



## Six Steps to a Sustainability Transformation

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If you think the disruption caused by digital has been far-reaching, just wait. That impact will pale in comparison to the changes coming as companies wrestle with how to transform their businesses to become truly sustainable.

Sustainability, a company's ability to create positive environmental and societal impact, is rapidly reshaping competitive advantage. It is remaking whole industries, blurring and in some cases obliterating boundaries between industries, and generating new waves of growth. The scale of the disruption that will play out over the next few decades, along with the opportunity it creates, will be staggering. Just the push to limit global temperature increases to 1.5°C—the central sustainability

challenge of our time—will drive a massive transformation of the global economy and **require investments totaling an estimated \$100 trillion to \$150 trillion by 2050.**

But while the opportunity is clear, the way to drive a successful **sustainability transformation** is less obvious. To succeed and create a competitive advantage, companies must simultaneously integrate an environmental, social, and governance (ESG) lens into every element of the business and capture the value that this transformation creates.

On the basis of our extensive experience working with companies and investors to drive sustainability transformations, we have identified six actions that distinguish leaders from the rest of the pack:

- Develop a sustainability strategy anchored in purpose.
- Capture business value.
- Build new sustainable businesses.
- Make the core sustainable.
- Build capabilities.
- Own the narrative, and engage investors and stakeholders.

Companies that fail to take up the challenge, and instead continue to view sustainability through a compliance or ESG reporting lens, will miss the opportunity to tap into lucrative new markets and create new, winning business models. They will also see their space for creating shareholder value narrow dramatically. On the other hand, companies that execute effectively in all six areas will truly transform their business and turn sustainability into a competitive advantage.

## **DEVELOP A SUSTAINABILITY STRATEGY ANCHORED IN PURPOSE**

Companies must devise a strategy that takes as its starting point the principle that sustainability is a source of durable competitive advantage. The strategy must clearly connect to the **company's purpose**, focus on long-term value creation, and be driven from the top, including the CEO and board.

To outline a clear strategy, companies should step back and look at their performance in all material environmental, social, and governance (ESG) areas. Then they should focus on the areas that matter the most to all stakeholders—not just to investors—today and in the future, and where outperformance can contribute most significantly to long-term business success. That prioritization is critical to helping companies avoid the all-too-common pitfall of creating a profusion of siloed initiatives that ultimately have little impact.

At the same time, companies can reassess their existing business model with the objective of understanding its degree of sustainability. This assessment will likely reveal opportunities to enhance the environmental and societal benefits that the company generates, but it will also strengthen the company's competitiveness by improving the resilience of its business model.

## **CAPTURE BUSINESS VALUE**

Companies that lead in sustainability, as reflected in ESG performance, can also outperform their rivals financially. But capturing the value that sustainability efforts create can be challenging.

That's why companies must be intentional and systematic about capturing this value. To start, they must develop a robust business case that accesses all sources of value that their sustainability efforts create. These sources are numerous and varied:

- Enhanced brand equity and loyalty
- Price premiums
- Fresh growth in the form of share expansion, penetration of new markets, or new businesses

- Operational cost savings
- Advantages in sourcing, including reliable supplies of scarce inputs
- Improved access to or reduced cost of capital
- Reduced risk
- Valuation premiums

Once they have clearly articulated those business cases, companies should ensure that key areas of the business—including marketing, sales, product development, and finance—have the capabilities not only to capture the value created, but also to track and measure it accurately.

Companies can move quickly to test and scale changes and initiatives in areas where value capture is straightforward and likely to yield immediate financial results. Such efforts will validate the power of the overall sustainability transformation and can be the source of revenues or cost savings to fund other aspects of the journey.

Take, for example, decarbonization for auto OEMs. According to BCG analysis, eliminating 60% of scope 1 and 2 carbon emissions during an initial phase of decarbonization will generate significant annual savings, and those cost reductions can help fund the costs of eliminating the remaining 40%. Even in cases where manufacturing a sustainable product leads to higher costs, the increase often proves to be marginal and more than offset by the enhanced value perceived by customers. For instance, [the increased cost associated with creating a smartphone with a net zero supply chain is less than 1%](#) for a \$400 smartphone, according to BCG analysis.

## **BUILD NEW SUSTAINABLE BUSINESSES**

Companies have a major opportunity to unlock new sources of growth, particularly in relation to the trillions of dollars that the public and private sectors will be investing every year to drive the global economy to net zero carbon emissions.

They should look for places in those new markets where they have unique advantages, and create new offerings and business models to leverage those advantages.

Digital tools and technology will be critical in building new businesses and helping companies create solutions that fulfill customer needs in new ways. For example, Norwegian mobile operator Telenor partnered with microfinance bank Tameer (with additional support from the Bill and Melinda Gates Foundation, the International Finance Corporation, and the Consultative Group to Assist the Poor) to launch a mobile-based financial services platform for unbanked and underbanked consumers in Pakistan. By the end of 2019, the operation had become the largest branchless banking service in Pakistan, with 6.4 million users. Companies also have an opportunity to invest in **deep-tech innovation**, including in artificial intelligence (AI), synthetic biology, nanotechnologies, and quantum computing—to **generate and commercialize breakthroughs in areas such as decarbonization**.

In addition, companies that embrace **sustainable business model innovation** can help transform entire value chains and ecosystems. They can, for example, introduce new circular business models to reshape the whole product usage cycle. And they can create new business models or make investments in ventures that address the looming **scarcity of critical sustainability inputs**. Consider recycled plastic. Some 45% of demand for recycled polyethylene terephthalate will be unmet by 2025, according to BCG analysis. Already, a number of companies are investing in innovation to address the gap, including through investments in R&D and recycling infrastructure.

## **MAKE THE CORE SUSTAINABLE**

Companies that aim to become sustainability leaders must assess and enhance the sustainability of their existing portfolio and operations.

In **supply chains**, for example, they have an opportunity to create end-to-end transparency, from sourcing through distribution. New tools and technologies are



critical in this area. **AI can help companies monitor, predict, and reduce their carbon emissions.** At the same time, companies can engage suppliers to impose standards, track and improve their performance, and push the ecosystem in which they operate toward greater sustainability. Companies should also re-engineer product designs to make existing products sustainable. This may involve reformulating products with more sustainable ingredients, reducing packaging, and developing refillable products or concentrated versions that reduce weight (and therefore carbon emissions tied to transportation), water consumption, and packaging. Beyond Meat, for example, leveraged **plant-based proteins** to re-engineer one of the world's most famous dishes—the burger. That innovation not only launched a popular new alternative to meat, but also helped fuel one of the most successful IPOs of 2019.

## **BUILD CAPABILITIES**

Companies that want to drive a sustainability transformation must ensure they have the right capabilities and foundation in place to succeed.

First, they must design robust governance of sustainability efforts, both at the board level and within the company itself, including accountability and incentives linked to ESG targets. Second, they need to develop strong, granular data capabilities and robust ESG reporting processes to enable the business to direct and adjust efforts on the basis of real-time performance data and to meet increasingly stringent regulatory reporting standards. Third, they should build new partnerships that allow them to pool resources, combine expertise, co-invest in ways that minimize risks associated with high-fixed-cost investments, and deliver sustainable outcomes at scale more quickly. Fourth, they must embed sustainable business model innovation in the organization.

This last element is particularly critical. Companies will need to continue to adapt their operations, product portfolio, and business models as the bar for sustainability inevitably rises over time. What qualifies as leading performance in carbon footprint or equitable business practices today, for example, will likely be table stakes in the future. As a result, companies must embrace an “always-on” mentality

toward innovating in sustainability. The process of driving sustainable business model innovation will be central to that mentality, allowing companies to assess the degree to which their current business models create positive environmental and societal impacts and to improve that performance over time.

## **OWN THE NARRATIVE, AND ENGAGE INVESTORS AND STAKEHOLDERS**

Leading companies must create a compelling and distinctive narrative around their sustainability strategy—one that connects and amplifies their purpose. At the same time, they can own their sustainability story in the public markets and share that story in a way that resonates with investors, rather than letting ratings agencies and investors tell their story for them. This means going beyond sharing the relevant information with rating agencies, and instead going directly to investors with an effective narrative that includes four key elements:

- A well-defined point of view about what is most material to the business
- A clear connection to purpose and an overall sustainability strategy
- Targets, milestones, and initiatives to get there
- Robust measurement and disclosure of ESG performance

The measurement and disclosure component is particularly critical, as it will provide evidence to investors that the business is hardwiring the narrative into the organization. Companies should go beyond the annual or biannual reporting cycle and instead provide real-time ESG measurement and reporting mechanisms that increase investors' confidence in the company's ability to monitor progress and correct course. Companies can also use ESG measurement to establish clear incentives and accountability mechanisms for employees and leaders.

As companies share their narrative with investors, they should proactively engage with shareholders, and they should do so not just during the release of quarterly earnings. In particular, they should maintain a strong dialogue with active investors who, unlike ETF or index investors, may move in and out of the stock over time.

They should also share the narrative with other critical stakeholders, including customers, employees, and members of communities in which they operate. The buy-in of these stakeholders is ultimately what drives value creation.

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Driving a successful sustainability transformation requires a fundamental shift in mindset. Company leaders should view the push toward sustainability not as a compliance exercise or a cost of doing business, but rather as an opportunity to create new value. Companies that do so will expand their competitive advantage and develop the muscle to continue to rethink and remake their business as expectations about sustainability inexorably rise in the years ahead.

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