Sustainability-Linked Value Creation: Real World Examples

This document serves as a companion to the NYU Stern Center for Sustainable Business' *Sustainability-Linked Value Creation Guide for Private Equity Limited Partners*. It is designed to be shared with investment teams and private equity firms, as well as anyone interested in understanding how sustainability-linked value creation is applied in practice.

Sustainability-Linked Value Creation

General Partners (GPs) have traditionally approached sustainability primarily through the lens of risk mitigation, focusing on ESG factors to reduce exposure to potential downsides. While risk management is a critical component, it represents only one of the nine mediating factors of financial performance outlined by the NYU STern CSB Return on Sustainability Investment (ROSI™) framework. The remaining eight factors emphasize value creation opportunities, such as innovation, operational efficiency, employee relations, and customer loyalty. This highlights the significant untapped potential for sustainability initiatives to move beyond a defensive strategy and become powerful engines for growth and profitability.

Freya Williams' book, *Green Giants: How Smart Companies Turn Sustainability into Billion-Dollar Businesses,* further reinforces this perspective by showcasing how leading companies such as Tesla, Chipotle, and IKEA have embedded sustainability into their core strategies, creating a strategic moat around their businesses that drives financial success. It also presents examples of product lines, such as Nike's Flyknit technology and the Toyota Prius, that have fundamentally reshaped their respective companies. The Nike Flyknit technology allowed for athletic shoes to be woven instead of sewn together, resulting in a lighter, higher performance shoe that also reduced waste by 80% compared to conventional shoes. The Flyknit technology sparked a wave of innovation, creating a product line that generated over $1 billion in revenue.[1] Similarly, Toyota's Prius revolutionized the automotive industry by introducing hybrid technology, blending environmental stewardship with consumer appeal to achieve widespread market adoption and an estimated $15 billion in revenue in 2013.[2]

While sustainability experts are generally well-versed in these examples, mainstream investors often remain unaware of the transformative potential of sustainability as a value driver. A persistent gap—or even a wall—frequently exists between sustainability professionals and investment teams, hindering the effective integration of sustainability expertise into investment strategies. Freya Williams' *Green Giants* and our research at the NYU Stern Center for Sustainable Business (CSB) underscore the immense opportunity to bridge this divide. Both demonstrate how sustainability-linked value creation leverages environmental and social responsibility as powerful competitive advantages. By aligning operations with long-term sustainability goals, businesses not only fulfill their sustainability goals, but also unlock substantial financial benefits. For private equity GPs, a growing body of evidence highlights the untapped potential to identify and support sustainable business models capable of delivering measurable impact alongside significant profitability.

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[1] Freya Williams, *Green Giants: How Smart Companies Turn Sustainability into Billion-Dollar Businesses* (New York: AMACOM, 2015), pg 6.

[2] Ibid, pg 7.

NYU Stern CSB Sustainability-Linked Value Creation Examples

Value Creation Through Decarbonization Initiatives

Decarbonization strategies offer numerous advantages for businesses. First, reducing carbon emissions often leads to significant cost savings by optimizing energy efficiency. Transitioning to clean energy sources tends to reduce exposure to energy pricing volatility, aiding financial stability. Furthermore, by lowering carbon emissions, companies can avoid potential carbon tax fees and penalties, ensuring compliance with evolving regulatory frameworks and market demands.

Adopting a decarbonization strategy can also enhance market positioning, allowing companies to attract environmentally conscious consumers, achieve higher market share, and potentially command premium pricing. Such strategies can foster stronger relationships with supply chain partners, enhancing resilience and reliability. Lastly, demonstrating a commitment to sustainability can lead to a lower cost of capital. Below are a few examples from NYU Stern CSB ROSI™ research:

Capital Power

Capital Power is a Canadian electricity generator with approximately $1bn in annual revenues. The company evaluated the business case for an early exit from coal-generated electricity and transition to wind and solar energy. Upon applying the ROSI™ framework, three primary benefits were identified:

- Improved employee retention and lower turnover due to sustainability commitments, valued at $4 million
- Increased competitiveness for new customers interested in renewable energy, valued at $41 million
- Lower cost of capital for sustainability initiatives, valued at $189 million

The total estimated benefit from this early decarbonization strategy was approximately $234 million, demonstrating the significant financial upside of sustainability-driven initiatives in the energy sector.

GUNDERSEN HEALTH SYSTEM®

Gundersen Health System is a healthcare organization with seven hospitals and 35 clinics across Wisconsin, Minnesota and Iowa. As part of the company's energy management initiatives, it implemented energy retrofits and incorporated net zero design features in an outpatient clinic. Gundersen created up to $35,000 or $1 per sq.ft in annual benefits from energy retrofits, and up to $66,000 or $2 per sq.ft in annual benefits from net zero building design. This strategy led to an estimated 72% reduction in emissions compared to standard building design.

EILEEN FISHER is an American fashion brand founded in 1984. In 2019, it instituted a transportation optimization strategy, by shifting its transportation mix away from air towards sea and land. The company achieve significant financial and environmental benefits:

- Reduced transportation costs by approximately $1.6 million in 2019 compared to 2015
- The shift resulted in a cumulative societal benefit of around $150,000 from 2015 to 2019 due to the reduction in greenhouse gas emissions

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Value Creation Through Sustainable Sourcing Examples

Sustainable sourcing is increasingly critical as it addresses pressing environmental and social challenges while meeting investors' and customers' expectations for ethical practices. It can enhance market share, command premium pricing, and foster customer loyalty by aligning with growing consumer demand for responsibly sourced products. Moreover, through third-party certifications, sustainable sourcing reduces reputational, operational, market and regulatory risks by ensuring compliance with environmental and social standards. It also cultivates stronger relationships with resilient, loyal, and high-quality suppliers, improving supply chain reliability. Additionally, these practices support community engagement, securing a social license to operate and strengthening the long-term viability of the business. Below are a couple of examples of our ROSI™ work at NYU Stern CSB:

McCormick & Company, Inc. is a global food company that manufactures spices, seasonings and condiments. It's a Fortune 500 company with nearly $7 billion in annual revenues. It worked with NYU Stern CSB to quantify the benefits of its Sustainable Sourcing Program (SSP) associated with its five iconic herbs and spices: black pepper, red pepper, cinamon, vanilla and oregano. The findings using the ROSI™ methodology were:

- Program benefits monetized were: sales & marketing, lower cost of capital, risk management and earned media
- Benefits were estimated at $6 million annually
- The benefits were expected to increase by 60-70% by 2025

NYU Stern CSB collaborated with McDonald's, Carrefour, slaughterhouses, ranchers and NGOs to monetize the benefits of a deforestation-free supply chain for beef in Brazil. Here are the results:

- **Rancher benefits**: 2.3x increased productivity and 7x increase in profitability, resulting in a $29 million NPV over 10 years
- **Slaughterhouse benefits**: $100 million NPV over 10 years from reduced risks, improved supply chain stability and premium pricing
- **Retailer benefits**: $40 million NPV over 10 years from reduced risks, talent enhancement and premium quality
- **Societal benefits**: 20% reduction in Greenhouse gas emissions

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Value Creation Through Circularity Examples

Circularity offers a range of benefits for businesses. By optimizing resource use and minimizing waste, companies can achieve significant cost savings while reducing their environmental impact. Introducing circular practices can unlock new product opportunities, attract environmentally conscious consumers, and strengthen customer loyalty, often leading to higher market share and price premiums. Additionally, closing resource loops enhances supply chain security and reduces exposure to material shortages. Verified sustainability claims through third-party certifications build trust, and positive media coverage further elevates the brand's reputation, driving long-term competitive advantage. Below are recent case studies:

AdvocateHealthCare

Advocate Health Care is part of Advocate Health, the third largest nonprofit integrated system in the U.S. It collaborated with NYU Stern CSB to find and quantify operational efficiencies from switching from single use devices (SUDs) to reprocessed devices (rSUDs). Findings included:

- **Reduced procurement costs**: Average annual benefit of $3 million (3% of operating income) and a $17.4 million NPV over a 10-year period
- **Reduced waste disposal costs**: $287k per year ($1.7 million NPV over 10 years)
- **Reduced GHG emissions**: There was an 857 MT reduction in CO2e (GHG emissions) over a 10-year period with an annual earnings benefit of $187K per year and $1.1 million NPV over 10 years.

Reformation

Reformation, a clothing brand founded in 2009 with sustainability at the core of its strategy, partnered with thredUP, the world's largest online consignment and thrift store, to enhance its circularity efforts. Through this partnership, Reformation offered shopping credits to customers who successfully consigned items with thredUP. Using the ROSI™ methodology, four key benefits of this initiative were identified and quantified, totaling $1.9 million in 2019:

- Profit generated through partnership program: $1,000,000
- 2,500 new customers added to Reformation's customer base, generating incremental profit: $400,000
- Reduction in customer acquisition costs: $100,000
- Increased earned media from partnership visibility: $400,000

Value Creation Through Employee Satisfaction, Safety and Well-Being Examples

Quantifying value creation in the social component (the "S" in ESG) often presents greater challenges than measuring environmental impact, primarily due to its complexity and lack of standardization. Unlike environmental metrics, which benefit from widely accepted frameworks, social metrics vary significanlty across organizations and industries. Social issues are inherently multifaceted and interconnected, making it difficult to isolate the impact of specific interventions. However, by leveraging the ROSI™ methodology, organizations can overcome these challenges, enabling them to better measure and unlock value in arguably their most valuable asset: their employees.

Employee satisfaction, safety, and well-being are critical drivers of organizational success and offer a clear pathway to creating measurable social value. A supportive and safe work environment enhances productivity and fosters loyalty, reducing turnover and recruitment costs. Prioritizing safety mitigates risks of workplace injuries and lowers insurance expenses. A focus on sustainability and purpose drives employee recruitment, engagement and retention. Additionally, companies that invest in their workforce's well-being build a positive corporate reputation, strengthening relationships with both employees and customers. By aligning workplace policies with these principles, organizations not only ensure compliance and reduce the risk of lawsuits but also cultivate an engaged, motivated, and resilient workforce. This, in turn, drives customer satisfaction and overall business success.

Recreational Equipment Inc. (REI) is the largest consumer co-op and specialty outdoor retailer with over 180 stores in 41 states. In 2019, the company implemented a sustainability program and collaborated with NYU Stern CSB to better understand the impact of its embedded sustainability strategy.

- **Employee Wellbeing Programs:** REI provided employees with two paid "Yay Days" for outdoor activities. In addition, it closed stores on Black Friday through its #OptOutside campaign, giving employees a paid day off.
- **NYU Stern CSB assessed the impact:** Using the ROSI™ methodology, CSB found that REI's program led to $34 million (or 5% of total payroll) in net benefits from increased productivity, retention and overall satisfaction in 2019
- **Conclusion:** REI's investment in sustainability and employee-focused programs not only aligned with its core values but also with positive financial outcomes

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KKR's Broad-Based Employee Ownership Program

Kohlberg Kravis Roberts (KKR), a leading private equity firm with $190 billion in assets under management (as of September 2024), has implemented a broad-based employee ownership program to drive financial success, address wealth inequality, and foster greater employee engagement within their portfolio companies. The program allocates a portion of a company's future value into an Employee Ownership Pool, ensuring all employees, including front-line hourly workers, benefit financially. On average, employees receive payouts equivalent to 6-12+ months of compensation upon the investment's exit.[3] The program addresses several interconnected issues in their portcos:

- Low employee engagement and high turnover
- Lack of shared success
- Wealth inequality
- Operational inefficiencies

[3] Thomas, Graham. 2024. Driving Financial Success Through Shared Ownership. NYU Stern CSB Private Equity Sustainability Practicum, December 10, 2024, New York, NY.

Results from companies adopting this approach highlight its transformative impact. For example, CHI Overhead Doors achieved reduced work-related injuries, enhanced employee morale, and a significant expansion of its operating margin, ultimately leading to a high valuation at exit (see details in the box below). At Ingersoll Rand, extending ownership to all 16,000 employees reduced quit rates from 20% to 3% while boosting employee engagement scores from the 20th to the 90th percentile. Similarly, Insight Global's ownership program for its 4,500 employees lowered quit rates from 45% in 2017 to 14% in 2022.[4]

CHI Overhead Doors - KKR's Broad-Based Employee Ownership Example

KKR acquired CHI Overhead Doors in 2015. Initial employee surveys revealed significant challenges: only 30% of employees responded, reflecting low morale and a widespread belief that the survey would have no impact. Workplace safety was also a concern, with 14% of employees sustaining a reportable injury annually.[5] More broadly, the company faced operational inefficiencies, such as wasted scrap metal and inefficient delivery routes.

KKR set aside $1 million a year for capital improvements and empowered employees to choose the improvements. The workers' first request was for an air-conditioned factory—an almost unheard-of investment in an open-floor uninsulated plant – but KKR agreed. Implementing the workers' request boosted morale, lowered injury rates and increased summer productivity.[6] KKR also implemented other strategies to collaboratively tackle the scrap metal and delivery route problems. Over time, small improvements added up and profit margins increased to 35% from 20%, – a truly remarkable profit margin for this industry.[7]

In 2022, when KKR sold CHI for $3 billion, it generated a 10x return on the equity it had invested. It amounted to KKR's most successful deal in two decades. It paid out $360 million to its 800 employees,[8] with the average hourly worker earning $175,000.[9]

Conclusion

Our NYU Stern CSB ROSI™ real-world examples as well as others presented in this document underscore the transformative power of embedding sustainability into core business strategies, serving as a compelling blueprint for aligning financial success with positive societal impact. By leveraging initiatives such as decarbonization, sustainable sourcing, circularity, and employee engagement, companies and private equity firms can unlock financial gains while addressing critical environmental and social challenges. These efforts not only drive operational efficiencies and enhance profitability but also build stronger stakeholder relationships, mitigate risks, and create long-term competitive advantages.

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[4] Will Stone, "Shared Success: KKR's Vision for Employee Ownership to Increase Productivity," Business Today (December 1, 2023) https://journal.businesstoday.org/bt-online/2023/shared-success-kkrs-vision-for-employee-ownership-to-increase-productivity

[5] Rouen, E., & Campbell, D. (May 2023). How KKR Got More by Giving Ownership to the Factory Floor: 'My Kids Are Going to College!' Harvard Business School Working Knowledge. https://www.library.hbs.edu/working-knowledge/how-kkr-got-more-by-giving-ownership-to-the-factory-floor

[6] Ibid.

[7] Ibid.

[8] Ibid.

[9] Emily Bonta, "KKR's Co-Head of Global Private Equity Shares How Employee Ownership Drives Long-term Business Value," *JUST Capital* (Mach 16, 2023) https://justcapital.com/news/kkr-pete-stavros-how-employee-ownership-drives-long-term-business-value/.