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Synthesis

The Sustainability Agenda: More Important—and More Valued—Than Ever

By Akiba Smith-Francis

Before the COVID-19 crisis hit, corporate sustainability had been enjoying a tremendous amount of progress and visibility. Yet now, while companies' ambitions have scaled back to, in some cases, mere survival, is there any room for the sustainability agenda? Egon Zehnder spoke with 14 corporate sustainability leaders to get their perspective—and it was a surprising one: While we expected to hear concern about reversing the progress made in recent years, the sustainability leaders we spoke with remain bullish—and believe that this crisis actually may build support for ESG.

In the near term, established corporate sustainability goals will likely need to be extended or re-designed as businesses have had to focus on the immediate challenges presented by the virus. "A lot of reporting will be delayed," says one Chief Sustainability Officer. However, there seems to be a consensus that in the medium- to long-term, ESG may even increase in prominence.

COVID-19 has made clear how vulnerable many companies are to external shocks and systemic risk that can compromise business continuity. This includes geopolitical risk, cyberattacks and severe weather events expected to occur more frequently as a result of climate change. While sustainability leaders are hopeful that the pace of change with accelerate, they also believe that ESG will look different than it did six months ago. What follows are some of the changes corporate sustainability leaders expect:

A New, Broader Definition of ESG

If one thing has become clear during this crisis, it is that corporate leaders are now essentially obligated to use their resources to support the communities in which they operate. As companies now focus on keeping their employees safe, and to the extent possible, employed, the social contract between employer and employees is being rewritten. "Customers are going to ask, 'what did you do during the COVID-19 Crisis?'" says one CSO.

Some companies have repurposed their manufacturing facilities to make medical equipment or personal protective equipment for healthcare workers; others realize that they must provide direct care for their workers, as the crisis has exposed the degree of financial insecurity that many workers have been living with. One sustainability leader shared, "This pandemic has shown us the vulnerabilities we have. There is no question that the social component of ESG will dramatically shift, from employees to diversity metrics, there is a whole range," says one Chief Sustainability Officer. Employees are demanding extra protections to keep them physically safe, hazard pay to work during the pandemic, and paid sick leave where that benefit was not already offered. They will likely continue to push for greater protections and security from employers.

At the same time, consumers may punish companies they perceive to be exploiting or endangering employees, while rewarding those seen to be treating them fairly. Said one sustainability leader, "Happy, clappy engagement surveys are not going to cut it anymore. Investors and asset owners in particular are going to push companies to go beyond carbon reduction and focus on an issue that has not been front and center in most companies' minds – talent."

Increased Focus on Supply Chain

In a post-COVID world, the Supply Chain function will be critical in helping companies become more agile and adaptable. As one CSO shared, as supply chains are redesigned, companies should view this an opportunity to include an environmental review. Well-capitalized organizations focused on the long-term will take this disruption as an opportunity to consider building more resilient and environmentally sustainable systems. Following up on our "Chain Reaction 2020" link) survey of Chief Supply Chain Officers, Egon Zehnder conducted a flash survey of our respondents in March 2020 to get a sense of what had changed since the crisis and how prepared they felt. Said one respondent, "Resilience design in the supply chain is critical."

Without robust business continuity plans, some businesses were left scrambling, struggling to make or deliver goods in the midst of the COVID-19 crisis. "We have had such massive disruption that there will need to be guard rails for the supply chain," comments one sustainability leader. After conducting post-mortems of how they managed through the pandemic, Sustainability and Supply Chain leaders may partner more closely to take advantage of this opportunity. The opportunity for greater collaboration is timely. Egon Zehnder's recent conversations with supply chain leaders in Asia highlight the function's the reprioritization of long-term resilience over near-term cost and the embrace of new thinking in the face of crisis.

More Collaboration and Innovation

Like politics, a crisis can make strange bedfellows. Tackling challenges, for which there is no precedent or blueprint, like responding to global systemic threats, is already leading to more partnerships between competitors, suppliers and the public and non-profit sector. Two major pharmaceutical companies, GlaxoSmithKline (GSK) and Sanofi have announced a collaboration to develop a COVID-19 vaccine.

Of course, this is not the first time that competitors come together to solve outsized challenges. For instance, in 2019, Nestle, Unilever and PepsiCo were among many consumer goods companies (the world's largest palm oil buyers and producers) that formed a coalition to fund the development of an early-detection system for deforestation. Radar Alerts for Detecting Deforestation (RADD) is being developed in conjunction with Wageningen University in the Netherlands and World Resources Institute.

But the urgency has removed many of the roadblocks to collaboration. The more companies partner with other organizations, the more comfortable they will become with sharing information and resources to decrease cost and improve efficiency. Over time, they will get better at executing these partnerships by developing the systems and relationships that facilitate collaboration.

Investors are Further Prioritizing ESG

Contrary to expectations, so far there has been no movement away from investor support of ESG—and many sustainability leaders forecast continued, if not amplified, pressure. “Investors are clear that the full ESG agenda is still important to them,” says one sustainability leader, concluding that institutional investors “are in it for the long term.” That interest means that boards, as long-term stewards of corporate performance, must stay focused as well. As one sustainability leader put it, “[as long as] investors are interested, boards are paying even more attention to ESG.”

In March, a group of pension funds, including Japan’s Government Pension Investment Fund (GPIF), the California State Teachers’ Retirement System (CalSTRS) and the UK’s Universities Superannuation Scheme (USS) announced that they are forming a partnership for sustainable investing. They released a statement encouraging companies and asset managers to focus on the long-term and integrate ESG factors in their corporate strategy and investment process, saying that otherwise they “are not attractive investment targets for us.” BlackRock Chairman and CEO Larry Fink also recently published a statement reaffirming the company’s commitment to placing sustainability at the core of its approach as an investment manager, following up on his 2020 letter to clients. This pressure from investors may well accelerate; even during the COVID-19 crisis, ESG funds have continued to outperform their traditional counterparts.

On March 26, 2020, an Investor Statement on the Coronavirus Response, published by a group of over 300 institutional investors representing nearly $8.5 billion in assets under management, urged the business community to provide paid leave, prioritize health and safety and for those for whom it is possible maintain employment, offer child care assistance and extend health benefits for employees who have been laid off. Their perspective is that the long-term viability of the companies in which they invest is dependent on the wellbeing of employees, suppliers, customers and communities – and that not attending to issues related to employee and public health represents a significant financial risk.

Corporations will need to take care to invest in truly substantive actions or risk being seen as green-washing or virtue signaling, which would likely be punished by investors and consumers alike. Said one sustainability leader, “People will remember what companies did in this crisis.”

Our Take: Sustainability Leaders' New Approach

The ability to influence others and collaborate across functions has always been important for sustainability leaders. Their roles are relatively new in corporate structures and many do not have large teams or control a significant budget. Since this structure is not likely to change in the near future, the increased visibility and prominence of ESG will mean that Chief Sustainability Officers will need to be even more effective at collaboration and influence – understanding where power is located in organizations and getting others to take action. The ability to integrate plans into corporate strategy in ways connect to the profit-making objective will be equally as important for those coming from technical or commercial backgrounds. As one leader put it, "Sustainability professionals need to quickly begin talking about environmental and social issues in terms of risk and the size of the financial impact they could have on the company. They can be material to the business."

Leaders will also need to develop processes that enable measurement of metrics relevant to sustainability rating agencies such as Sustainability Accounting Standards Board (SASB) or Sustainalytics. Said one leader, "there are now klieg lights on disclosure." Given their stakeholders' increased focus on ESG, it will be even more important for sustainability leaders to interpret the data they have collected and use it to tell a compelling story – to investors, employees, regulators and the community at large.

Sustainability leaders are often also responsible for Corporate Social Responsibility. CSR has historically been focused on employment issues related to manufacturing and procurement in the developing world, specifically issues of child labor and trafficking. With the increased spotlight on how companies treat employees in wealthier countries, CSR leaders may now need to begin addressing issues like health (and other) benefits, living wages and the pay gap. As one corporate sustainability leader shared, "The health and safety of employees is much more visible and represents a substantial risk. Corporations will also likely play a bigger role addressing income inequality."

If there is a silver lining to the COVID-19 crisis, which has had a tragic impact on so many lives around the world in terms of loss of life and income, it may be that the role of ESG moves from one that is "nice to have" to one that companies finally realize is essential for survival- both of the organization and the wider community.

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Covid-19 Micro-Website

We have launched a micro-website where this and other informative pieces are posted. This site will be regularly updated: click here for further details.

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