

## **HANSA PODCAST – EPISODE 003: SUSTAINABLE GROWTH – WHY EVERY BUSINESS SHOULD MAKE IT A PRIORITY**

In our previous podcast we discussed the topic of how to value your business. As a continuation of that topic today we will discuss sustainable growth. You may wonder what the link is between valuation and sustainability we will address that in this podcast.

We are very passionate about sustainable growth and sustainability and we would like all SME's to embrace the concept and build better businesses.

Most business owners we meet find it easy to understand growth. But the word 'sustainable' is something they don't understand. They usually think its some management jargon or a PR jargon we are using to look good.

We have structured today's podcast into three sections

1. Understanding what 'sustainable growth' means and why it should become a priority for all businesses
2. We will give you 8 practical tips to pursue 'sustainable growth'
3. We will explain 3 things you should avoid when it comes to sustainability

So let's start get into the first section, which is...

### **Section 1: Understanding what 'sustainable growth' means and why it should become a priority for all businesses**

The term has two parts to it 'sustainable' and 'growth'. Let's first understand the meaning of word 'sustainable'.

The term 'sustainable' is not new. It has always existed, and most people are aware of it. The goddess of wealth in Hindu religion is called Lakshmi Devi. And if you ask people in India what Lakshmi stands for the most common answer is 'wealth' and money. But this goddess has 8 forms called as 'Astha Lakshmi'. 'Astha' means eight and all these 8 forms provide things that create a sustainable life. These include good health, food, knowledge, family, courage. To lead a sustainable life you need all these and that is the definition is 'wealth' that goddess Lakshmi provides.

When it comes to businesses the same principles apply. You create businesses to generate profits and create wealth but in the process of doing that you need to consider people or society, and the environment. This holistic approach to business is what we call 'sustainable'.

For a long time we have had excessive focus on the profit and have ignored social and environment aspects. But we have reached a point where that needs to be corrected and it needs to be corrected with a sense of urgency.

To make this more specific the UN (United Nations) has defined 17 sustainability development goals. I would urge all of you to google the term 'SDG' and read more about the 17 UN sustainability development goals.

We spend a lot of time with SME's owners, management teams, employees, workers, and their customers and to some extent understand the reality of small and medium sized businesses in a developing country. At the same time we have worked extensively with global sustainability experts, investors, fund managers and also understand their perspective. So while we understand the global approach and definitions of sustainability we are firmly rooted in local reality of doing business in India.

Most people we speak to in India understand sustainability as CSR (or corporate social responsibility) type of work or Non-profit type of work. This is a common misconception.

In India the companies act of 2013 defines that all companies above a certain size should allocate 2% of their net profit to CSR initiatives. You can see the annual reports of most listed companies in India and you will see a lot of good work done in CSR. We have recently reviewed an investment case whose business model was to take a share of these CSR funds in companies and allocate them to achieving a certain sustainability development goal. But the point here is that the CSR work that these companies are referring to is something that is not related to the main business. The main business could be a construction business and they could be building a lot of schools as part of the CSR work. *Sustainability that we are referring to forms the core business model. Its not something you do on the side. For example if the construction company starts pursuing affordable housing projects then sustainability becomes core of its business model.*

When we talk about environment and taking care of employees, many people feel that they are already doing it. And they are absolutely right. But the approach is that of compliance. Companies and governments have long focused on this and there are strict regulatory guidelines to adhere to. Take the case of pollution (air or water), we have a pollution control board of India which monitors this in all industries and sets emission standards. They conduct regular audits and without their permission most large projects cannot start or industries that are not conforming to the set targets can be closed. *Our definition of sustainability is much beyond complying to regulatory norms.*

So in summary 'sustainable' refers to a business that is pursuing profits but is also taking care of the social and environmental aspects. Also the core business model of the company is addressing one or more sustainability development goals defined by the UN.

Now lets understand the meaning of the term 'growth' in this context.

Most people are aware of global mega trends like climate change, rapid urbanization, pollution, scarcity of water, demographic changes, and technology disruptions. Many of these mega trends have become an every day reality for people living in cities like Delhi because of very bad quality of air they have to breathe everyday. It's a reality for people in the city of Chennai in India who are facing an acute water shortage. So the common man and society at large are worried about themselves and their future. This worry is resulting in fundamental changes in what people buy, whom they want to do business with, where they want to invest their money. Take the example of an Indian consumer products brand called Patanjali. People are worried about their health and want to lead a healthier lifestyle. When a company addressed that need at an affordable price point, people rapidly adopted their products. The company reported sales of more than 10,000cr or 100billion rupees in 2017. There are many more such examples of companies that have understood this fundamental shift in consumer preferences and are making use of that to enable growth.

Sustainability is a global mega trend resulting is several new growth opportunities and business models. That's the reason SME's should make 'sustainable growth' a priority. I recently visited Norway. The last time I was there was in 2016. A friend of mine in Oslo asked me what the biggest change I saw in Oslo. I told him that it was the EV's (Electric Vehicles) on the roads. I saw so many Tesla's and VW E-Golfs on the roads. Tesla is a great example of benefiting from the mega trend when it comes to using renewal energy and reducing emissions from automobiles. Its market cap is above 40 billion dollars.

In the last few decades, technology has fundamentally changed the way we communicate and has resulted in new business models and many established companies have been disrupted. Focus on sustainability will do the same in the coming years and decades. Industries and business models that are not sustainable will not survive.

Having understood what 'sustainable growth' means lets understand how an SME business owner can work towards achieving that.

## **SECTION 2: 8 things you can do to achieve 'sustainable growth'**

1. **Leverage mega trends in your niche for GROWTH.** In your specific domain look at the mega trends and see which specific trend you can benefit from. We worked with an IT services company which was catering to the needs of global customers. There were about 200 employees in that business – so it was pursuing the sustainability goal of ‘creating decent work’. We identified an innovation in that industry which significantly reduced construction project costs and brought about transparency into large projects. This innovation was then made the focus of future growth and that how the core business model become more sustainability focused. Many businesses will face this challenge that what they are addressing right now is commodity products or services and so you will have to do that exercise of identifying the mega trends in your domain and see what you can do to better address them. Pursuing new things is a big risk in most SME’s but its better then gradually becoming an unviable business.
2. **Improve governance to reduce RISK.** We met a business owner recently who said that they recruited someone in their Board who comes with a lot of experience in a large company. He was paid a big fee each month but this person has no understanding of the realities in his business. He felt it was a complete waste of his money to have such people. Most people underestimate the power of good corporate governance, of external experts, of new ideas, and of an opinions from someone who is not lost in operational details. Most Indian businesses appoint company secretaries to take care of all their compliance work in Boards – that’s their understanding of corporate governance. *If you need fresh new ideas about sustainability, if you need oversight about strategy creation and execution, if you need someone who can review the business owners’ limitations you can use corporate governance as that tool. So go ahead and do that.*
3. **People = Profit;** Treat your people well and they will in turn treat your customers well. Profits will follow. But if your focus is on profits only without taking good care of your employees then you will never build a sustainable business model. An extraordinary example in this regards is an entrepreneur whom we met an year ago. He manages a high growth business which is doubling each year and reached the 100cr sales level. He is blind from birth. He employees mostly blind people in his company and one of his mottos is that we also employ able people. He has created a business model that is disrupting their industry. It’s a great example of creating superior businesses by also taking good care of your people. *There are simple tools that can use to empower people in your organization and that will in turn drive innovation, growth and profits.*
4. **Recruit more women in senior positions.** We have met 50-60 companies in the past year and have come across 4-5 women in key decision making positions. Most promoters spouses and children are listed as directors in the companies – it’s a common thing in India but they don’t have any active role in decision making. I attended a conference in Oslo in April 2019 and it was about having women in senior positions in investment companies. Even in the most progressive countries, in some industries the ratio of women at decision making levels was less than 10%. They had mentioned about a research that showed that having more women in decision making roles leads to better decisions and hence better results. *There is significant potential to recruit more women in companies in senior positions. Create the right kind of environment to facilitate that.*
5. **Get access to specialized funding** – At the beginning of this podcast I mentioned that I will tell you about the link between valuations and sustainability. I will do that now. Impact investing has become very popular these days. Why is that the case? Have many investors suddenly started thinking about investing in good causes. The answer again lies in changing preferences of people that I had mentioned earlier. The biggest investors in the world are pension funds and insurance companies. Their customers are ordinary citizens, teachers, factory workers, and nurses. These people are also worried about sustainability and want their pension funds to be invested in a socially responsible manner. That is putting pressure on investors to create special funds to invest in certain sectors and that is leading to the creation of Impact Funds. But that is the case as of today. Very soon, the difference between investing and impact investing will vanish. Today’s impact funds are looking for investments in specific sectors like clean energy or micro-finance, healthcare etc . If you are in that space, your chances of getting funding from such investors is higher. Given the size of opportunity that sustainability presents the valuations can also be

attractive. *Every business owner should have a good knowledge of the investors that focus on their space. A good source of who those investors are, are the newspapers. Keep making note of such investors and get in touch with them. Investors may say no to your current proposal but its good to understand their focus and investment criteria.*

6. **Access to talent:** The most important resources required for growth is people – most owners think its capital but we feel its people. I spoke to you about changing preference among people and that is much more prominent among younger generations. The challenge here is that the owners of most businesses are 50+ where as the bright talent with fresh new ideas are in their 20's. These younger generations want to work for companies that are socially responsible. *To attract talent you need to highlight what you are doing in the company to be socially responsible and to retain them you will have to be genuine about that, else they will leave you.*
7. **Have good mentors:** I was very fortunate to have two extremely well-informed mentors from whom I learnt about sustainability and how to practically implement that in businesses. My first mentor is Knut Kjaer who was the CEO of the Norwegian pension fund and also helped launch the Principles of Responsible Investing at the UN. My second mentor is Frode who is the managing partner of FSN Capital, who taught me on how to make sustainability as a priority in a business and implement that into every process. So Knut and Frode, if you listen to this podcast, a big thanks to you. *Similarly, we encourage SME business owners to choose mentors who have some experience or interest in sustainability. Gather new ideas and gradually work towards making sustainability the core of your business.*
8. **Live the sustainability values in your own life –** Someone recently asked me, that most companies have values statements – do they serve any purpose?. My answer was that if those values don't reflect the values that the owners demonstrate on an everyday basis in their interaction with employees, customers, and investors, the values are not worth the paper they are printed on. If 'Integrity' is a value of your company but you don't act with integrity then it means nothing. Same is the case with sustainability. *If you are not living a sustainable life, they will also not reflect in your business.* Mr. Motilal Oswal is an accomplished businessman in India. I follow him on twitter and today morning his tweet was "There are very few people who are successful, wealthy and happy. U need to decide what makes you happy'. We believe that pursuing 'sustainable growth' will ensure that you will lead a happier life.

In this section we told you some practical things you can do to pursue 'sustainable growth'. We will end this podcast with 3 things that you should not be doing.

### **SECTION 3: 3 things you should avoid doing when it comes to sustainability**

1. **Avoid Greenwashing:** Greenwashing is a phenomenon where you claim to doing something sustainable but actually that's may not the case. Most companies project themselves as clean and green companies but they are the most polluting companies, violating even the basic norms. When it comes to clean energy or organic products the regulations are still weak and so many companies are taking shortcuts and launching substandard products. Don't do that. Look of artificial intelligence in tech start-ups. Almost every start-up company claims to using AI. When you take a closer look at their basic software functionality that is usually not the case. So avoid greenwashing and pursue sustainability in a genuine way.
2. **Being sustainable is not about being unprofitable:** We have looked at several businesses in the renewable energy space in India. Many have experienced rapid growth because they are several government funded projects. But the business models are still not fully established and most of the business models are unviable. When a new sector opens up, the barriers to entry are low and a lot of technical people rush into setting up businesses. Many of such businesses will get funded because there is a dearth of such investment opportunities but that doesn't mean that the business model is viable in the medium to long term. Some of the experts in the field of sustainability are of the view that their definition of impact investing is investing in companies

with low returns on capital. For example an investor we spoke to recently mentioned that they don't invest in companies in the south or west of India. They focus more on the companies in the North and East of India as they don't have access to funding and capital. It take all types of companies and investors to address the big sustainability goals. *As far as SME's are concerned, focus on sustainability but always build profitable and scalable business models.*

3. **Don't get lost in jargon related to sustainability – focus on making a real impact:** Many companies and investors are lost in jargon like CSR, ESG, Impact Investing, sustainability development goals (SDG's), Principles of Responsible Investing (PRI), Sustainability Metrics etc. This has also become a big business in itself. Don't get lost in this jargon. I will end this podcast with the example of a very good friend of mine who is also an impact investor. His name is Anders Lier. Anders played a key role in establishing Araku Coffee which sourced from India as is now a premium coffee brand in Europe. Anders is making an attempt to create a more sustainable livelihood for coffee farmers in Araku (it's a hill station close to Visakhapatnam in Andhra) and have created a successful 'for profit' international brand. *As the owner of an SME business focus on sustainability as a mega trend and use that to scale your business.*