



# CRAFTING XELLA GROUP'S ESG STRATEGY FOR THE 2020s

By Michael Leicht, Alexander Brunst, Claudia Kellert, Martin Feth, Patrick Herhold, Holger Rubel, and Matthias Tauber

**I**N THE LAST FEW years, environmental, social, and governance (ESG) strategies and ratings have become increasingly important to many stakeholders, including banks, investors, regulators, customers, and employees.

BCG analysis shows that strong ESG performers have an advantage when it comes to attracting talent, securing financing at a lower cost of capital, and reducing regulatory risk. For these players, having a potent ESG strategy leads to greater profitability and higher market valuations.

That's why the Xella Group—one of the world's leading manufacturers and suppliers of building and insulation materials—decided to partner with BCG in 2020.

But many companies in the construction materials industry hesitate to develop robust ESG strategies because they mistakenly believe that it is impossible for firms in hard-to-abate sectors to obtain good ESG ratings. Some may believe that companies can only score well once they have already implemented multiple ESG initiatives. The

truth is that ESG rating agencies look not only at a company's current behavior (at its environmental footprint, for example) but also at its commitments and plans to lower emissions in the future. Other companies might hesitate out of fears that ESG projects involve high costs and yield few financial returns. In fact, ESG-related improvements have the potential to bring down spending.

Despite these concerns, a handful of leaders in the building materials industry have already started developing ESG targets, increasing transparency, taking steps to reduce their environmental footprints, and pursuing favorable risk ratings. These are important strategic moves for companies that wish to be good corporate citizens amid rising regulatory pressure and greater public scrutiny.

## An ESG Strategy Built for the 2020s

After launching multiple ESG pilot projects, Xella Group wanted to coordinate

and bolster its ESG activities in order to reduce costs, improve profitability, and stake out a reputation as an ESG leader in its field. Therefore, Xella partnered with BCG's global network of sustainability experts, who have helped develop strategies for leading players in many industries, including building materials, steel, chemicals, and mining.

A team of BCG consultants worked with Xella over a ten-week period to update the company's existing ESG strategy and to develop ambitious targets.

### FOCUS ON MATERIAL ESG TOPICS

The first step in the project was to analyze company data and conduct dozens of interviews with senior managers and other key executives to map 30 of Xella's ESG initiatives at different stages of maturity and implementation.

From an environmental perspective, Xella's products are energy efficient and sustainably produced using recycled inputs and cradle-to-cradle processes. In terms of social performance, the company has a proven track record of safeguarding the health of its employees, and it has lowered the frequency of lost-time injuries by more than 50% since 2017. Xella encourages employee engagement and has made strides toward building an inclusive workforce. Women make up 20% of Xella's management team—one of the highest percentages in the materials industry. Finally, when it comes to governance, Xella demands ethical conduct from its own employees and has a zero-tolerance policy toward fraud, bribery, and any sort of anticompetitive or discriminatory behavior among its suppliers.

After mapping these initiatives, our team then leveraged BCG's databases to benchmark Xella's performance against key competitors across a range of metrics, including carbon intensity, energy consumption, employee satisfaction, and the ratio of women to men in the workplace. This enabled Xella's leadership to define key ESG strengths and discover areas for further development.

Next, Xella and BCG conducted a thorough materiality assessment to set the right focus areas for the revised ESG strategy. Using frameworks from the Global Reporting Initiative (GRI) and the Sustainable Accounting Standards Board (SASB), as well as industry reports and publicly available data on peers, our team compiled a long list of the ESG topics that were most likely to impact Xella's financial condition or operating performance. We also gathered input from more than 100 internal and external stakeholders—including employees, customers, suppliers, investors, and industry associations—to identify additional critical items.

Xella then prioritized the 15 topics it considered to be the most important to stakeholders and critical for business success. We clustered these topics into four focus areas:

- **Environmentally Friendly Production.** Both internal and external stakeholders expect that Xella will take ongoing actions to make its production processes as environmentally friendly as possible. By conserving resources, improving energy efficiency, and reducing emissions, Xella can reduce its carbon footprint and help mitigate climate change.
- **Low-Carbon and Circular Products.** The delivery of sustainable housing solutions forms the core of Xella's corporate strategy. By continuously innovating to develop low-carbon products and improving established processes, Xella can advance the development of a more sustainable building sector based on circular-economy principles.
- **Social Responsibility for Employees.** Xella's employees drive the innovations that form the foundation of its long-term success. The company seeks to meet and exceed stakeholder expectations regarding employee health, safety, development, and satisfaction worldwide.
- **Responsible Corporate Governance and Supply Chain.** Xella has a reputa-

tion as a responsible company and business partner. Xella recognizes that all stakeholders—including employees, customers, and suppliers—expect that the company will adhere to the law and local regulations while engaging in competitive and ethical business behaviors.

### SET THE RIGHT ESG AMBITIONS

Having determined the most-important ESG focus areas, Xella and BCG set out to define the right level of ambition for the company over the next decade. Exhibit 1 reveals Xella’s selected ESG goals for this period. To establish a set of ambitious, yet realistic targets, our team applied a combination of different external and internal lenses, including:

- Target Benchmarking Against Peers.** To ensure that the new ESG targets were suitably ambitious, BCG performed a benchmark analysis against a group of more than ten of Xella’s international peers. Certain metrics were straightforward, such as those used to measure the reduction in CO<sub>2</sub> emissions or the percentage of women in managerial roles. Careful context-specific considerations and adaptation were needed to benchmark participation in the circular economy and other dimensions that are harder to quantify.
- Science-Based Targets.** As a second external lens, we considered science-based targets, such as those set forth in the Paris Agreement, which was signed in 2016 by world governments committed to trying to limit the rise in global temperature to 1.5°C above preindustrial levels. Science-based targets show companies how much and how quickly they need to reduce their greenhouse gas (GHG) emissions to prevent the worst effects of climate change.
- Senior Management Guidance.** Building on these external perspectives, we ran a series of workshops based on the “comply-compete-lead” framework to help Xella’s leadership set high-level ambitions across the company’s four ESG focus topics. For each ESG dimension, senior managers decided whether the organization should focus on meeting legal requirements, staying competitive with most peers, or differentiating itself as a leader in a particular area.
- Bottom-Up Estimates.** Our team explored how much it would cost and how long it would take to achieve the ambitions of senior management. We explored any technical constraints that might come into play and investigated

EXHIBIT 1 | A Selection of Xella’s ESG Targets for the Next Decade



Sources: Xella; BCG analysis.

Note: EOY targets used.

<sup>1</sup>Compared with 2019 numbers. Includes Scope 1 and Scope 2 emissions.

whether Xella might be able to shoot for a more ambitious ESG target with only limited incremental costs.

### LINK ESG AND BUSINESS STRATEGIES

Once Xella had defined its updated mid- and long-term ESG targets, our team identified a set of initiatives and quantified business cases for reaching these targets. We formulated a guiding principle that each ESG initiative should also make Xella’s business model more robust, profitable, and ultimately more sustainable in the long run.

The business impact of many environmental initiatives is relatively easy to quantify. For example, if a company installs solar panels on top of its factories to replace some grid electricity and reduce CO<sub>2</sub> emissions, the initial capex spending from the installation is quickly paid for by lower electricity costs. Similar logic applies when old equipment, such as curing ovens, are replaced with newer, more energy-efficient technology. Xella is taking these steps—and others—to become more sustainable. (See Exhibit 2.)

Implementing initiatives for participating in the circular economy will also contribute to Xella’s long-term business performance. By using a new crusher to process production waste, Xella will be able to reduce disposal costs and either reuse its waste or sell it in secondary markets to

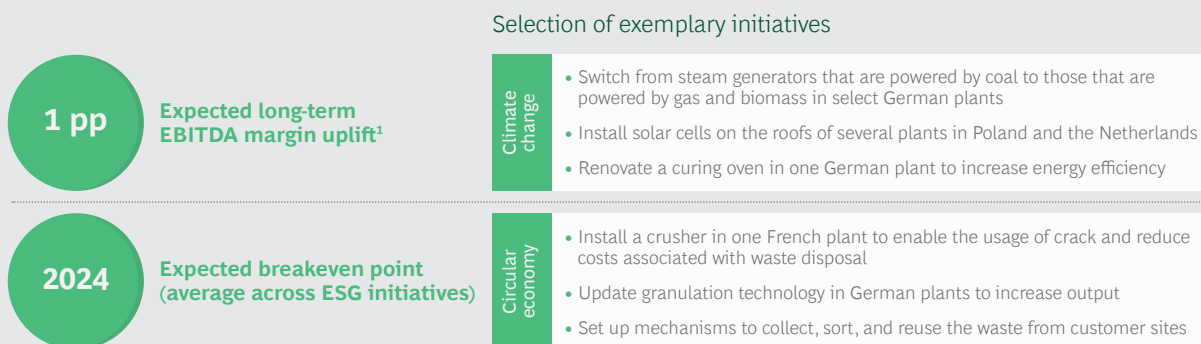
generate additional revenue. Such activities as gradually increasing granulation quotas will allow the company to reuse more recycled materials and save on purchases of primary raw materials. Finally, by putting mechanisms for collecting waste from customer sites in place, Xella can increase customer satisfaction and gain access to a new stream of relatively inexpensive feedstock for its production.

All businesses can generate further indirect benefits by carrying out social and governance initiatives. A highly engaged, well-trained, and safe workforce will naturally be more productive and motivated to deliver stronger results. Higher levels of diversity are often associated with increases in creativity, productivity, customer orientation, and better decision making. Having a strong focus on compliance and a zero-tolerance policy toward corruption and bribery can go a long way in mitigating business, legal, and reputational risks. Companies should consider pursuing well-executed social and governance programs to produce such outcomes.

### Achieving External Recognition

Once they have developed a comprehensive ESG strategy, companies should take the next step of communicating their ESG commitments to the world. This process can be hard to navigate, as more than 100 players operate in the complex global

EXHIBIT 2 | Xella’s New ESG Initiatives Will Contribute to the Company’s Long-Term Success



Sources: Xella; BCG analysis.

Note: All figures are based on estimates from November 2020. pp = percentage point. EBITDA = earnings before interest, taxes, depreciation, and amortization.

<sup>1</sup>Approximate figure used for EBITDA margin uplift.

ESG-rating-and-reporting ecosystem, where a wide range of methodologies exist. Public companies receive ratings automatically, while private entities must choose whether to receive a rating and which agency (or agencies) to work with.

Xella was eager to receive an ESG rating because of its strong track record and the ambitious targets it has set for the 2020s. The company asked Sustainalytics, one of the largest and most respected rating agencies, to initiate coverage and perform an objective external assessment of Xella's ESG performance. Xella and BCG provided Sustainalytics with full transparency into Xella's ESG activities, policies, risk-mitigation strategies, management structures, and targets.

In November 2020, Sustainalytics named Xella the top ESG leader among 115 rated peers in the construction materials industry. The Sustainalytics rating objectively confirms that "the company is at low risk of experiencing material financial impacts from ESG factors, due to its medium exposure and strong management of material ESG issues."

BCG also advises firms to take the initiative in publishing a high-quality sustainability report. Investors value ESG scores from rating agencies, but many investors also engage directly with companies and view these documents as key research tools when making their own assessments of ESG performance. In addition, rating agencies often treat the sustainability report as a primary source of information, so having a comprehensive report allows companies to tell their own stories and present their ESG accomplishments in the best light possible, instead of waiting for agencies' ratings to define them. BCG helped collate the data and other material that Xella is currently using to develop its own sustainability report.

## The Journey Toward Better ESG Performance

After helping many private and public companies, BCG has identified seven actions that companies should take to develop their ESG strategies, just as Xella is doing today:

- Fully integrate ESG considerations into the broader business strategy.
- Determine those ESG topics across the value chain that are most likely to have the greatest financial materiality now and in the future.
- Develop a deep understanding of investor priorities and practices for ESG investing.
- Take a proactive approach to engaging and educating current, as well as potential, investors on ESG issues and priorities.
- Maintain clear, effective, and consistent communication on ESG topics with all stakeholders.
- Build time or space for ESG topics in planning sessions, meetings, and dashboards (across business units and functions).
- Implement clear processes to ensure the reliable measurement and internal reporting of ESG data.

By executing strongly in these seven areas, companies can improve their ESG performance and gain recognition as ESG leaders in their fields.

## About the Authors

**Michael Leicht** is Xella's Head of Group HR and the CDO member of Xella's executive committee. He is also the ESG Sponsor on the ExCom. You may contact him by email at [michael.leicht@xella.com](mailto:michael.leicht@xella.com).

**Alexander Brunst** leads Xella's Digital Transformation and ESG programs. You may contact him by email at [alexander.brunst@xella.com](mailto:alexander.brunst@xella.com).

**Claudia Kellert** is Xella's lead for public and investor relations and maintains Xella's relationships with ESG rating agencies. You may contact her by email at [claudia.kellert@xella.com](mailto:claudia.kellert@xella.com).

**Martin Feth** is a partner and an associate director in the Munich office of Boston Consulting Group. You may contact him by email at [feth.martin@bcg.com](mailto:feth.martin@bcg.com).

**Patrick Herhold** is a managing director and partner in BCG's Munich office. You may contact him by email at [herhold.patrick@bcg.com](mailto:herhold.patrick@bcg.com).

**Holger Rubel** is a managing director and senior partner in the firm's Frankfurt office. You may contact him by email at [rubel.holger@bcg.com](mailto:rubel.holger@bcg.com).

**Matthias Tauber** is a managing director and senior partner in BCG's Munich office and the head of BCG for Germany, Austria, and Central Eastern Europe. You may contact him by email at [tauber.matthias@bcg.com](mailto:tauber.matthias@bcg.com).

## About BCG

Boston Consulting Group partners with leaders in business and society to tackle their most important challenges and capture their greatest opportunities. BCG was the pioneer in business strategy when it was founded in 1963. Today, we help clients with total transformation—inspiring complex change, enabling organizations to grow, building competitive advantage, and driving bottom-line impact.

To succeed, organizations must blend digital and human capabilities. Our diverse, global teams bring deep industry and functional expertise and a range of perspectives to spark change. BCG delivers solutions through leading-edge management consulting along with technology and design, corporate and digital ventures—and business purpose. We work in a uniquely collaborative model across the firm and throughout all levels of the client organization, generating results that allow our clients to thrive.

## About Xella Group

With over 7,000 employees, Xella Group is one of the leading, internationally operating solution providers of building materials. Xella is headquartered in Duisburg (Germany), with 95 plants and sales organizations in more than 25 countries. Xella is the parent company of renowned brands such as Ytong, Silka, Hebel, Multipor or Urso and is one of the pioneers in digitally supported building processes. In many of its markets Xella holds a leading position.

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