeholder pressure may actually help to speed up internal alignment.

As experience grows, more confident decisions on fundamental organizational changes move the organization from relatively low, to higher levels of integration, coordination and coherence. Accordingly, **the strategic intent shifts from 'do no harm' to 'do good'** – in all areas of management. The successful completion of this route should result in a long-term strategic advantage for the organization in order to solidify (see Chapter 8).

1. PERSONAL [MOTIVATIONAL] ‘BEARS ON THE ROAD’

To become ‘active’ from an initially ‘reactive’ attitude, people need to experience that they are working on an interesting challenge that is within their reach – yet not too easy. People may also be motivated by social norms and adjust their behaviour to what they feel is expected from them. Becoming ‘active’ requires letting go of routine decision-making, making better-motivated choices and prioritization based on principles and values. It also demands a deeper understanding of what one could actually achieve with one’s capabilities. Individuals are not always as much in control of their decisions as they think. Accordingly, they need to overcome several challenges, including:

- ***Knowledge gap***. Individuals may not be fully knowledgeable about the magnitude of certain sustainability problems, nor realize what the consequences are of not addressing them appropriately. This is especially true for issues that are rather abstract, ill-structured, non-quantifiable and complexly interlinked with other sustainability dimensions – as is the case with so-called ‘wicked problems’ (see Chapter 4 in *Principles of Sustainable Development*).

- ***Desirability gap.*** Individuals may not always be fully aware of the preferences they have, and why, and how that relates to their choices and actual behaviour. This lack of insight becomes particularly evident when having to decide on difficult trade-offs between many different dimensions of sustainability.

- ***Action gap***. How individuals align their capabilities to perceived sustainability challenges depends on the size of the previous two gaps in terms of (a) experienced ambiguity/clarity, and (b) the predictability of consequences and events in order to plan and prepare.

- ***Developing the right capabilities.*** How to place oneself in the position where the greatest contribution to the organization or community can be made? Reaching excellence requires combining strengths with deeply-felt motivation. It also demands serious investment in continuous learning. Individuals have to consciously ask themselves what it is that makes them not only willing but also capable to bring specific goals to realization.

- ***Getting past no***. There are many reasons why people refuse or evade change and stick to reactive attitudes. Out of fear, discomfort or feelings of incompetence and guilt, for instance. Getting to a resilient 'Yes' requires that people are able to distinguish between a 'reactive No' and a 'principled, positive No'. Only a principled and positive 'No' enables a powerful 'Yes'. Put differently: knowing what you absolutely *do not want* to see in the world, helps you realize what you *do want* to strive for.

- ***Getting rid of 'bad' habits.*** Letting go of inadequate mindsets (e.g. perfectionism, the need for certainty and confirmation, anxiety) can be accelerated by developing a mentally strong and resilient mindset. Mentally strong people have been found to show a greater willingness to take (calculated) risks, to accept and take responsibility, to develop staying power and tolerance for discomfort, to be reflective and evaluative on one's behaviour and progress, to being kind, to not be afraid of failing, and to not feel intimidated by the success of others.

- ***Dealing with the Halo effect,*** which refers to people's inclination to attach too much value to one earlier (positive or negative) judgement about something or someone, as a sign of broader or greater (positive or negative) characteristics. The halo effect constitutes a particular 'cognitive bias' that reinforces personal preferences and prejudices.

- ***Specifying trade-offs***. When faced with a large number of complex issues, people have a tendency to define all issues as important. They intuitively choose the middle ground as a 'safe option' ('the truth lies in the middle'). But they often don't realize that this approach constitutes a decision too: one that is based on routines, time limitations, denial or ignorance instead of a rational, conscious and proper assessment of the kind of sustainability trade-offs faced (and the possibility of alternatives). This makes it difficult to prioritize those strategic issues that require focus.

- ***Rebound effect***. People tend to compensate positive action (e.g., buying energy-saving LED lights) with negative habits (leaving the lights on longer), thereby reversing the impact of their intention to behave more sustainably. The rebound effect is related to the concept of 'moral self-licensing'.

- ***Lazy thinking,*** or 'system 1 thinking', refers to the impulsive, impatient, intuitive and non-reflective 'rule of thumb' mode of thinking, prompted by the urge for instant gratification.

More information: *GatMR*, pp. 62–70[1]

[1] The abbreviation 'GatMR' refers to the publication *Getting all the Motives Right. Driving International Corporate Responsibility (ICR) to the Next Level* (2018), which is freely downloadable from: https://www.robvantulder.nl/wp-content/uploads/2019/12/Getting-all-the-Motives-Right-part-1.pdf

2. ORGANIZATIONAL [MOTIVATIONAL] ‘BEARS ON THE ROAD’

In moving from a ‘reactive approach’ (sustainability as an externally imposed norm) to an ‘active approach’ (sustainability as a strategy), the development of dynamic capabilities becomes pivotal. On the capabilities route [C], companies particularly invest in the development of organizational capabilities that enable them to become more proficient in identifying and unlocking promising opportunities for change, and in tackling sustainability challenges more effectively and efficiently by addressing them in an integrated manner. Typical organizational challenges and barriers along the capabilities route include:

- ***Selection bias*** refers to a (too narrow) focus on the more ‘easy’ or ‘obvious’ sustainability-related topics. This occurs, for instance, when organizations concentrate on ecological issues only (e.g., minimizing energy use, reducing emissions, countering overexploitation) whilst largely ignoring inherently related social dimensions (e.g., living wages, gender equality, human and labour rights). Companies may also interpret CSR as an essentially ‘charitable activity’, directing all CSR efforts to social philanthropy activities unrelated to the core business. Picking ‘low hanging fruit’ might deliver efficiency, cost reduction or reputational gains in the short run. However, *not* prioritizing and investing in longer-term material issues will get organizations side-tracked, and eventually inhibit them from reaping longer-term strategic advantages.

- ***Copying ‘best practices’ is hard***. Large organizations can be inspired by the sustainability approach and performance of, for instance, innovative and successful social enterprises. But social enterprises usually serve niche markets, whereas large enterprises generally target larger markets of mainstream consumers. Large companies hence face different types of challenges – in particular related to internationalization, scale, and networked supply chains – than most social enterprises do. Social enterprises typically focus on a specific sustainability topic and customer segment, leaving many of the broader sustainability trade-offs open. Large companies have tried to internalize the experience of frontrunner social enterprises through acquisition (L’Oréal acquiring The Body Shop, Unilever acquiring Ben&Jerry’s). This not seldom resulted in internal power battles and organizational unrest, however.

- ***Trust gap.*** Even when corporate leaders are serious about their motives to engage in sustainability and move away from the reactive business model, they are still likely to face two trust-related challenges. On the one hand, societal stakeholders express ever greater expectations of business to act sustainably and drive impact. On the other hand, research by Edelman’s Trust Barometer over consecutive years indicates that the general public perseveres in its limited trust in companies to address societal issues correctly, or to make ethical and moral decisions. Failure of leadership has made distrust the default. A prime objective along the capabilities route, therefore, is to (re-)gain a societal ‘license to exist/ operate/scale/experiment’ by reaching a minimum level of trust.

- ***Understanding tipping points***. A tipping point on the capabilities route is the breakthrough moment at which a new balance in the organization of the business model is achieved, at a higher level of sustainability. Reaching a tipping point is not necessarily based on big or sudden changes; minor changes are often accumulative, but can nevertheless become an irreversible reality once they reach a critical threshold. Tipping points in corporate transition processes arise when business case and business model match up. To illustrate: investing in sustainability initially costs money and may seem a drain on corporate financial performance. But eventually, it results in a positive return once the financial tipping point is surpassed. The investment curve for most sustainability issues resembles that of a ‘normal’ investment curve: costs always precede benefits.

- ***Addressing trade-offs.*** Despite the 'win-win' frame used in the popular CSR discourse, transitioning towards enhanced sustainability performance is, in practice, laden with strategic and operational trade-offs. It is unlikely that everyone will win; some tough decisions 'for the better' inherently come with (temporary) uncertainties and organizational frictions. Hence, a key internal alignment challenge for corporate leaders is how to effectively involve internal stakeholders in strategic discussions about defining relevant trade-offs and making hard choices in the transition process. If this process is not managed adequately, a relapse in reactive organizational thinking looms.

- ***The crowding-out paradox***. Linking financial incentives (bonuses) to sustainability KPIs has been found to create a perverse effect: it may actually attract 'the wrong kind' of employees – that is, opportunists with a relatively weak intrinsic motivation for sustainability, yet a high extrinsic motivation to earn money. A well-founded CSR reputation proves more conducive for attracting intrinsically-motivated employees – who not only have been found to be more committed to the organization, but also more productive and loyal in times of crisis as long as the organization upholds its ambition and truly 'walks its sustainability talk'.

- ***Positive perception gap.*** Although organizational transitioning processes may run into some level of 'resistance to change', underutilized organizational 'potential for change' may exist as well. Research points to a substantial perception gap among employees of frontrunner companies between: (1) what they think their company *is* doing, (2) what they think their company *should* be doing, and (3) what they think their company *is capable of* doing. A too positive perception about the organization's actual sustainability progress realized can exacerbate the intention-implementation gap. Conversely, employees who feel that their company should and can do more than it is presently doing, potentially constitute a powerful driving force towards a more 'active' corporate sustainability attitude. They can provide decisive internal support for corporate leaders with ambitious sustainability objectives and may actually act themselves as 'intrapreneurial change agents'.

- ***Negative perception gap***. Companies lagging behind in terms of their sustainability agenda might face the opposite mechanism: employees who are sceptical about the sustainability ambition of the (new) corporate leadership, or who are not convinced of the authentic need to change. This mechanism applies in particular when the CEO drives sustainability in a non-coherent manner (e.g., a concentrated implementation effort in marketing, but not in HRM, sustainable procurement or responsible supply chain management).

- ***Technology trap and techno-optimism***. End-of-pipeline 'solutions' may be an easy way out of the many transition dilemmas, but are generally insufficient to tackle the more fundamental causes of most sustainability problems. See, for instance, the 'Carbon Capture and Storage' (CCS) technology that is to reduce the amount of CO_2 -emissions coming into the atmosphere, by storing it into empty subterranean fields. Costly investments in CCS technology and (intermediary) infrastructure crowds out investments in more effective process innovations that minimize, or altogether preclude, carbon emission. The danger of naive techno-optimism lies in the path dependencies, unintended side-effects, sunk costs and blind spots it creates when a certain technology is introduced as the primary or ultimate solution for far more complex organizational, behavioural or systemic challenges.

- ***Labelling dilemma.*** Organizations often seek to distinguish themselves and inform their customers (and stakeholders) about their sustainability efforts through the adoption of (certified) consumer labels. The result is an overwhelming number of sustainability-related labels, which: (1) is confusing, (2) requires a lot of knowledge from customers in order to make an informed choice, and (3) may lead the average consumer to believe that labelled products are more expensive, of mediocre quality, or merely for the elite. How to deal with this ever-expanding labelling jungle without jeopardizing the organization's marketing need to offer a clearly distinguishable sustainable product or service?

- ***Leadership challenge.*** Post-conventional leadership for an 'active' corporate sustainability attitude requires a deeper understanding of context, greater insight in the interdependencies within and between systems, and higher awareness of environmental and social implications over longer time frames. Organisations that come out of a reactive position often need new leadership to enable change (see section 9.6, in *Principles of Sustainable Business*).

- ***Incumbent's curse***. Large incumbent companies – those with a dominant position in a particular sector – may block sustainable change because of vested interests in the 'old way' of doing business and embeddedness in established industry networks that don't necessarily value innovative societal ambitions. Incumbent companies struggle with sunk costs, the risk of their assets stranding, lack of adaptive capacity and the vast switching costs involved.

- ***Using stakeholder pressure appropriately***. Sustainability-minded CEOs or managers might actually use external stakeholder pressure to trigger internal change. Corporate leadership may purposely engage with critical stakeholders to create an internal 'sense of urgency', mobilize and activate their reactive organization, and realign it towards a more 'active' sustainable business model and CSR attitude.

- ***Richer value proposition***. Transitioning from a 'reactive' to an 'active' CSR attitude makes the development of a richer value proposition imperative. A 'narrow' or 'poor' value proposition, in general terms, is short-term oriented, instrumental, simplistic, risk averse ('don't do harm'), quantitative ('being the biggest'), company-oriented only and directed towards creating shareholder value. A 'broader' or 'richer' value proposition reflects how an organization sees itself positioned within society and its sector, its take on its fiduciary duties and responsibilities, and whom it considers primary and secondary stakeholders. It has a societal orientation, is directed towards organizational resilience (rather than growth), is inspirational and articulates how the organization wants to contribute to long-term value creation (see section 9.4 in *Principles of Sustainable Business*).

- ***Upgrading the business model - a broader value portfolio.*** A successful sustainable business model not only achieves a positive net-value in terms of profits (based on cost structure and revenue streams), but also in terms of social and ecological added value. In addition to creating, designing, capturing and scaling value (conventional CANVAS business model), transitioning towards an 'active' CSR attitude requires that organizations give substance to the value dimensions of the CANVAS 'Plus' model too: 'not destroying value' (addressing negative externalities), 'spreading value' (creating positive externalities), and 'sharing/co-creating value' (see sections 9.4–5 and Tool 9.2 in *Principles of Sustainable Business*).

More information: *GatMR*, pp. 97–114

3. INTERNATIONALIZATION [MOTIVATIONAL] 'BEARS ON THE ROAD'

The international dimension of organization-internal alignment on sustainability topics adds several strategic and operational International Corporate Responsibility (ICR 3.0) challenges to transitioning, including:

- ***Transfer pricing and tax scheme engineering***. Multinational companies may be tempted to manipulate internal transfer prices between their subsidiaries, shift debt, or assign profits to those countries of operation with the lowest tax rates or where they have the biggest lever on tax authorities (through 'rulings'). Companies that want to become more 'active' in sustainability should pay due taxes fairly and appropriately in the relevant countries, and support the OECD BEPS initiative to avoid that other companies become free-riders. They also need to rethink their internal transfer-pricing mechanisms in order not to deprive the countries in which they operate from sufficient income to invest in public goods (e.g., infrastructure, education, healthcare, housing, effective institutions), which is in the long-term interest of the organization too.

- ***Coordination, scaling and distance***. With regard to their scaling potential, multinational companies are well-positioned to propagate good ICR practice and experiences across and between their local subsidiaries. Internal alignment requires headquarters and subsidiaries to collaborate and learn from each other. However, the greater the 'distance' (e.g., geographical, cultural, administrative/governance/political, economic, institutional) between headquarters and the host country, the greater the span of control becomes. 'Active' multinationals have sophisticated management capabilities in place to timely address all distance dimensions, especially when they operate a broad portfolio of countries representing distinct CSR regimes (see sections 6.5.1 and 10.4.3 in *Principles of Sustainable Business*).

- ***Governance and funding***. Research on the relationship between 'governance type' and organizational capabilities for implementing ICR, indicates that large family-owned companies and cooperative organizations tend to be more capable of implementing coherent international sustainability strategies. They tend to have a richer value proposition and – due to their reliance on own capital – adopt a slower, more organic internationalization strategy, which is easier to coordinate and less susceptible to the short-term influence of anonymous shareholders.

- ***Cross-cultural leadership challenge***. Obviously, there are many cultural differences between countries, which makes it harder for international organizations to implement and coordinate their sustainability goals at a global scale. Global company leaders can choose between three strategies to manage the 'cultural distance' within their country portfolio: (1) they can try to find a compromise between the distinct values, orientations and social-cultural realities of each of the operating countries; (2) they can search for a synthesis that transcends the various cultures and develop 'hyper norms' (see Box 10.7 in *Principles of Sustainable Business*); or (3) they can restrict their portfolio to those operating countries that are culturally close.

- ***Global mindset.*** Dealing effectively with various cultures and a wide range of highly contextualized problems at the same time, requires a specific kind of mindset. It has been found that leaders with a 'global mindset' can make decisions and act appropriately in the face of many options. They interpret ICR challenges more as an opportunity than as a risk, despite the complexity and trade-offs involved. They have intellectual capital (attributes: global business savvy, cognitive complexity, cosmopolitan outlook, active interest in contexts), psychological capital (attributes: open and active, passion for diversity, thirst for adventure, self-assurance) and social capital (attributes: intercultural empathy, interpersonal impact, diplomacy).

- ***Resilience and dealing with setbacks***. The more complex internal and external alignment processes are, the higher the odds that critical observers will find cases of failure. Cynical NGOs will use indications of wrongdoing – especially those relating to big multinationals with global brands – as evidence of their fundamental distrust in companies doing good. In case of such setbacks, well-aligned companies will defy the inclination to immediately install stricter control measures to enforce compliance ('reactive'). Instead, they will emphasize that they recognize what is going wrong, what needs to be corrected and how, and what is going well but can still be improved – and act accordingly. An acknowledged track record of an 'active' and credible stakeholder engagement strategy is an important precondition for the trustworthiness of this approach.

- ***HR challenges***. Active rotation of senior managers between countries and management areas is a common practice that is part of global companies' internal alignment approach. Rotation builds loyalty and a strong company culture, yet also creates ICR implementation problems. First, the planning horizon is generally too short to effectively deal with sustainability issues in a particular location/country; appropriately addressing them usually takes more time than the typical 3-4 year rotation cycle. Second, knowledge about local operating conditions remains limited, which inhibits proper contextualization and an effective embedding of sustainability initiatives. Managers need an appropriate time frame to get to know their new country and learn about what approaches are effective, in order to avoid making the same mistakes as their rotating predecessors.

More information: *GatMR*, pp. 181–190