NEWSLETTER

GROWTH OF ESG INVESTMENT IN INDIA

"SUSTAINABLE INVESTING IN THE INDIAN MARKET & FUTURE PROSPECTS AND CHALLENGES"

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Environmental, Social and Governance (ESG) investing, also known as sustainable investing, represents an investment approach where funds are allocated to companies that comply with ethical practices alongside profitability.

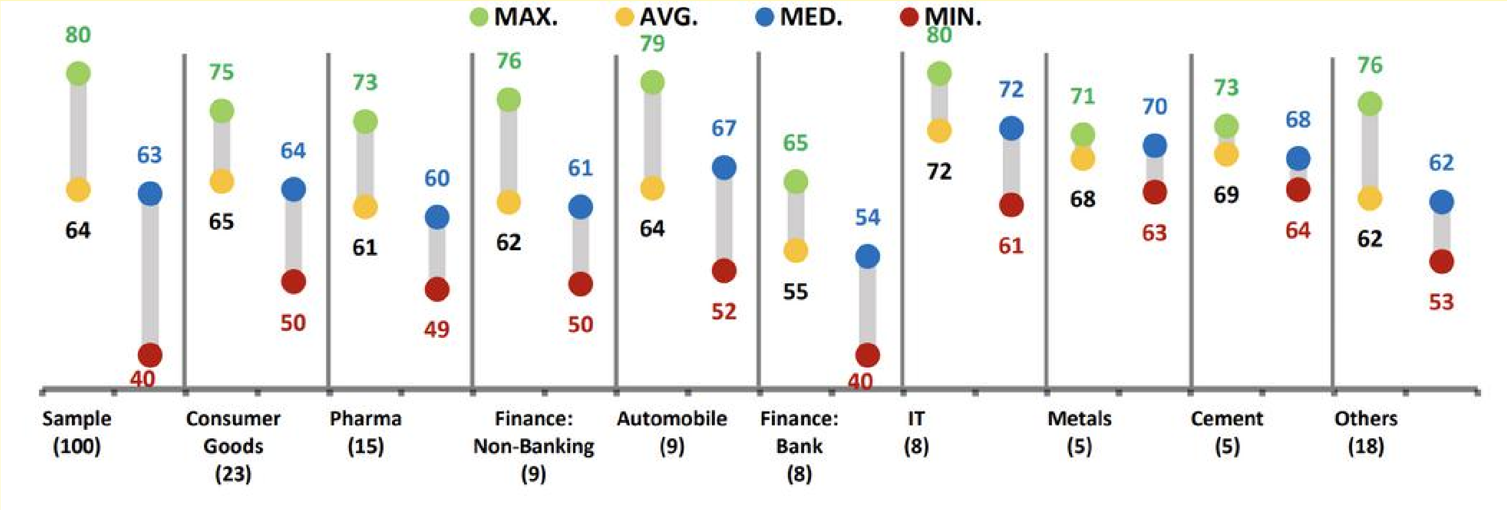
The ESG criteria evaluates how public companies uphold environmental responsibility, contribute positively to their communities, and maintain high standards of management and corporate governance.

Investors focusing on ESG criteria exclude stocks of companies that fail to meet specific environmental, social or governance standards. Examples include chemical companies responsible for significant pollution or firms with poor labour practices.

WHAT IS AN ESG SCORE AND HOW IS IT CALCULATED?

A company's adherence to ESG standards can be assessed through an ESG score provided by research entities such as MSCI, Sustainalytics and Morningstar. These scores, reflect a company's compliance with ESG criteria and are subject to changes in regulation and compliance and to changes in a company's ESG efforts. While not obligatory, having an ESG score serves as a beneficial metric for organizations. Research organizations employ their unique evaluation frameworks to assign scores to companies and mutual funds. The MSCI ESG score assesses how effectively a company manages its ESG risks compared with others in the industry. Companies attaining AA or AAA ratings are recognized as ESG risk management leaders. Morningstar's ESG score quantifies the ESG risks associated with a specific company or mutual fund on a scale from 1 to 50, where 1 represents the lowest risk while 50 is the highest. Additionally, Morningstar provides detailed scores for ESG factors.

ESG SCORING PATTERN ACROSS DIFFERENT INDUSTRIES



• On average basis, IT industry tops the list of being the highest scoring industry with an average of 72, followed by Cement (69) and Metals (68).

• Least divergence was observed in Metals (8) and Cement (9) Industry, clearly reflecting impact of regulatory push as not following has negative impact.

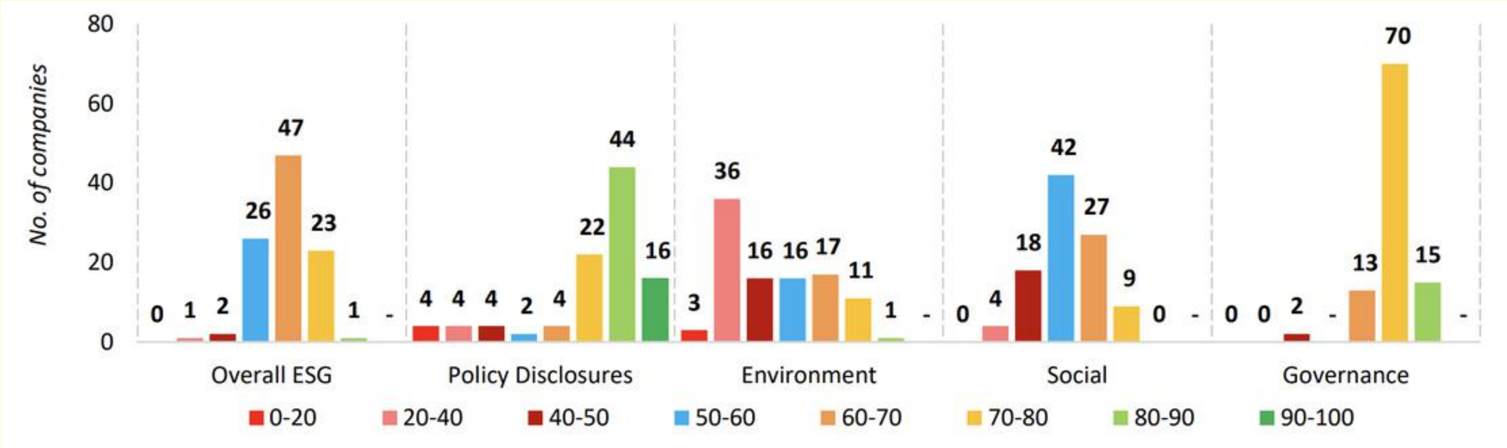
• The top 3 industries have better disclosures on E & S, compared to other industries in the sample.

• Lowest average score was observed in Banks and non-banking finance companies, reflecting very limited disclosures on E factor.

• Evaluation model for banks was modified to include indirect environmental impact such as sustainable financing, responsible lending, economic risk parameters etc, considering the role Banks play in the corporate world, in addition to scoring on direct environmental parameters such as emissions, water consumption and effluents.

Grade	Rank	Company Name	Industry
A	1	Infosys Ltd.	IT
B+	2	Mahindra & Mahindra	Automobile
B+	3	Tech Mahindra Ltd.	IT
B+	4	Housing Development Finance Corporation	Finance: Non-Banking
B+	5	Adani Ports and Special Economic Zone Ltd.	Services

SCORE DISTRIBUTION-FACTOR WISE



On policy disclosures 60 companies scored 80+, whereas on governance factor 15 companies scored 80+, with only 1 company having overall ESG score at 80+. Similarly, 64 companies have scored less than 60 on Social factor, compared to 71 companies scoring less than 60 on Environment factor.

Majority of the companies have scored 70+ in governance. This is on expected lines; higher governance score is result of almost two decades of regulatory efforts, whereas, E&S are voluntary and missing the mandatory push. Apart from lack of regulatory push, proper appreciation of E & S factor is not yet become DNA of corporates, as much as one would like it to be.

IMPORTANCE OF ESG IMPLEMENTATION

- Global Regulatory Landscape: The establishment of ESG-focused policies post-2008, including commitments to the United Nations' Sustainable Development Goals and rules adopted by the European Commission, reflects a global shift towards sustainable practices.

- Integrated Reporting and Accountability: The International Integrated Reporting Council (IIRC) standardization framework, introduced in 2013, underlines the increasing importance of accounting for broader impacts beyond financial metrics.

- <u>Growing Significance of ESG</u>: ESG as a concept has gained prominence since the turn of the century, and its growth, particularly after the 2008 financial crisis, is indicative of a global trend toward recognizing the interconnectedness of corporate actions and sustainable performance.

- <u>CSR and ESG Nexus</u>: The synchronicity between the growth of Corporate Social Responsibility (CSR) activities and the significance of ESG performance emphasizes the link between firm actions and the measurement of performance concerning environmental, social, and governance issues.

- <u>EU Leadership and Rapid ESG Investment Growth</u>: The European Union's firm stance on regulating and promoting ESG concerns has led to rapid growth in ESG investments within the EU, showcasing the impact of regulatory support on industry practices.

CHALLENGES FACED BY INDIAN INDUSTRIES IN ESG ADOPTION

- Limited awareness and understanding of ESG principles
- Dynamic and evolving ESG regulations
- Difficulty in collecting and verifying reliable ESG data
- Balancing financial objectives with sustainability goals
- Meeting varied investor expectations
- Risk of greenwashing
- Perceiving initial ESG implementation costs as barriers to long-term gains

FUTURE OF ESG INVESTING IN INDIA

The push behind ESG investing in India is being driven by three main factors:

India's commitment to achieving its 2070 Net Zero target, which is projected to necessitate US$ 8-10 trillion in capital expenditure over the next five decades; SEBI's introduction of BRSR mandates, providing a regulatory framework for listed companies to prioritize sustainability; and the United Nations' Sustainable Development Goals (SDGs) that is serving as a benchmark for measuring a company's attractiveness and capital-raising capacity.

Analysis reveals a negative correlation between the corporate governance score of S&P BSE-listed companies and stock beta, suggesting that companies with higher governance scores tend to experience lower stock price volatility.

CONCLUSION

The expanding ESG model in India reflects a strong path driven by regulatory, corporate governance scrutiny and strategic alignment with global sustainability goals.

The ongoing trend, supported by strategic sectors and regulatory frameworks, positions ESG investments as a strong force in molding India's financial ecosystem, contributing to a more sustainable and resilient economy for the years ahead.

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