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Green Insights: ESG Matters

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Why ESG Matters?

There is now an increasing acknowledgement that for sustainable development, profitability must coexist harmoniously with principles of sustainability and responsibility

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Editor's Note

Dear Readers,

I welcome you to the *First Edition* of our ESG Newsletter **'Green Insights: ESG Matters'**. As we witness a fast pace of change in our global sustainability landscape, the need for sustainable practices has become imperative. We now observe that efforts being made towards integrating ESG into business practices are now redefining success, acknowledging that profitability must coexist harmoniously with principles of sustainability and responsibility.

In this edition, we delve into the multifaceted realm of Environmental, Social, and Governance factors, exploring not only their significance but also the strategies being employed to integrate them into corporate agendas. This Newsletter has two sections: News in India [covering latest developments in the area of ESG in India]; and News in the World [covering global developments].

We hope, you find it useful. We encourage you to share your perspectives, and become part of our endeavours towards a more equitable, resilient, and prosperous world for all.

Warm regards,

[T S Vishwanath]

What is ESG?

The term ESG is an acronym, where the "E" comprehends environmental factors, such as a company's carbon footprint, waste management, and resource conservation; the "S" refers to social factors, including labour practices, community engagement, and diversity and inclusion; and the "G" encompasses governance aspects, like board composition, executive compensation, and transparency in decision-making (see Figure 1 for ESG Framework).

Figure 1. ESG Framework

Source:https://www.bio-powder.com/

The ESG framework, which is practically investors' driven, has several benefits for the corporate entities in terms of their sustainability and also people at large. Some major benefits for the businesses and the society at large are delineated below (Figure 2).

Figure 2. Summarising Gains from ESG

ESG has gained prominence in the recent years, and matters because it aligns with broader societal and environmental goals, contributes to better risk management and financial performance, enhances reputation and brand value, ensures regulatory compliance, meets stakeholder expectations, fosters innovation and efficiency, and improves access to capital. In view of the above, businesses have been increasingly focusing on ESG to ensure sustainability of their businesses.

How is ESG governed in India?

There is not any single policy, rule, or regulation that govern ESG in India. Rather the approach to ESG is guided by various pieces of legislations. Major legislations which guide India's approach to ESG are provided below (see Figure 3). In addition, there are laws with respect to the payment of minimum wage, bonus, gratuity, welfare activities, health and safety, which contribute to ESG compliances in India.

Figure 3. ESG Governance Framework in India

News in India

Increasing level of awareness on the need to integrate ESG with CSRs

The COVID-19 pandemic established the interconnectedness of life, livelihood, health, poverty, equity, climate change and the sustainability of businesses. The impact of Covid-19 made it abundantly clear that a sustainable future to mankind is critically dependent on collective efforts of the governments, development agencies on the one hand, and businesses and individuals on the other. Furthermore, there is widespread realisation that actions towards a more responsible business ecosystem cannot be delayed further, and a strong sustainability implementation is the only way forward into the new normal.

The sharp focus on ESG is a consequence of the need for building a better business ecosystem and bringing in resilience for the future. There is a strong push from the various stakeholders with respect to ESG integration. Stakeholders are expecting organisations to take tangible steps which need to be planned for short-term, medium term and long term. Short-term plans include prioritising key issues, protecting human capital and engaging with stakeholders. Medium-term strategy should include proactive measures to build resiliency and manage social and environmental risks across supply chain and organisation. Long-term roadmap generally includes plans on updating sustainability and ESG strategy to manage and measure impacts that will support long-term value creation in a new world.

There are several indications that over the last few years, India has made good progress with regard to adopting ESG. With a growing awareness of climate change, social inequalities, and corporate accountability, both investors and consumers are demanding a more sustainable and responsible approach from businesses. Companies that integrate ESG principles into their strategies are gaining a competitive advantage in the Indian market.

Emergence of Business Responsibility and Sustainability Reporting

Aligned to the global ESG disclosure requirements, a new reporting format namely Business Responsibility and Sustainability Report (BRSR) has evolved in India. In this regard, the Securities and Exchange Board of India (SEBI), in its continued efforts to enhance disclosures on ESG standards, introduced new requirements for sustainability reporting by listed companies with the aim to establish links between the financial results of a business with its ESG performance (Figure 4).

Figure 4. Business Responsibility and Sustainability Report

Source: *https://lexplosion.in/brsr-raises-the-bar-for-esg-disclosures-in-india/*

It is mentioned that the BRSR is a reporting framework that mandates obligated entities to disclose their ESG performance from 2022–23 onwards. This reporting framework aims to establish links between the financial results of a business with its ESG performance. This requirement makes holding companies accountable for their identification of ESG responsibilities and their incorporation in corporates' annual disclosures.

Mandating the use of this reporting framework, makes it easier for regulators and investors, and other stakeholders to have a fair understanding of overall business stability, growth and sustainability, which was hitherto based on financial disclosures alone. This SEBI mandated BRSR framework which was applicable to the top 1,000 listed entities (by market capitalisation) for reporting on a voluntary basis for 2021–22 has become mandatory from 2022–23.

Furthermore, from 2022–23 onwards, this BRSR report has turned into a more comprehensive BRSR as it requires disclosure of nearly 1,600 data points across different aspects of ESG.

News in the World

Global Waste Management Outlook 2024

A UNEP report, jointly published with the International Solid Waste Association (ISWA), provides an update on global waste generation and the cost of waste and its management since 2018. The analysis uses life cycle assessments to explore what the world could gain or lose through continuing business-as-usual, adopting halfway measures, or committing fully to zero waste and circular economy societies. The report also evaluates three potential scenarios of municipal waste generation and management, examining their impacts on society, the environment, and the global economy. Furthermore, it presents potential strategies for waste reduction and enhanced management to treat all waste materials as valuable resources.

The report reveals:

- Municipal solid waste generation will grow from 2.3 billion tonnes in 2023 to 3.8 billion tonnes by 2050.
- In 2020, the global direct cost of waste management was an estimated USD 252 billion. When factoring in the hidden costs of pollution, poor health and climate change from poor waste disposal practices, the cost rises to USD 361 billion.
- Without urgent action on waste management, by 2050 this global annual cost could almost double to a staggering USD 640.3 billion.

Furthermore, the report's modelling result highlights importance and gains through promoting circularity in waste management.

- Getting waste under control by taking waste prevention and management measures could limit net annual costs by 2050 to USD 270.2 billion.
- However, projections show that a circular economy model, where waste generation and economic growth are decoupled by adopting waste avoidance, sustainable business practices, and full waste management, could in fact lead to a full net gain of USD 108.5 billion per year.

The report stresses the need to act on priority in order to avoid the worst scenario. In addition to the above findings, the report provides guidance and suggested actions for multinational development banks, national governments, municipalities, producers and retailers, the waste management sector as well as citizens.

Evolving ESG Framework in the US and the EU

The ESG reporting in the world has witnessed significant regulatory shifts over the last several years. This is reflected by the adoption of voluntary ESG reporting. For instance, as per an EY report, in 2022 about 96 percent of S&P 500 companies and 81 percent of Russell 1000 organisations voluntarily published their ESG reports. The number of companies publishing their ESG reports are expected to increase in the times to come.

The European Union, in January 2023, adopted the Corporate Sustainability Reporting Directive (CSRD). The CSRD requires EU and non-EU companies with activities in the EU to file annual sustainability reports alongside their financial statements. The CSRD also requires that these reports must be prepared in accordance with European Sustainability Reporting Standards (ESRS), for which first set of standards was adopted by the EU on 31st July 2023. The ESRS soon will become law and will apply directly in all 27 EU member states. Companies will need to report in compliance with these new ESRS in the 2024 reporting period.

40 percent of procurement leaders ignoring sustainability, study reveals

While supply chains are facing new pressures to reduce costs, and both consumers and governments are ramping up efforts to adopt sustainability as a core value in businesses, a survey conducted by Sedex, a sustainability software provider organisation, finds that a significant portion of procurement leaders are ignoring sustainability efforts. Many of them are also not even aware there are regulations around sustainability practices.

Sedex surveyed over 250 senior procurement leaders at North American companies at the end of 2023 and found that 40 percent are ignoring sustainability in their procurement operations. 37 percent of the surveyed people said they are unaware of sustainability-related legislation that impacts their businesses.

These findings are a wake-up call for any business that is serious about its social and environmental performance. The research underscores the urgent need for executive teams to realign ESG commitments and operational goals, to truly embed sustainable practices in their organisations.

As companies seek to reduce costs, and increasingly target the supply chain and procurement functions, it may not be a surprise that so many organisations are not considering sustainability when making procurement decisions. The Sedex survey found that 50 percent acknowledged that sustainability remains an afterthought, or isn't considered at all, for business decisions generally. This, despite the number of public proclamations by companies, 90 percent of who are in the Russell 1000 that produce annual ESG reports.

Another report by the Hackett Group found that cost reduction is now the top priority for procurement professionals, topping 2023's number-one item, supply continuity. The survey backed up research from Boston Consulting Group that found 65 percent of executives are prioritising supply chain and manufacturing costs as the biggest levers for organisations to pull for cost savings.

ESG data – Issues and Challenges

As per reports, at least 10,000 large companies worldwide are outdoing each other in reporting more and more ESG data in sustainability reports. A major purpose of this sustainability reports is to market themselves to investors, regulators and the public.

In line with the increasing focus on ESG reporting, several ESG rating agencies have come up over the last few years supported by a booming ESG rating market, which presently runs into billions of dollars. However, when it comes to correlation of ESG ratings by various rating agencies, serious inconsistencies are observed. A recent study by MIT with a subtitle 'ESG data are noisy and unreliable' reveals that the ESG ratings of the largest agencies have an average correlation of just 0.54, compared with credit ratings' correlation of 0.92. This lack of uniformity in ESG ratings should make companies question their utility.

Still, preference for financial returns among investors prevails over ESG. A PwC's survey of investors revealed that 81 percent are not willing to give up financial returns for ESG. Because of this, businesses may be prompted to avoid the need for reporting financially irrelevant ESG data. Investors focus on key performance financial data and may find non-financial ESG data a bit detracting.

There is also issues relating to redundancy of ESG data. While significant shifts have occurred with regard to report standards in the world, including the US, and the EU, there is also a feeling that several components of the data requirements as part of ESG are unnecessary, and businesses are getting burdened because of requirements of unnecessary data to comply with regulations.

A study of ESG reporting by 4,500 US and European companies finds between 50 percent and 75 percent of 2022 ESG data reported was unnecessary to comply with regulations and satisfy the guidelines of relevant investment funds.

The study also mentions that the average listed company (in the US and EU) spends $675,000 annually on ESG data and ratings. This stands to increase in the coming periods as 92 percent of companies planned to spend 10 percent more in 2023 and 18 percent expected to increase their expenses by 50 percent.

In view of the financial and time cost involved in ESG reporting, there is need for taking a holistic view and creation of an ESG ecosystem where compliance becomes rewarding for both businesses and the investors, along with other stakeholders.

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National CSR Network (NCN), an initiative of Strategic CSR Alliance - a Section 8 Company, was established in 2015 with a vision to empower organisations and individuals for meaningful social development. NCN follows the A (Alliance) A (Advisory/ Capacity Building) A (Assessment) approach, striving to identify and address the pain points of stakeholders while providing an interactive platform in CSR, ESG & Sustainability.

NCN is dedicated to spearheading training and development initiatives in the area of CSR, ESG, and Sustainability, by leveraging its expertise to deliver impactful workshops, webinars, and training sessions. Its tailored approach focuses on bridging the knowledge gap through industry-led programs, ensuring that organisations and their NGO partners are equipped with the necessary skills and knowledge to create positive and lasting impact on society and the environment.

For more information about in-house programs and upcoming workshops, kindly connect with Shivika at 9717314507 or email at shivika@nationalcsrnetwork.in info@nationalcsrnetwork.in