Achieving Economic Sustainability through ESG

The reason why we are living in a polarised world despite the recognition of the need for overall sustainability is the dominant nature of self-centred economic sustainability on the part of certain powerful nations, often at loggerheads with each other leading to power blocs. This scenario seriously threatens to derail the attainment of UN mandated SDGs to which 193 nations have given their commitment.

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AN EYE-OPENING PERSPECTIVE!

For any economic activity (business carried on with profit motive or charitable or other activity carried on without profit motive) to be viable, there should result some surplus after meeting the costs of carrying on the activities. Viable business activities yielding surplus over a long period of time lends itself to sustainability more effectively than those that do not generate reasonable surplus. However, it should be remembered that economics is not the only important pillar of Sustainability. The other two pillars of Sustainability namely Environment and Society are also equally crucial, not necessarily in that order. With this background, an attempt is made in this article to correlate the concerns of these three pillars of Sustainability, so that they can be reconciled and prioritised in an effective manner, such that the overall sustainability is not considerably impacted.

IMPORTANCE OF ECONOMICS IN SUSTAINABILITY

Simply put, Economics is the study of relationships and interactions between individuals and groups in a society that shape the nature of households, firms, markets and other economic entities. Regarded as the father of Economics, Adam Smith, has defined economics as "the science of wealth". The focus of his definition has been on wealth creation that would help us develop nations and find solutions to economic problems. Though this classical theory of economics was widely criticised as being incapable of finding solutions for all economic problems, it has got great relevance to today's enterprises which are driven by the motive to create Profit and Wealth. While Profit and / or Wealth Maximisation as the only goal apparently excluded other considerations, the concept of economics underwent shift of focus from "Wealth" to "Welfare". Lionel Robbins regarded as the father of "Welfare Economics" described economics as "the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses". This definition appropriately addresses the problems of finite and scarce resources which need to be used as well as preserved in a rational manner thereby highlighting the importance of the concerns of environment and society. Viewed from this background, Economics is regarded as a branch of study that helps us understand the phenomenon of scarcity of resources and efficient allocation through the three main economic problems:

1) What to produce / what services to give?;
2) How to produce / How to give services? and
3) For whom to produce / offer services?

These economic problems are further classified into Microeconomics and Macroeconomics.

Micro-economics: The branch of economics that studies economic problems at the level of individual units such as households and firms.

Macro-economics: This is the branch of economics that deals with theorizing and understanding economic problems at the level of the economy as a whole. With the advent of globalisation, macroeconomics can meaningfully extend to

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the whole world with inclusive focus, but with continuing polarization, it is expected that there would only be bit and pieces of globalised macro-economic policies unless all the economies (the developed, developing and the underdeveloped economies of the world) whether in the global north or the global south come together truly in the spirit of concrete consensus and commitment to meet the UN mandated 17 Sustainable Development Goals (SDGs), which are all pervasive in the sense that it truly covers the three pillars of Sustainability. If this is regarded as a pipe-dream then truly inclusive Sustainability is destined to meet the same fate. Let us hope that there is realisation of this stark reality staring at our face – better act late than never.

FACTORS OF PRODUCTION AND SERVICES

Enterprises utilise Capital, Labour, Land and other available Natural resources for production of goods and services. These activities will result in profits which is made available to the stakeholders. Ideally the fruits of these economic activities shall be distributed to the stakeholders which can lead to Economic inclusiveness rather than exploitation of one or more factors of production and / or services without giving them their deserved share of the fruits they are entitled for.

GROWING EMPHASIS ON STAKEHOLDERS

Profitability has been and is the driving force behind any economic activity. Entrepreneurs come with their ideas, ambitions and dreams with an ultimate goal to run a profitable business. The shareholders/ owners of the business all along regarded that the profits belonged only to them and the other stakeholders were either ignored or their concerns were addressed only when they registered their protests. In the mid-1990s with the concept of social and environmental responsibility for business houses gaining traction, the business models giving value to the social and environmental responsibility of business houses alongside their profit motive started evolving which was described as the 3Ps model namely (People, Planet and Profit). This model which got to be referred as the Triple Bottom line model calls for considering the social and environmental implications in the decision-making process of Companies/Business houses alongside of course the economic implications, which is discussed in a later paragraph.

Consequently, the focus of business decisions towards profit motive shifted towards well-being of the society as a whole, whereby more emphasis was started to be given to the stakeholders rather than the shareholders alone. This is similar to the Gandhian vision of holistic development and respect for all forms of life, influenced by the Sanskrit phrase *"Vasudeva Kutumbakam"* meaning "The World is one family".

ECONOMIC INCLUSIVENESS

These developments have led to the concept of sustainable business. Sustainable business refers to the economic activity utilising the available resources in such a manner that the requirements of the future generations are not affected. This necessarily means that the finite natural resources are utilised by the enterprise in a judicious manner and conserved for the future necessities of the enterprise, society and environment. Sustainable business involves the pursuit of activities and initiative to ensure that their economic activities address the current environmental concerns apart from making profits. Corporate Sustainability is part of the overall sustainability infrastructure where the Corporates apart from profits focus on environment protection, preservation of natural resources, work towards social justice and equality. The Corporate plans and procedures have inbuilt optimum mechanisms to achieve the above factors so that the corporate moves towards attaining sustainability.

With the shift of the main focus of economic activity from profit-making for the shareholders to obligations towards the society and environment (stakeholders) also, business cannot survive ignoring the requirements for the stakeholders. So, the health of a Business is not necessarily measured by the bottom line of the financial statements of the enterprise but also the measurements of its efforts towards social ethical and environmental factors which allows the business of the enterprise to be sustainable. Hence, the overall fulfilment of the business obligations towards the stakeholders should be calculated and reported in the same sanctity as the financial statements of the business.

TRIPLE BOTTOM LINE (TBL) ACCOUNTING AND REPORTING

TBL is an accounting framework which includes Social and Environmental bottom lines in addition to the traditional financial bottom line. TBL consist of three "P"s. Profit, People and Planet. These 3 Ps are referred to as the three pillars of TBL

- **People:** This refers to the best practices adopted by the enterprise for the well-being of the Labour, community and the region in which the enterprise has its operations. This measure of social sustainability of the firm indicates how the enterprise is socially responsible.

- **Planet:** This component of the bottom line measures the sustainable practices adopted by the enterprise towards preservation of environment and indicates how much the enterprise is environmentally sustainable.

- **Profit:** The measure of the financial profit of the enterprise after deducting the cost of inputs and cost of capital involved. This depicts the Economic sustainability of the enterprise.

ESG CONCEPTS

ESG, which stands for Environment Social and Governance is a framework used by responsible investors in assessing an enterprise for making investments. In the process ESG factors are analysed in addition to the financial factors for assessing the risk associated with the Investee. It analyses how the company takes care of the environmental aspects of its business and how the policies and procedures are integrated with steps towards environmental protection. With respect to the social factor, it considers how it considers its employees and other stakeholders. In the Governance module the composition of Board, conduct of the Company leadership, Internal controls, shareholders rights, audit process etc. are considered.

The data generated may be utilised by the Company for its management decisions and by the investors to assess the investee company in addition to the usual financial parameters to arrive at the enterprise valuation.

The concepts of TBL, ESG and Sustainability have inherent overlaps. For a better understanding, the relationship between the three is presented in the form of a linear equation.

TBL = (Profits as per GAAP) + (Environmental & Social (E&S) benefits)

ESG = E & S + Governance (G)

Sustainability = TBL + ESG

Source: *Conceptualised by the authors*

It can be readily seen that the overemphasis on one of the aspects can lead to distorted outcomes which can have countervailing effect on sustainable progress and development. A balanced approach is required. Further, it may be noted that Sustainable business involves a cost to the entrepreneur when a share of his / her profit is being allocated to the environmental and social aspects of Sustainability. This cost is not expected to be exponentially high for an entrepreneur if the social and environmental aspects of Sustainability are duly factored and integrated into the strategic management process of business decision making. Here it is not suggested that Profits as well as additions to wealth should be disregarded, as no entrepreneur or investor will or is expected to work free or stay invested in the long run and therefore cannot be taken for granted from a sustainability point of view for long. However, it follows that unless all factors of production and services that are utilised at the macro-economic level are duly compensated, achieving Economic Inclusiveness coupled with Sustainability will remain as an utopian dream. The situation calls for integration of the three pillars of growth namely Strategy, Governance and Sustainability at enterprise level as also at the national level.

INTEGRATION OF STRATEGY, GOVERNANCE AND SUSTAINABILITY

For the management of Sustainability, an enterprise shall have a good governance structure which integrates the Strategies with focus on Sustainability. For this there need to be a strong and committed leadership, clear direction and a robust governance structure. The Company's goals and priorities determine the business model for sustainability and each enterprise will have to structure its own Sustainability management structure to integrate its strategy and governance towards an optimal sustainable business.

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As the sustainability reporting is comparatively new and not mandated for majority of business enterprises, its integration into the normal individual business process is not being done. The focus continues to be on the audited financial results and sustainability measurements are not part of the same. A strategic management process which integrates the sustainable parameters will address the sustainability concerns for the Business in the long run. ESG reporting framework bridges the gap and though significant progress has been made on this front, there is a great deal required to be done towards achieving convergence in reporting towards which the regulators are working very hard.

Globally, there are a number of ESG reporting frameworks, though the Integrated Reporting framework and the GRI (Global Reporting Initiative) framework is widely used. The Business Responsibility and Sustainability Reporting (BRSR) format prescribed by SEBI, which is mandatorily applicable to top 1000 listed entities by Market Capitalisation largely draws upon the GRI framework, though the framework of reporting in the BRSR is industry / sector agnostic which is not the case with GRI or Integrated Reporting frameworks.

BUSINESS RESPONSIBILITY AND SUSTAINABILITY REPORT (BRSR)

In India, the Ministry of Corporate Affairs (MCA) and Securities and Exchange Board of India (SEBI) had initiated steps towards sustainability reporting.

In July 2011, MCA came up with the National Voluntary Guidelines on Social, Environmental and Economic Responsibilities of Business, 2011.This was followed by SEBI in July 2012, introducing ESG reporting which was mandated for top 100 listed Companies which was later extended to top 500 listed entities in April 2016. The requirement was to file a Business Responsibility report (BRR) as part of the Annual Report of the said Companies.

SEBI further amended the SEBI (Listing obligations and Disclosure Requirements) regulations 2015 (SEBI LODR) on May 10, 2021 to introduce Business Responsibility and Sustainability Report (BRSR) replacing the BRR regime. BRSR requires the applicable listed entities to report their performance against the nine principles of the "National Guidelines on Responsible Business Conduct" (NGRBC).

BRSR mandates reporting under each principle which is divided into essential indicators and leadership indicators. The essential indicators are mandatory whereas the leadership indicators are voluntary in nature. This framework lays emphasis on sustainability reporting by the applicable listed entities and the objective of the BRSR framework is to function as a single comprehensive source of sustainability information focusing largely on non-financial data. It is estimated that the BRSR contains more than 100 data points on which the listed entities have to report. The BRSR is made applicable at present to top 1000 listed companies by market capitalization and going forward the net for reporting is expected to be widened. Thus, India is moving towards introducing and establishing a comprehensive framework for Sustainability Reporting in its pursuit towards fulfilling its commitment on UN mandated SDGs adopting the route of sensitized ESG compliance and reporting.

G20 PRESIDENTSHIP - A BUS WHICH INDIA CANNOT AFFORD TO MISS!

India assumed the G20 presidency on December 01, 2022, and is poised to play a vital role in global matters. With our concept of *"Vasudeva Kudumbakam"* or One Earth, One Family, One future, as the theme of its Presidency, it affirms the value of all living beings and environment. The theme also focuses on LiFE (Lifestyle for Environment) which portrays a cleaner greener and bluer future. This will also be a great opportunity for India to sow the seeds of long-term impact.

EPILOGUE

All the Indian regulators such as MCA, SEBI, RBI and other sectoral regulators have got a wonderful opportunity to scale up to become the Vishwaguru to show the path and the way forward with respect to the direction required to be taken up by India as well as what the other countries of the world may follow when it comes to sustainability through ESG. Here it is hoped that our regulators would adopt a more flexible approach in their endeavour with respect to ESG and Sustainability, keeping in mind the implications that it has over a much larger world as compared merely to their current areas of regulation such as corporate world, financial sector, banking system etc. The Indian regulators generally have hitherto resorted to a rule-based approach to regulate the various sectors, but possibly the demands of the situation now will call for a calibrated approach so that economic inclusiveness can be achieved in a holistic manner in sum and substance.

"Arise, awake and stop not till the goal is reached"

– Swami Vivekananda

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