

WHAT REALLY MATTERS

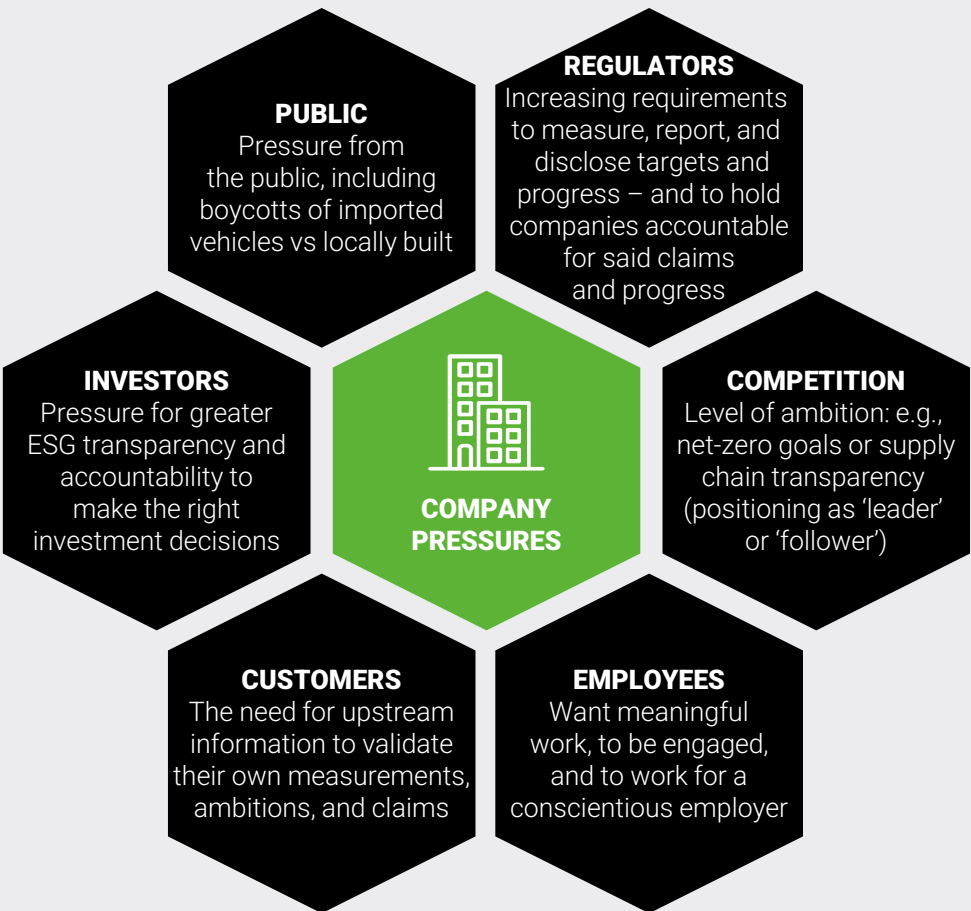
ESG disruption and its impact on the
Automotive Industry

EXECUTIVE SUMMARY

Globally, automotive firms are struggling with increasing market pressure. Investors want transparency, regulators require greater reporting, customers demand more information, employees want more from their workforce, and competitors are ‘upping their game’. But how should organisations be set up to meet these challenges head on?

Most OEMs have committed to achieve net zero to appeal to the different parties’ demands. While half target net zero by c.2040, the remainder aim for closer to 2050. What we find of particular interest is that there appears to be no big difference (publicly) in the approach of the two groups in achieving their net zero goals.

Furthermore, our research suggests that significant industry disruption is needed to hit these net zero goals – yet the ESG or sustainability related investments announced to date do not appear significant enough to achieve the ambitious goals outlined.



To mitigate the impact of these pressure points and prepare them for the future, companies must understand how regulations will impact them, know what they want to target, gain greater control over their data, and understand how they will reach those targets (both interim goals and resources required), as well as ensure that their organisational structure is fit for purpose.

Our **ESG Readiness Assessment** helps organisations prepare for and mitigate potential regulatory actions – from assessing where you are today to helping you set targets and monitor your progress in a way specifically tailored to you.

If you would like to discuss our ESG Readiness assessment in more detail, please contact one of our experts [here](#).

DESPITE GREATER CLARITY ON REGULATIONS, GAPS PERSIST IN CSRD REPORTING READINESS

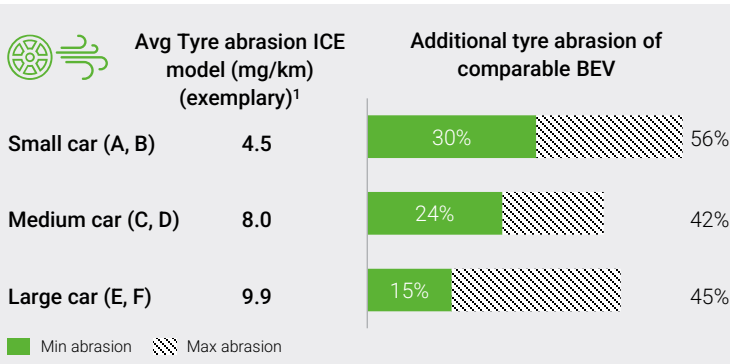
REGULATORY PRESSURES

Across Europe, businesses scramble to react to increasing reporting requirements. These are focused on building greater transparency and comparability for investors and accountability in limiting global warming to a 1.5°C.

Euro 7 – applicable to new cars from July 2025 [\(Read more AlixPartners insight on this topic\)](#)

Recent developments indicate that Euro 7 will be less drastic than originally proposed: new test procedures and new emissions thresholds for light vehicles will no longer be considered.

However, new with Euro 7 is the technology-independent approach that will apply equally to Internal Combustion Engines (ICE) and Battery Electric Vehicles (BEVs). Specific to BEVs, the newly-introduced emission limits – especially for tyres – could prove challenging, as tyre wear primarily depends on a vehicle’s total weight and torque (BEVs are typically 20-30% heavier than ICE, see chart below).



As the exact limit is still pending, actual costs associated with potential mitigating actions (e.g. high-end tyres, overall vehicle weight savings initiatives) remain unclear, including whether actions are needed at all. Thus, further tyre abrasion tests are needed to check compliance with future tyre emission thresholds.

Despite an unlikely earlier phase-out of ICEs with Euro 7, the biggest challenge for OEMs is the need to continue operating on two fronts, reflected in conflicting requirements against the expected continuing demand for ICE vehicles in North America and parts of Asia, even after the EU ICE ban in 2035.

Corporate Sustainability Reporting Directive (CSRD) – first application in FY2024 [\(Read more AlixPartners insight on this topic\)](#)

Our outside-in assessment of a number of top automotive players shows a big gap in readiness for reporting against CSRD, across OEMs and suppliers alike (see table below).

As to be expected, most organisations show better levels of reporting to date around emissions (‘climate change’) and ‘own workforce’ – albeit still with quite some room for improvement.

The biggest potential short-term concern lies with the lack of transparency and due diligence throughout the upstream supply chain, impacting ‘workers in the value chain’. This factor is already of significant importance in Germany with the Lieferkettenschutzgesetz (or German Supply Chain Due Diligence Act) and is expected to soon become of greater importance with the EU Corporate Sustainability Due Diligence Directive.

ALIXPARTNERS’ OUTSIDE-IN CSRD READINESS ASSESSMENT ²		PREMIUM OEMS	NON-PREMIUM OEMS	TOP 10 SUPPLIERS
ENVIRONMENT	Climate Change	High	Mid ~ high	Mid ~ high
	Pollution	Mid ~ average	Mid ~ average	Mid ~ Low
	Water & Marine	Mid ~ average	Mid ~ Low	Mid ~ average
	Biodiversity and ecosystems	Mid ~ average	Mid ~ Low	Mid ~ Low
	Resource use and circular economy	Mid ~ high	Mid ~ high	Mid ~ average
SOCIAL	Own workforce	Mid ~ high	Mid ~ average	Mid ~ high
	Workers in the value chain	Mid ~ average	Mid ~ average	Mid ~ average
	Affected Communities	Mid ~ Low	Mid ~ Low	Mid ~ Low
	Consumers/end users	Mid ~ average	Mid ~ average	Mid ~ Low
GOVERNANCE	Business conduct	Mid ~ high	Mid ~ high	Mid ~ average

High Mid ~ high Mid/average Mid ~ Low Low

1. Segment classification according to EV volumes definition
2. Caution: assessing sustainability reports alignment with CSRD reporting categories assumes equal levels of materiality across all topics
Sources: KBA SV 2.2.1 & FZ_14; OECD Non-Exhaust Emissions; company reports; AlixPartners analysis

INCREASING REGULATORY PRESSURES – WITH RISK OF DIRECT IMPACT ON P&LS

REGULATORY PRESSURES (CONTINUED)

Lieferkettenschutzgesetz (LkSG) and Corporate Sustainability Due Diligence Directive (CSDDD)

([Read more AlixPartners insight on this topic](#))

The timing for CSDDD adoption and implementation is still to be confirmed. However, the implications are expected to be similar to the German LkSG (effective from January 2023). The first mandatory LkSG reporting is required within four months of the end of FY2023 for organisations operating in Germany with at least 3,000 employees.

“There are clear boundaries that not every large company has adhered to: the obligations under the LkSG may not be indiscriminately shifted onto suppliers”¹

TORSTEN SAFARIK, PRESIDENT OF THE BAFA²

LkSG places a greater duty of care upon organisations far beyond their own operations. Companies are now held accountable for the full value chain and must act as soon as they become aware of any breach. The penalties for negligence can be significant (up to 2% of annual turnover).

LkSG violations can now be flagged through a mandatory third-party whistle-blower system. Given the global interconnectivity of the automotive supply chain, with footprints often in high-risk countries, the risk of a LkSG breach is high, as highlighted in [Sheffield Hallam University's whitepaper](#) that associates almost every automotive OEM to forced labour.

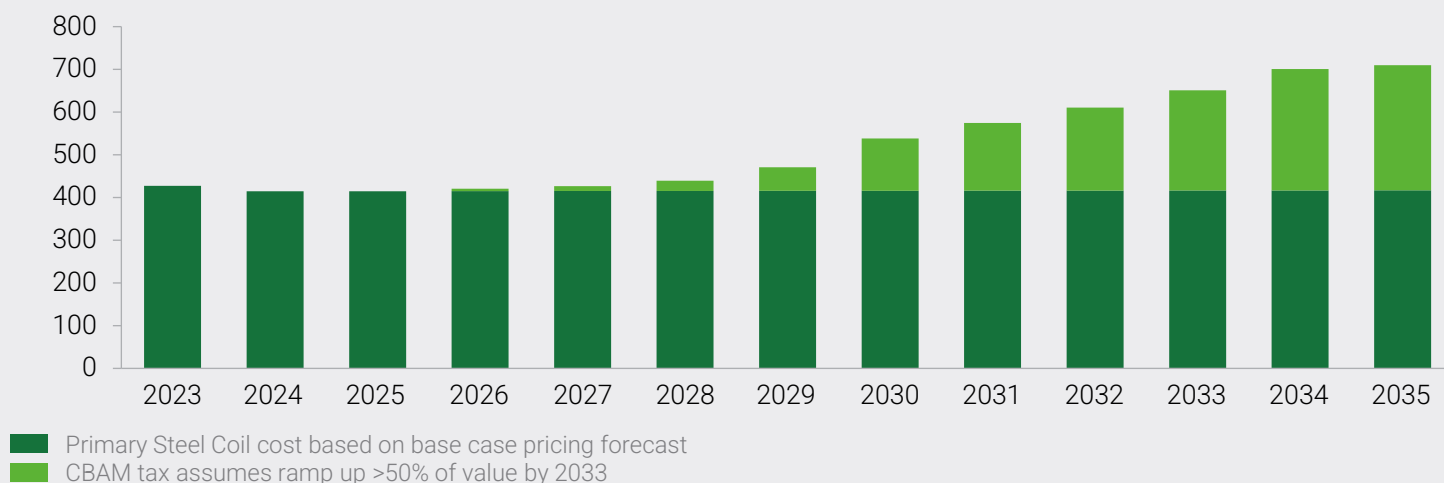
Carbon Border Adjustment Mechanism (CBAM) Tax – reporting from Q4 2023 with taxes starting from Q1 2026

CBAM has been brought in as a part of the EU's 'Fit for 55' legislation. It aims to reduce greenhouse gas emissions by 55% by 2030, driving down the risk of carbon leakage of carbon-intensive imported goods. Although many details on CBAM are yet to be finalised (e.g., calculation methods expected by Q1 2025 at the latest), we can draw some initial conclusions.

For imported vehicles, current CBAM documentation suggests minimal impact of c.€180 additional cost per vehicle, based on current emissions allowances. The real monetary risk, however, lies for suppliers importing products with high steel, aluminium, or chemical content. An indicative pricing analysis on potential tax implications is shown below.

POTENTIAL FINANCIAL IMPACT OF CBAM STEEL COIL³ (INDICATIVE ONLY)

Steel costs (€)



Note: additional cost implications likely (e.g., CBAM certificate cost) on top of above items.

Assumptions: Steel Price as of End of September 2023 / FX Rate 1.07 USD / EUR; from 2024 0.5% y-o-y; Steel-FC Q4 2024: -3% vs Q4 2023; Price for CO₂/to 90€ in 2024, 3% growth y-o-y thereafter; 2.35 to CO₂e / per to Steel

1. [TextilWirtschaft](#); 2. BAFA = Federal Office for Economic Affairs and Export Controls; 3. Steel Hot-Rolled Coil - N. Asia

CIRCULAR ECONOMY – AN AVAILABILITY AND TECHNICAL SPECIFICATION CHALLENGE

CIRCULAR ECONOMY CHALLENGES

Many organisations are incorporating a greater focus on ‘circularity’ to reduce emissions and build brand reputation with current and potential customers.

Recycled content to reduce embedded carbon

Recycled material content in new vehicles is a primary element in the circular economy – and one that many OEMs already specify as an ambition in their ESG roadmaps. Targets for sustainable and recycled materials range from 15% to 40%. Sourcing recycled materials of the right quality and grade is thus becoming critical.

Typically, recyclability targets often focus on metals (aluminium, steel and lithium, plus rarer or higher risk metals such as cobalt and copper). Use of these materials (primary or recycled) is often to target reducing tailpipe emissions or longer battery life (e.g., aluminium for lightweighting), whereas recycling alone is an essential lever to efficiently reduce embedded carbon emissions, with reductions approaching or even exceeding 90% when using recycled materials. ([Read more AlixPartners insight on this topic](#))

Challenges to achieve recycled content targets

Some of the most ambitious recycling targets include Volvo’s 40% recycled aluminium target by 2025 and Stellantis’ SUSTAINera vehicles, which can have reportedly up to 80% recycled content and 50% in avoided emissions.

OEMs, however, face major challenges in achieving their recycled content targets. Take the recent ‘green steel’ trend as an example – given the increasing demand and long transition lead time, demand is currently outpacing supply. Automotive is a leading industry seeking supply agreements for green steel and needs to secure its sourcing.

For all recycled content targets, organisations must ensure they can obtain (i) enough recycled material and (ii) at the grade and quality required to ensure vehicle safety and performance and safety is not compromised.

Defining optimal grades for respective usage

Research recently conducted by AlixPartners into recycled aluminium from End-of-Life Vehicles (‘ELV’) shows that current ELV management yields mixed material properties – that is, lower grade secondary aluminium than desired. This challenge only intensifies as we transition away from ICE (decreasing demand for lower grade aluminium) to BEV.



New technologies such as Laser Induced Breakdown Spectroscopy (LIBS) may yield better results in post-scrappage sorting, though it is likely that more fundamental change is needed – and pilots to ‘test the water’.

Closed loop-systems becoming a requirement

While collaboration with third parties on closed-loop systems was previously preferred, OEMs are now looking to develop in-house capabilities to collect and recycle materials before cars go to the mill.

One priority is to obtain and retain battery ownership to secure the sourcing of raw materials, allowing OEMs to derive value from second-life batteries. Recycling also lowers the risk associated with the increasing ‘duty of care’ being placed upon organisations through the likes of LkSG and CSDDD. Further, this ‘in-house’ circularity management may soon no longer be an option but a requirement.

EU regulations will follow soon

On the specific matter of circularity, EU regulations are playing catch-up. A [recent proposal](#) has been published by the European Commission, which seeks to address recycled content and management of ELVs, including stipulating that ELVs are managed separately from other waste to enhance the quality of recycled materials that can then be reintroduced into new vehicles.

STRUCTURE FOLLOWS ESG STRATEGY: ORGANISATIONS WILL NEED TO KEEP PACE

ORGANISATIONAL STRUCTURAL CHANGES

As the importance of ESG has become a priority agenda item for boards and executives, so too has the matter of organisational structure to support delivery on ESG targets.

74%

of organisations increased their sustainability budgets in 2021, up from 40% in 2016.

50%+

have increased the size of their ESG function in the past two years.

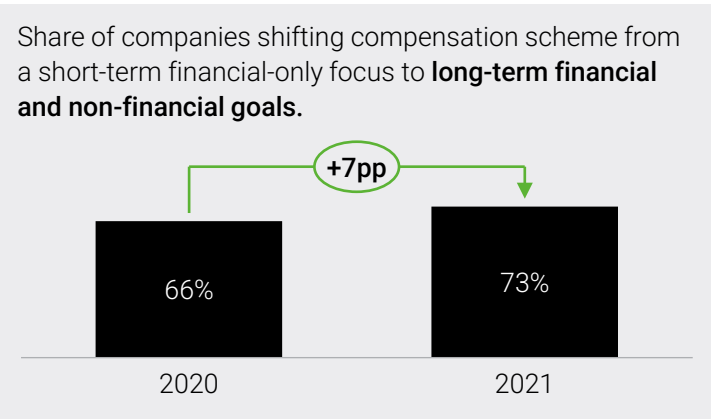
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ESG executive roles increased by 15 percentage points between 2010 and 2022.

Climate change is almost unanimously considered the highest priority across all OEMs...

MATERIALITY ASSESSMENT 'HOT TOPICS'		PRIORITY
ENVIRONMENT	Climate change (incl. GHG emissions, renewable energy)	High
	Air pollution	Low
	Water usage	Low
	Circular economy (incl. waste, recycling)	Mid
	Biodiversity	Low
	Electric/zero emission vehicles	Mid
SOCIAL	Human rights (incl. forced labour, freedom of expression)	Mid
	Diversity, Equity & Inclusion	Mid
	Employee wellbeing (incl. development, H&S)	High
	Community engagement	Low
GOVERNANCE	Governance	High
	Data privacy/cybersecurity	Low
OTHER	Supplier specific initiatives	High
	Product (incl. quality, safety, connectivity autonomous)	High

High Mid Low



Specific to the Automotive industry, our research has outlined a misalignment between 'material' or priority topics and executive compensation – suggesting vast opportunity to better prioritise and incentivise executives to ensure long-term sustainability ambitions can be met. Despite varying levels of alignment between auto companies' ambitions, targets, and ESG organisational structures, we see those with higher levels of ESG accountability (more senior heads of ESG within the organisation, greater ties to compensation etc.) typically demonstrate higher levels of planned investment and better-defined action plans towards delivering on their ESG ambitions.

Sources: OEM and Tier 1 supplier websites, sustainability reports and AlixPartners Analysis; GreenBiz Group; Harvard Law School

WHAT REALLY MATTERS: ENABLING BUSINESS DECISIONS ALIGNED WITH ESG PRIORITIES

AUTOMOTIVE ORGANISATIONS (SUPPLIERS OR OEMS) SHOULD FOCUS ON A RAPID AND COMPREHENSIVE ESG ASSESSMENT, FOCUSING ON FOUR KEY PILLARS:

i

REGULATORY IMPACT



The ESG regulatory landscape is fast evolving with added complexity of cross-border differences.

The first step in avoiding compliance issues is proactive monitoring, aiding answers to the following key questions:

- What regulations are coming through?
- Are they applicable to us?
- When do we need to report what?

In addition, a primary obstacle will be to find ways to translate broad regulatory stipulations into **everyday operational processes and controls**.

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ACTION ROADMAP



Setting clear targets and translating those into implementable actions is not only a regulatory requirement (see: CSRD) but very often a stakeholder requirement.

Some fundamental questions to ask include:

- What are our ambitions? Are these aligned with what our stakeholders require from us?
- What do we need (and want) to prioritise? Where do we need to improve most?
- How will we address those priorities?

A critical requirement is to **gain clear stakeholder alignment** on setting targets and prioritisations as well as **allocating the appropriate resources** to meet these objectives.

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DATA STRATEGY



Data governance metrics are key to monitor progress and assess success against targets.

Questions to consider include:

- What do we need to measure?
- What do we currently measure?
- From whom and from where do we need to get information to fill those gaps?
- How do we govern our data and ensure consistency over time?

While gathering such an extensive amount of detailed data will incur extra expense, embedding **ESG reporting into current operations** may reduce costs in the long run.

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ONGOING ESG MANAGEMENT



Organisations need to carefully review how they are structured, including the seniority of their lead ESG role within the organisation and whether executive and board compensation are tied to ESG targets.

Key questions to consider include:

- What resources do we need in place to ensure the right level of influence?
- How do we incentivise our people to ensure they make the right decisions?
- What steps do we put in place to ensure longevity, consistency and robustness of new business decisions?

Companies should ensure their **ESG leadership team is set up with genuine executive power**, to set themselves on the path to 'ESG success'.

WHAT REALLY MATTERS: ACT NOW TO ADD VALUE TO YOUR ORGANISATION

OUR EXPERTS SUPPORT CLIENTS IN DELIVERING PRAGMATIC, IMPLEMENTABLE SOLUTIONS BASED ON REAL LIFE EXPERIENCE

1 ACT NOW AND PREPARE FOR THE 'LONG GAME'

Frontloading today to ensure all key elements are in place will save time (and money) in the long run – and reduce compliance risks. Getting started on data gathering and **understanding where you stand today** will reap huge benefits. For example, we identified **significant data infrastructure gaps** with one client that had been causing them great challenges in assessing their current status.

2 TRANSPARENCY AND COLLABORATION OVER THE RECENT 'HARD BALL' TREND

Our work with automotive companies has highlighted a trend of OEMs using – or exploiting – 'transparency' to apply commercial pressures; now is the time to take a more collaborative approach. Incentivise suppliers: **sharing the pain and benefits** to build a **more transparent and resilient supply chain** will be win-win for both sides.

3 FOCUS ON THE WHOLE VALUE CHAIN

Your direct suppliers are within reach and easier to work with, but this won't get you far enough and won't address your biggest issues – you must work with those further up the chain. We have worked across the value chain to help our clients **develop the best solution for both themselves and their connected value chain**.

4 ADD VALUE – TAKE ADVANTAGE OF THE OPPORTUNITIES

Create momentum: don't view this purely as a 'tick-box' exercise. More often we have found opportunities with clients to **add value to their organisations** and the way they operate. To yield benefits, you must invoke a culture change – and this starts by demonstrating to your employees that you are taking this seriously.

5 REORGANISE FOR THE FUTURE

Ensure your head of sustainability is positioned such that they **hold proper authority** to be part of the senior business decision making process – and that your **leadership are appropriately incentivised to make balanced decisions** fit for long-term company ESG and financial growth ambitions.

6 BE AGILE – LEARN FAST, FAIL FAST, AND PIVOT

The best approach is to **set up pilots to test, learn, and celebrate quick wins**. Typically, we advise our clients taking this approach with a few key, strategic partners. This will feed the culture change necessary in a relatively safer environment.

Start smaller and focus on your greatest 'hot spots'. For example, before deploying a large-scale closed-loop recycling system, start with a battery recycling factory. Or, as we've executed with one client, run a trial at a site that is more open to change. Capitalising on this experience will ultimately accelerate deployment, drive change, and create momentum while requiring limited resources.

AlixPartners is at the forefront in helping automotive organisations 'when it really matters', from developing and implementing strategic ambitions through to rapidly delivering immediate impact in a continuously evolving ESG ecosystem.

To discuss our **ESG Readiness Assessment** in more detail, please contact one of our experts [here](#).

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ABOUT US

For more than forty years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork-in-the-road decision. But it's not what we do that makes a difference, it's how we do it.

Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.

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