

Transforming the professional service industry towards circular service

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INTRODUCTION - A CIRCULAR ECONOMY CREATES CIRCULAR SERVICES

If we would continue to produce and consume in the way the western world is doing now, our ecological footprint would greatly exceed the biocapacity available per person on the planet (WWF 2006).¹ There lies a great challenge in achieving a minimum level of welfare for the world's population while reducing our ecological footprint. Circular economy aims at accelerating the transition from a linear to a circular economy: a systems change in thinking about our current economic system. The model moves away from the 'take, make, and dispose' model. It is a restorative model to businesses and the economy.

Clean technology, sustainable value chains and innovation alone cannot provide for the solution when dealing with this tremendous challenge. We need all industries to redesign the current capitalistic linear economy towards a circular economy. So far, circular economy has mainly addressed the redesign of industrial economies. It reasons from a closed loop model²: natural ecosystems serve as an example of how human beings should produce and consume. Therefore, circular economy is in the first place directed at the physical regeneration of materials and energy. If we look at some of the schools of thoughts on which circular economy is based, such as performance economy (Walter Stahel) and Cradle to Cradle (Michael Braungart), we see that also the professional service industry can learn a lot from its principles.

As we will see later in this paper, one of the derivatives of circular economy is the notion of a service model, whereby consumers do not buy products but pay for service³. In this light, new business models are inevitably to be developed. Circular business models are based on the notion of value retention and on offering service solutions instead of products. Particularly the rise of circular business models can be applied to the professional service industry as well. We identified five sectors in which circular economy can be applied: the financial sector, insurance companies, pension funds, employment agencies and head-hunters, and the IT sector. This paper describes in what way circular economy thinking is conducive to these professional service sectors.

¹ World Wide Fund for Nature (WWF), 2006

² Walter Stahel, 1970s

³ Performance Economy - Walter Stahel, 1970s

SCHOOLS OF THOUGHT

Circular economy draws from different schools of thought that date back to the late 1970s:

Regenerative design – The idea of regenerative design, developed by American professor John T. Lyle in the 1970s, is that processes within all systems renew or regenerate their own sources of energy and materials that they consume. The needs of society are fulfilled within the limits of nature.

Performance Economy – Walter Stahel, architect and industrial analyst, also in the late 1970s, coined the vision of an economy in loops, including the principles of product-life extension, long-life goods, reconditioning activities, and waste prevention. Selling services instead of goods is an important notion in his thinking: one pays for the performance that products deliver. This resulted in the notion of ‘performance economy’.

Cradle to cradle – In the cradle to cradle model, developed by the German chemist Michael Braungart, materials involved in industrial and commercial processes are considered to be nutrients for both technical solutions as biological reutilisations. Technical nutrients should not have components that harm the environment, while biological nutrients should be biodegradable.

Industrial Ecology – Industrial Ecology is the study of material and energy flows through industrial systems and falls under the Centre for Environmental Strategy at the University of Surrey. Again, waste within industrial circles serves as an input. Production processes are shaped in such a way that they perform as close to living systems as possible.

Biomimicry – Biomimicry is an approach by Janine Benyus, inspired by nature. It imitates nature’s designs and processes for solutions in human society.

Blue Economy – Blue Economy is initiated by former Ecover CEO and member of the Club of Rome Gunter Pauli. By watching natural systems, sustainable ways to produce and consume can be found. Blue economy gains knowledge from the way in which organisms are formed and work with the purpose of finding solutions for the challenges that we face, all determined by their local environment and physical or ecological characteristics.

PRINCIPLES OF CIRCULAR ECONOMY

The Ellen MacArthur Foundation and The Circle Economy refined the ideas of these schools of thought into main principles of circular economy. Most of the underlying notions can be applied to industry types broader than merely the industrial economy. The relevant principles are:

- 1. Circular economy is a non-linear economy.** Non-linear goes further than optimization of isolated parts of the value chain. This striving for efficiency, which has been the status quo since Michael Porter⁴ introduced the concept, does not touch on the alteration of production and consumption habits, and disregards other aspects such as human development. Efficiency alone does not reach the resilience needed to deal with shocks. A non-linear economy does not assume a value chain, but a value *cycle* instead.
- 2. Thinking in terms of (eco)systems is key.** Circular economy is based on schools of thoughts such as the Blue Economy (Gunter Pauli) and biomimicry (Janine Benyus), which takes natural ecosystems as an example. Physically, all materials serve as nutrients: technological materials for new products and biological components for nature. The natural balance between all components has to be restored. Systems thinking is the understanding of things within the context of a larger whole. Everything is connected and consists of a quantity of nodes, and diversity within these systems ensures the resilience of external shocks.

⁴ Porter, M. (1985). *Competitive Advantage: Creating and Sustaining Superior Performance*. The Free Press: New York

3. **Pricing must tell the truth. Distribution of value must be honest.** Our economic model is based on a pricing scheme where externalities are not incorporated in the price of products and goods. The damage that is done to our ecological system should be translated in the prices we as consumers pay. Moreover, the distribution of the created value worldwide is highly unequal. To find a way in that we can all share the resources and strive for welfare, this distribution must be honest and flow back to all parties involved in the economic cycle.
4. **Thinking in value creation is key.** Value creation refers to the new type of business model that discards ownership. Instead of focusing on value maximization for the own good, circular economy is very much focused on value creation.

UNDERLYING VALUES

Taking these principles as a departure, circular economy thinking touches on some important core values. First of all, it restores the thought of striving for **well-being** instead of wealth. Our planet does not have enough resources to provide all human beings with the wealth that Western societies entitle to themselves with the current economic model. In light of ecological and social sustainability, collective welfare is more important than the right of the individual. We need to restore this well-being by taking responsibility for our actions and help others to achieve the most fundamental basic needs.

Associated with this thought is the idea of **reciprocal relations** based on trust. Trust in the current economy and professional service industry is lost, mainly due to the way in which the service industry has acted. If we are to take resources from our planet, we have to ensure that we give something back as well. Only then are we able to survive: 'nice guys finish first'.

Schools of thoughts such as the Blue Economy and Walter Stahels adopt knowledge from natural ecosystems, which has led to circular economy thinking. In that sense, restoring the **connection with our environment** is one of the main values that drive circular economy thinking. In our capitalist world, we have drifted apart from the very nature of all processes. As human beings, we are part of the ecosystems we live in and this balance has to be restored.

All circular principles come together in what can be called **blended value**, or the creation of value for society *and* ecology all together. One-dimensional, fragmented thinking is transformed towards a more holistic and integrated way of doing business. Measuring the impact of the created value contributes to mainstreaming the idea of creating shared value.

Peter Senge⁵ states that a **learning environment** must be created to enable true systems thinking. A linear model does not allow for those learning processes to take place, as transactions just move up in the value chain. A circular model on the other hand is the ultimate model to continuously stay in contact with the environment, to anticipate on the interconnectedness and to detect constantly changing processes.

HOW THE PROFESSIONAL SERVICE INDUSTRY IGNORED THOSE VALUES

Transition towards a sustainable future is not only taking place in the industrial economy and in the social domain. The service industry is directly related to the economic crisis and is very much part of this transition. We are facing a revolution of the necessity to change current systems.

The opportunistic idea of everlasting economic growth and wealth has come to an end. In the past 30 decades Western capitalism has taken a form that is currently showing cracks. The need for more and greed for money

⁵ Senge, P. M. (1990). *The Fifth Discipline: The Art & Practice of the Learning Organization*. Random House: London.

has led to complex systems that are being created and maintained by ourselves. Prosperity that people are experiencing, consumers as well as the professional service industry, kept them from controlling what the service sector was doing with our investments⁶. Unrealistic optimism led to the idea that economic growth is the norm⁷. The free market is by many perceived as the most enlightened economic model. This perception gave every sector within the services industries the opportunity to create oligopolies, resulting in enormous power of the market. Services such as financial products have become so complex that consumers can hardly scrutinize the risks that their service companies are taking.

The financial sector is stated to be the 'mirror' of the economy. Yet the financial sector is far bigger than the real economy⁸. The financial crisis shows how the collapse of the virtual economy has a tremendous impact on the real economy. A virtual economy has emerged: Large parts of the financial sector for example merely exists of internal trade in derivatives. These form an unstable source for the real economy⁹. Moreover, American and European scientific research has indicated that size and efficiency negatively correlate, meaning that larger banks perform worse than their smaller counterparts¹⁰. Transaction-oriented banking, such as trading and financial market activities, has cost frictions with the regular relationship banking¹¹.

Going back to the essence of the service industry, service companies' goals are to service their customers in their best interest. The current economic situation shows that the customer is all but served. Besides being a facilitator for customer needs, the service industry has become an independent business sector, making profits for their own accounts. Perverse incentives to maximize profits for shareholders induce excessive risk-taking at the expense of long-term value creation for customers, or even viability of companies. Managers are incentivized by compensation in the form of bonuses to reach financial targets that are too often focused on short-termism¹². Moreover, the hedging of risks instead of focusing on long-term value creation prevents sustainable innovation to take place. As everything is connected in systems, we need the service sector to come along in the transition towards a circular economy.

CIRCULAR SERVICE THINKING IN PRACTICE

By adopting circular economy principles and values, the professional service industry can overcome the issues and challenges it is facing. Circular economy reasons from the fact that new business models are required as resources are depleting and current consumption patterns are not tenable forever. One-off consumption of physical resources has to be transformed to recycling resources and paying for use instead of ownership. If we look at the service industries, these principles can be applied in a similar manner: The relationships with customers, employees and suppliers is violated as customers are used to sell one-off products, employees are incentivized to deliver certain performances and suppliers are merely chosen based on lowest prices. The values of trust, reciprocal relationships and being in touch with the environment are therefore among the main starting points for circular services.

In practice, the circular economy has two different implications for the service sector. First of all, new circular business models in the industrial sector require new service models. The leasing scheme type of business model that the circular economy is moving towards requires the service sector to provide service products

⁶ *Het Snelle Geld: 25 jaar Hollands kapitalisme, van 1987 tot nu*. VPRO (2012).

⁷ Chandran Nair, in *Tegenlicht: Cleantech: de schone toekomst* (23 april 2012).

⁸ Blom, P. (2009). *Het Nieuwe Bankieren: De duurzame oplossingen van bankier Peter Blom*. Kosmos Uitgevers: Utrecht/Antwerpen.

⁹ Wijffels, H. (2011). Sustainable Finance Lab: Outcomes and conclusions.

¹⁰ Oostwouder, W.; Schenk, H. (2009). De governance van banken. *ESB*, 94.

¹¹ Boot, A. W. A. (2011). Banking at the crossroads: How to deal with marketability and complexity? *Review of Development Finance*, 1, p. 167-183.

¹² Bebchuk, L.A.; Fried, J.M. (2010). Paying for long-term performance. *University of Pennsylvania Law Review*, 158, 1915-1959.

conducive to these systems. Financing and securing circular systems is a totally new approach than the approach where deals are solely closed on a bilateral basis. This requires long-term vision and reciprocity within the system. Value creation is the ultimate goal, and this goal has to be leading at all times. One can image that this is quite a paradigm shift for the service sector, which is used to hedge risks as much as possible and aims at short-term returns. The Ellen MacArthur Foundation also determines two other possible developments¹³: New businesses will arise that facilitate the circular service provision of production companies. These new companies need funding and insurances. Moreover, it is expected that corporate lending will exceed consumer financing, which means that more robust types of products and services are needed.

Secondly, the service sector itself has to adopt circular economy thinking as well and take the principles and values as a starting point to restore the system. The above implementation is secondary and mostly facilitative of industrial circular systems. Changes in the banking system are already implemented to prevent banks of being too vulnerable: banks are omitted to trade for their own account. Moreover, the 'Commissie de Wit' pleads for the separation of business banks and consumer banks, the so-called 'nuts' banks¹⁴, whereby the public transactions such as deposits and payments are separated from activities on the financial market. Supervision is becoming more rigorous. However, we need to go beyond rules and regulations that try to overcome these issues. The sector has to completely alter its **culture** and way of doing business. This requires the sector to not only look at individual institutions, but to re-evaluate the system as a whole.

We have to go back the very nature of service companies: delivering certain types of service for its customers. This **servant role** has to be restored. Why do we allow banks in our society? We need institutes that can safeguard our savings for the future and grant us loans to enable us to buy things in the present. Moreover, we need them to provide for efficient payments. This means that the service sector has to take its stewardship responsibility by reasoning from the customers' and society's point of view. Hence, many committees and individual economists or politicians recommend to split business parts from service parts of banks¹⁵. Circular economic models are all about **value retention**. Profits that are made can therefore be reinvested in innovation or society, instead of added to the bank accounts of the companies themselves.

The service products that the service sectors, in particular the financial sector, are offering have become highly complex¹⁶. The customer lacks the knowledge to judge how this product is actually going to benefit him or her. Taking these products **back to basic** will restore trust and satisfy the basic needs of individuals. Service products have to meet certain conditions and necessary requirements: clear and simple products that cut to the chase and deliver what they promise. People understand these services, and by being transparent, peoples' trust is being restored. Education is an important aspect in this light. The back to basic principle also accounts for the profile of the organization: recognizable specialization, either on type of services or geographically, can deliver added value for customers¹⁷.

The service sector is too much shareholder driven. Shareholders are threatened as the only relevant stakeholders. To alter towards circular service, all **stakeholders** must be taken into account. Not only shareholders, but also customers, suppliers, employees and society at large are part of the circular economy. All together, they form closed cycles where everyone has its share and commitment, and contribute based on trust and reciprocity. The service industry is part of these systems and cannot be ignorant to other stakeholders. This means another way of dealing with stakeholders:

¹³ Ellen MacArthur Foundation & Founding Partners. *Towards the Circular Economy: Economic and business rationale for an accelerated transition*.

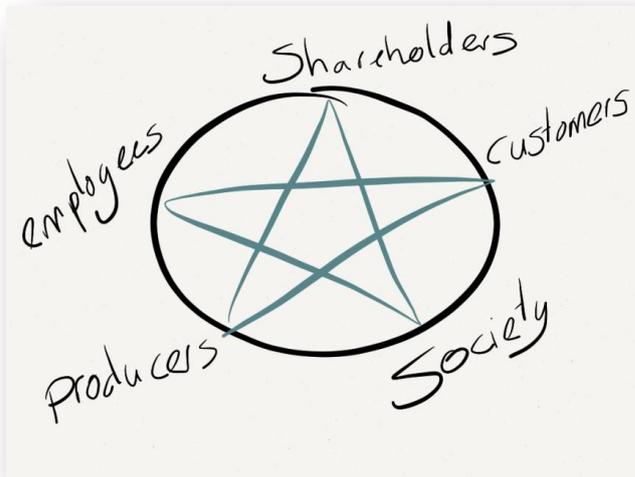
¹⁴ Schenk, H. et al. (2010). Overzicht en analyse van het (inter-)nationale toezichtstelsel binnen het financiële stelsel. *Onderzoek in opdracht van de Tijdelijke Commissie Onderzoek Financieel Stelsel, Tweede Kamer der Staten-Generaal*.

¹⁵ See for example publications of authors within the Sustainable Finance Lab.

¹⁶ Van der Slikke, P. (2012). *Ontmaskerd: Hoe de financiële wereld echt werkt*. Einstein Books: Amsterdam

¹⁷ Blom, P. (2009). *Het Nieuwe Bankieren*. Kosmos Uitgevers: Utrecht/Antwerpen.

- Employees receive a fair share and are treated from a reciprocal relationship based on trust,
- Customers receive actual value and share in the system's profits,
- Shareholders are involved and stimulated to act in the long-term interest of all stakeholders,
- Suppliers are involved in chain responsibility and become partners,
- Society is the main focus of all activity and the strategic course of the company, and costs that are made at the expense of society are internalized.



The above two practicalities closely align with the notion of restoring the connection with the environment. By being in close collaboration with its environment and by offering basic products, simplicity and personal connections can be made. Being more in touch with the environment can mean that companies become **smaller** or that companies are organized through a system of many small parts. Smaller banks and banks that are specialized for example, prove to be more efficient and productive¹⁸. Smaller companies are better recognizable in character and the services they deliver. This promotes the transparency and fosters personal contact with customers.

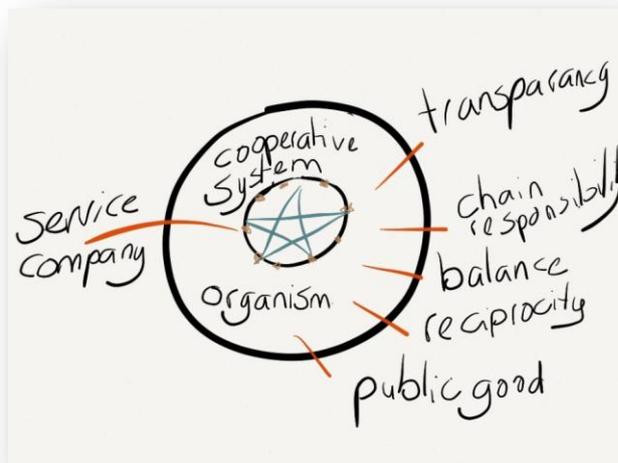
The service industry is pre-eminently the industry that can set an example when it comes to delivering services to its customers. Companies, whether they are production-based or service-based, are increasingly competing on providing the best service. Companies can become mature through price differentiation or product differentiation. However, companies in a mature state are increasingly becoming aware of the necessity to differentiate on service delivery. From a marketing point of view, it seems only logical that all companies eventually have to transform to optimizing their services.

RENEWED GOVERNANCE MODELS ARE ABOUT TO ARISE

Banks, pension funds and insurance companies are mostly shareholder-owned. The dynamics that this ownership model induces is a shareholder-focused strategy, thereby losing sight of customers' best interests. The essence of listed companies is that the ownership is based on financial incentives. Making profits for shareholders becomes the main goal. Circular service restores the focus on society instead of on profit for shareholders. This requires new governance models. A **cooperative company** is gaining more ground. The interest of the owners becomes the company's interest. The relationship cooperatives or employee-owned organisations have is very different from the other type of companies. Cooperatives "share the values of democracy, solidarity, equality, self-help and self responsibility, creating businesses that serve the greater good

¹⁸ Oostwouder, W.; Schenk, H. (2009). De governance van banken. *ESB*, 94.

as opposed to maximising profit for the very few”¹⁹. Cooperation from shared interests is the basis of such a governance model. Contradictions are not part of these organisations as they serve society and exercise their social task. They strive for social improvement, more than profits. Profits are used as buffers and invested in innovation, said PGGM. Thus, the relationships and the transactions are in balance. Companies such as pension fund PGGM and insurance company Univé are companies that are organized by this governance model. Univé states that the interests of the members are their number one priority. Members benefit by sharing in the distribution of profits, by receiving discounts, and improved products and services (“Daar plukt ú de vruchten van”).



CAPABILITIES NEEDED FOR CHANGE

The transition to a circular service industry will take time. How this transition can take place is a question to be answered. Different phases of improvements will be determined to facilitate the transition. Certain capabilities are needed to allow for circular economy thinking. First of all, change is only possible when we act out of intrinsic motivation. A culture change within the service industry is inevitable. Greed, bounded rationality, excessive risk-taking for the own good, and unrealistic optimism have to change in generosity, intrinsic motivation, striving for wellbeing for society, and reconsidering the capitalist system.

A first step towards another culture is strong **leadership**. Leadership is needed to take the lead in changing the current governance systems. Leaders serve as examples for employees and their actions have an effect on the perceptions of outsiders. Their innovations have to become rooted in the organisation, also after they leave the company. There lays a large task for supervisory boards to appoint the right people and not be drawn in the competition between peer companies and compensation benchmarks.

Systems thinking is inherent to **openness and transparency**. Together with stakeholders, circular economic models form inclusive systems. The whole is greater than the sum of the parts. This implies that service companies have to open up to their stakeholders and allow them to contribute to their operational business and strategic course. Moreover, innovating towards circular economy thinking cannot be seen as separate from the interaction with the organizational environment. Open systems interact with the larger system and the environment. This requires self-governance and learning through networks, interfaces, and feedback loops.

¹⁹ Pauline Green, President of the International Cooperative Assembly

Diversity is another important capability. A culture change is more easily realized when human resource policies stimulate a diverse management team and workforce. Diverse opinions and backgrounds allow for more creativity and innovation. Moreover, a diversity of people can ensure that the organisation is protected from short-sightedness and moving in the wrong direction.

SECTOR IMPLICATIONS & BEST PRACTICES

Looking at the different sectors that we identified, it can be seen that circular economy has different implications for each sector. How do we get large, institutionalized companies such as banks, insurance companies, pension funds, employee agencies and IT companies to restore their legitimacy and identity by using circular economy thinking? Changing linear business models to circular economy thinking requires a step by step approach. We identified companies that are already frontrunners in the transformation towards circular service.

In the **financial industry** connection with the environment and the servant role are increasingly visible. Serving the greater good by investing in enterprises with a sustainable character is developing at a fast pace. Connection with the environment is facilitated by investing in social ventures, thereby creating value in environmental, social and cultural ecosystems. Rules regarding the division of service parts and business parts, changes in governance such as constraining executive compensation, closer supervision and solvability regulations are first steps in changing the culture of financial institutions towards more customer-focused, service companies. Moreover, the financial industry plays a major role in financing circular systems.

- **De Lage Landen (DLL)** evolves its financial products in such a way that they better facilitate a circular economy: By rethinking ownership for the user of equipment and the business model for their manufacturing partners. In cooperation with leading manufacturers, they aim at extending the life cycle of assets. By managing assets from their production day, through 1st, 2nd and other lives with different users till the day the assets are disposed. E.g. customers do not have to own products such as forklifts, copiers, MRI scanners, harvesters or trucks in order to operate their business. They even don't need "new" equipment. DLL builds financial products that enable manufacturers to operate a service based business model. Moving away from "selling" a technical piece of equipment towards "providing" a guaranteed usage for a guaranteed period of time. Such as lift pallets, make copies, scan for tumours, harvest corn or drive kilometres. By retaining ownership of the assets, DLL can redirect large quantities of equipment back to their manufacturing partners for refurbishment, remanufacturing, component harvesting and in utopia even raw material re-use. By carefully analysing and managing the economic, technical, fashionable and innovation lifecycles of equipment with the manufacturers, DLL grows from a asset-based, linear business model towards a service-based circular business model.
- **Turntoo** is an example of how a closed circular system could be created. This raw materials bank offer performance based consumption. Consumers rent products while the producers remain owners of the raw materials. At the end of the life cycle, the materials are returned to the producer. By this way, the materials remain available for future generations. **Triodos Bank** is one of the partners of Turntoo that make this construction possible. All partners have a long-term mindset, as the return on investment has a much longer life cycle. In a circular system, all partners bear the risks and invest in the long term value that is being created.
- That **Triodos Bank** is moving towards circular services is also manifested in their social responsible investment policy. Triodos invests their savers capital in local companies and social enterprises. By being transparent in their investment portfolio and by providing customers the opportunity to get

insights in those companies, the customers are closely involved in where their money is invested in. Social return is key.

Changing business models and integrating transparency is common ground nowadays in the **insurance landscape**. Back to basic systems are introduced in which customers collectively get money back when costs of damage are covered. Value propositions towards customers are communicated more transparently by explicitly defining added value in a clear and concise way.

- **Achmea, CZ, and Menzis** are among the partners of WeHelpen.nl, a marketplace where any sort of aid is being connected, shared and offered. An alternative value system eliminates the need for money: people receive credits for their aid, which they can spend on aid themselves. WeHelpen.nl offers an alternative to the growing expenses of health care in the Netherlands.
- **Inshared** lives up to their slogan 'We all benefit': customers get back their premium when they have not done any claims. By providing incentives to stimulate prevention, Inshared shows that it considers its role in closing the circle: they take the responsibility to contribute to the wellbeing of their customers and society as a whole.

Investing in circular systems is to be executed by **pension funds** as well. Extending the portfolio by investing in sustainable initiatives embraces a long term focus and creates a sustainable advantage. Another key indicator of pension services includes moving towards circular service and the circular system by investing part of the returns in today's needs, thereby investing in the future of their savers. Pension funds can invest in housing, healthcare and the local economy, which benefits their customers not only when they claim their pension at retirement, but also now. Cross boundaries and develop new connections with members and other organizations. Capital can be used to create non-monetary value. Saving for pension does not only have to be returned into money, but can also be traded for health services.

- As a cooperative pension fund, **PGGM** has the interest of the owners as its main interest. In cooperation with other companies, such as VGZ, they are experimenting with concepts based on non-monetary value systems. 'Nieuwe oude dag' actively thinks about how to design healthcare in the future²⁰. Creating communities, exchanging aid, and investing in healthy workplaces shows that PGGM and its partners are taking a first step into designing new circular systems that have a progressive view on pensioners.

When it comes to the **employment and recruitment agencies**, the stakeholder group 'employees' is their main asset. These companies act in the service of their people by investing in their development and education. The large group of self-employed deserves much more respect when agencies organize their staffing at different companies. A culture change in the dynamic system of employment and recruitment agencies is developing: all stakeholders are involved and connected. Everything good for an organisation needs to be considered good for employees, suppliers, government and society. Creating opportunities for individual development and social integration set the learning environment and add value to the circular economy as a whole. In addition, flexibility is created in the chain of human resources which reduces risks and makes the industry more robust against future challenges.

Anywhere, anytime, any device: data is easily accessible through asp, cloud services and freeware these days. Besides, processes are transformed into environmental friendly and reducing CO2 emissions by integrating smart IT processes. Identifying opportunities to create sustainable performance, measuring indicators, evaluate and take appropriate actions further enhances understanding of the value chain. In addition, it creates awareness throughout organisations to take responsibility for the environment and society in the long run.

²⁰ <http://www.nieuweoudedag.nl/Zorgflorijnen.pdf>

END NOTE

The Circle Economy and dutch Group b.v. aim at accelerating the transition to a circular service sector. The above examples show a positive movement of the service sector towards the implementation of circular principles and values. Yet creating true closed loop systems in which the service industry plays a facilitating and supporting role requires more underlying implications. We need the whole sector to be part of this transition in order to succeed in creating a circular economy. We would gladly invite the different players in the industry to elaborate with us on the statements that we make in this paper, so that we can build new business models and identify projects on which these ideas can be applied.