Can ESG help future proof your business?

August 2021

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What is shaping the post-COVID scenario?

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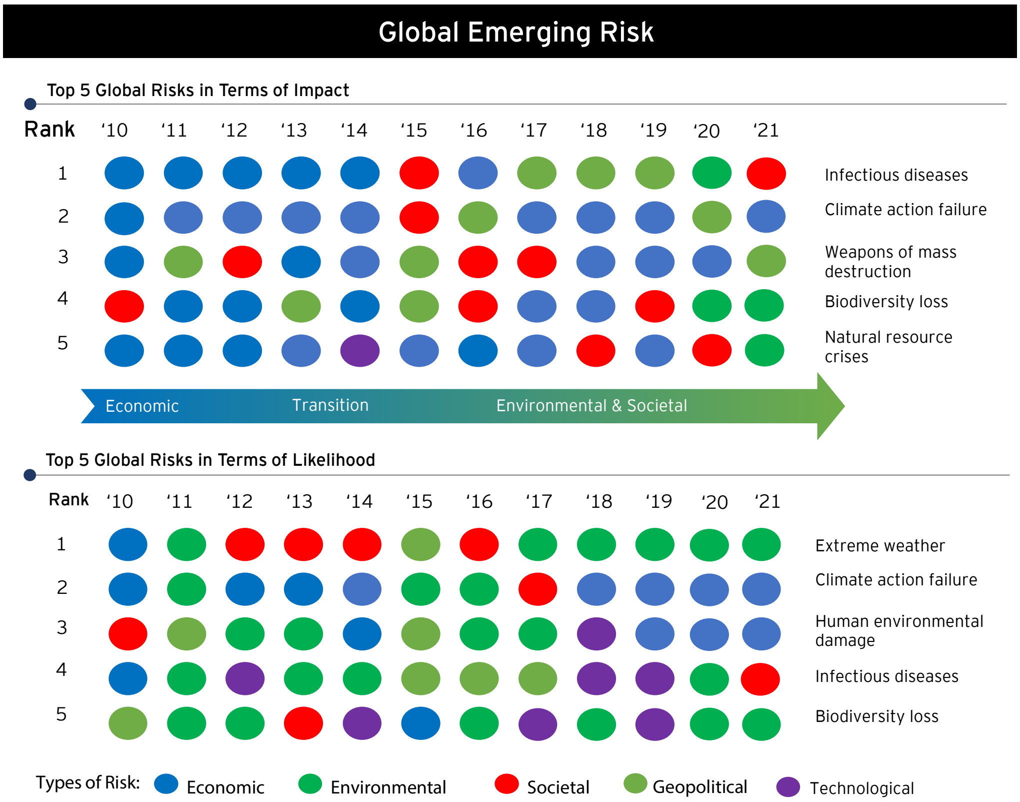
The COVID pandemic has acted as a strong trigger to reshape global economies and how businesses operate. By exposing the fragility of the current businesses and economic models, it has forced the world to hit the reset button. It has also acted as a warning for the challenges of climate change and biodiversity loss that lie ahead and how much greater they would be in terms of their magnitude of impact and extent of the damage. A growing number of business leaders are acknowledging the threat posed by these risks and are working to protect the interest of the stakeholders. A case in point is the evolution of how business leaders perceive risks with the changing composition of the Global Risks (as depicted by World Economic Forum), where over the past decade, the top 5 global risks have shifted from economic focus to environmental and societal focus.



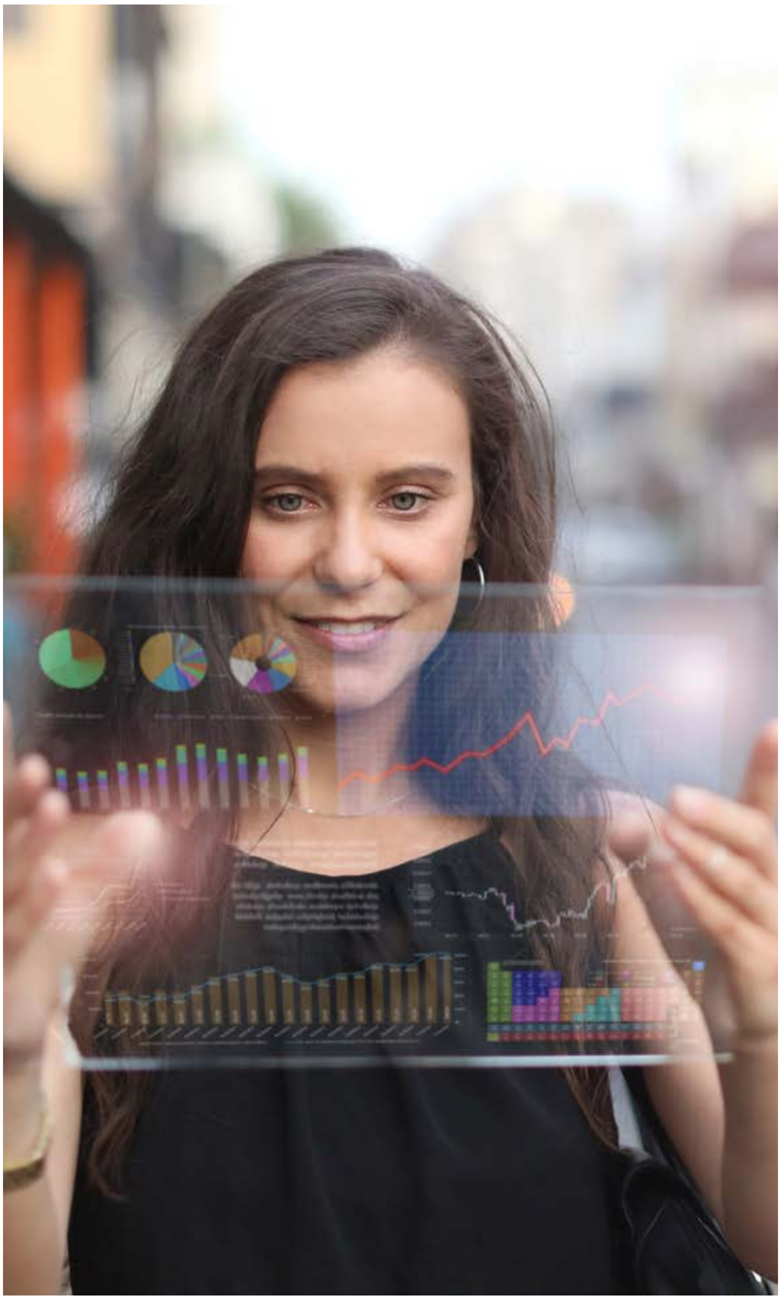
Source: *The Global Risks Report 2021 - WEF*

The pandemic has aggravated this response as more businesses are looking towards the integration of non-financial parameters into business decision making. Further, the uptake of these parameters is triggered by the recent phenomenon of increased natural disasters, melting of polar ice caps, changing weather patterns, growing cases of insect infestation with a parallel rise consumer awareness of such issues. Just last year, India witnessed one of the costliest cyclones – Amphan - which caused a loss of about US$ 14 bn , which is over 35 times Indian environment ministry's budget for FY22 (environment ministry budget is US$ 396.5 million). India has recently suffered another two such cyclones on both eastern and western coasts, Cyclone Tauktae and Cyclone Yaas, with cyclone Tauktae leading to a death toll estimated at 104, which is higher than the death toll from any single cyclone from the Arabian Sea over the last one decade.

Given these scenarios, it is no doubt that integration of Environmental Social Governance (ESG) into business models is an absolute must for building in resilience and future proofing businesses from further shocks. ESG is gaining traction as an important strategy and is leading to optimization of business processes.

Indian businesses are strongly waking up to gear up against the ongoing challenges and the ones that future holds. The year has witnessed some of the very significant developments:

- **Commitment towards responsible investments:** The number of Indian signatories to United Nations–Principles of Responsible Investment (UNPRI)[3] tripled in 2020
- **Growing environmental social governance (ESG) funds:** From just two ESG mutual funds, India now has eight such funds focused on ESG
- **Climate risk in investments:** Task force on Climate-related Financial Disclosures (TCFD)[4] supporters from India have grown three times in 2020-21
- **Growing disclosures:** 220 India-based companies are now disclosing to their investors and customers through CDP[6]



1 State of Global Climate 2020, World Meteorological Organization

2 INR 2869.93 allocated as per budget speech at INR 72.38 = 1 US$ as on 31 May 2021 as per XE currency converter

3 UNPRI is a UN-supported network of investors, that works to promote sustainable investment through the incorporation of ESG centric principles)

4 TCFD was established by G20's Financial Stability Board to develop recommendations for climate-related disclosures to promote informed investments, understand the concentration of carbon-related assets in the financial sector and the financial system's exposures to climate-related risks

5 https://www.cdp.net/en/india

6 CDP is a not-for-profit that runs the global disclosure system for investors, companies, cities, states and regions to manage their environmental impacts)

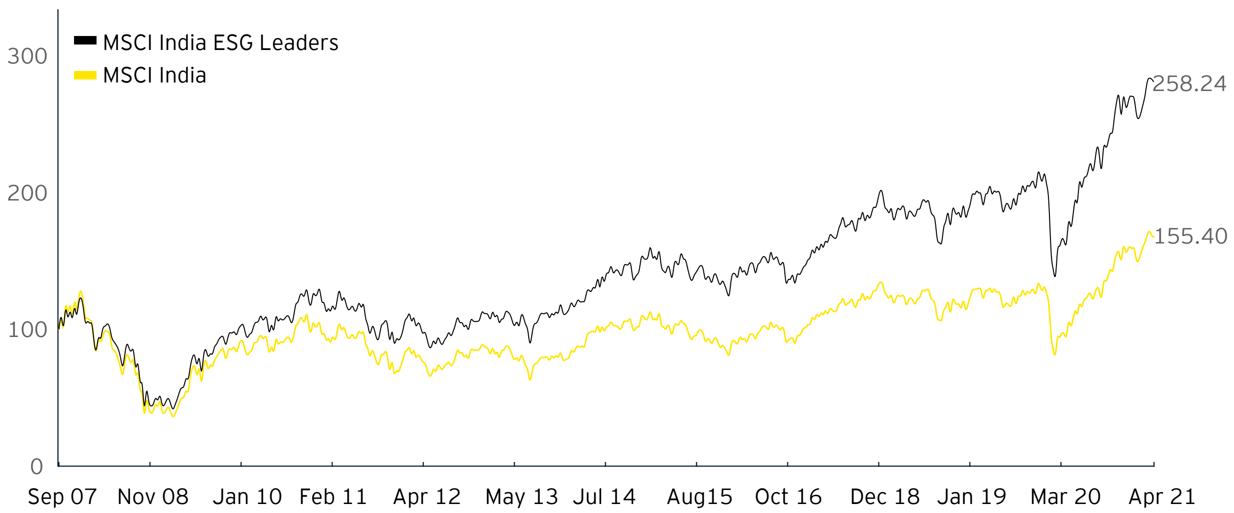
2

Can ESG Future Proof Your Businesses?

ESG for future proofing your business

In an increasingly uncertain and volatile world that is throwing up new challenges for the businesses, ESG provides a framework for businesses for staying resilient by holistically safeguarding people, the planet and profits. Environmental, social and governance is used to categorize aspects that were conventionally associated with sustainability and corporate responsibility but have material financial impact on the organization's short and/or long-term value. These aspects vary basis the industry of operation, business model, geography, scale of operations, supply chain, investor base, core values and business strategy of the organization. Such an ESG centric approach has helped investors and organizations unearth hidden risks in environmental and social aspects, mitigate them and identify new opportunities, which may not be possible from conventional approaches. The relevance and value of ESG is also clear from how the markets reward ESG focused companies as compared to traditional players.

Cumulative Index Performance - Net Returns (USD)
(SEP 2007 - APR 2021)



Source: The MSCI ESG Indexes use ratings and other data supplied by MSCI ESG Research Inc.

Can ESG help future proof your businesses?

The imperative for ESG has been mounting for two decades but has been growing on an accelerated path over the last few years. Key trends which are being witnessed across sectors include:

Growing evidence of climate change: While scientists have been pointing towards the impact that climate change may have on our economies and businesses for decades, there is a growing consensus about climate change in the business community as well. This is primarily led by the increasing frequency and economic impact of natural disasters, supply chain disruptions and resource constraints. The growing consumer awareness and growing regulations adds an additional layer of severity.

Product Stewardship: Businesses have been under increasing pressure from different stakeholders to be responsible for the product and the associated supply chain. Earlier, in certain cases, businesses outsourced environmentally / socially risky operations and distanced themselves from any accidents and risks involved. Stakeholders are now questioning the traceability and transparency of the supply chains and product procurement practices. With growing regulations, manufacturers are also being pushed towards greater ownership around extended product responsibility. Certain organizations are now looking at utilizing resources from disposed products to create newer ones and concepts like urban mining (used for extracting valuable resources from disposed products in urban areas which form the centers / hubs of waste generation)

ESG moving to core: Unconventional threats from climate change, environmental challenges and social awareness together have pushed sustainability agenda from a back-office CSR assessment to an engagement model that proactively tries to deliver value as the core priority for many businesses

From Shareholder to Stakeholder: Conventionally, businesses catered to specifically investors and shareholders and drive profits. However, the impact of other non-tangible parameters on profits is clear now and hence the focus has shifted from the shareholder to a stakeholder model to account for diverse needs of different stakeholders

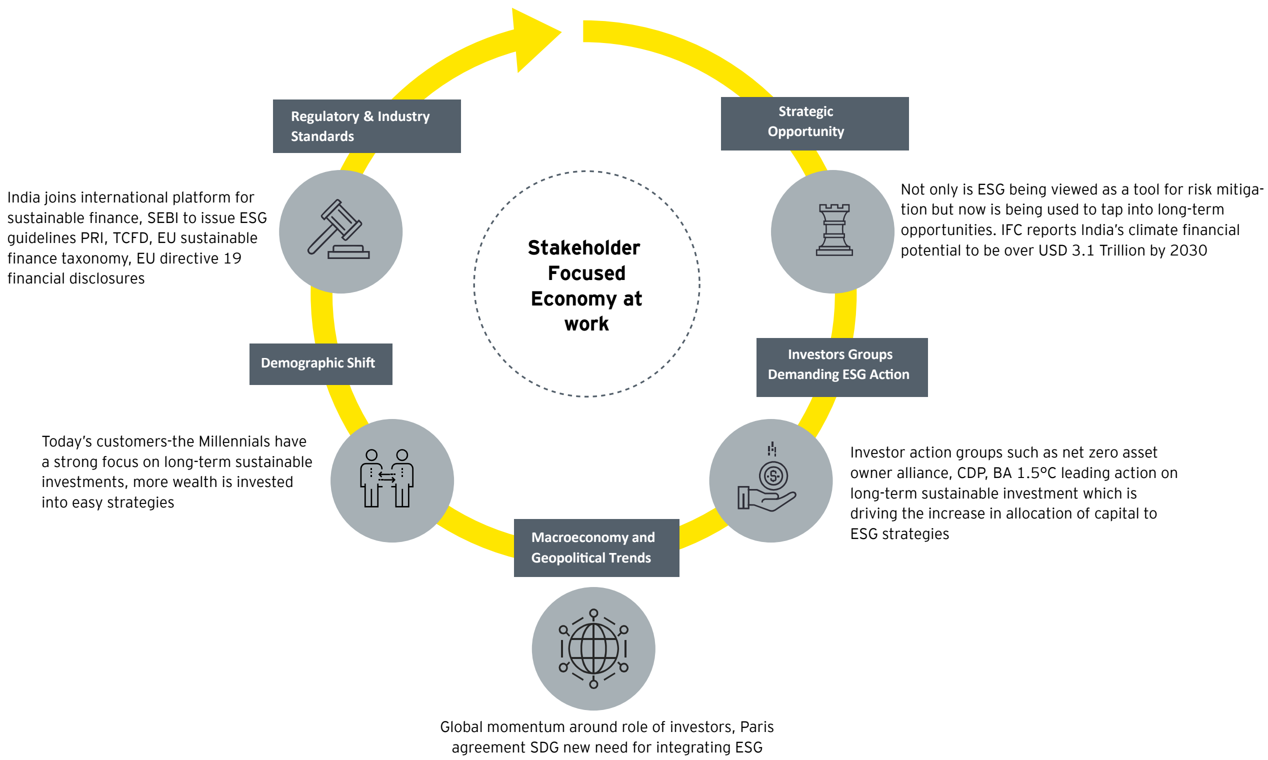
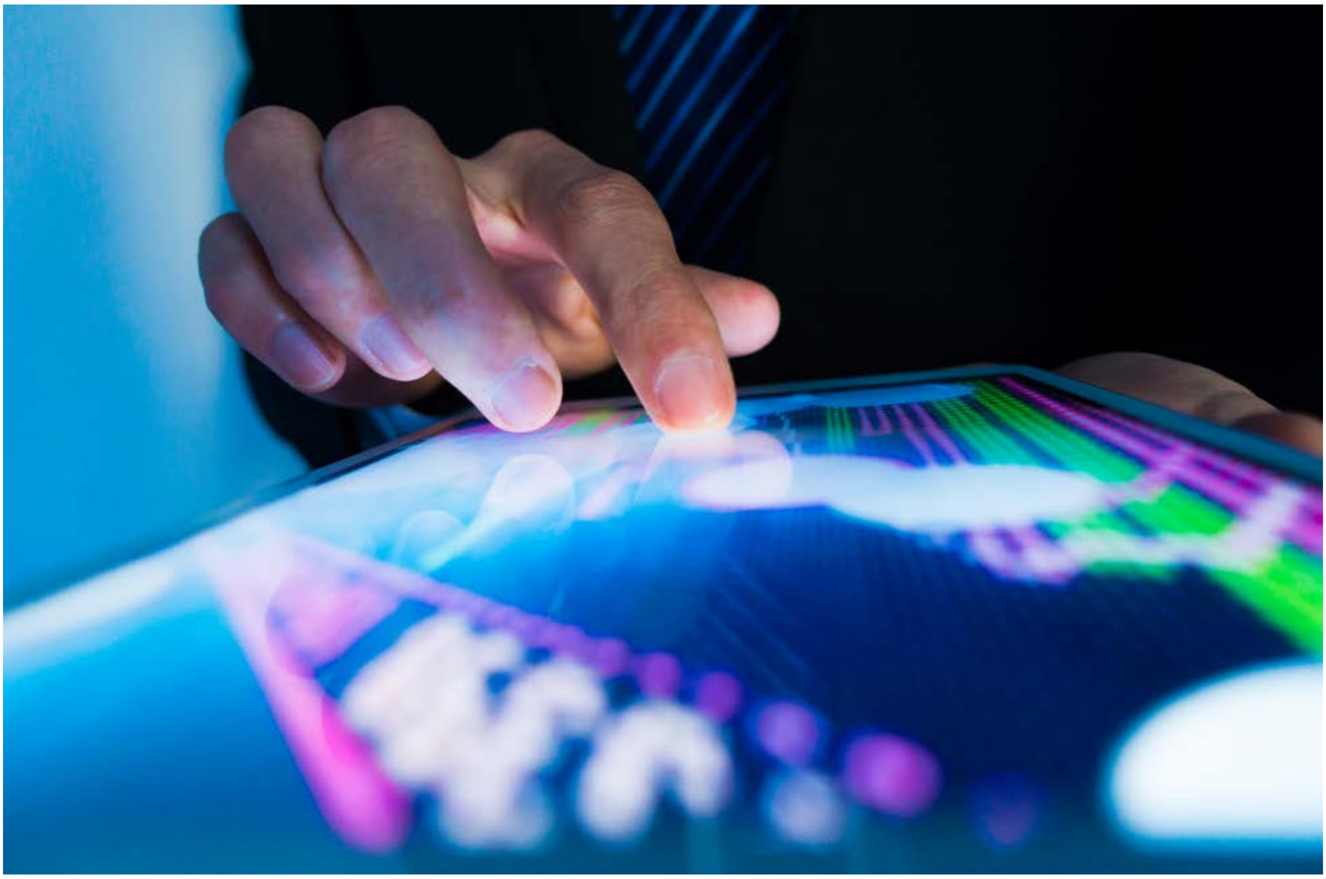

Stakeholder Focused Economy at work
Regulatory & Industry Standards
India joins international platform for sustainable finance, SEBI to issue ESG guidelines PRI, TCFD, EU sustainable finance taxonomy, EU directive 19 financial disclosures
Strategic Opportunity
Not only is ESG being viewed as a tool for risk mitigation but now is being used to tap into long-term opportunities. IFC reports India's climate financial potential to be over USD 3.1 Trillion by 2030
Demographic Shift
Today's customers-the Millennials have a strong focus on long-term sustainable investments, more wealth is invested into easy strategies
Investors Groups Demanding ESG Action
Investor action groups such as net zero asset owner alliance, CDP, BA 1.5°C leading action on long-term sustainable investment which is driving the increase in allocation of capital to ESG strategies
Macroeconomy and Geopolitical Trends
Global momentum around role of investors, Paris agreement SDG new need for integrating ESG

Figure: 1



3

How can ESG deliver long-term value?

How can ESG deliver long-term value?

With growing stakeholder capitalism, the business ecosystem has become more complex over the years. As the focus of businesses shifts from profit to holistic value creation for stakeholders, the means to determine value have also evolved from non-financial reporting to integrated profit loss statements which attempts to correlate or monetize the positive and negative impact of business operations and products through a range of capitals. In fact, investors are increasingly seeing value of such reporting and that has been one reason of integrated reporting gaining momentum globally. The International Integrated Reporting Council's (IIRC) integrated reporting framework provides the guidance for six capitals which can be reported – social, human, intellectual, natural, manufactured and financial capitals. Such a combination of financial and non-financial reporting forms the basis for developing integrated profit loss accounts.

This enables the access to the right set of information for informed decision making, risk mitigation and opportunity identification, thereby delivering value. This can make sense to an organization which, through safety focused initiatives, reduces on time lost to injuries and leads to reduced lost man hours as a payback to the investment made for the safety initiative. A corporate social responsibility focused livelihood initiative can be as value delivered to society as increased incomes. Further, in certain situations, comparisons about trade-offs based on actual quantitative data rather than being governed by qualitative criteria can also be made. Companies such as Puma, Novo Nordisk, Kering are increasingly adopting this practice of integrated profit loss to measure and value the impact in different capacities.

EY Total Value approach

To support such efforts of organizations move towards integrated value statements, EY has developed the Total Value approach to address this need and measure the value created by the company, the value it shares with its stakeholders and the broader impact of the company on society at large. A Total Value analysis provides insights on the monetized impacts, outcomes and their materiality.

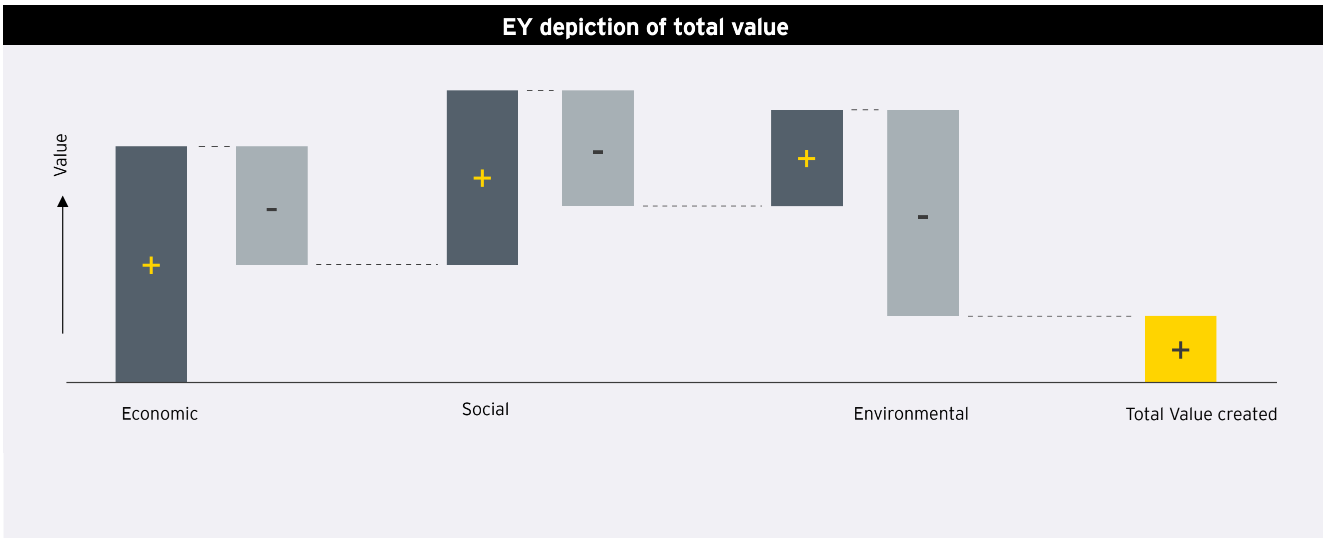


Figure: 2

Application of Total Value analysis:

- Act as a single ESG account of all credits and debits made from the holistic ecosystem that the organization thrives in
- Bring in the aspect of outcome, when conventional scorecards address activity-output based KPIs
- Standardize comparison in case where project portfolio is complicated and multi-dimensional
- Incorporate environmental and social risk and socio-economic benefits in portfolio decisions
- Define strategic focus basis impacts by assessing an organization's key impacts
- Lead product innovation by providing more detailed information such as an assessment of the life cycle impacts
- Serve as a solid decision support mechanism by creating transparent, both positive and negative value

Business value of the Total Value analysis over time

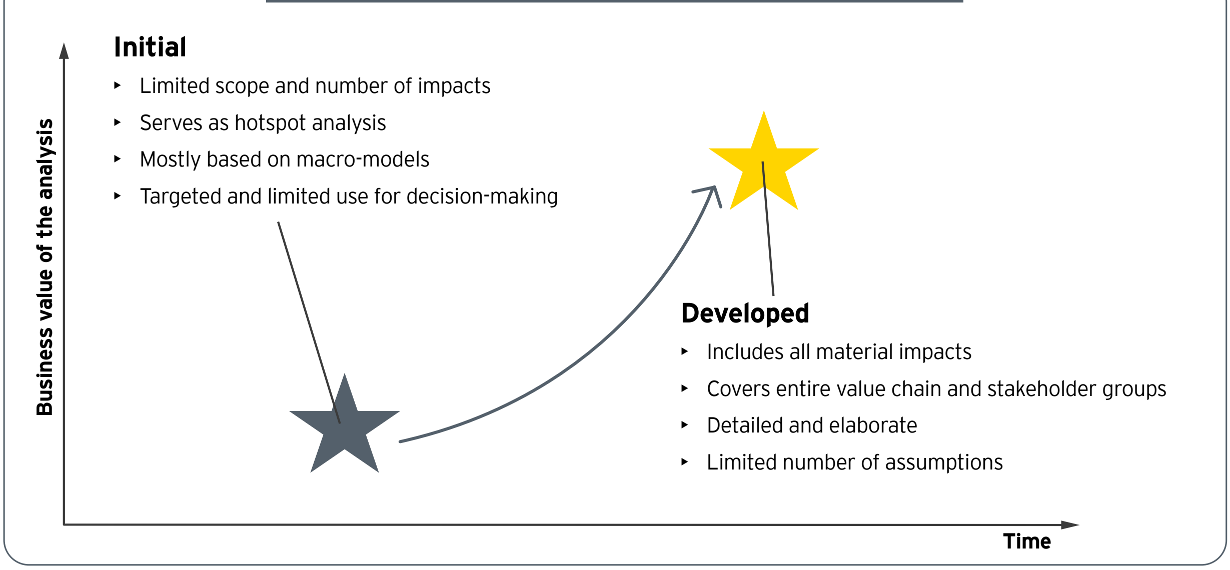


Figure: 3

Principles of Total Value approach

Stakeholder inclusiveness: As Total Value analysis measures the impact of an organization on stakeholders, it is quintessential to involve impacted stakeholders

Materiality: Total Value analysis by default focuses on "valuing the things that matter" and therefore includes the impacts that are most material to the organization and its stakeholders

Transparency: Transparent, auditable, traceable and reproducible analysis provides trust and improved utility in decision-making

Accuracy, reliability and timeliness: Data sources of sufficient quality should provide the users of the Total Value analysis with high-quality results to enable proper decision-making

Balanced view and fairness in attribution: Total Value analysis includes positive and negative aspects to prevent greenwashing and a balanced view. A Total Value should not be used as a medium to "over-claim" social benefits or "under-claim" negative environmental externalities, as it may defeat the overall objective

Consistency and comparability: A consistent approach to valuing the various impacts is required to provide comparability. A similar scope, boundaries and time horizon should be applied to the various impacts whenever possible

Conceptual presentation of a Total Value analysis

Value exchanges with society at large examples:
- Induced creation of jobs
- Emissions
- Supply chain biodiversity impacts
- Scarcity of natural resources
- Systematic economic impacts

For whom:
- Society at large

Value exchanges with stakeholders examples:
- Incidents due to unsafe working conditions
- Community investment
- Employee learning
- Product environmental impacts
- Social impact of products or services

For whom:
- Suppliers
- Customers
- Local communities

Intrisic value

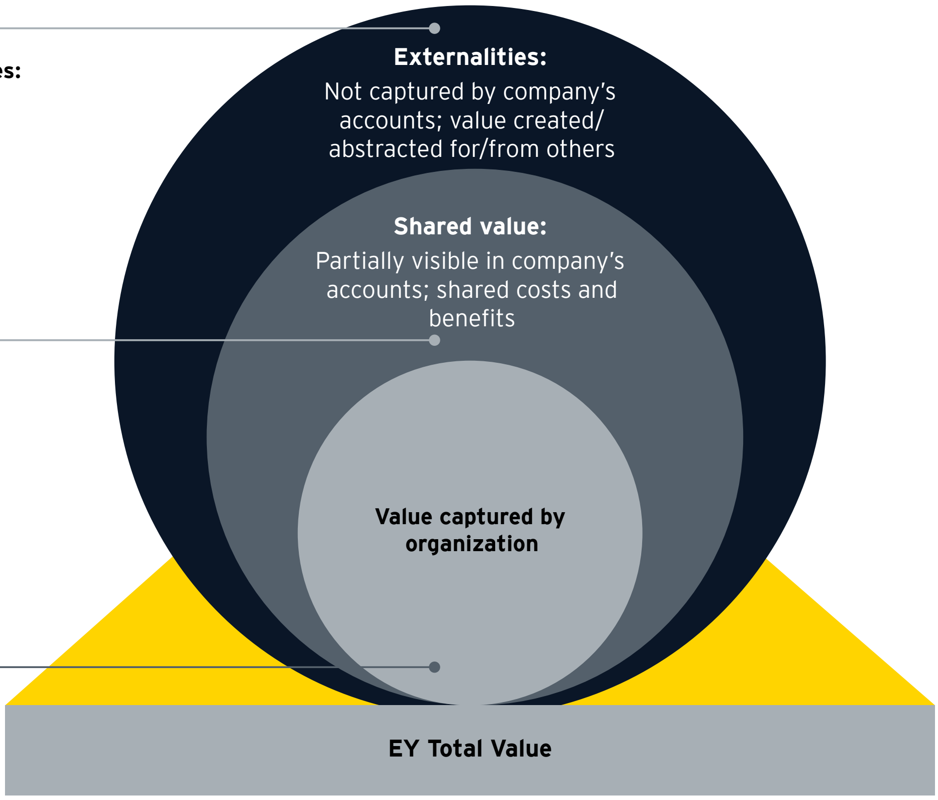


Figure: 4

Total Value methodology

	Steps Involved in Total Value Analysis	Interlinkage between Total Value Analysis and SDG
Objective	Determine the objective basis the end use of total value. This may be with respect to strategic repositioning of accelerating innovation of products or services or greater social impact or whether the analysis will be forward-looking or backward.	Terming SDGs matter to your organization as a business opportunity or from an impact perspective
Materiality Analysis	Assess which aspects are most material ‣ Understand which form of capital is most impacted ‣ Identify the boundaries of the impact ‣ Identify the scope of impacts in line with the objectives	To seize business opportunity and mitigate risks it is important to: ▸ Focus on material SDGs ▸ Map current and potential high-impact areas (positive and negative)
Impact Pathways	Conduct qualitative mapping of key impact areas, within the value chain and capital is affected. This mapping follows the format of input = activity = output = outcome = impact.	▸ Understand which business activities most effectively contribute to SDGs ▸ Identify relationship between activities and impacts
Measurement & Valuation	▸ Develop a model and established what should be measured ▸ Identify relevant performance indicators, and sources of data ▸ Identify possible limitations and estimations in the value creation model	Setting KPIs for measurement and valuation
Data Collation and Analysis	▸ Collate data and execute modelling to arrive at total value ▸ Inter-relations between capital ▸ Stakeholder distribution of value ▸ Identify levers that can increase total value?	
Assurance & Communication	▸ Third-party assurance to improve accuracy and credibility ▸ Disclose results internally and externally	▸ Using SDGs as a common language for reporting in enabling comparison between organizations ▸ Planning SDG impact into corporate strategy as an effective tool
Action Plan	▸ Understand levers of change to further optimize impacts ▸ Define the action plan to optimize and improve the company's overall value creation	Integrating SDG into core business, embedding targets across functions and using partnerships for greater impact across the value chain.

Figure: 5

3

Are you framing the ESG turnaround or is the ESG turnaround framing you?

Total Value methodology

While methodologies such as Total Value provide a framework for organizations to calculate the overall impact, there remains a necessity to act, transform and implement the transition towards an ESG agenda, which requires unusual speed from all actors. Market demand from investors to integrate ESG and related non-financial parameters.

Given the vast expanse of the ESG arena, organizations often wonder where to start from and how to align the pieces together to draw a strategic picture. The answer to where to start lies in the question what's most important to the business? Post identifying what matters most, organizations look towards measuring their performance on key qualitative and quantitative aspects and benchmarking it against peers and leaders. It is also important to have a continuous dialogue with the stakeholders and build a strong engagement and communication strategy that integrates ESG. This would also involve disclosing ESG performance through the relevant reporting frameworks. Finally, the organizations which have evolved to leadership stage have a clear ESG approach, vision and targets and work with industry peers to propagate greater uptake of ESG.

01

- Understand what are the key material aspects that impact business
- Identify key stakeholders and prioritize among categories of stakeholder
- Understand the baseline performance on key ESG parameters

02

- Benchmark performance with peers and industry leader
- Identify gaps and Best practices
- Identify roadmap with short, medium and long term targets for all/ specific ESG parameters
- Track performance and Trends
- Commence reporting on ESG (Internal/External)

03

- Work towards formulating clear ESG vision, goals and roadmap based on performance trends and opportunities considering specific aspects as SBTs, carbon pricing etc.
- Device engagement strategy with specifics to communicate with relevant stakeholders including modes and frequency of communication
- Disclose ESG performance at public domain

04

- Implement roadmap to integrate ESG into core business
- Work with industry shapers such as industry associations to propagate greater adoption of ESG and share best practices
- Adopt a systemic and futuristic approach to assess evolving risks or opportunities for long term perspective

Figure: 6

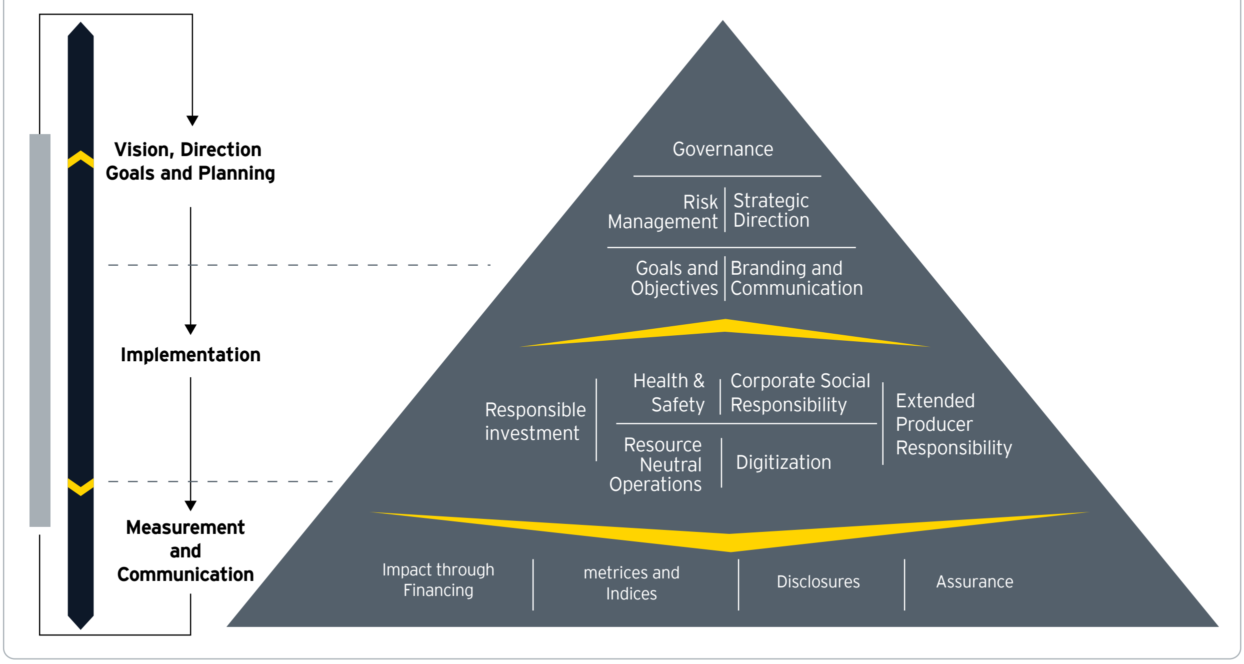
Over the past few decades, EY's Climate Change and Sustainability Services (CCaSS) team has been delivering value to its clients by supporting them in identifying and managing ESG risks and opportunities. EY has also been engaging with the key industry leaders both, at an India level and also at a global level. For EY, helping organizations build in resilience and maximize value is the core objective of deploying an ESG focused approach.

At EY, we believe capital and talent will shift from organizations that only create value for their shareholders to those that create value in the long term, across a broader group of stakeholders, including employees, consumers, suppliers, communities, government, investors and shareholders. In line with this next wave strategy we are trying to help our clients build the long-term value framework to help define and measure ambition

Recently at a global stage, EY forged a partnership with The Prince of Wales's Sustainable Markets and communications company Freuds to launch S30, which brings together Chief Sustainability Officers from some of the world's most influential companies to speed up business action on sustainability. S30 members represent companies with a total market capitalization of US$6.7t, revenue over US$2.3t and over 5 million employees.

Further, to support its clients maximize the value from ESG, EY has developed the 'Sustainable by Design' framework. The framework has been developed with the objective of assisting organizations in generating long-term sustainable value by integrating sustainability principles across the product value chain. To thrive in the new normal, organizations need to steer their strategies and products toward sustainability to remain relevant and resilient. The sector agnostic framework puts together 15 core elements across three key categories of planning, implementation and measurement.

Sustainable by design - an EY framework



Source: EY research

How EY is working towards creating better and sustainable world?

Apart from the deployment of the Sustainable by Design model, EY teams also support organizations in a variety of ways move ahead on the ESG curve.

ESG advisory:

- ESG strategy
- Materiality assessments and benchmarking
- Stakeholder engagement
- ESG risk assessment
- Circular economy
- Policy development supply chain sustainability management
- Training and capacity building

Climate change:

- Carbon strategy and internal carbon pricing framework
- Product carbon footprint
- Development of roadmap for commitments like EP100, RE200, SBT
- Adaptation strategies, climate resilience studies
- Energy optimization, water and waste management
- Renewable energy strategy

Environmental, health and safety:

- Sustainable purchasing strategy
- Gap analysis
- EHS management systems and assurance frameworks
- Resource efficiency, waste and packaging advice
- Due diligence reports
- Supply chain audit – EHS and Social
- Safety culture and behavioral maturity assessment

Outcomes measurement:

- Outcomes measurement framework
- Social and natural capital impact assessments
- Staff engagement programs
- Building internal capacity to measure/report impact
- Community investment and aid strategies

ESG reporting advisory:

- Non-financial, integrated annual reports
- Corporate governance risk disclosures
- Management reporting, reporting performance to the board
- Benchmarking of non-financial reporting
- Internal and external reporting strategies

Non-financial reporting assurance services:

- Integrated and sustainability reports
- Environmental and social management systems
- Claims related to social and environmental outcomes of specific products or services
- Carbon credits or offsets issues under voluntary and/or regulatory standards
- Product carbon footprint

Why EY?

EY Sustainable Finance

Leading Initiatives

EPIC: build out of non-financial metrics including innovation and human capital.

Long Term Value: Helping companies understand and articulate how they generate shareholder value.

WEF ESG 'scorecard' - IBC Long-term Prosperity Project: Proposal recommending a common set of universal ESG metrics / disclosures on non-financial factors.

UNEP FI: EY supports the working groups for Positive Impact Finance.

Thought Leadership

EY on Carbon Neutrality

"Protecting the planet for future generations is an important issue for EY people and becoming carbon neutral this year is a real step forward on the EY sustainability journey. As an organization that spans more than 150 countries with varying views and ambitions on climate change, we recognize this is no easy feat. However, with over 284,000 EY people who are dedicated to our purpose of building a better working world, EY has a once-in-a-lifetime opportunity to take immediate action to create sustainable, inclusive growth for generations to come."

Carmine Di Sibio, EY Global Chairman and CEO, January 2020

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2,84,000+
people

150+
countries

700+
offices

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Amongst **Working Mother** and AVTAR **Top 10 Best Companies** for Women in India award 2017, 2016

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Present across
15 locations in India

World's #1 professional services employer Universum ranking **2017**

14 years
on Diversity Inc's "Top 50 Companies for Diversity" list

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