Environmental strategy: Six capabilities to avoid the big spill

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Six capabilities are identified as critical for creating value and establishing a competent, competitive and proactive environmental strategy.

"Environmental strategy" - the set of initiatives that a company puts in place to mitigate the impact of its activities on the environment - has become a crucial component of a firm's strategic management. Only recently have big corporations begun to place emphasis on energy conservation and the use of sustainable resources. The movement has given way to the natural resource-based view (NRBV) of the company, and thus has become the dominant theoretical paradigm in environmental strategy literature.

Back in the 17th and 18th centuries, colonial powers worried little about the environmental impact that their mining activities or rubber harvesting might be having on the societies in which they operated; the fact that thousands of people died as a result of their policies never met much resistance in boardrooms.

In more recent times, catastrophic events such as the 1984 escape of chemicals at Union Carbide's Bhopal plant in India and the 1989 Exxon Valdez oil spill off the Alaskan coast have served to galvanize environmental strategies among large companies, especially those participating in resource extraction. Such accidents, which cost billions of dollars to rectify, have convinced companies that having a better environmental strategy in the first place carries greater long-term benefits, not just in terms of saving money, but also lives.

Added to this are today's rising energy costs, which is making all companies, not just

resource extraction firms, revisit their environmental strategies. While there is much discussion around environmental friendly policies, there is little consensus over whether they achieve that at which they aim.

To help understand and measure environmental strategies, Judith L. Walls (Ross School of Business & School of Natural Resources and the Environment, University of Michigan), Phillip H. Phan (Carey School of Business, Johns Hopkins University) and Pascual Berrone (IESE Business School) studied more than 180 resource extraction firms from the U.S. S&P 500.

Their paper, "An Assessment of the Construct Validity of Environmental Strategy Measures," compares the standards of the natural resource-based view with strategies used by other researchers and establishes a valid environmental strategy system that firms can use to measure and predict their environmental performance.

Six environmental capabilities

A firm's NRBV can be established through a rigorous study of companies' annual reports. The authors categorized the data found in these reports into six major categories: historical orientation; network embeddedness - supply chain and stakeholders; endowments; managerial vision; top management team skills; and human resources skills.

The authors explain how each of these categories, or "environmental capabilities," is path-dependent and socially complex. For example, "a company's unique historical conditions of its establishment dictate how it acquires and exploits resources, and therefore how well it performs," the authors write.

Similarly, "the stakeholder network influences environmental strategy through social pressure and can determine the type of environmental strategy a company pursues."

Visionary leadership is considered a "unique capability" since good leaders do not grow on trees. As most successful environmental strategies depend on making long-term commitments and investments, visionary leadership is required.

Once those categories have been determined, the firm's environmental strategy can operate within the dimensions of NRBV. The paper sets out an environmental strategy guide for conducting future projects and considering investments.

Improved financial performance

The authors also attempt to determine the predictive validity of the environmental strategy, and whether this strategy is capable of creating value in terms of improved environmental performance.

Through analytical research and statistical equations, the authors provide the reader with a large database from which to measure environmental strategy. The environmental strategy put forth is a lead indicator of forward-looking strategies that companies pursue in order to gain competitive advantage.

While the results show that a strong environmental strategy can lead to an improved environmental performance and possibly an improved financial performance, the strategy can be utilized as a guide to future investments and environmental capability development.

And with natural resources diminishing rapidly in our world, environmental performance, rather than mere financial performance, may perhaps be the more urgent consideration.