



Executive Insights

Sustainability: Six Big Themes From the Boardroom

Partners from the Executive Board of L.E.K.'s Sustainability Centre of Excellence met to talk about what sustainability means across their sectors and regions. The sustainability and environmental, social and governance (ESG) agendas for corporations and investors are evolving apace, with expectations growing and best practice rapidly changing. Businesses are under pressure from a range of stakeholders — including investors, customers, regulators, and often their own boards, leadership teams and employees — to improve the sustainability of their business models and operations.

The 2021 climate change report from the United Nations Intergovernmental Panel on Climate Change has drawn even greater attention to the environmental side of the matter. According to the report, scientific evidence points to human activity as the “unequivocal” cause of climate change.¹ The statement marks a tonal shift that’s now being reflected by the sentiment of corporations globally.

Most companies understand that to successfully address sustainability, it must be at the heart of strategy, operations and value creation. However, companies can play offense or defense depending on the level of ambition and desire for a transformative approach. The financial impacts are complex, but an established consensus is clear — sustainability is an imperative that presents real opportunities for businesses in driving innovation, developing new products, offering new services and meeting rapidly evolving stakeholder needs.

Our Partners share their thoughts around six key sustainability themes observed across L.E.K. Consulting’s global practice areas and client base.

Observation #1: There is now consensus that sustainability is one of the most substantive and complex issues facing boardrooms this decade

The philosophies and themes behind sustainability have been around for many decades with the notions of corporate responsibility, sustainability and ESG. One of the most critical areas of sustainability, addressing the climate crisis and the decarbonization required to do so, has increased in urgency. That’s been evident even in the past few months, with a confluence of events across political, governmental and societal forums driving an even greater commitment to a net-zero carbon world. In parallel, there have been developments in corporate sustainability reporting and a general rise in expectations around businesses’ sustainability plans.

Sustainability: Six Big Themes From the Boardroom was written by **John Goddard, Rebecca Scottorn** and **Amar Gujral**, Partners, and summarizes the observations of the [L.E.K. Sustainability Centre of Excellence Executive Board](#). John and Rebecca are based in London, and Amar is based in Houston. For more information, contact strategy@lek.com.

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Momentum is building, with about one-third of the largest 2,000 companies globally already having a net-zero emissions target in place. Concerns are now translating net-zero targets into real actions,² and L.E.K. has written on the importance of considering the trajectory to net zero, not just the end date.³ Capital inflows to sustainable investment funds and financial institutions are growing as well, with examples of single fund raises geared to carbon transition exceeding \$1 billion, not to mention the growing number of socially responsible exchange-traded funds now on the market.

- *Those who grasp the nettle early will be well placed to build back better, giving them a cutting-edge advantage in a decarbonized future.* — David Ogilvy, Partner, Industrials (Melbourne)
- *As businesses pursue their pathway to zero, they'll also need to demonstrate their social license to grow — that is, convince governments and customers that they're taking all reasonable steps to address wider ESG issues.* — Becrom Basu, Partner, Transport and New Mobility (London)

Observation #2: The recovery from the pandemic is only reinforcing priorities and accelerating corporate sustainability initiatives

While the COVID-19 pandemic initially brought new and pressing priorities for companies, governments and society more broadly, there's strong evidence that it has reinforced the need to prioritize sustainability. JP Morgan and the Carbon Trust each conducted surveys on the early financial recovery from COVID-19 in late 2020. JP Morgan's survey found that 55% of respondents believed the impact of COVID-19 would be positive on ESG investment momentum over the next three years. Carbon Trust's survey validated that perspective, showing that sustainability and the environment had become more important for 74% of respondents for the future after COVID-19.

A number of parallels have also been drawn between the pandemic and the climate crisis. There's been a recognition that we were woefully underprepared to deal with a high-impact catastrophe, and mitigating that is important in the face of the next climate-related catastrophe. We see further parallels in behaviors — the pandemic has demonstrated that people will actually change their behaviors quite dramatically if required.

However, the pandemic has also thrown up challenges (e.g., the lack of a global coordinated response), and the climate crisis requires behavioral change over a much longer period. As companies seek to recover from the impact of lockdowns, we've seen a rise in interest from clients seeking development and mobilization of their sustainability strategies across geographies and sectors.

- *Sustainability, defined in its broadest sense of ESG issues, is now seen as a boardroom-level concern. Although many feared COVID-19 would derail momentum, it caused only a brief distraction while reinforcing for many sectors the importance of prioritizing these themes.* — Rebecca Scottorn, Partner, Sustainability and Industrials (London)
- *To survive the initial pandemic-related lockdowns' volume declines, businesses responded fast by streamlining cash flow and optimizing their operational footprint. That same newfound agile muscle also provides an opportunity to develop a new, sustainable identity in a world that otherwise risks companies being overlooked by investors, customers and governments.* — Harpreet Singh, Partner, Industrials (London)

Observation #3: What sustainability means — and what matters for stakeholders — varies by geography and industry, and is evolving over time

Consumer-focused businesses are leading on circular economy initiatives and responding to increasing demand to provide products with strong sustainability credentials, while maintaining the functionality and costs consumers are asking for.

Industrial companies face both challenges and opportunities from the Energy Transition together with a drive to establish resilient and sustainable supply chains. Their aim is to ensure diversity and inclusion in the workforce and adopt strong work practices around the globe.

Healthcare companies are innovating in areas such as value-based care models, personalized and precision medicines, supply, manufacturing, and novel patient engagement.

Life sciences companies are confronting the environmental impact of manufacturing, packaging and waste management; issues of affordability; and the gap between high- and low-income countries in their access to medicine.

Energy companies are focusing on two angles to sustainability. On the conventional side, capital is flowing to decarbonizing operations. For example, Exxon is driving development of a carbon capture hub in Houston⁴ and certifying natural gas methane emissions management for customers.⁵ On the other side, the rise in renewables and solutions such as electric vehicles is driving demand for storage (e.g., battery technology) and further innovation in new technologies such as green fuels and hydrogen.

Travel and transportation companies are wrestling with the challenge to fund the move to more expensive zero emission fleets in an environment of increasing government regulations and requirements.

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The European region is generally ahead of the curve on several dimensions, particularly those related to the environment, but there has been a distinct acceleration of intent from North American businesses. Although environmental issues are often front and center in discussions, diversity and inclusion issues have become more important across sectors and regions. So has governance in the wake of corporate controversies, getting to the heart of corporate responsibility.

One of the most common observations is the importance of sustainability in its broadest sense to younger employees irrespective of sector or geography. This is a critical constituency for today's corporate leaders to engage and show progress with.

- *Industrial technology companies are playing a major role in facilitating the Energy Transition through the development of cleaner generation sources, the optimization of increasingly complex power grids and new forms of electrical storage.* — John Goddard, Partner, Industrials and Transport (London)
- *More consumers are taking sustainability seriously. For consumer products companies and retailers, sustainability is now becoming a must — not merely better or nice to have.* — Takayuki Kito, Partner, Consumer (Tokyo)
- *What sustainability means for energy is evolving. Ten years ago, it was all about energy conservation and reducing the need for power or reducing hydrocarbons through various energy- and fuel-efficiency initiatives. Today, sustainability encompasses ESG as well as the broader sector lens of the world's Energy Transition.* — Amar Gujral, Managing Director, Energy and Environment (Houston)

Observation #4: The financial impact is hard to unpack

On the investment side, there's significant uncertainty about how costs of key technologies are expected to evolve, impacting decisions around investment choices and timing. It's clear that capital allocation is becoming that much more important with trade-offs requiring careful analysis and longer-term perspective. The potential returns can be challenging to quantify; while investors value a strong sustainability strategy, isolating the impact on multiples and profitability can be difficult — and arguably misleading given the rate of change of key considerations.

Some companies are looking for clear evidence that investment in sustainability will improve financial performance. But this is complicated⁶ and, if not carefully assessed, may lead to unintended consequences as regulation and/or external pressure tightens.

Alternative narratives focus on the fact that businesses have to become more sustainable, and so the key is getting it right. As far as addressing climate issues and the Energy Transition, we increasingly see that as the approach to take. The transition will happen; it's about navigating it as successfully as possible and ensuring a proactive approach can provide strategic advantage.

Navigating a clear path is difficult, but a lack of clarity can create tension within organizations over where activities should fall in the hierarchy of strategic sustainability.

- *The cost of implementing sustainability strategies must be carefully weighed against consumer willingness to pay and ROI, which varies greatly by category, subcategory and SKU.* — Lauren DeVestern, Managing Director, Retail and Consumer (Boston)
- *In packaging, clients are serving brand owners that have ambitious sustainability goals without a clear path on how they'll get there. In waste and recycling, the U.S. recycling infrastructure resists real change, making it difficult for organizations to have impact beyond the local or regional level.* — Amanda Davis Winters, Managing Director, Industrials (New York)
- *Healthcare and life sciences companies need to address the sustainability agenda without impacting research and development productivity — without impeding the development or efficiency of new drugs, for example — as that saves lives, which is an important sustainability objective in and of itself.* — Andre Valente, Partner, Healthcare and Life Sciences (London)

Observation #5: Companies differ in their level of ambition

Divergence is emerging across organizations, with some taking defensive- versus offensive-minded positions toward sustainability. For some companies, sustainability is all about compliance and minimizing risk. It's worth pointing out that even such a seemingly passive approach can often still require significant change and investment.

Other companies then seek to take more of a leading role among peers. What counts as leading is changing rapidly as companies improve — and so a once-leading strategy can very quickly become table stakes. For example, in Europe, a 2050 net-zero target is increasingly not seen as ambitious or leading, even in difficult-to-abate sectors. Within the leaders, there are the true innovators, the game changers that make sustainability their essence and mission. This is increasingly being recognized by investors and the financial markets.

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- *Not surprisingly, there's a disparity in the amount of resources devoted to ESG issues between large and midsized pharma companies and small biopharma, which tend to struggle the most with keeping up with emerging trends due to a lack of resources and capital. However, strong ESG perception will be increasingly critical for all.* — Verena Ahnert, Partner, Life Sciences (London)
- *Consumer businesses cannot afford to wait. They need to be thinking — and thinking hard — about how they might respond to an environment where consumer decisions are influenced, if not led, by ESG considerations.* — Mark Boyd-Boland, Partner, Consumer (London)

Observation #6: Sustainability is creating substantial opportunities

Consensus continues to build around sustainability, creating substantial opportunities. New markets are becoming established (e.g., electric vehicles), new technologies are being developed (e.g., e-fuels) and new products and services are being launched (e.g., more sustainable food production methods and new sustainable packaging offerings).

However, companies need to act now to realize the potential opportunities that sustainability can bring. Success will require adept management of uncertainties, assessment of evolving market preferences, and an ability to reflect the pace and tone of government policy responses — such as potentially material implications coming out of the 2021 United Nations Climate Change Conference (COP26).

- *Our clients see — and realize — opportunities by focusing on health outcomes at the population and individual levels.* — Max Cambras, Managing Director, Life Sciences (Los Angeles)
- *Once started with a structured approach, clients see opportunities along their entire value chain and ecosystem. And that's crucial. Managing sustainability is nothing that can be done in just one part of a company's value chain or by only a handful of companies.* — Sebastian Olbert, Partner, Industrials (Munich)

Maximizing the opportunities presented by sustainability issues

All businesses have the chance to make their products, services, operations and supply chains safer, circular and less emissions intensive. They can develop a diverse, inclusive workforce and make a positive impact on local communities. And they can choose best-in-class governance structures to inform sustainability choices on an ongoing basis.

By taking a structured approach, L.E.K. clients can capture opportunities throughout their entire value chains and ecosystems in terms of:

- Developing net-zero and sustainability strategies
- Deploying new technologies in support of sustainability goals
- Aligning growth initiatives around products and services to address climate change

In M&A, we increasingly see ESG issues impacting inorganic growth strategies, approaches to due diligence, valuation considerations and ultimately deal outcomes. Meanwhile, more boards are bringing sustainability front and center to corporate decision making.

These are exciting yet complex times for businesses as they balance near-term financial performance with the desire to set and deliver on sustainability targets. Successful players will put sustainability at the heart of strategy and steer their “where to play” and “how to win” choices accordingly.

The L.E.K. Sustainability Centre of Excellence draws together the expertise, best practices and strategic insights necessary to support your approach, address the challenges and capitalize on the opportunities that sustainability brings.

Endnotes

¹TheGuardian.com, “Climate crisis ‘unequivocally’ caused by human activities, says IPCC report.” <https://www.theguardian.com/environment/2021/aug/09/climate-crisis-unequivocally-caused-by-human-activities-says-ipcc-report>

²LEK.com, “Early Mapping of a Pathway to Net Zero Is Essential for Future Competitiveness.” <https://www.lek.com/insights/ei/early-mapping-pathway-net-zero-essential-future-competitiveness>

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⁴Energyfactor.exxonmobil.com, “The Promise of Carbon Capture and Storage, and a Texas-Sized Call to Action.” <https://energyfactor.exxonmobil.com/insights/partners/houston-ccs-hub/>

⁵Corporate.exxonmobil.com, “ExxonMobil to Certify Natural Gas, Help Customers Meet Environmental Goals.” https://corporate.exxonmobil.com/News/Newsroom/News-releases/2021/0907_ExxonMobil-to-certify-natural-gas-help-customers-meet-environmental-goals

⁶WSJ.com, “How ESG Stocks Perform Depends on Who Ranks Them.” <https://www.wsj.com/articles/how-esg-stocks-perform-depends-on-who-ranks-them-11623403803>

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About L.E.K. Consulting

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