

# Take5

for business

Volume 9 Issue 3 - 3 June 2021

Re-modelling  
strategies with  
ESG

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow diagonal line is positioned above the 'Y', extending from the top right towards the center.

Building a better  
working world

# ESG, a core strategy to build resilience and sustainability

Today's new normal is characterized by heightened public concerns about environmental, social and governance (ESG) issues and increasing demands by institutional investors, financiers, buyers and stakeholders - boards, employees, customers and communities - for organizations to deliver and step up their ESG responsibilities.

The recent 12 months have seen ESG gaining traction as a core strategy to reset business models and restore not just short-term and medium-term resilience but also build long-term sustainability.

Further, recent updates in the Malaysian Code on Corporate Governance 2021 (MCCG 2021) have highlighted the urgent need for boards and senior management of public-listed companies to manage ESG risks and opportunities. To strengthen board oversight, MCCG 2021 recommends five best practices. Among the prescribed areas<sup>1</sup> are:

- ▶ Board ensures company's sustainability strategies, priorities, targets and performance are communicated to stakeholders.
- ▶ Performance evaluations of the board and senior management include reviews of their performance in addressing the company's material sustainability risks and opportunities.

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To navigate a new normal of disruptions and challenges, ESG is the organizations' moral compass to re-model business strategies whilst exploring new business opportunities.

Mainstreaming ESG can strengthen organizational resilience and build long-term value and sustainability.

**Dato Rauf Rashid**

EY Asean Assurance Leader  
Malaysia Managing Partner  
Ernst & Young PLT

## What are the ESG strategic priorities and objectives?

ESG priorities are focused on sustainability, corporate responsibility and their material financial impact on an organization's immediate, medium-term and long-term value. The strategic priorities and objectives of the three ESG pillars include:

<b>E</b> <b>Environmental</b> Climate change is the main priority	<b>S</b> <b>Social</b> Delivering to all stakeholders	<b>G</b> <b>Governance</b> The guiding force
The impact of climate change on an organization's business model	The value that businesses create that potentially impacts investors, employees, customers and communities	The system by which all core business activities are directed, controlled and monitored as it is critical to create long-term value

Note:

<sup>1</sup> Prescribed areas are sourced from the MCCG 2021 - practice notes 4.2 and 4.4.

Sources:

- ▶ *How to respond to rising investor expectations around ESG*, EY, February 2021
- ▶ *How ESG creates long-term value*, EY, October 2019
- ▶ *Malaysian Code on Corporate Governance (2021 Revision) - Media Technical Briefing*, SC, 27 April 2021
- ▶ *Malaysian Code on Corporate Governance*, SC, 28 April 2021

# What are CEOs' and investors' new ESG perspectives?

The COVID-19 crisis and climate change risks have pushed ESG to become the core pivot strategy in resetting business models. Major institutional investors are prioritizing ESG factors in their investment selection and portfolio allocations.

**80%** of CEOs believe putting humans (employees, customers and other stakeholders) at the centre of decision-making will be a core value driver.

*EY CEO Imperative Study 2021, part 2*

**79%** of CEOs surveyed say companies that maintain their focus on long-term value will emerge stronger in a post-pandemic world.

*EY Long-Term Value and Corporate Governance Survey 2021*

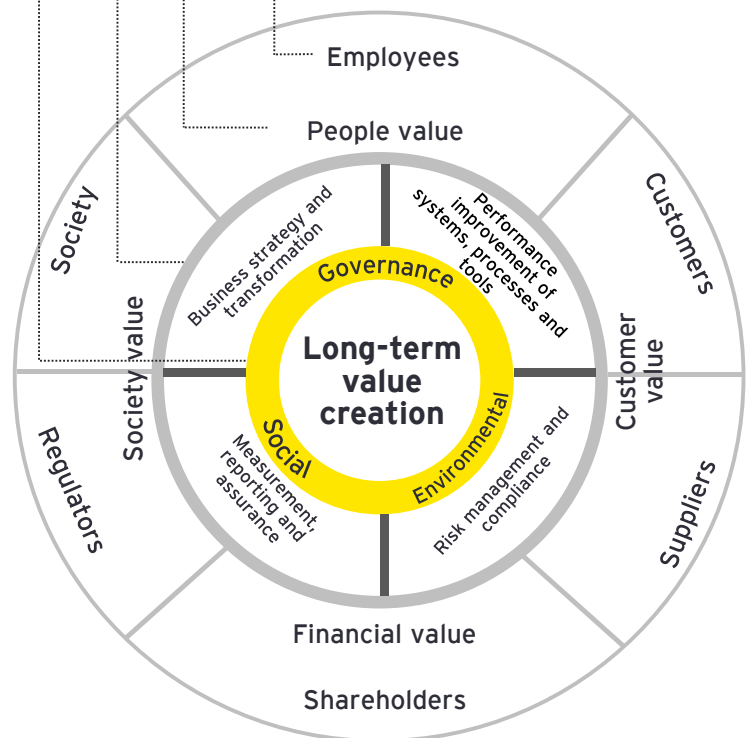
**73%** of respondents plan to increase ESG investment either significantly or moderately by end of 2021.

**52%** of investors surveyed have adopted an ESG framework.

*MSCI Investment Insights 2021 Global institutional investor survey*

## Strategic focus on long-term value creation across stakeholders

Why? How? What? Who?



**COVID-19 crisis and climate change risks have pushed ESG to become the core strategy.**

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It is time to shift sustainability from a reporting-led conversation to a value-based narrative and turn sustainability into a business opportunity.

Aligning to ESG requires integrating ESG pillars into strategic planning and business operations, in tandem with board oversight and senior management focus.

**Terence Tan**

Partner, Climate Change and Sustainability Services  
Ernst & Young PLT

Sources:

- *How can today's CEO bridge the gaps to realize tomorrow's opportunities?*, EY, March 2021
- *Will there be a 'next' if corporate governance is focused on the 'now'?*, EY, February 2021
- *How will ESG performance shape your future?*, EY, July 2020
- *MSCI Investment Insights 2021 Global institutional investor survey*, MSCI, January 2021

# What is the ESG regulatory focus for Malaysia?

Malaysia's regulators are increasing their attention on ESG. The Securities Commission (SC) has issued the MCCG 2021 (28 April 2021) with significant updates and Bank Negara Malaysia (BNM) has released the Climate Change and Principle-based Taxonomy (30 April 2021) to guide financial institutions (FIs).

SC's new and enhanced practices include the urgent need by boards and senior management to jointly manage material ESG risks (including climate risks) and opportunities. Among the recommended corporate governance practices are the setting of a company's sustainability strategy, priorities and targets, as well as stepping up on sustainability reporting and relevant ESG communications to internal and external stakeholders.

## SC MCCG 2021: new enhancements and practices for board oversight of sustainability

Strengthening oversight of sustainability  Five (5) best practices:	4.1	Board, together with senior management, takes responsibility for the governance of sustainability in the company, including setting the company's sustainability strategy, priorities and targets. Strategic management of material sustainability matters should be driven by senior management.
	4.2	Board ensures that the company's sustainability strategies, priorities and targets as well as performance are communicated to external and internal stakeholders.
	4.3	Board takes appropriate steps to ensure it stays abreast with and understands sustainability issues, including climate-related risks relevant to the company.
	4.4	Performance evaluations of board and senior management include reviews of their performance in addressing the company's material sustainability risks and opportunities.
	4.5 (Step up)	Board identifies a designated person within management to provide dedicated focus to manage sustainability strategically.

BNM's Climate Change and Principle-based Taxonomy (CCPT), aimed at encouraging the adoption of ESG principles in FIs, complements the Value-based Intermediation Financing and Investment Impact Assessment Framework (VBIAF) Guidance Document. The VBIAF sets out ESG considerations in the governance, business strategy and operations, reporting and risk management systems.

## BNM CCPT: guiding principles - ESG

Assessment of economic activities	<ul style="list-style-type: none"> <li>▶ <b>Guiding principle 1: <u>Climate change mitigation</u></b> <ul style="list-style-type: none"> <li>▸ Reduce or prevent greenhouse gas (GHG) emissions</li> </ul> </li> <li>▶ <b>Guiding principle 2: <u>Climate change adaptation</u></b> <ul style="list-style-type: none"> <li>▸ Increase resilience to withstand the adverse impact of current and future climate change</li> </ul> </li> <li>▶ <b>Guiding principle 3: <u>No significant harm to the environment</u></b> <ul style="list-style-type: none"> <li>▸ Take into account the impact of economic activity and overall business on the wider ecosystem</li> </ul> </li> <li>▶ <b>Guiding principle 4: <u>Remedial measures to transition</u></b> <ul style="list-style-type: none"> <li>▸ Address the significant harm identified at economic activity level and/or the overall business level</li> </ul> </li> <li>▶ <b>Guiding principle 5: <u>Prohibited activities</u></b> <ul style="list-style-type: none"> <li>▸ FIs should finance economic activities that are not illegal and do not contravene environmental laws</li> </ul> </li> </ul>
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### Sources:

- ▶ *Malaysian Code on Corporate Governance (2021 Revision) - Media Technical Briefing, SC, 27 April 2021*
- ▶ *Malaysian Code on Corporate Governance, SC, 28 April 2021*
- ▶ *Climate Change and Principle-based Taxonomy, Bank Negara Malaysia, 30 April 2021*

# How to measure long-term value

Questions C-Suites can raise in strategic discussions about ESG, sustainability and the provision of long-term value include:

<b>Board</b> What can drive commitment to deliver long-term value to stakeholders?	<b>CEO</b> Is the current business model able to deliver positive values to all stakeholders?	<b>CFO</b> How does integration of ESG into corporate strategy enhance financial performance?
<b>COO</b> How to operate more efficiently considering resources across our operations?	<b>CSO</b> How can sustainability strategies create competitive advantage?	<b>CRO</b> How to help ensure corporate resilience to challenges caused by environmental and social risks?

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To maintain competitive advantage and stay ahead of the curve in our rapidly changing ecosystem, businesses need to continuously innovate solutions to address the specific sustainability concerns of stakeholders and to drive a fit-for-purpose business model.

**Arina Kok**

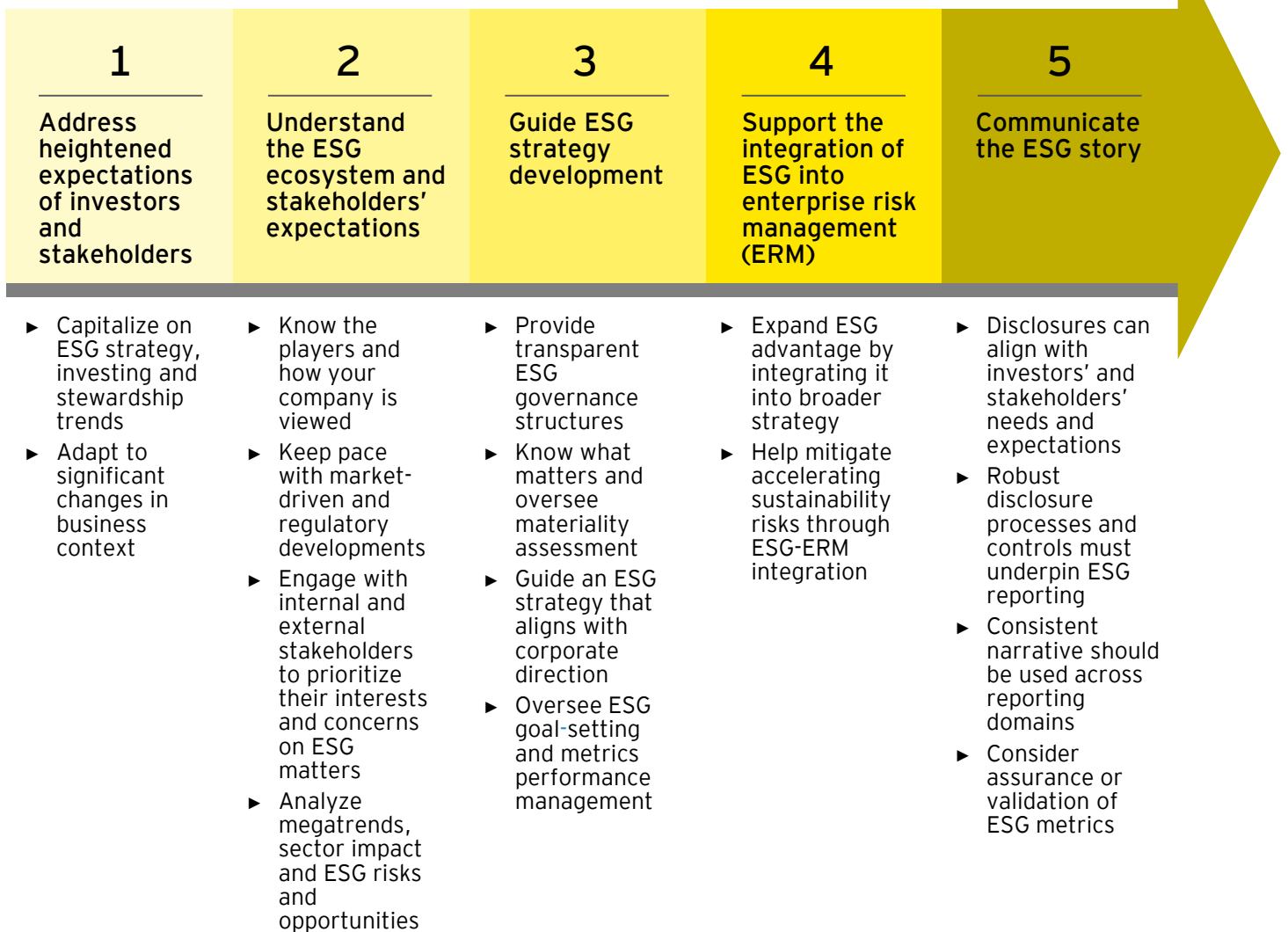
Director, Climate Change and Sustainability Services  
Ernst & Young Advisory Services Sdn Bhd

Source: *Why moving ESG up this decade's business sustainability agenda is key*, EY, March 2021

# Priority 1: How to strengthen board oversight of ESG

COVID-19 disruptions, accelerating “new normal” transformation, stakeholder capitalism and concerning climate change risks have elevated ESG to become a strategic business imperative. Boards can strengthen ESG oversight to build company resilience and unlock long-term value creation through the consideration of five (5) actions:

## Five ways boards can enhance oversight of ESG



Source: *Five ways boards can unlock ESG's strategic value*, EY, December 2020

# Priority 2: How to remodel strategy, transform business and measure impact

To re-model your organization, there are three steps to consider:

## 1 Reshape strategy

How do you define a corporate strategy that aims to deliver optimum value to stakeholders?

- ▶ Refresh market context, demand drivers and purpose definition
- ▶ Define business focus, strategic capabilities and competitive advantage
- ▶ Assess and prioritize stakeholder outcomes (risks, opportunities)
- ▶ Develop narrative on stakeholder value proposition
- ▶ Define measurable outcomes
- ▶ Develop capital allocation model and drive organizational alignment
- ▶ Appoint a designated person to strategically manage sustainability

## 2 Help transform business

How will you transform your business to successfully implement your strategy?

- ▶ Develop future scenarios and strategic planning across horizons
- ▶ Identify capability gaps across employees, consumers and supply chains
- ▶ Set strategic roadmap, define and prioritize actions and initiatives
- ▶ Drive the optimization of portfolio in alignment with stakeholder risks and opportunities
- ▶ Undertake valuation, modeling and economic impact measurement
- ▶ Adjust compensation and incentive structure to support strategy

## 3 Demonstrate and measure impact

How will you measure, report and communicate success across stakeholders?

- ▶ Set improvements in company's governance structure, including evaluation of ESG effectiveness
- ▶ Develop metrics and reporting across key stakeholder outcomes
- ▶ Performance evaluations of board and senior management to include reviews of their performance in addressing company's material sustainability risks and opportunities
- ▶ Help determine the appropriate level of remuneration for directors and senior management, taking into consideration the company's performance in managing material sustainability risks and opportunities
- ▶ Conduct stakeholder engagement
- ▶ Communicate value delivered to the market

# EY thought leadership



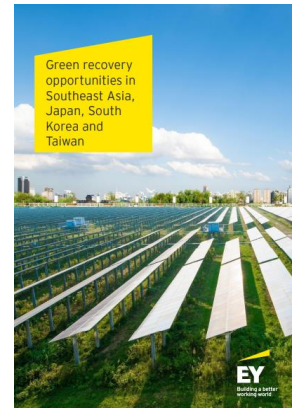
**How will ESG performance shape your future?**  
July 2020



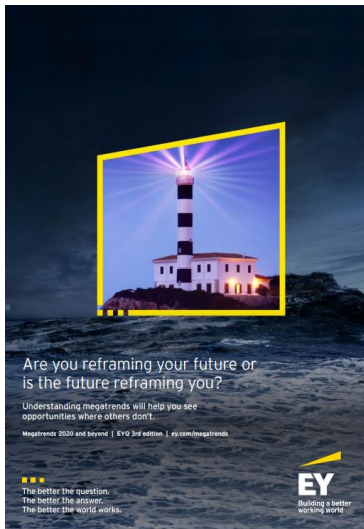
**TCFD report playbook**  
September 2020



**Climate change and sustainability: Global regulators step up the pace**  
January 2021



**Green recovery opportunities in Southeast Asia, Japan, South Korea and Taiwan**  
April 2021



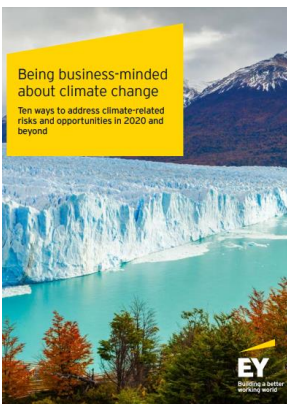
**Are you reframing your future or is the future reframing you?**  
June 2020



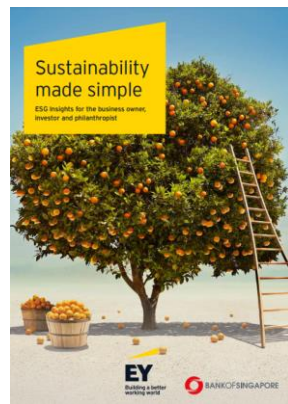
**Climate Risk Disclosure Barometer 2020 Malaysia**  
December 2020



**Fortifying governance: MCCG 2021 updates**  
May 2021



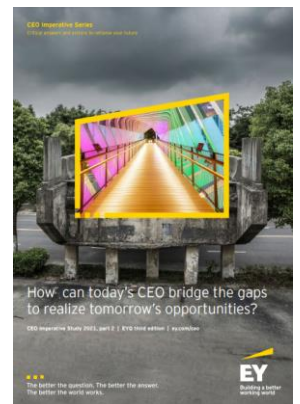
**Being business-minded about climate change**  
October 2020



**Sustainability made simple**  
November 2020



**CEO Imperative Study 2021**  
March 2021



**CEO Imperative Study 2021, Part 2**  
March 2021



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