

# Session 1 – Solving the net-zero equation

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**26 April 2022**

From awareness to action: a five-step programme with McKinsey & Company. A summary of session 1.

On 26 April, Chapter Zero and McKinsey hosted the first event in a series focused on turning climate change awareness on corporate boards into concrete actions. The partnership will provide five sessions focussed on creating the change we need in boardrooms to drive the net-zero transition. Following on from the initial scene-setting session, the four subsequent sessions will deliver important tools for 1) strategy setting in uncertainty; 2) developing quality plans to enable those strategies; 3) supporting leadership and cultural change required to deliver plans; and 4) a forward look at how COP27 may impact companies.

When it was founded three years ago, Chapter Zero's mission was to put climate change on the agenda of boards in the UK. Chapter Zero's membership has since grown to over 2,000 directors and has helped spur an international movement of similar membership organisations – there is still work to be done, but climate change is clearly a concern on many directors' minds. Still, the world continues to fall short of international climate targets and businesses must play a key role in changing this. It is time to turn ambition into action.

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## Climate risks and the net-zero equation

Reaching net zero requires reducing greenhouse gas emissions as far as possible and balancing the residual emissions with carbon capture and greenhouse gas removal. Despite progress on some key fronts at COP26, the world is still falling short of its climate targets and needs to take large-scale action within the next few years to meet targets set under the Paris Agreement.

[Recent IPCC reports](#) have made clear the impacts of climate change. Aside from the clear moral imperative to act, these impacts pose a myriad of business risks including supply chain disruptions, productivity loss, and damage to physical assets. Of course,

the actions needed to mitigate climate change also pose significant transition risks to businesses.

Meeting global climate targets will require action across the entire global economy, and McKinsey describes [six key characteristics](#) that define the worldwide [transition to net zero](#). It is:

- **Universal:** All major energy and land-use systems would need to be transformed to achieve net-zero emissions. Every country and every sector of the economy would be affected.
- **Significant:** Spending on physical assets would be \$9.2 trillion annually, up \$3.5 trillion per year from today and up \$1 trillion per year after accounting for current policies and expected growth in population and incomes. Total spend to 2050 would reach ~\$275 trillion.
- **Front-loaded:** Spending would rise to 8.8% of GDP from 2026 to 2030 vs. just under 6.8% today, before falling back down.
- **Uneven:** Developing countries and fossil fuel-rich regions are most exposed. Sectors accounting for 20% of GDP are disproportionately exposed.
- **Exposed to risks:** There would be increased risk of supply shortages, price increases, and volatility. Switching from high to low-emissions assets could strand assets (~\$2.1 trillion of power assets by 2050).
- **Rich with opportunity:** The transition would minimise the further build-up of physical risks. It could create more efficient operations from decarbonisation as well as new markets for low-emissions goods and services.

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## How businesses should respond

McKinsey has identified [nine key requirements](#) for ensuring an ‘orderly transition’ that mitigates climate change whilst managing transition risk. Attendees had different views about the requirements towards which their organisations had made the most progress, but generally agreed that there had been significant action on technology and innovation and good progress in other areas such as the implementation of governing standards and effective institutions. In general, NEDs expressed that there is room for improvement in commitment and enabling mechanisms including collaboration between public and private sector leaders.

To properly navigate the net-zero transition, businesses must ensure strategic resilience in an era of certain volatility. Each sector and each business will face different challenges, but [six key steps](#) will help any organisation chart their journey through this transition:

- **Develop capacity to conduct climate risk assessments and scenario analyses.** These should include a granular understanding of risks and opportunities and be run iteratively as new information becomes available.
  - **Build resilience as a source of competitive advantage.** Bolstering a business' financial, operational, and physical resilience to climate risk will require holistic action, including community engagement and shifting to a circular business model.
  - **Accelerate digitalisation efforts.** Digital adoption tends to drive efficiency and can be a good starting point for businesses looking to become more sustainable.
  - **Relax key constraints on climate action.** Consider all options and solutions when thinking about the net-zero transition.
  - **Promote and utilise private-sector solutions.** Governments at all levels are creating positive and negative incentives for private sector actors to take climate action – this trend will likely increase in the coming years.
  - **Play offense.** Organisations that focus only on defending against climate change will fall behind those that shift into fast-growing subsectors and seize climate-related opportunities.
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### Key questions and ways forward

Attendees had the chance to discuss the climate questions that motivate them and their organisations. Some key themes emerged, the most prominent of which was the importance of collaboration. Collaboration is vital at all levels, including between different sectors, between businesses and other stakeholders, between incumbents and disruptors, and between large corporations and SMEs. Collaboration might involve setting appropriate standards, sharing relevant data, and ensuring that entire supply chains are minimising their contribution to climate change. Boards play a key role in setting the culture in organisations that will foster collaboration. Participants also felt that fostering cooperation between industry trade groups could unlock new ways of working across supply chains.

Participating NEDs noted uncertainty around conditionality. Which actions will be voluntary, and which will businesses be forced to take? This is relevant not only to legislation and regulation, but to the conditions that businesses impose on each other – for example those attached to loans and equity investments. The urgency of the net-zero transition cuts across all of these points – the action that business leaders take within the next decade will determine whether their organisations and industries survive the net-zero transition.

Participants showed a strong appetite for more concrete steps they could take with their boards. In subsequent sessions, we will incorporate a 'What Next?' segment to help NEDs crystallise next steps with their boards to move forward confidently.