Sustainability: Myth, Madness, and Magic

DON ANDERSON
CHIEF SUSTAINABILITY OFFICER
EXECUTIVE DIRECTOR, PORTFOLIO OPERATIONS
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Sustainability

Smart investments in environmental sustainability can be win-win propositions for businesses. Improving environmental performance can help reduce energy costs and improve efficiency, while also helping address Environmental, Social, and Governance (ESG) concerns from customers, investors, and other stakeholders.

Nonetheless, many companies fail to deliver effective results – either from a bottom line or environmental perspective – when pursuing sustainability initiatives. That raises the question: Why do so many companies fail to get a strong return on investment from their sustainability efforts?

Blackstone’s position as a leading global asset manager provides a unique perspective on that issue. Our private equity business alone has 81 portfolio companies with more than 500,000 employees across a diverse set of industries and geographies. Our real estate business has one of the most expansive residential and commercial footprints in the world. These businesses collectively represent a telling cross section of the global economy.

Based on that wide-angle lens, we are able to produce evidence-based insights into what works and what doesn’t in driving better environmental results.

The Blackstone Approach

Blackstone’s approach to sustainability is directly tied to our business mission. By more efficiently managing energy and water use, and reducing waste across our portfolio of companies, we can achieve significant cost savings that create value for those companies and, in turn, our investors. This also delivers benefits to all stakeholders in terms of environmental sustainability.

In short, we pursue measurable, action-oriented operational interventions that improve a company’s bottom line and its impact on the environment. We consistently stick to this simple formula.

We care more about impact and less about popular jargon. Surprisingly, we find we can move fastest and have the deepest impact by framing these efforts as part of our broader mandate to improve a company’s operations rather than applying labels such as “green” or “sustainable” that cause some managers to tune out, compartmentalize, or bucket these efforts as tangential, rather than mission critical.
For Blackstone, the decision over six years ago to add energy performance as a sixth, distinct category of intervention for our Portfolio Operations Team (“Ops Team”) was easy – utility costs are significant and controllable for many of our portfolio companies, cost savings drive EBITDA growth, and investors respond well to our approach and associated success. Like our other categories of intervention, it was a sound business decision based on fiduciary responsibility. We like the results from an operational standpoint, and continue to strive to stay focused on that objective as “true North” for our sustainability efforts. The fact that our efforts result in more sustainable companies and better environmental outputs wasn’t lost on us, it just wasn’t the sole focus.

Many companies start from a different place, of course, and in doing so may tackle sustainability in a way that is costly and does not ultimately improve performance. The following three examples (each representing more than one year of corporate time, effort, and expense) demonstrate how easy it is get distracted and not achieve real results.

- **Company One:**
  Interested in carbon trading, a US-based manufacturer engages a consultant whose first question is, “How is your data?” Many months and a lot of money are spent collecting data from various divisions and regions to allow the calculation of a proper “carbon footprint”. While this is happening, a separate “green team” with representatives from across the firm simultaneously ponders the question: “What does sustainability mean to us?”

- **Company Two:**
  Having hired a senior, full-time sustainability lead, a massive global real estate portfolio owner and manager creates a stakeholder-facing website focused on sustainability. They join a number of organizations dedicated to environmental performance improvement and public disclosure. Then, they run a Request for Proposal (RFP) process to select a vendor that can produce a web-based tracking solution to mitigate risks surrounding the quality of disclosed carbon emissions data.

- **Company Three:**
  A foreign manufacturer develops a carbon calculator, but their development team does not build in support for environmental impact, baselines, performance improvement, emissions mitigation, energy efficiency, utility cost savings, or carbon footprint reduction. They clearly heard their customers’ requests for carbon footprints, and hope that many of their thousands of environmentally concerned customers will pay to use this tool as a calculator. But this company (and their environmentally concerned customers) missed the potential to drive performance improvement.

None of these activities reduced these firms’ environmental footprint, produced cost savings associated with reduced energy use, or created a corporate culture for future impact. They also did not meaningfully impact core business. As such, none of these activities would qualify as first-tier interventions for Blackstone’s Team. That is because they are not direct paths to performance improvement for any company with action-oriented leadership and results-oriented stakeholders.

The current concept of “sustainability” is difficult for senior leaders to operationalize. Well-meaning, full-time corporate sustainability leads, a relatively recent phenomenon, often do not have business or operational backgrounds adequate to drive fast, measurable change. In the worst-case scenario, these professionals seek to educate and convert core business leaders rather than first seeking to imbed measurable, high return-on-investment (ROI) strategies that drive earnings and improve environmental performance.
Myths and Madness

If you peruse the web for key concepts associated with sustainability or solicit proposals from sustainability service providers, you will hear some consistent themes that have been around for well over a decade. At first blush, these make sense. One would expect proven best practices to emerge over time with the benefit of hindsight and experience. However, in the end, these strategies do not motivate action or deliver results with the same intensity expected in a business transformation setting. That is why we consider them to be “myths and madness” associated with sustainability.

- **Myth One:**
  “We need a Green Team” – A team assembled with representatives from key departments across a firm, tasked with defining a corporate position on sustainability and associated options for activity, seems like the right way to put a toe in the sustainability water. But these teams usually have no budget or authority, and, by definition, are kept separate from existing core business initiatives. If the urgent mandate is to quickly and dramatically reduce environmental impact followed by continuous improvement over time, this approach will be costly in both time and focus. And worse, when business or economic headwinds emerge, Green Teams will be the first to disassemble in favor of core business needs.

- **Myth Two:**
  “This will cost money” – The marketplace for sustainability services, specifically regarding energy performance, is dominated by companies selling services, technology, creative financing, and shared savings deals that make it easy to commit capex. At the same time, EPA’s Energy Star Program conducted studies using performance data from U.S. buildings that showed weak correlation between energy performance and the presence of energy efficient technology. In fact, if a company does not have structured leadership around efficient operations and maintenance of key mechanical systems, new, potentially efficient equipment can actually exacerbate inefficiencies by introducing new challenges for unsophisticated operators.

- **Myth Three:**
  “It should be easy to get the right data in front of the right people” – Environmental performance improvement, whether measured in reduced carbon footprint or reduced energy costs, demands accessible tracking over time. Corporate accounts payable and accounting functions usually handle payment of utility bills. They are the best source of both consumption and cost data, but are often reluctant to give up control of this responsibility and unequipped to share data in a useful format on a routine basis. And these functions may not move at the same rhythm as operators that influence energy consumption. Data over time may be challenging to access or may aggregate too slowly to provide a useful enterprise view. The worst case for companies that have never viewed energy as a controllable cost is that these data points can be the equivalent of utility bills in a shoebox. Never underestimate the challenge of putting useful, complete data in the right hands at the right time on a routine basis.


WHAT’S WRONG WITH SUSTAINABILITY TODAY?

The current concept of “sustainability” is difficult for senior leaders to operationalize. Well-meaning, full-time corporate sustainability leads, a relatively recent phenomenon, often do not have business or operational backgrounds adequate to drive fast, measurable change.
**Madness**

- **“We need to start with a carbon footprint”** - Climate scientists initiated the careful process of carbon accounting to get a “carbon footprint.” This has been absolutely critical to ranking the environmental impact of power plants and other electricity generating options, and to estimate regional and global carbon emissions, past and future, along a timeline. But at some point, carbon scientists and enthusiasts determined that they could also footprint products, events, buildings, factories, people, and corporations. This shift was accompanied by the ability to “offset” carbon by purchasing others’ achievements; the concept of “carbon neutrality” where enough offsets are purchased to claim zero emissions; and the ability to trade carbon on the open market. These activities are unlikely to be associated with quickly moving a majority of global businesses to a sustainable position associated with improved business practices that deliver investment grade upside and increased earnings.

For corporate leaders seeking fast environmental performance improvement, carbon footprinting presents the following challenges: it is fussy, requiring special consultants with their own new language; it is disconnected from operators; unlike utility bills, which are ubiquitous, carbon data is not close to being useful for performance benchmarking; and, its value compared to more accessible and accepted metrics (again, energy consumption and utility costs) must be continuously argued based on limited evidence. There is much debate as to whether Carbon is a well-supported, conventionally accepted Key Performance Indicator (KPI). When companies are faced with a wide variety of urgent operational interventions, introducing carbon as a focal point can either delay or prevent real environmental and cost impacts at a time of maximum potential for measurable change.

**PROS AND CONS OF CARBON FOOTPRINTING**

<table>
<thead>
<tr>
<th>PROS:</th>
<th>CONS:</th>
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<tbody>
<tr>
<td>Raise awareness on pollution levels</td>
<td>Costs time and money to educate, collect data, and calculate</td>
</tr>
<tr>
<td>Estimate regional and global carbon emissions</td>
<td>Misses change over time, may mask progress in a fast-growth setting</td>
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<tr>
<td>Measure environmental impact of energy production facilities</td>
<td>Disconnected from operators that already use energy data</td>
</tr>
<tr>
<td>Spur investment and innovation in clean energy tech</td>
<td>Disconnected from leadership that already use utility spend</td>
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<tr>
<td></td>
<td>Carbon data not yet useful for performance benchmarking</td>
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Somehow, carbon has become the maypole for the sustainability community and the “E” in ESG, including attempts to make public disclosure of carbon footprint a mandate associated with corporate transparency. This can be a distraction from simpler and more direct paths to better operations and maintenance and real environmental impact. Since most successful private equity arcs include a growth mandate via market expansion, M&A, and/or increased throughput – the best deals actually can increase footprints despite significant success in improving environmental performance. When looked at in total, any private equity portfolio is perpetually in flux with new acquisitions and exits. So when footprints are shared or tracked over time, caveats and context are essential and results may not tell a useful story.

- **“We haven’t yet reached the point where this matters”** – A final piece of madness – the prevailing, inclusive definition of sustainability is easy for traditional business leaders to dismiss, at a time when many millennials care intensely about environmental impacts. In some sectors, HR has determined that talented young candidates will turn down a job if the company’s environmental sustainability record is not strong and consistent. In other sectors, a compelling sustainability position is desirable for many buyers and customers.
Magic

The following examples from Blackstone’s playbook were selected to take the mystique out of results-oriented sustainability and demonstrate to senior leaders what a fast, upside-oriented, operational approach looks like. Our first-tier interventions can deliver more than 15 percent energy usage reduction without significant expenditure, and have proven perennially successful in over three decades of support to corporations seeking energy efficiency and associated cost cuts. Some of these are so simple and obvious that they elicit eye rolls from operators and service providers, but experience has shown repeatedly that these are the last places routinely leveraged to achieve fast savings. Low-hanging fruit grows back. Since businesses typically run fine without addressing these issues, leadership and persistence are key.

Strengthening the case beyond “sustainability,” focus on operation and maintenance of key mechanical systems does more than save money and improve environmental performance. These interventions increase resilience, support growth initiatives, reduce safety risk from equipment failure, and speed management alignment during M&A. They also make for impressive anecdotes for stakeholders. And, most notably, these examples represent an easy path to earnings growth in cases where other options are more challenging.

Focusing on the following three categories can allow a motivated leader with no experience with sustainability to kick off a program tomorrow:

1. **Handheld Tools** – Fully leverage the recent revolution in better, cheaper, and smaller tools that improve engineers’ visibility into performance issues.

2. **Motivation and Verification** – Fundamental to all transformational initiatives, this approach creates a clear path to improvement and a view of who is on that path.

3. **Control of Outdoor Air** – Expensive to heat, cool, and dehumidify to meet human comfort requirements, this is usually the Achilles heel in an otherwise well-controlled office, hotel, or retail space.

*Steam in the air is a tell-tale sign of energy waste in industrial settings*
1. Routinely Deploy Handheld Tools

Unlike the telecom revolution, this has been largely missed by real estate and industrial operators. For example, infrared cameras cost around $50,000 apiece in the 1980s and were the size of a small child. Now, for $250, you can get a plugin for your iPhone. These tools can find: gaps in roof, wall, and pipe insulation; bad motor bearings before they fail; roof leaks before water enters the building; unsafe electrical panels before anyone gets hurt; plus any number of temperature-related conditioning, hot water, and steam issues. Despite this, it is still atypical to find infrared cameras and a suite of similar tools driven by “PMs” – preventive and predictive maintenance tasks that are completed on a set schedule by individuals that are formally held accountable. Blackstone has assembled two kits – one for industrial sites (around $20k worth of tools), and one for offices, hotels, and other assets (around $4k worth of tools). These are eagerly received by operators who are properly trained to routinely use them. We often see a return on investment from these strategies within days or weeks of deployment.

Handheld tools are simple, easy to use and deliver valuable information to operators

WHAT KIND OF TOOLS DOES BLACKSTONE USE?

A revolution has occurred in the availability, size, and pricing of a variety of handheld tools, dataloggers, and meters – these can fundamentally change how operators “see” building and industrial systems.

The toolkit contains a common set of tools that are low-cost and easy to utilize.

DATA LOGGER
(Temperature, Humidity, and Lighting Levels)

DATA LOGGER
(Magnetic Field)

DIGITAL/LASER THERMOMETER

MULTI-METER WITH AMP CLAMP

INFRARED CAMERA

PSYCHROMETER/IAQ METER

ULTRASONIC LEAK DETECTION TOOL

HOTWIRE ANEMOMETER
2. Motivate and Verify Good Practices

The Blackstone Operations Team leverages unique synergies between sustainability and procurement. In particular, we place our larger energy using portfolio companies on Schneider Electric’s global energy procurement platform to obtain better pricing for electricity and gas while also improving our global view of energy usage across our portfolio. This relationship typically touches around 20 of our portfolio companies and 80 percent of our total energy consumption (which equates to carbon emissions). As a result of this relationship, these companies’ monthly consumption and spend data get loaded into a database that is web accessible via Schneider’s fully featured Resource Advisor tool. Because of the scale of our business with Schneider, we have been aggressive and instrumental in improving this platform to support performance improvement efforts. The result is notable program assets that could otherwise cost each company a lot of time and money:

- Utility bill payment is outsourced and automatic, eliminating late fees and billing errors, and ensuring that data is logged in a timely manner;
- Our companies can track their cost and consumption reduction efforts over time;
- Dashboard views have been designed to track the progress of companies’ portfolio-wide programs;
- A scorecard module tracks leaders and laggards as they perform key program interventions;
- A survey module allows scorecard updates to be collected monthly, automatically and via email, from each site;
- Leader / laggard scatterplots, regression analyses, benchmarking, and weather normalization assist companies in both proof of concept and focus at a programmatic level;

In combination, this set of capabilities forces portfolio-level – not just site-level – thinking, allowing Blackstone portfolio companies to drive a homogeneous playbook approach across all sites, usually for the first time. In our experience, this is a big managerial shift. If the right low- and no-cost opportunities are selected, over 15 percent performance improvement can result. Additionally, carbon footprints are available at the push of a button for our companies whose stakeholders demand this information, based on Schneider’s up-to-date, global database of emissions factors.

Display signage on the factory floor can lead to most consistently executed best practices
3. Control Outdoor Air

All buildings need to supply fresh, outdoor air, both to replace air that is exhausted from rest rooms, kitchens, and industrial operations, and to prevent the buildup of carbon dioxide associated with human respiration. Across much of the U.S., it is also possible to use outdoor air to provide cooling, reducing energy costs associated with the use of mechanical cooling equipment. In most cases, the timing and amount of outdoor air brought into buildings is poorly controlled – outdoor air dampers remain open when they don’t need to be, fans run 24/7, and opportunities for “free cooling” are missed. Put another way, it is rare to find a building of any kind that is handling outdoor air as designed or in the most environmentally or cost effective manner. This is usually a result of operator intervention (control systems overrides, dampers propped open), neglect (invisible problems often ignored by busy operators), and hardware failure (dampers and actuators rusty and inoperable). Since outdoor air needs to be heated, cooled, dehumidified, or humidified upon entering a building, poorly controlled outdoor air is among the most expensive (and least discussed) issues associated with environmental performance. The following low- and no-cost interventions, from easy to advanced, are almost always a dominant element in performance improvement at Blackstone portfolio companies:

1. Shut off fans and close dampers whenever occupants are not in buildings. We accomplish this via automated controls and prevent control overrides and mechanical failures (dampers, actuators) that commonly thwart this simple strategy.

2. Maximize the use of cool outdoor air anytime it is adequate to reduce or eliminate mechanical cooling, and as in #1 above, ensure that this automated function is sustained over time. Once a company has mastered this, it should take on “precooling” of building mass so that mechanical cooling “startup” demands are reduced when occupants enter buildings.

3. Deliver the right amount of fresh air to occupants. CO2 sensors are cheaper and more reliable than ever and can be tied to the building control system to allow just the right amount of fresh air to be brought into buildings.

Not only will these recommendations save money, but they will also extend equipment life and ensure occupant comfort and safety.

**HOW IMPORTANT IS FRESH AIR?**

*All buildings need to supply fresh, outdoor air, both to replace air that is exhausted from rest rooms, kitchens, and industrial operations, and to prevent the buildup of carbon dioxide associated with human respiration or carbon monoxide associated with cars and trucks.*

For large multifamily properties like Stuyvesant Town - Peter Cooper Village, benchmarking comparative performance can drive intervention and result in recognition of excellence.
Is Private Equity Sustainability Sustainable?

Blackstone’s focus on “the magic” of action-oriented sustainability has yielded considerable results and critical lessons. Although we continuously learn from experience, these examples prove that our position allows us to scale, act nimbly, and start fast out of the gate. And this approach is replicated again and again across our portfolio companies:

- **Playbooks** - Playbooks codify good practice, including dashboards, scorecards, PMs (utilizing Toolkits), and guidance on finding and fixing low- and no-cost operational and maintenance issues. These are easy to explain to CEOs, CFOs, COOs, and operators as conventional elements of business transformation under a Blackstone investment. And, as a structure, every company can integrate their best practices and get started.

- **Summits** - We have held over a dozen “Summits” and conferences where COOs or operators from many companies are brought together to learn how to launch and run a performance improvement program. This is completely different from the more common service provider approach of single-site audits, and it allows the type of networking and knowledge share that is unique to PE’s aggregate owner model.

- **Legislation** - In response to the EU Energy Efficiency Directive (EED), we were able to quickly organize two events in London that gave over a dozen companies the understanding and tools required to aggressively comply with this dynamic legislation. We will continue to support this effort and share best practices, since mandatory compliance will also result in real savings.

As with our other Ops Team segments, the intent is for this approach to endure well past Blackstone exit from each portfolio company. New leaders seldom ditch dashboards, scorecards, and associated tools that have proven their effectiveness. And companies that deploy and master these tools quickly see the value of an action-oriented approach to sustainability, and better operations and maintenance. Stakeholders get it, and the money saved talks.

**WHY DOES OUR IMPACT LAST BEYOND OUR INVESTMENT?**

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companies that deploy and master these tools quickly see the value of an action-oriented approach to sustainability, and better operations and maintenance. Stakeholders get it, and the money savings talk. We have found over 15 percent savings in resorts, limited service, and select service hotels at scale. We have proven that 20 to 25 percent energy cost reduction is possible across global portfolios, and companies are signing on to deploy programs faster and with more ease.

Having distilled sustainability down to its essentials is serving Blackstone and our companies well. Our ability to weave improved environmental performance into our ownership cycle touches a significant amount of the workforce and global economy – with surprisingly significant impacts.
About the Author

Don Anderson is an Executive Director and Chief Sustainability Officer in the Private Equity Group, based in New York. Mr. Anderson is responsible for evolving sustainability initiatives that deliver cost effective quantitative and qualitative results across the Blackstone’s Private Equity and Real Estate portfolios. Before joining Blackstone in 2011, Mr. Anderson was Vice President of Global Strategy and Business Development at ICF International, where he sold and managed energy efficiency and sustainability projects in the BRIC countries and Europe. Prior to that, he provided strategic consulting to corporations, ENERGY STAR, and The US Green Building Council (LEED) associated with operational excellence and sustainability in large portfolios. Mr. Anderson is currently Secretary-Treasurer on the Green Business Certification Inc. (GBCI) Board.