

Focus on ESG – Business opportunity or cost?

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Environmental, social and governance (ESG)

1. As we eagerly anticipate the exit of the Coronavirus pandemic, there is recognition and acceptance that there is a strong link between sustainable business practices and strong financial performance by businesses. As a result, we are seeing increased focus and attention by businesses on environmental, social and governance (ESG) issues bolstered by prospects of long-term sustainable business performance.

This move is evidenced by the significant rise in ESG driven investments and ESG activism by various stakeholders. Reports indicate that ESG investments in 2018 were estimated to be +-\$30-trillion and this is anticipated to reach \$50-trillion by 2040. The point is, investors, now more than ever, believe that businesses that pay attention and invest in ESG will build and achieve greater resilience and competitiveness and enjoy sustainable performance in the long term.

The rise of environmental, social and governance

2. With the rise of ESG, investors, funders and other business stakeholders are applying various measures to mount pressure on businesses to change behaviour, embrace and integrate ESG oriented policies into their business strategy as a matter of priority. These measures include, *inter alia*:

1. financiers globally including South Africa announcing the intention to stop funding coal projects in order to drive carbon emission reduction goals and promote the implementation of climate change policies;
2. lenders incorporating ESG related contractual obligations in funding contracts. Businesses who are unable to give these contractual undertakings may pay more for funding;
3. corporate customers are putting sustainability obligations in contracts requiring suppliers to commit to certain ESG goals/commitments, failing which they face the prospect of losing customers;
4. consumers are demanding businesses to adopt ESG friendly policies and punishing companies with dodgy practices through boycotts;
5. employees preferring purpose driven, employee friendly employers that resonate with their values. Laggard companies in this regard may lose out in the battle to attract and retain talent.

Investing in ESG

3. The above clearly demonstrates that businesses that are investing in ESG have a competitive advantage. However, the fact that the elements and themes covered by ESG are too broad and numerous poses a big challenge to business. These themes range from anything from closing pay gaps, executive remuneration, climate change, diversity and inclusion, sustainable sourcing, etc. Whilst it is abundantly clear that all businesses face ESG risks however the type of risks associated with ESG differ from business to business.

Given the multitude of ESG themes/issues, some businesses are lost and overwhelmed as to where to start addressing the ESG challenges facing them. This need not be the case. We set out hereunder some practical steps (which are by no means exhaustive), that can be applied by business to address this challenge and improve their performance on ESG:

1. boards of companies should establish a specific committee to drive and oversee ESG issues as a matter of priority;
2. such committee should –
 1. identify and focus on two or three key ESG issues that are critical to the business and which, if addressed, will have a positive impact on that business and its key stakeholders;
 2. after consultation with the key stakeholders and advisors, develop an ESG action plan/strategy with measurable and realistic targets and timelines to address those key issues;
 3. disclose the ESG plan to stakeholders and report on progress on implementation of same in order to manage stakeholders' expectations;
3. the ESG plan must be a live document that is constantly reviewed and updated.
4. Although environmental considerations are currently at the forefront of business planning in the context of ESG, social and governance issues should not be relegated to the back burner if we are to build socially inclusive and stable businesses and economies going forward.

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