

Sustainability in Supply Chains: Are Multinational Corporations Rising to the Challenge?

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Do you know where the goods you purchase come from? The answer isn't as simple as you might think.

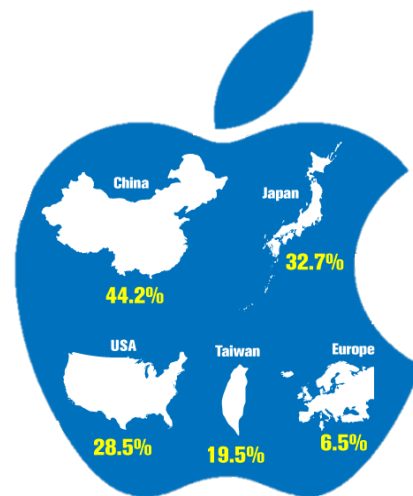
Let's consider a smartphone. Most would likely assume that their phone was made in China. After all, 30% of all manufacturing takes place in China (Richter, 2020). However, the many components that make up a smartphone don't usually come from the country of manufacture, it is simply the place of assembly.

So where do all the components come from, and how do they get there?

Most companies use a network of suppliers (supply chain) to source the various parts and/or services required to produce goods ready for distribution. These suppliers are often dispersed around the world. For example, when manufacturing the iPhone, Apple purchases components from suppliers in 43 countries, over 6 continents, which are sent to factories in China for assembly, before being shipped to warehouses and finally retailers across the globe (Ross, 2020).

The criteria for selecting these suppliers vary from company to company and industry to industry but typically include price, quality, delivery, service, convenience, risk, etc. In more recent years, multinational corporations (MNCs) have started to include social and environmental responsibility as a key criterion. As part of their Corporate Social Responsibility (CSR), MNCs request that their direct suppliers (first-tier) comply with their social and environmental standards. To be fully compliant, those suppliers must ensure that their suppliers (lower-tier) comply with the same standards, and so

on, going right back to the original suppliers. In theory, this should develop a sustainable supply chain from raw material to delivery of goods or services to the consumer. But is it adequate to simply trust that suppliers are following through on their commitments and ensuring that their suppliers are also compliant?

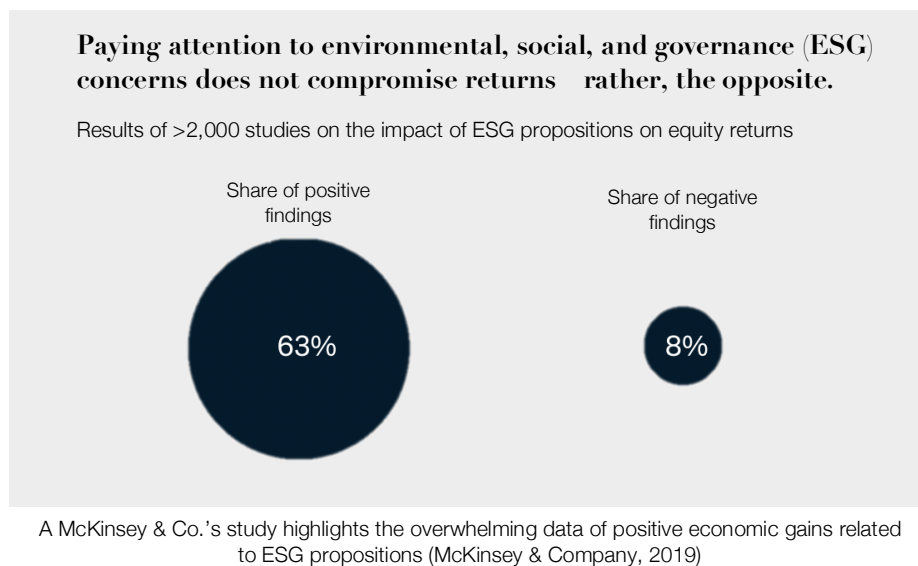


Apple's global supply chain: 198 suppliers and 759 subsidiaries account for iPhone core components (Grimes & Yutao, 2016)

What is “Supply Chain Sustainability Management” and why is it important?

Sustainable supply chain management is defined as: integrating socially, environmentally, and financially viable practices into the complete supply chain lifecycle (Sustainable Supply Chain Foundation, n.d.). This includes every process in the product lifecycle from raw material extraction to return and disposal. This hierarchy of organisations, known as the “value chain”, account for 80-90% of an MNC’s total environmental impact. Therefore, it is imperative that we factor in an organisation’s entire value chain when discussing its environmental impact (McKinsey & Company, 2016).

Above and beyond reducing environmental impact, creating a sustainable supply chain is hugely beneficial for an organisation.



The Bottom Line

There is a common misconception that operating sustainably negatively impacts profitability. On the contrary, operating more sustainably will in most cases lead to efficiencies. Through reduction of resource usage, waste, and processing times (and the associated labour cost), operational expenditure can be considerably reduced.

When Nike applied a sustainable mindset to their shoemaking processes in 2012, it reduced labour costs by 50% and material costs by 20%, resulting in a 0.25% increase in margins (Prologis, n.d.).

Brand Equity

In the era of information, it has become increasingly easier for consumers to learn about—and scrutinise—companies’ supply chains. Paired with the rapidly growing popularity of sustainable goods (Climate Action, 2021), a well-marketed sustainability campaign can significantly increase the brand value of an organisation. A

consistent and strong stance on ethical and ecological practices have been largely attributed to the success of outdoor clothing manufacturer, Patagonia. The company known for its environmental sustainability efforts saw a whopping 30% increase in revenue shortly after running a campaign that read “Don’t Buy This Jacket” (Thangavelu, 2020).

Furthermore, a survey conducted by McKinsey US showed that 66% of respondents (and 75% of millennial respondents) said that sustainability is a consideration when purchasing luxury goods (McKinsey & Company, 2020). Consumers want to know that the goods they are purchasing are ethical (e.g. conflict-free or responsibly farmed). With consumers increasingly viewing environmental and ethical practices as a key differentiator when purchasing goods, it is easy to understand why so many MNCs are making sustainability a priority.

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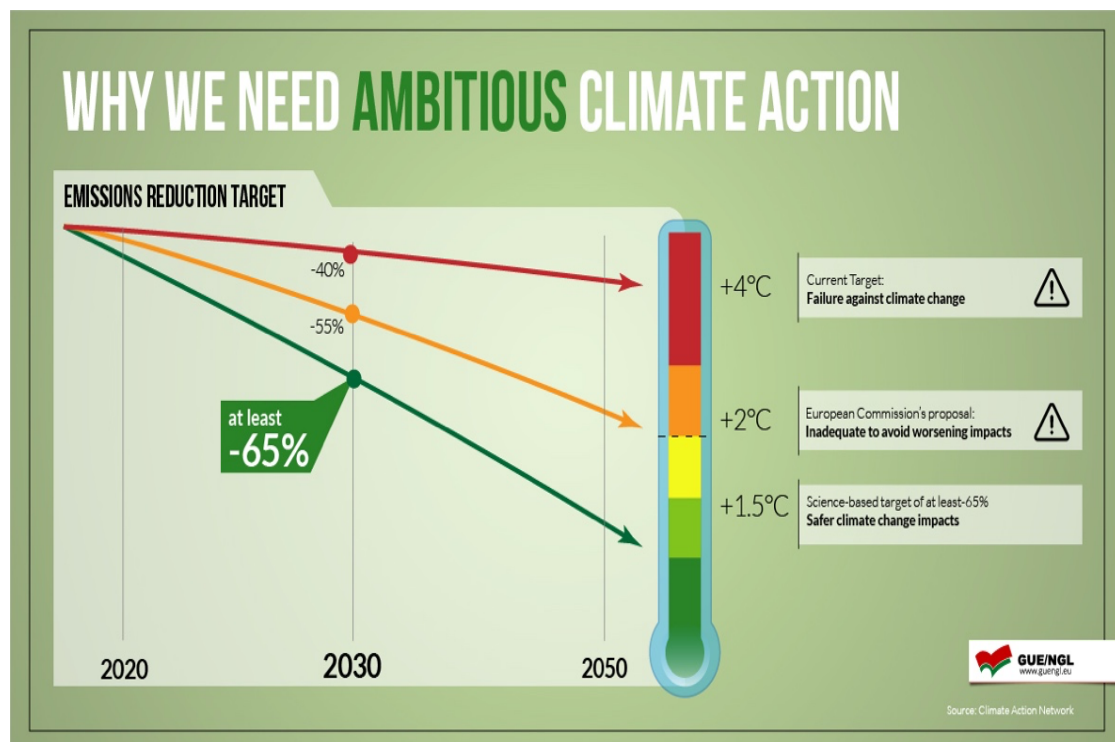
Resilient Sourcing

Supply chain diversification is important for many reasons. Eliminating over-dependence on individual suppliers creates a more resilient supply chain. In 2011, the consequences of vulnerable and over-dependent global supply chains were felt across the world when the market was hit by world-wide shortages and steep price increases of hard drives due to Thailand being hit by floods during a particularly severe monsoon season (Scott, 2013). Additionally, spreading requirements over multiple suppliers reduces excessive demands on single suppliers, mitigating the need for unethical work practices to meet

unreasonable demands. Diversification also helps grow the minority market by providing small or minority-owned companies with the opportunity to be awarded procurement contracts. Smaller companies are inherently more agile and innovative, giving them an edge when it comes to quickly adapting in a fast-paced and volatile market (Harvard Business Review, 2020).

Climate Law

Finally, as sustainability has gained prominence over recent years, companies have experienced an increase in related regulations. Over the last decade, we have witnessed the introduction of several new sustainability-focused regulations, such as REACH (Registration, Evaluation, Authorisation and Restriction of Chemicals) and the Illegal Timber Law in the EU. A sustainable supply chain can help ensure a company’s suppliers can adapt to these changes, similarly to the necessary diversification of supply chain, in regulations and legislation, reducing the risk of potential liability (BSR, 2010).

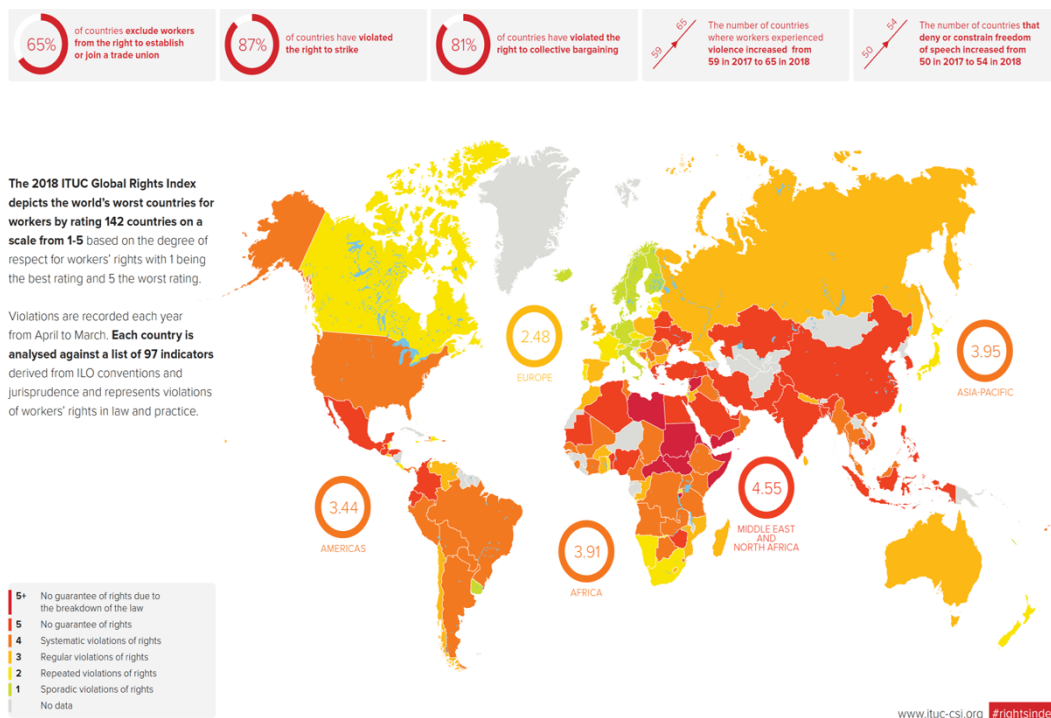


The Left highlight that the target of 55% by 2030, as set out in the EU's Climate Law, falls short of the ambitious efforts required to meet the target of +1.5 degrees Celsius by 2050, demonstrating the need for tougher laws (The Left, 2020).

Current Challenges with Supply Chain Sustainability

If sustainable supply chains are so beneficial, why do we see so many scandalous headlines involving MNCs' suppliers operating unethically? Unfortunately, there are considerable barriers to achieving a fully sustainable supply chain. Ensuring all suppliers within the supply chain adhere to the same standards is far from simple, with any shortcomings being detrimental to the MNC's reputation, as they will likely be scrutinised by the media, consumers, and in some cases, the courts. Even tech giants like Apple are susceptible, such as when they experienced major consumer backlash when it was reported that a manufacturing partner of the Cupertino-based organisation violated Chinese labour laws (Gurman, 2020).

During Verónica H Villena's research on three MNCs, widely regarded as "sustainability leaders", she discovered that many of their suppliers, first- and lower-tier, were committing multiple unethical environmental and human rights violations, conflicting with the MNCs' 'sustainability standards (Villena, 2018). Again, we return to the very little reliability MNCs have when it comes to the lower-tier suppliers' commitment to sustainable and equitable practices in sourcing materials. Even with the best of intentions, it is difficult for MNCs to know, let alone regulate, whether their lower-tier suppliers' operations align with their own social and environmental standards. Not all MNCs even know who their lower-tier suppliers are; many lower-tier suppliers are small or medium-sized companies, operating out of the public eye. Lower-tier suppliers are often located in developing countries, where laws regulating unethical practices are sometimes fewer (if any) and lenient compared to those of developed countries where those corporations' headquarters may be based. Eluding pressure from the media, stakeholders, and non-government organisations, many lower-tier suppliers do not have any incentive to operate sustainably and are rarely held accountable for failing to do so. Besides, many of these suppliers lack the expertise and resources to incorporate sustainable practices or simply haven't had the MNC's standards cascaded down to them from their clients. The combined lack of accountability and autonomy of these suppliers—far removed from the MNCs sphere of influence—makes lower-tier suppliers high-risk.



2018 ITUC Global Rights Index: Violations of Workers Rights (ITUC, 2018)

Although lower-tier suppliers are the riskiest, first-tier suppliers are often at the forefront of major MNC scandals. In 2011, Adidas and Nike found themselves the subject of a Greenpeace report that linked the two clothing brands, along with many others, with a supplier responsible for polluting two of China's major rivers with hazardous chemicals (Greenpeace, n.d.). However, most of, if not all, the MNCs involved in the "Dirty Laundry" scandal, had some form of sustainable supply chain strategy in place.

So where did the system fail?

The problem, in part at least, lies directly with the MNCs. In pursuit of profit maximisation and satisfying stakeholders, many MNCs are scaling their operations at an unsustainable speed, creating vast and complex supply chains without sufficient due diligence on new suppliers. At the time of the "Dirty Laundry" report, Nike had "more than 900 contract factories in nearly 50 countries around the world" (Nike, 2011). Another outcome is excessive seasonal demand on suppliers; during the build-up to a new product launch, for instance, it becomes necessary for suppliers to increase their workforce for short periods of time, resulting in rapid onboarding of temporary, and often unqualified, staff, who frequently exceed maximum working hours.

"Prioritisation of profit maximisation results in unsustainable, vast, and complex supply chains."

The systemic prioritisation of profit over sustainable development prevents procurement units from forming fully sustainable supply chains. Equally, the lack of collaboration and consensus on standards among MNCs is problematic for first-tier suppliers; many first-tier suppliers work with several MNCs, with no viable solution to incorporate the various standards from each of their clients.

How can MNCs improve the sustainability of their supply chains?

Maintaining an open and continuous dialogue with suppliers is essential. Sharing an inspired and specific vision will help create awareness around the issues at hand and give purpose to the requests being made of them. The guiding principles need to be supported by tangible and clearly defined sustainability targets. Monitoring the progress of these targets, along with the supplier, will provide the stimulus for developing and implementing strategic improvement plans. The addition of lower-tier supplier targets will encourage first-tier suppliers to think about what can be improved with their own suppliers. Working with first-tier suppliers to map out their network will assist them in identifying high-risk, lower-tier suppliers and deploying appropriate risk-mitigation programmes.

Delegating the management of lower-tier suppliers to first-tier suppliers provides them with the responsibility and impetus to make necessary reforms before insisting on the same from their suppliers. Offering proper training and incentives will help ensure the responsibility is taken seriously. Incentives do not necessarily need to be financial either; the opportunity to become a "preferred supplier" will increase their likelihood of being awarded contracts and provide them with the opportunity to network with other preferred suppliers to develop and share best sustainability practices. Sustainability awards is another way to incentivise suppliers to cascade best practices down the supply chain.

Working collaboratively, MNCs can influence legislative and regulatory changes that can better support lower-tier suppliers and enforce stricter sanctions on those caught violating the rules—whether formally regulated or adopted within the industries as best practice. A collaborative effort will also help standardise practices, making it easier for suppliers to conform to the relevant industry standards.

Many collaborations take place today through industry associations, such as Responsible Business Alliance (RBA), which primarily focuses on establishing, and holding members accountable to, sustainability standards. Enrolling first-tier suppliers into an association requires them to meet industry standards, including conducting assessments of their own suppliers' sustainability practices. RBA ensures members audit 25% of their high-risk facilities and then 25% of their suppliers' facilities (Responsible Business Alliance, 2021). The competitive edge provided by the recognition of complying with these standards is also an added incentive for suppliers.



The RBA Code of Conduct holds businesses accountable to four main areas, which are revised every three years to ensure progressive adherence to industry standards (Responsible Business Alliance, 2021)

Collaboration with international organisations and NGOs provides MNCs with critical data on environmental impact. For example, the Carbon Disclosure Project's supply chain programme not only creates transparency on the environmental impact of its members but also provides comprehensive data that supports decision making on how to reduce an organisation's carbon footprint. The sharing of specific data on a company's environmental sustainability enables MNCs to leverage this information to make more informed decisions during their supplier selection process (Carbon Disclosure Project, n.d.).

Immediate and collaborative change is a must.

The benefits of sustainable supply chain practices and the efforts already undertaken by MNCs are undeniable. However, there is still a lot of room for improvement. With the demographic of consumers expected to increase by 75% from 2010 to 2025, it is critical for MNCs to make significant changes to improve sustainability throughout their entire supply chains to avoid unprecedented levels of environmental impact (McKinsey & Company, 2016). The increasing consumer interest in sustainability further underpins the importance of a sustainable supply chain; the bottom line impact alone should galvanise organisations who are less concerned with social and environmental issues. But even with ample incentive, MNCs cannot achieve true sustainability without collaboration and regulation. It will require a systems approach to drive meaningful, lasting, and scalable change at a global scale. It has never been more important for intergovernmental organisations, such as the United Nations, to make MNCs accountable for their social and environmental impact, including that of their supply chain.

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