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WEBINAR SUMMARY REPORT

Regulations Drive the ESG Agenda

October 08, 2024

by

Mr. Amit Tandon

Founder and Managing Director
Institutional Investor Advisory Services
India Limited (IiAS)

Moderator:
Prof. Neerav Nagar
Associate Professor
Finance and Accounting, IIMA

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Webinar on

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Founder & Managing Director,
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Moderator: **Prof. Neerav Nagar**, Associate Professor of Finance and Accounting, IIMA

October 8, 2024 5:00 p.m. IST

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About the Speaker

Mr. Amit Tandon

Amit Tandon is the founder of Institutional Investor Advisory Services India Limited (IiAS) and its managing director since July 2011. IiAS is a SEBI-registered advisory firm, dedicated to providing participants in the Indian market with independent opinion, research and data on corporate governance issues as well as voting recommendations on shareholder resolutions.

Before IiAS, Amit was the managing director and CEO of Fitch Ratings India from October 2001 to June 2011. Prior to joining Fitch, he was with the ICICI group for 17 years (from May 1984 – September 2001), where he rotated through various roles and businesses including project finance, leasing, and the merchant banking division. His last role with the ICICI group was as head of investment banking at ICICI Securities.

Amit is a member of the SEBI Committee to Review Takeover Regulations, SEBI's Alternative Investment Policy Advisory Committee as well as SEBI's Expert Committee for facilitating ease of doing business and harmonisation of the provisions of ICDR and LODR Regulations. He has been a member of various other committees, including the Kotak Committee on Corporate Governance, SEBI advisory committee on ESG, the Reserve Bank of India's Technical Advisory Committee on Money, Foreign Exchange and Government Securities Markets, a member of one of the working groups convened by the Ministry of Corporate Affairs to review comments received on the Companies Act and a member of the disclosure sub-group on the Ministry of Finance's Task Force on Sustainable Finance. He is a trustee of the Foundation for Audit Quality.

Amit studied economics at St Stephens College, Delhi. He has an MBA from the Faculty of Management Studies, Delhi and an MPhil degree from the University of Cambridge, UK.

Webinar Summary Report
Regulations Drive the ESG Agenda

About the Moderator

Dr. Neerav Nagar

Neerav Nagar is a Fellow of IIM Calcutta. His teaching and research interests lie in the areas of financial accounting, financial statement analysis, corporate governance and earnings manipulation. His research work has been published in leading journals like Journal of Business Finance and Accounting, Corporate Governance: An International Review, Journal of Accounting, Auditing and Finance, Journal of Business Research and Journal of Contemporary Accounting and Economics.

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Abstract

The webinar explored the evolving landscape of ESG (Environmental, Social, and Governance) regulations in India and assessed their effectiveness in shaping responsible corporate behaviour. The discussion delved into the role of ESG ratings in driving accountability and transparency within businesses and examined how proxy advisory firms contribute to strengthening the credibility of ESG systems. By providing a comprehensive overview of these key components, the speaker shed light on the critical regulatory forces driving the ESG agenda in India.

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Introduction

The concept of Environmental, Social, and Governance (ESG) factors has become central to the way businesses operate and are evaluated globally. ESG represents a framework through which companies are assessed not just on their financial performance but on how their practices impact the environment, society, and corporate governance. While it may seem straightforward, the practical implementation of ESG has proven to be complex and often fragmented. Mr. Tandon, a seasoned professional in the sustainability domain, addresses these challenges and offers insights into why ESG is both a necessary and evolving aspect of modern business.

Mr. Tandon argues that despite being grouped together, the “E,” “S,” and “G” components are often at odds with each other. Environmental concerns focus on sustainability and minimising harm to the planet, while social aspects address the well-being of employees and communities, and governance ensures transparency and ethical business practices. The only cohesive thread linking them, he asserts, is the broader impact these factors have beyond financial outcomes, which forces companies to look beyond profits and consider their broader responsibilities. Due to this inherent complexity, ESG is frequently perceived as challenging, with regulations playing a critical role in advancing the agenda.

The regulatory landscape surrounding ESG is diverse, with national and international standards guiding companies’ reporting and compliance. Different regions adopt varying approaches; Europe leads with strict ESG disclosure rules, while the U.S. is split between a profit-maximisation mindset and a growing inclination toward broader societal accountability. In India, ESG has taken a socially-oriented approach, reflecting the country’s unique developmental context. The Securities and Exchange Board of India (SEBI) has been instrumental in this journey, introducing the Business Responsibility and Sustainability Reporting (BRSR) framework that emphasises both transparency and accountability, while seeking to address the nation's specific sustainability needs.

Tracing the evolution of sustainable development, Mr. Tandon highlights milestones such as the 1972 Stockholm Declaration, the 1992 Rio Earth Summit, and the Paris Agreement in 2015, which collectively set the stage for global environmental and social accountability. These milestones not only shaped policies but also established frameworks for businesses and governments alike to tackle environmental and socio economic challenges in tandem. In India, regulatory developments like the introduction of CSR guidelines and SEBI’s BRSR have underscored the need for companies to integrate sustainability into their business models.

In this context, Mr. Tandon explores how ESG adoption is no longer a voluntary or solely altruistic endeavour, but an essential part of corporate strategy influenced by investor expectations and regulatory mandates. He emphasises that the evolution of sustainable finance and investor attitudes toward ESG, particularly in India, signals a shift toward long-term value creation.

Webinar Summary

Diving straight into the topic of ESG (Environmental, Social, and Governance), Mr. Tandon stated that the terms E, S, and G do not sit well together with each other. He asked the following question: What does E have to do with S and what do the two have to do with G? Consequently, the only thread binding them all together is not just financial numbers but areas and data that go beyond financial numbers. According to Mr. Tandon, once you stop looking at the financial numbers, you start considering what impact the company's activities are having on the environment, what impact they have on communities, and finally, how good the company's governance practices are. This is the reason why the three terms would sit well together, because otherwise, there isn't much that will bind them together. As a result, ESG is a fairly complicated subject, and for a while now, the belief has been that regulations will be driving the ESG agenda more than anything else due to its overarching impact.

The general idea with regard to environment and sustainability is that small companies believe these issues are for the large companies to worry about. The large companies believe that these are concerns of the government, while governments think that sustainability issues should be addressed by the more developed countries. In response, the developed countries feel that when it comes to environmental sustainability, the focus of worry should be on India and China. Mr. Tandon views this as simply "passing the buck", with no one taking ownership of the problem. He believes that either each person should feel strongly about the environment and sustainability and take individual action or we let regulations push from the top, which will force people to seriously work toward solving this problem. Having spent a considerable amount of time in this space and having interacted and worked with various companies, Mr. Tandon believes that unless regulations drive the ESG space, we will not see the outcomes that we want.

Against this backdrop, Mr. Tandon aimed at discussing three crucial aspects of ESG: How has it evolved since its inception? What has taken place in this space? Given that this is an arcane subject, how are companies looking at it from an investment perspective?

Environmental, Social, and Governance are non-financial factors of which some can be seen across industries and can be quantified, while some of them are not easily quantifiable. These factors are also not commonly a part of financial reporting, but companies make them a part of their annual report or release a standalone sustainability report. In the case of India, most companies come up with an annual report and a few months later, they report their emissions based on the Business Responsibility and Sustainability Reporting (BRSR) of the Securities and Exchange Board of India (SEBI). However, only a handful of companies combine their annual accounts with their sustainability activities. On the other hand, there are numerous institutions at the international level, such as the Global Reporting Initiative (GRI), Sustainability Accounting Standards Board (SASB), Carbon Disclosure Project (CDP), and many more, which have created different frameworks, disclosure standards, and definitions of materiality. Furthermore, national and regional level bodies, such as the US Securities and Exchange Commission (SEC), have their own specific standards. The point here is that because there is a surfeit of disclosure norms, companies find it difficult to navigate them and many a time lost about where to begin and which standards to adopt. Even though Europe and the US have established reporting norms much before India, there is neither any standardisation nor any clear thinking on the topic. For example, some company boards have special committees that look into environment and sustainability, while some only have one director that is responsible for the organisation's sustainability actions and reporting. In some cases, companies hire an

external advisor to manage their reporting activities, while others believe that it is the responsibility of the entire board. The reason why this development needs to be highlighted is that there are countries that have begun their sustainability journey with far greater vigour than what we have and yet they have not been able to devise a fixed or a standardised way of implementing it. This means that there are different ways of approaching the ESG issue and even more different ways of adopting it.

Talking about the evolution of sustainable development, Mr. Tandon pointed out that its origins can be traced back to the Stockholm Declaration, which happened in 1972. It was the first conference of its kind to make the environment the centre of focus in the economic development process. Even though the discussions were riddled with geopolitics due to the conflict between the West and the Russian bloc during the initial years, the Stockholm Conference still managed to start a dialogue between the industrialised and developing countries regarding economic growth and environmental problems, such as air and water pollution. From the perspective of India (and other developing economies), environmental degradation has been a consequence of the rampant industrialisation of the West and therefore, businesses and industries go hand-in-hand with environmental sustainability.

The other aspect during this time was that people were still digesting the new narrative and there were long periods of lull in the interim, although there were several recommitting conferences on the issue. One major outcome was the setting up of the World Commission on Environment and Development (WCED), also known as the Brundtland Commission. It came out with a report called Our Common Future, which stated that governments cannot address the issue of environmental protection separately from other crises of the time, such as the energy crisis and the development of economies. This recognition that the environmental crisis and other crises go hand-in-hand became a significant turning point in how the debate on the topic was to be shaped in the forthcoming years.

A few years later in 1992, after the Cold War was over, the Rio Summit, better known as the Earth Summit, took place. It was at this summit that the role of business in driving sustainability was discussed and debated more openly. The summit witnessed an active participation of NGOs, who brought in a considerable amount of scientific evidence that showed how businesses impact the climate by emitting carbon and other greenhouse gases (GHGs), which deplete the Ozone Layer and damage the environment. The next pivotal development on the issue of environment and sustainability was the Kyoto Protocol of 1997, which demarcated the responsibility of the developed nations toward the non-industrialised economies. The protocol devised different mechanisms for the industrialised countries to facilitate the implementation of environmental projects in the less-developed part of the world. Next came the Paris Agreement at COP21 in 2015, which aimed to limit the increase in the average global temperature to 1.5 degrees Celsius, with a flexibility to go up to 2 degrees Celsius.

Between the Kyoto Protocol and the Paris Agreement, a few other developments took place. One of these was the formation of the UN Global Compact, which was born in 2000 as a voluntary initiative based on commitments made by CEOs to implement universal sustainability principles and to take steps to support UN goals.[1] This was an attempt to broaden the scope of the discussion on sustainability to include socio economic issues, such as eradicating extreme poverty, achieving universal primary education, reducing child mortality, and combating life-threatening diseases. The formation of the UN Global Compact also coincided with the roll-out of the Millennium Development Goals (MDGs). The idea behind these initiatives was to recognise that advancing the sustainability agenda will require addressing core socio economic issues. Since this cannot be done by governments alone, the private

[1] https://unglobalcompact.org/about

sector will need to get more actively involved in tackling these challenges. At the 2012 Rio Summit, which was held twenty years after the Earth Summit, nations took stock of the progress that had been made in the last two decades. While the significance of the MDGs was acknowledged, it was felt that more tangible goals need to be formulated and this resolution led to the Sustainable Development Goals (SDGs). The SDGs were 17 in number, as opposed to the MDGs, which were only 8, and provided a fairly comprehensive list of what economies need to achieve.

However, while other nations were devising ways to pursue the SDGs, the US remained noncommittal, US businesses in particular, as they interpreted the SDGs as being militant and conflicting with their profit maximisation interests. On the other hand, economists like Raghuram Rajan view that profit maximisation happens only after corporations have met their other concerns, including societal and environmental. Given the history of evolution of the corporate sector in the US, companies have always been primarily concerned about maximising gains for their shareholders. This was reiterated by the Business Roundtable, which is a large group of the most influential businesses in the US and includes the likes of Jeff Bezos and Jamie Dimon. As a result, the debate around sustainability has become highly polarised in the US, especially along political lines. On the one hand, Democrats believe that businesses need to worry about not just the shareholders but also the community; the Republicans, on the other hand, state that the business of business is business, that is, they need to only worry about the shareholders. Their stand gets further reinforced through taxes, whenever they are in power. Europe has gone in the other direction by creating more stringent rules for sustainable finance development and disclosure regulations.

According to Mr. Tandon, the US and Europe are currently a hotspot of rules and regulations, with different standards, indices, and reporting mechanisms overlaid by the SDGs, the UN Global Compact, and each country's national guidelines on responsible business conduct. The existence of multiple such rules and regulations has enhanced the need to standardise them. For example, there is an attempt to merge the Integrated Reporting Framework (IRF) with the Sustainability Accounting Standards Board (SASB), while the Task Force on Climate-related Financial Disclosures (TCFD) is trying to bring all reporting standards together, which is a welcome step for companies operating in different geographies.

Coming to India, Mr. Tandon observed that the seeds of ESG investment were sown in the Eleventh Five Year Plan (FYP), whose theme was inclusive growth, and it was quickly followed by the introduction of the Corporate Social Responsibility (CSR) Voluntary Guidelines. While today there is a mandated percentage for CSR, in 2009, it was entirely up to the companies how much they wanted to spend on social or environmental causes. The whole CSR agenda at the time was driven by the Ministry of Corporate Affairs (MCA) and the guidelines, which were nine broad principles for firms to adopt in their business practices, derived from the UN Global Compact. These guidelines were essentially meant for businesses to go beyond their profit motive and promote other areas impacted by their activities, such as ensuring the well-being of employees, including those in the value chain, and providing goods and services in a safe and sustainable manner. With the guidelines in place, the next question that arose was: How should companies report on their CSR activities? This led to the formulation of the Business Responsibility Report (BRR) of the SEBI, which was introduced in 2012 as a voluntary reporting framework. With the SDGs becoming a part of the global lexicon and the changes brought about by the Companies Act of 2013, the need to revisit the BRR was felt. Following this growing sentiment, the government conducted a study of the 490

companies reporting under the BRR and found that there were several issues regarding accuracy and clarity due to the entities using different units of measure. For example, when a company reported on their effluent discharge, it was unclear how and what they were measuring. What emerged from this study were the National Guidelines for Responsible Business Conduct (NGRBC). The government also decided to stick with the nine principles enunciated in the Voluntary Guidelines and mapped the SDGs to these principles, which brought clarity to companies as well as the investors on what each term meant and represented. As per Mr. Tandon, once SEBI also got involved by reviewing and adopting these principles and rechristening the BRR to the Business Responsibility & Sustainability Reporting (BRSR), the ownership of ESG reporting in India was jointly taken up by SEBI and the Ministry of Corporate Affairs. The good part of this development was that the underlying principles, whether it was the Voluntary Guidelines or the NGRBC, essentially remained the same. While earlier the primary reporting values were integrity and ethics, now they have shifted to transparency, cross-reporting and interlinking of various standards, better defined parameters and performance matrices, and uniformity across industries. Today, companies are making sustainability disclosures an integral part of their annual report. What SEBI and MCA have managed to identify through these regulations are core leadership principles.

Moving to the BRSR, Mr. Tandon explained how the framework is divided into three sections: the first section deals with general disclosures, the second is about process disclosures, and the third covers performance disclosures, which are primarily concerned with leadership. The framework currently applies to the top 1,000 listed companies in India and SEBI is rolling out a glide path for companies to start reporting under the BRSR. The attempt is to derive comparability between what companies are disclosing and what measures they are using to make these disclosures. SEBI also recognised two crucial elements - one was that even though E, S, and G do not sit well together, they do find application in certain sectors, such as manufacturing, power, and coal mining; the second was that in India, the thrust of sustainability was on the social sector, which included gender equality and employee well-being. In contrast, in the West, the thrust has been on energy efficiency and clean energy, both of which work on a per-unit basis. However, being at very different stages of development, India cannot focus entirely on energy efficiency and therefore, according to Mr. Tandon, our emphasis has been on using resources efficiently over a period of time and bringing down emissions. Since the concerns of the US and Europe are significantly different from those of India, the private sector in India is channelling their CSR spending on social initiatives, such as educating the girl child, financing midday meal programmes, and skilling the workforce. The "S" in India's ESG landscape is, thus, at the forefront, even if globally ESG is seen from a different lens. Furthermore, SEBI asserted that India now has a defined ESG standard, which must be accepted by stakeholders in the West. This standard has been set keeping in mind India's economic growth stage and its socioeconomic makeup. Mr. Tandon believes this assertion was directed toward the ESG ratings agencies in Europe and the US, with the underlying message being that if Indian companies abroad are given lower ESG ratings because they are not in compliance with European standards, it would not be acceptable.

The other area that SEBI directed its attention toward was greenwashing, which occurs when a company claims that its products are more environmentally friendly than they actually are. For instance, a company may say that it's printing its reports on recycled paper while its emissions are increasing significantly. To address this issue, SEBI introduced the BRSR Core - Framework, which comprises ESG indicators that are verified by third-party agencies to lend authenticity to the company's claims. These developments have essentially characterised the history of ESG in the Indian context.

Next, Mr. Tandon spoke about the role of Indian banks in advancing sustainable finance in the country. He observed that some areas are low-hanging fruit for the banks, such as supporting green power projects or financing rooftop solar projects, since India is still in the early stages of climate finance. When one looks at the data, it becomes clear that huge sums of money is currently being pumped into green projects. Globally, the number stood at around US$ 2.8 trillion in 2023[2]; in India, it hovers around US$ 4.3 billion dollars, as per the 2023-24 Budget[3], which shows that India is far behind the world in employing financial resources to drive sustainability. This topic led to the discussion of how investors view ESG and their understanding has changed over the years. According to Mr. Tandon, in the initial phases, investors used negative or exclusionary screening criteria to determine if they would invest in a company. For instance, investors refrained from putting their money in fuel companies and defence manufacturers, which was the easiest approach to take at that time. A telling example of the exclusionary criteria is the Norwegian Pension Fund, whose market value currently stands at US$ 1.71 trillion[4] and which refused to invest in fossil fuel companies in the early stages. That stance, however, has changed today due to other geopolitical developments, such as the on-going Russia-Ukraine war, which has made investors rethink the negative approach. As a result, the focus today has moved to ESG integration that investors expect companies to follow, even as they pursue their financial ambitions. In other words, the new approach being adopted by investors involves them considering ESG parameters that are important to them and assessing them alongside the financial parameters and then deciding whether to invest in the company. This approach is giving way to what is being known as "corporate engagement". If a company's auditors resign, for example, and if the social criteria is a core factor for the investors, then they investigate if the company still has merit and stay invested in it. If not, then it will be put on the exclusion list. Opposite to the negative approach is the positive approach, which involves themes such as "best in class". As per this approach, depending on which criteria holds the highest value, an investor will focus on companies that are only undertaking green energy projects, for instance, or invest in companies that employ more than 70% in their workforce. The Government Pension Investment Fund, Japan's investment fund, has made great strides in ESG integration, corporate engagement, and stakeholder action. The fund's view is that if it does not invest in a coal-fired plant, for example, some other entity will. Therefore, the best course of action is to invest in the company, engage with it from the inside, and help it bring down its emission levels over a period of time and supplement it with solar energy or include clean energy in its mix. For them, investing in ESG is critical.

[2] https://www.iea.org/reports/world-energy-investment-2023/overview-and-key-findings
[3] https://www.climatechangenews.com/2023/02/01/india-plans-4-3-billion-investment-in-clean-energy/
[4] https://www.nbim.no/

Q&A Session

Q. Could you give us some examples of the low-hanging fruit that you had mentioned that Indian banks can go after? And what are the tougher alternatives that these banks are looking at?
A. Let's break the answer up into two parts. First, an example of low-hanging fruit could be that a bank decides to install solar panels on top of its ATMs, so that some amount of power is generated through renewables. Similarly, a bank can remove the use of plastic bottles from its offices. These are some of the easiest options for banks to adopt sustainable practices. The other low-hanging fruit is lending to the microfinance sector and achieving certain ESG targets by mixing up your portfolio.

Q. If Indian banks were truly keen on integrating ESG values in their businesses, what changes will they need to make in their lending decisions?
A. The changes will primarily revolve around how the banks view the parameters when they are lending to companies. If a company has certain emissions ambitions, then what standards is it adhering to? What steps is it taking or planning to take to reduce its emissions? What banks can do is bake its ESG requirements into the project cost itself, which will then reduce emissions or discharge, depending on the project. While companies acknowledge that they can always do more to bring down their carbon emissions, for them it makes financial sense only up to a particular cost. Therefore, banks are now thinking of ways to fund such projects and bring down their costs. What they can do is turn to global multilateral agencies and negotiate with them for long-term loans, such as a 25-year loan, and finance renewable energy projects, for instance. Another way that banks can play a role in advancing sustainability is to identify the best-in-class practices in the private sector and explore ways in which they can be shared with other companies.

Q. In your opinion, regulations are picking up pace in India. Where do you think these regulations will be headed over the next five to ten years? What kind of conditions will the Indian market have to face?
A. The first question is the pace at which we want to move, and the second one is the depth to which we want to go. For example, if you are dealing with an auto company, you look at its key suppliers and categorise them into A, B, and C. Then, you start moving down the curve and say that by 2029, your Class A suppliers need to comply with these norms, by 2035, your Class B suppliers need to comply, and by 2040, all of your suppliers need to comply.

We are also learning as we are going along. Three years ago, fossil fuels were seen as highly damaging. Today, after the Russia-Ukraine war, suddenly fossil fuels have become good again. Another example is Tesla. Everyone believes that electric vehicles (EVs) are good, but there is a cost attached to them. This cost is in terms of the amount of mining you have to do to make the batteries, and after the batteries have run their course, how do you dispose of them? So, EVs are not green. Another aspect to consider is that if the whole world is going green, if companies are going green, then how are we investing for it? How are we training people for it? For example, we need solar panels. So, the question is whether we can manufacture solar panels in India rather than import them from China. Is it more efficient to make solar panels in India by sourcing the materials, such as silicon, from within the country itself? Looking at the trends, can we move this manufacturing into India? The key here is for policies to gear people up for the effects of climate change over the next 30 to 40 years.

Q. What should the ESG focus areas be for financial infrastructure companies, such as stock exchanges, that are generally in Scope 3 but are not in the financing business?
A. The low-hanging fruit for these companies is related to the cloud computing that they extensively use. If you are using cloud computing, where are your servers located? What is their power source? Is the source green or something else? That is the first aspect to consider. The second aspect is that bodies such as SEBI and the MCA have not put in those many efforts to develop the indices they have created and as a result, ESG reporting has been weak. Can these bodies not play a bigger role in parsing and splicing the data to identify the best in classes and make those data available to companies? This is their responsibility, if they begin to treat ESG as a national project. What they currently have is one index, the Nifty100 ESG Index, which they revise every four or five months. What exchanges can do is create greater awareness among companies by providing them with the necessary data and help them improve their disclosures so that there is better comparability. The other area exchanges can work on is use the data to direct investors towards companies that are showing good results or are improving on their ESG performance.

Q. Since the outcomes on ESG investments have a long gestation period, what are the suggested methods to push clients or companies towards such long-term investments?
A. That's always tricky. For India, the targets are pretty far out, somewhere around 2070 or thereabouts. Let's say a company sets its net-zero target to 2035 or 2040, which is much earlier than what the national commitment is. Nonetheless, it is still 15 years into the future. If you want to achieve your target in 2040, what are you expecting by 2028 or by 2030? Therefore, the best thing for a company to do is to set intermediate targets and monitor them. Next, once a company has its ESG targets, it becomes pretty straightforward. For example, one of the focus areas for SEBI has been the employability in aspirational districts, which is pretty low from a GDP perspective, but SEBI has turned it into a soft target for companies. They are asking companies questions such as how they are tapping into the aspirational districts, how much of their materials they are sourcing from these districts, or whether they are employing people from these areas under their internship schemes. How many of these are qualitative and how many are quantitative? SEBI can put these data points out there and see what they and the companies can do with it. What can be measured gets done. At the same time, not everything can be measured, but even that needs to be identified and get the work done. So, periodic reviews and resetting of targets needs to be done to see if you achieve the goal faster than what you initially expected.

The other area of concern is how to drive a company towards these issues. One way to do that is to hold town halls and other kinds of meetings with the staff and explain why these issues matter to the organisation and its leadership. To engage them deeper into the cause, the management can further ask the employees what suggestions they have to implement such projects. An equivalent to this approach is the Kaizen technique followed by the Japanese that focuses on continuous improvement through small, incremental changes at every level. What can be done on the social aspects? How can you improve ESG governance and processes in the company? This is what is going to get you a little closer to your targets, and maybe even a little bit quicker than you previously envisaged. Therefore, what is needed is a collective effort at the organisational level.

Q. When corporations are rated by ESG ratings providers, does it really have a tangible impact on their ESG performance, according to you? Secondly, will the exit of major ESG ratings companies from the Indian market affect or limit Foreign Institutional Investments (FIIs) and ESG investments in Indian equities?
A. As I mentioned earlier, SEBI has a set of parameters that they are focusing on, such as those related to aspirational districts. For global ratings providers, these parameters meant they would need to change their methodology in India and make it different from what they have employed in other geographies. They felt that this is an additional cost they have to bear and they weren't willing to make these changes because, at the end of the day, they want to use technology. This means they need to employ a similar methodology to compare companies across geographies with the same set of parameters. While SEBI has come out with its guidelines for ESG ratings providers, they are still a work in progress. There are a few things to note, though. One, SEBI has broken down the guidelines into two parts. The guidelines say that to prevent any conflict of interest, an individual can either work with the issuer or with the investor, but not with both. So, there's a subscriber model and an issuer model.

How much of an impact have these guidelines had at this moment? It is difficult to say but two things stand out. The first is that if I have done an analysis, I want to know if it's in the public domain. If it's not in the public domain, it means it is internal and therefore, I need to understand how much of an effort I have put in and how much more is required. The second is that the market has to evolve. It is currently stuck because of some of the assumptions I had mentioned earlier, such as the thinking on fossil fuels and EVs, which don't necessarily apply to India. Our view is that 70% to 80% of our economy is still reliant on coal, and we can't just wish it away, given our neighbourhood and everything else that is happening around the world. My sense is that till people get more clarity or their thinking evolves on these topics, the guidelines will remain a parameter. Is it going to be the primary driver in the immediate future? I don't think so. In the medium to long-term, I think once companies integrate ESG considerations into their decision-making, it will assume greater importance.

One of the factors to keep in mind is that if you look at the BRSR, it contains around 720 parameters. However, the ratings are based only on the core parameters, which are 120 in number. As a result, the impact of each individual parameter may not be material. For example, item 35 may be highly important with a weightage of 2%, but in the overall scheme of things, a low or high score in that item is not going to change my overall rating. I believe until you can bring down the core parameters to a much smaller number, they are not going to be the driver in the short term.

Key Takeaways

Mr. Tandon's insights highlight the fact that Environmental, Social, and Governance (ESG) factors are complex, interdependent, and challenging to navigate without consistent regulatory guidance. While these factors are often viewed separately, he underscores that their unity stems from shared non-financial impacts on society and the environment, beyond mere financial metrics.

One crucial point he raises is the global inconsistency in ESG standards. Different countries and regulatory bodies maintain unique frameworks, which complicates adoption and reporting for companies operating across borders. While Europe has advanced with stringent ESG policies, the U.S. remains divided, reflecting a shareholder-centric versus stakeholder-centric view on corporate responsibility. India, meanwhile, has adopted an "S-first" approach within ESG, prioritising social sustainability to align with its development stage, with the BRSR formulated by SEBI functioning as a key framework.

The evolution of sustainable development, from the 1972 Stockholm Declaration to the Paris Agreement, demonstrates a gradual but growing recognition of the link between environmental and socioeconomic issues. Key milestones, including the Kyoto Protocol and the UN Global Compact, have established international guidelines for sustainability, highlighting the need for corporate and governmental collaboration.

Looking at sustainable finance, Mr. Tandon explains that Indian banks are gradually advancing green finance, yet the sector remains underfunded compared to global standards. Investors are moving beyond exclusionary screening, choosing to engage with companies on ESG principles and encouraging them to adopt greener practices.

In conclusion, achieving global ESG alignment remains a challenging yet crucial endeavour. Mr. Tandon advocates that stronger regulations will be essential in driving this agenda forward, requiring sustained commitment from companies, governments, and investors alike. His insights underscore the potential of ESG to transform how businesses operate, ultimately benefiting society and the planet as a whole.

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