CREATING PRACTICAL CONSUMER VALUE FROM SUSTAINABILITY

By Knut Haanæs, Catherine Roche, Jonathan Sharp, and Marty Smits

Green products are in vogue. Consumers are increasingly interested in products that use resources more efficiently. But outside certain niches, consumers have resisted paying the high prices that these products usually require.

In order to profitably connect with environmental concerns, companies in the home improvement sector are beginning to reorient green products around the direct material benefits to consumers. They emphasize savings more than green credentials.

A Challenging Opportunity

The housing bust of recent years further dampened what was already a mature home-improvement market. With household formation and home construction slowed, companies in affluent countries are eager for any area of potential growth. On the face of it, sustainability offers a great deal of potential, but converting theory into commercial viability is difficult.

Like companies in many other industries, home improvement companies have worked on improving the sustainability of their products. They've developed new lines and features and explored emerging technologies. But the results of these efforts have so far proved largely disappointing.

The Boston Consulting Group's annual survey of executives worldwide, conducted jointly with *MIT Sloan Management Review,* indicates that most companies have changed their business practices in order to boost sustainability. Yet only 40 percent of the respondents from a variety of consumer goods businesses say that they have figured out how to boost sustainability *and* make a profit.

Similarly, a corresponding survey of consumers found that most were interested in buying green. But only 8 to 16 percent, by region, did so systematically, and these numbers have fallen with the global recession. High prices were cited as the major constraint in affluent countries, while in emerging markets, high prices ranked a close second to lack of availability. The vast majority of consumers just aren't willing to pay extra for sustainability for its own sake.

Adding to the challenge is consumers' confusion about what *sustainable* really means. A variety of terms get bandied about: low impact, energy efficient, renewable resource, local, and fair labor. Other feel-good concepts, such as healthfulness and "artisan made," get thrown into the conversation. The sustainability discussion can involve environmental, economic, and social resources. No wonder consumers are skeptical.

Breaking Through

Yet some companies in the home improvement sector are working on ways to make green profitable. The key, they have found, is to clarify and reposition the category of green products and services. Instead of sustainability for its own sake, companies need to offer concrete, direct-to-the-consumer benefits. A feel-good option must also become a rational consumer choice.

The first step is to pick one's battles. Sustainability can be compelling only in certain cost-benefit contexts. Basic consumer interest in sustainability can help tip the decision balance toward buying green, but it can't work by itself. Reducing carbon emissions, for example, is a worthy goal, but consumers are far more motivated to save on energy and water bills. Government regulations, subsidies, new technologies, and higher energy costs all work into the mix.

Just look at the success of the Energy Star program for household appliances in Europe and the U.S. Governments have mandated that manufacturers report the energy efficiency of their appliances and estimate consumers' likely savings on utility bills. A model whose performance falls within a certain range can be called an Energy Star. In certain categories, the government or local energy utility grants rebates to consumers who have bought those models. The program has encouraged manufacturers to give greater consideration to efficiency-boosting technologies such as reconfigured dishwasher drums that use less electricity at the cost of a longer cycle time. Energy Star appliances have also gained space in retail showrooms. Special markings on the appliances even promote "conspicuous conservation," appealing to people inclined to show off their virtue to visitors to their homes.

As a result, consumers who never before would have paid attention to energy efficiency can easily include this appliance attribute as a buying criterion. Those who live in areas with rising electricity rates have had the greatest incentive to buy these appliances. The overall energy efficiency of household appliances has risen dramatically under the program.

Focusing Green Products on Consumers' Concerns

In areas for which the cost-benefit ratios are favorable, companies still need to make the financial benefits easily understood by and relevant to consumers. That means focusing the products on what consumers care about and can relate to.

In most European Union markets, many of the programs for reducing household carbon emissions include subsidies for low-carbon energy generation (such as solar energy), subsidies for home insulation, and regulations that require the measurement and certification of the carbon emission status of houses for sale. In today's regulatory environment, the carbon-reduction home-improvement market is likely to grow significantly, generating many billions of dollars of new spending.

In order for retailers to go after this opportunity, they will need to develop their sales packages in a number of areas.

Customizable Options. Retailers need to develop a customer-friendly menu of options to match the variety of housing structures, energy costs and subsidies, and customer preferences. These options should allow homeowners to customize their purchases according to their available time, money, appetite for risk, and underlying interest in sustainability. This approach will also help retail-sales teams understand and communicate product features and benefits.

Specific Savings Estimates. Furthermore, retailers will have to demonstrate that these home-improvement purchases would be rational investments with financial payback. For most households, even with subsidies, such investments are big purchases, amounting to thousands of euros. Retailers cannot guarantee actual savings in energy bills, but they can show how the improvements would raise a home's ratings in the certification program for home sales, and they can explain the impact these changes would have on typical energy bills.

Convenient Installation. Price is not the only hurdle to conversion. Homeowners also weigh the inconveniences and risks of installation. Retailers need to establish a network of home surveyors and installers.

Long-Term Financing. A final barrier to sales in this market is the insufficient availability of financing for homeowners. Because of the long time between purchase and payback, new consumer lending products are needed to fund these projects.

As these markets develop and well-prepared retailers increase their share in them, product costs can fall rapidly. In Germany, for example, a better organized and more efficient solar-panel distribution chain led to prices falling 30 percent from 2004 through 2006, and another 30 percent from 2006 through 2009. The installed base of solar-panel capacity more than quadrupled as consumers reacted to the lower prices.

Timing the Market

Because these products and services are expensive and complex, manufacturers and distributors should proceed carefully. They should look carefully at the three key drivers in the marketplace: government requirements and incentives, local energy and water costs, and underlying consumer interest.

The importance of each driver varies a great deal by location. European countries, for example, are promising markets for energy, while Australia may be a leader in efforts to conserve water.

The drivers are evolving and their importance can change fast—moving in either direction. Concerns about sustainability have certainly increased in recent years. Yet the global recession has led many governments to pull back on sustainability initiatives.

A wait-and-see strategy, however, has risks as well. Aggressive, well-prepared first movers in this category can establish distribution networks, set standards for product packages, refine their selling and service models, and learn about household needs. Rivals would then have a harder time getting consumer acceptance for what they bring to the table. If a pioneering strategy seems too risky, companies should consider preparing now to jump in as fast followers.

Companies will also have to balance sustainability programs with other opportunities. Expanding into developing countries is on everyone's agenda, but expansion carries its own risks and complexities. In many sectors, the sustainability market represents one of the few organic domestic large-scale growth plays.

Whether because of stakeholder pressure, public image, or executive conviction, most companies have embraced sustainability as a concept and are searching for a hard business rationale. By orienting their products around solid consumer benefits—admittedly a less inspiring mission than saving the planet—companies can drive the strategic and organizational responses needed to make these efforts profitable. And that's the only way sustainability programs will themselves be sustainable.

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6/12