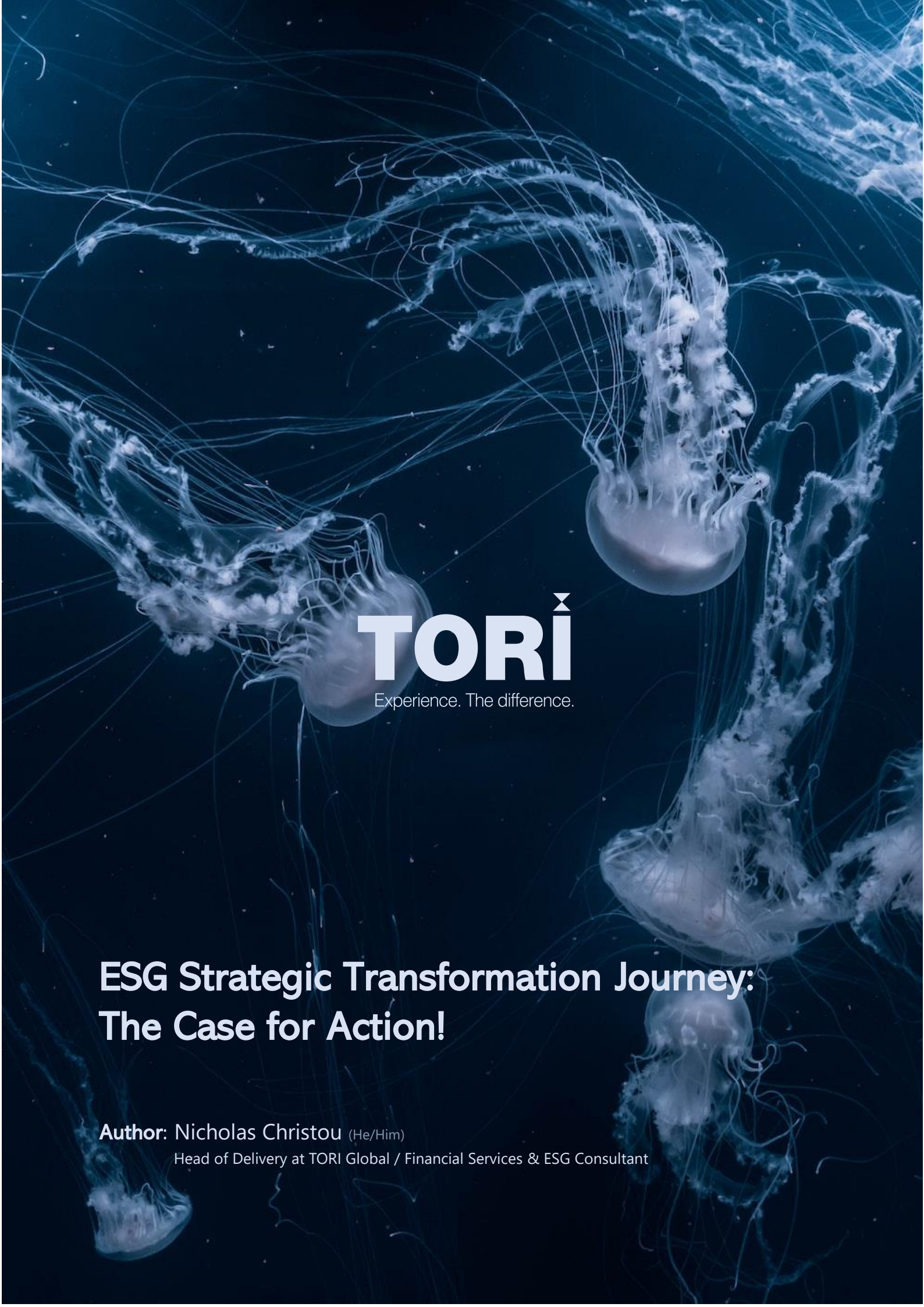


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ESG Strategic Transformation Journey: The Case for Action!

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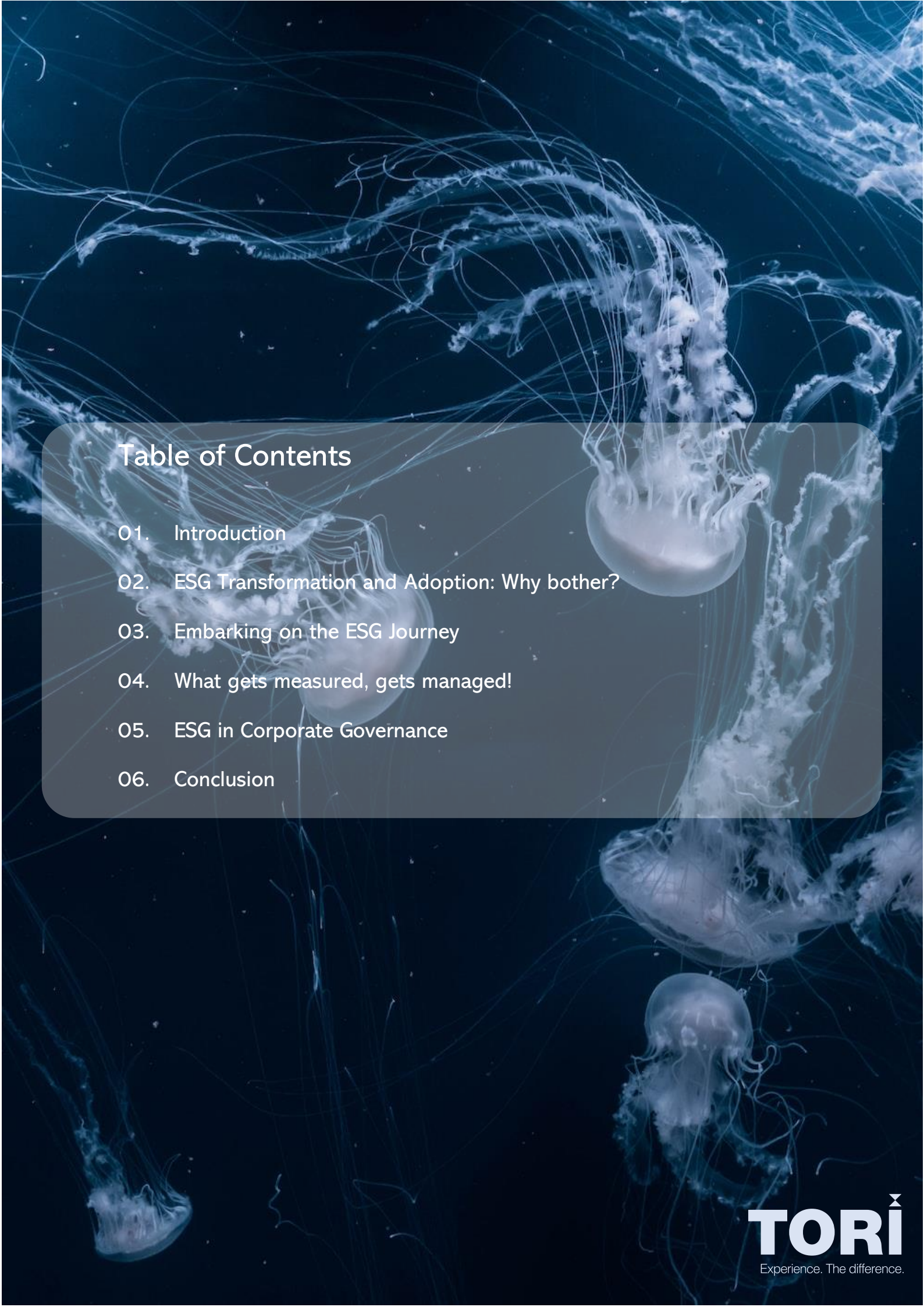


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01. Introduction

In today's world, the urgent need to address pressing global challenges, such as climate change, resource depletion, and social inequities, cannot be ignored.

The contemporary business and socioeconomic landscapes are changing. It is perhaps truer than ever before that economic players across the globe are becoming increasingly aware and conscious of issues like environmental degradation, social inequalities, and ethical corporate governance (or lack thereof).

As recently as the first half of 2023, we have witnessed the following:

- ⇒ **Environmental**: Extreme climate phenomena e.g., all-time high temperatures recorded across the UK and continental Europe, deadly blazing wildfires in Greece, devastating floodings in Slovenia, record-breaking drought in Spain etc.
- ⇒ **Social**: Unrest and protests e.g., strikes in France, USA, UK, amongst others
- ⇒ **Governance**: Fears for another potential financial crisis triggered by bank runs in the USA (e.g., Silicon Valley Bank) and a series of scandals that led to the failure of Credit Suisse in Switzerland

It is, therefore, not surprising that businesses and organisations are being called upon to embrace a profound transformation. **The Environmental, Social, and Governance (ESG) framework offers a comprehensive approach that integrates sustainability, responsibility, and accountability into business practices.**

ESG transformation emerges as a compelling solution which transcends conventional business operating practices and conformist motives and incentives. Organisations opting into this transformative direction position themselves as pioneers and agents of change, showcasing corporate good-will and contributing towards the betterment of their ecosystem (i.e., the environment and societies within which they operate).

Moreover, **embedding and integrating ESG principles into an organisation's operating model is not only a moral imperative, but also a compelling business case for growth.** The ESG framework places particular importance to enhancing and ring-fencing a company's operational resilience, improving employee morale and hence, productivity. It also ensures that the overarching governance principles of the organisation are holistic and take into account "non-traditional" business influences.

Having said that, it is vital to bear in mind that the ESG journey is an iterative process that requires a consolidated approach across the organisation. Nevertheless, and despite the hurdles that one may face during the journey of embedding an ESG mindset within an organisation, it has been proven that this process can act as a catalyst for initiating transformational shifts, which in turn lead to operational and strategic change.

By shedding light on the transformative power of ESG adoption, this paper aims to inspire and equip businesses with the necessary knowledge to navigate their journey towards sustainable, responsible, and ethical practices. Ultimately, it is hoped that organisations are encouraged to seize the opportunity to promote a more harmonious relationship between business, society, and the environment. Through collective efforts, the ESG transformation has the potential to create a world where economic prosperity, social progress, and environmental stewardship coexist synergistically, shaping a brighter and more sustainable future for business and the generations to come.

02. ESG Transformation Journey and Adoption: Why bother?

By harnessing the power of ESG, organisations can accelerate the institutionalisation of a sustainable future for business and construct solid foundations to navigate prevailing business challenges.

There are multidisciplinary reasons why one should be looking to integrate ESG into their operating model. ESG integration and compliance can assist, inter alia, in areas like risk management, business operations, organisational efficiency, talent retention, and brand value. As a quick overview, these are some of the key areas for which ESG adoption and implementation can foster positive business outcomes:

Adhering to Regulatory Standards	Regulatory bodies are now commonly demanding transparency from financial services companies pertaining to their ESG agenda. Most of the regulatory standards currently in place are not mandatory, however, by becoming ESG aware and compliant, companies can get a head-start in comprehending the overarching regulatory ESG framework, avoiding potential legal and reputational risks in the future.
Attracting Customers & Investors	There is an observed market trend whereby clients, including institutional investors, are increasingly keen for their spending decisions and/or investments to be directed towards ESG-compliant companies. Therefore, a companywide ESG transformation programme can help attract and retain clients for whom responsible investment practices are central in how they engage with the market. It is also true that companies that are ESG compliant are more likely to receive investment from ESG-focused funds or investors.
Strengthening Risk Control & Mitigation	A mixture of ESG metrics, KPIs, MI, and other financial information portray a company's long-term financial performance and risk profile. In order to better identify, track, and manage risks, companies need to incorporate ESG considerations into their investment and risk management processes.
Enhancing Reputation & Brand Value	By implementing ESG best practices, financial services companies can boost their credibility and establish trust with stakeholders, potentially resulting in greater brand awareness and improved customer loyalty in the long run.
Attracting & Retaining Talent	Studies have shown that employees place particular focus on companies which are ESG compliant and/or exemplify and prioritise the ESG values. As younger employees often bring valuable technological skills to the workplace, ESG compliance can attract and retain top talent, ultimately leading to improved business performance.

03. Embarking on the ESG Journey

"ESG isn't about corporate social responsibility anymore; it's about survival and growth."

If you are in the process of conceptualising your organisation's ESG strategy, then rest assured you are not alone! This relatively novel concept has shot up the contemporary corporate agenda over the last decade, and many businesses are currently trying to comprehend and adapt to what is expected of them under the ESG framework.

This process is driven by the desire to avoid any negative impacts to an organisation's brand value, reputation, and competitive edge, but also by the numerous benefits that such a transformational initiative can have on risk controls, talent acquisition, the customer-base etc. (See **Section 02** for more details).

The ESG journey is not a "clear-cut" path towards an end-target. To the contrary, for an ESG programme to succeed, senior leadership teams need to first and foremost understand how best practices within this domain can be applied to their individual organisations, given their intrinsic characteristics including process maturity, data maturity, culture, ways of working etc.

The diagram below depicts an end-to-end ESG transformation journey, commencing from the business impact assessment and spanning all the way to reporting on outcomes and progress.

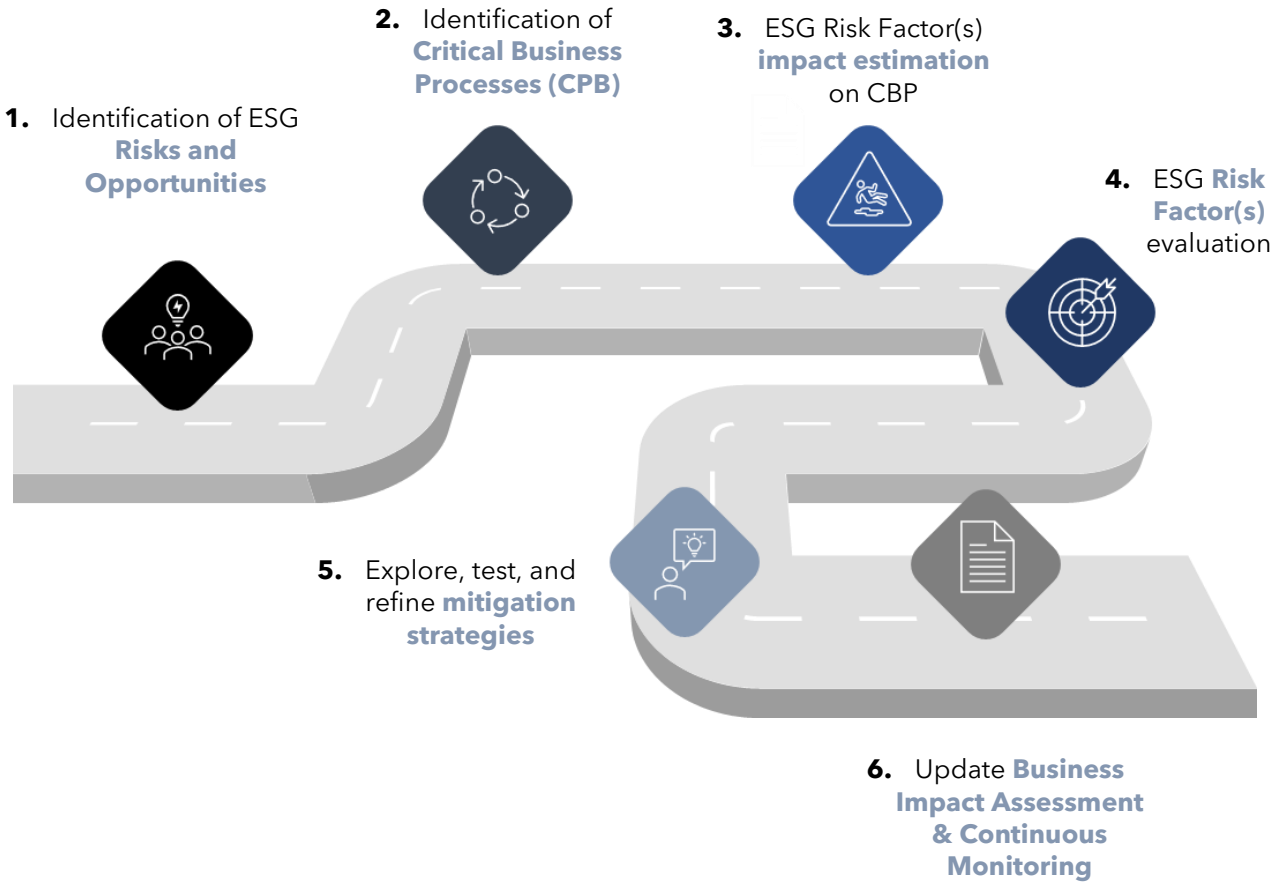


The table below specifies key details per step (01-07) along the journey:

01	**Business Impact Assessment**	Business Impact Assessments analyse and evaluate the impact of unforeseeable events such as natural disasters or accidents on core business operations. The assessments determine the criticality of these operations and the resource requirements that would ensure operational resilience.
02	**ESG Materiality Assessment**	ESG Materiality Assessment refers to the identification of the most significant and pertinent ESG parameters for the business and its stakeholders.
03	**ESG Maturity Assessment**	The ESG Maturity Assessment entails effective information gathering on the business' current ESG reality, creating a benchmark for comparison such that newly introduced ESG initiatives can be analysed for their effectiveness. "What gets measured, gets managed!".
04	**ESG Vision and Goals**	ESG goals articulate the organisation's vision and commitment to the three ESG pillars; environment, social, and governance – and ensure the organisation is held accountable for upholding and encouraging said vision and goals.
05	**ESG Strategic and Gap Analysis**	The ESG Strategic Roadmap is a framework articulating a clear and actionable path toward the organisation's ESG vision, goals, and future purpose. Developing an ESG roadmap is an iterative process that evolves as the organisation progresses and new priorities unfold. The development of the roadmap is dependent upon a detailed gap analysis, encapsulating the variance between the current "As-Is" ESG state and the desired "To-Be" state.
06	**Implementation**	Effective implementation is contingent on ESG initiatives being integrated into business processes - with oversight at the corporate level.
07	**Reporting**	Reporting on ESG initiatives and the progress made against the goals and milestones stipulated within the ESG Strategic Roadmap.

The sum of these steps can be seen as a **holistic ESG transformation journey**, but concurrently, each step on its own can be a **standalone initiative** that an organisation may wish to pursue, depending on which focal area(s) they are lacking at and/or which focal area(s) are more relevant to their modus operandi.

Each of the steps along the ESG journey constitute smaller journeys. For example, in order to conduct an ESG Business Impact Assessment (Step 01), then the following sub-steps should be considered:



As it may have become evident by now, developing an ESG strategy is not straightforward. This is particularly true for organisations that do not have the necessary inhouse skills and expertise to conceptualise, develop, implement, and track the ESG transformation programme. For these organisations, **augmenting skills and capabilities through engaging external advisors, who can work independently or collaborate with existing teams on the ground, may be the most efficient and cost-effective route to follow.**

Moreover, setting up an ESG strategy does not require "reinventing the wheel". With the appropriate guidance, organisations can draw upon a plethora of already existing frameworks and resources and adapt to what best suits them. Examples of such frameworks include:

- ⇒ United Nations' Sustainable Development Goals (UNSDG)
- ⇒ United Nations' Global Compact (UNGC)
- ⇒ Global Reporting Initiative (GRI)
- ⇒ Sustainability Accounting Standards Board (SASB)
- ⇒ Task Force on Climate-related Financial Disclosures (TCFD)

A pivotal point in drafting an ESG strategy relates to **risk identification, quantification, and mitigation.** This is a separate and parallel journey, the outcomes of which should be used to inform decision-making on the overall ESG journey going forward:

1. Identification of ESG Risks

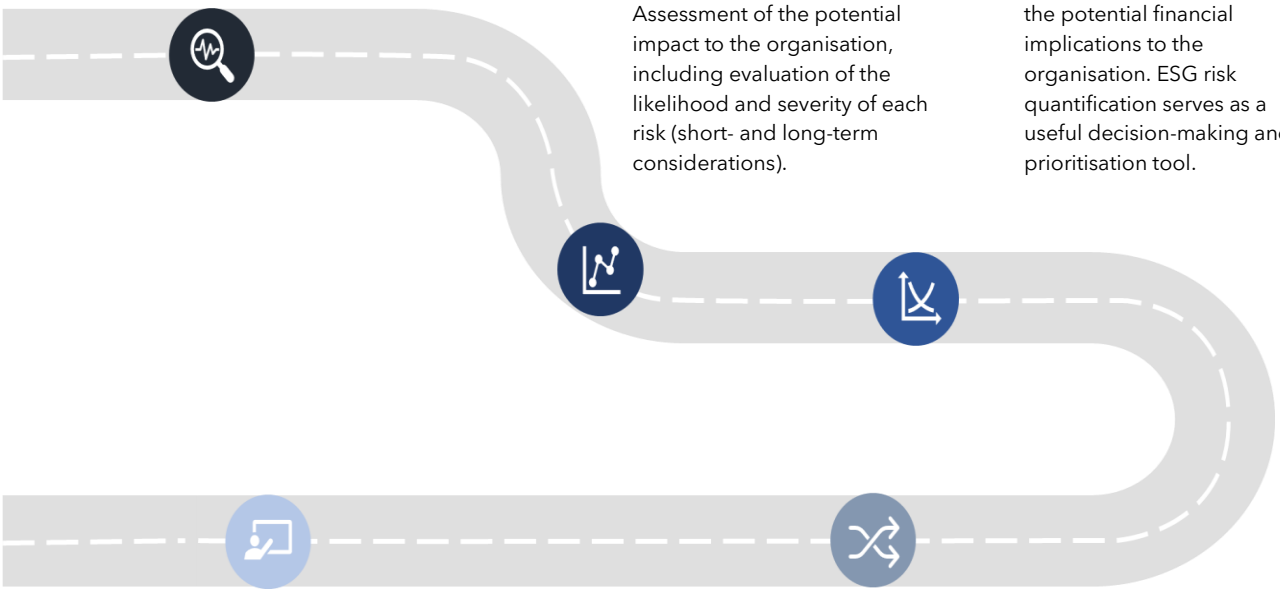
Identification of the ESG risks pertinent to the organisation, its operations, and wider network/ecosystem (industry, supply chain / third-parties, stakeholders). E.g., climate change, labour practices, data security, regulatory compliance etc.

2. ESG Risk Assessment

Assessment of the potential impact to the organisation, including evaluation of the likelihood and severity of each risk (short- and long-term considerations).

3. ESG Risk Quantification

Quantitative assessment of ESG risks including assigning metrics/values to measure the potential financial implications to the organisation. ESG risk quantification serves as a useful decision-making and prioritisation tool.



4. Integration into Enterprise Risk Management (ERM)

Integration of ESG risks into the Enterprise Risk Management programme, including updating risk registers, risk mitigation strategies, internal controls etc.

5. ESG Reporting and Disclosure

Transparently communicating the identified ESG risks, their quantification, and risk mitigation strategies to key stakeholders (including investors, regulators etc.,). Organisations may align themselves with global frameworks to guide their reporting e.g., SASB.

Similar to the overarching ESG programme journey, each of the steps along the ESG Risk journey contains important sub-components that need to be considered. For example, ESG Risk Quantification (Step 3), entails:

01	**Scenario Analysis**	Scenario analysis requires constructing hypothetical scenarios to ascertain how certain ESG risks could impact the organisation's financial performance. By conducting scenario analyses, organisations can estimate the extend of the ESG risk impact, assign probabilities to each possible scenario based on market trends, data challenges, and level of required SME advice.

02	**Financial Models**	Developing financial models that incorporate ESG factors could assist organisations in assessing the potential impact on revenue, cost, and overall financial performance e.g., a financial model could project the impact of reputational damage on the organisation's bottom-line.
03	**Management Information & Key Performance Indicators**	Developing ESG-pertinent KPIs and leveraging a standardised framework for measuring and comparing ESG performance will enable organisations to quantify and monitor risks across time. E.g., percentage of independent board directors, number of employee accidents etc.
04	**Benchmarking**	Leveraging benchmarking data, industry-specific data, and research reports to provide insight into the financial implications of ESG risks will enable organisations to validate their estimates and magnitude of risks.
05	**SME Input**	Where ESG data is limited and/or complex, SME judgement / knowledge is key to providing insights and estimates of ESG risks based on expertise and experience. SMEs can be leveraged to validate financial models, enhance risk quantification frameworks, address gaps etc.

ESG Risk Management Maturity Curve



Fundamental

- Adoption of a holistic approach to identify and review ESG risks across all dimensions of the organisation.
- Risk Appetite with reference to ESG targets, goals, and commitments, and the Risk Agenda have been clearly articulated by the Board.

Operational

- ESG Risk Management Baseline Assessment and identification of gaps that need to be addressed to achieve ESG objectives.
- Shared Risk language across the organisation.
- Management Information and Key Metrics produced, with reporting to CRO, Senior Management, etc.

Leading

- Data collection and ESG Management is centralised across all dimensions of the organisation, with Risk Executives driving the agenda and disseminating information concerning ESG strategic decisions.
- Strengthened and sustainable Risk Management Capability.

04. What gets measured, gets managed!

In a white paper published by the TORI ESG team in February 2023 titled "**ESG Data Production**", we explored how a structured approach for data production can be utilised to generate high-quality ESG data (and subsequently Management Information (MI) and Key Performance Indicators (KPIs)).

To sum up the findings of the ESG Data Production white paper –

a. *Similar to every other area of business, data plays a crucial and vital role in the success of your ESG journey. It helps to provide a snapshot of the 'As-Is' state of your organisation, while at the same time enhancing, enriching, and informing the decision-making process in order to achieve the desired 'To-Be' state.*

b. *However, the maturity of the processes underpinning ESG data collection, production, reporting, and communication are significantly less matured when compared to those for financial data.*

c. *Data collection, production, and communication is not a simple process. It requires clear allocation of roles and responsibilities, continuous measurement, reporting, and communication, and quality assurance to guarantee a truthful representation of the 'on-the-ground' reality.*

d. *ESG raw data can subsequently be formulated into a set of KPIs to track progress over time. Companies should choose from a wide range of KPIs across all three elements constituting ESG depending on, inter alia, their –*
    i. *Intrinsic business characteristics;*
    ii. *Operating models;*
    iii. *Industry standards; and*
    iv. *Corporate values.*

e. *All in all, the use of ESG data is still an evolving practice, however, most companies expect that their usage will increase in both volume and frequency over the next few years. To that end, it is important for businesses to consider instituting training to enhance the understanding of why ESG is needed, and explore potential investment in tools required to incorporate said data in order to enhance the overall decision-making capabilities.*

When drafting your overarching ESG strategy, **it is of the utmost importance that data plays a crucial role as an informative, instructive, and decision-making tool.** In order to ensure that organisational data (either collected and analysed internally or provided by third parties) delivers the required value-add to your strategy development process, you need to ensure that the following best practices are in place:

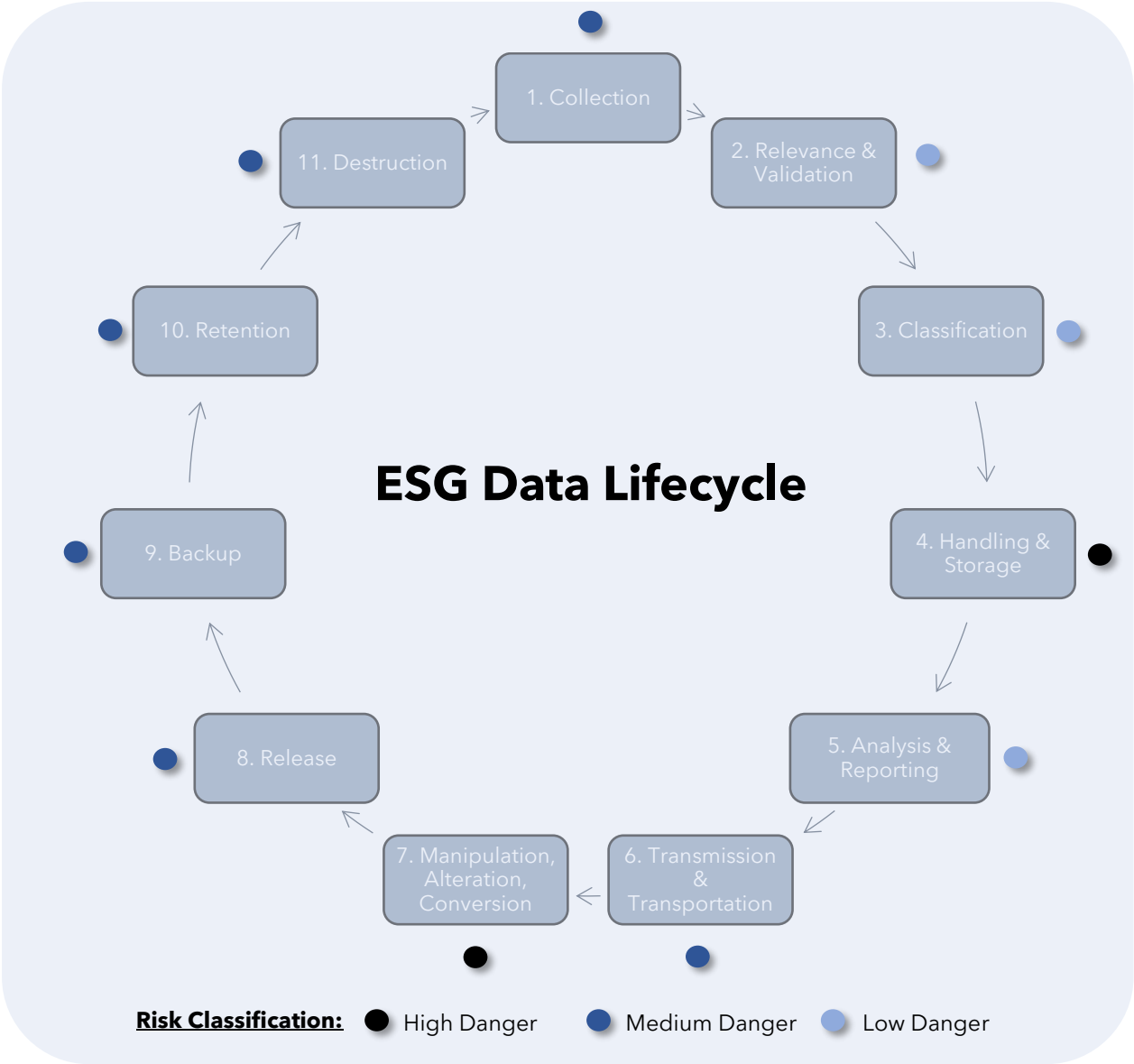
⇒ ESG data must be valued as a strategic enterprise asset, handled with integrity, transparency, and auditability.

⇒ ESG data quality is everybody's responsibility across the data lifecycle; from collection to classification, handing, and retention.

⇒ ESG data must be managed to follow internal and external standards and regulations, safeguarding sensitive and personally identifiable information.

⇒ ESG data is a shared asset and must be protected and managed consistently based on clearly defined accountability.

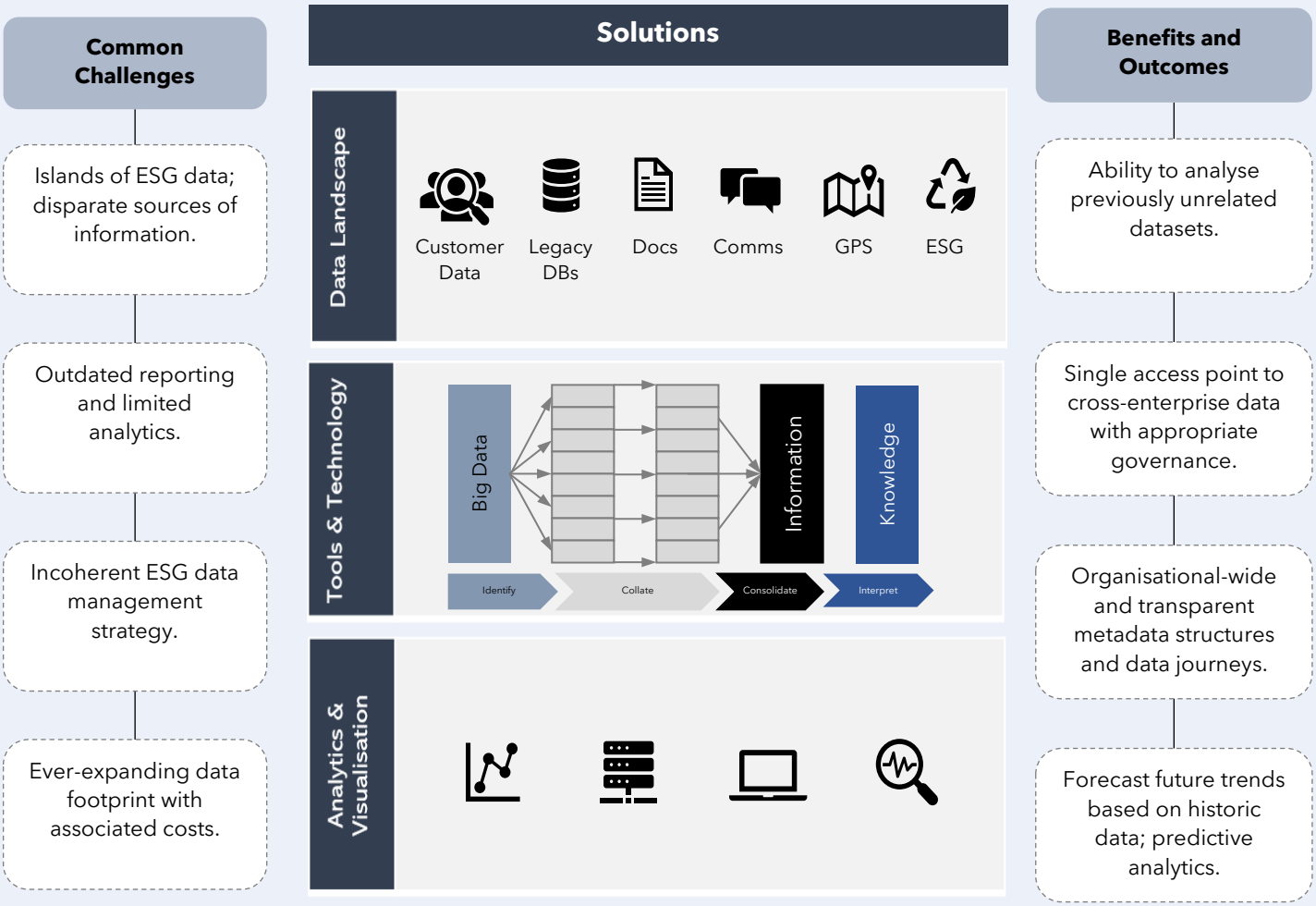
You will also need to consider the **end-to-end data lifecycle** to ensure that your organisation remains compliant with any data retention policies and/or regulation, and to assure that your analysis portrays an actual representation of your current state:



Additional key components that should be considered in data architecture include, but are not limited to:

- ⇒ Data strategy
- ⇒ Data governance
- ⇒ Data collection methodology
- ⇒ Data analysis (including statistical tools and/or models required)
- ⇒ Data storage
- ⇒ Data reporting practices (which should be consistent across time to enable meaningful time-series comparisons)

REMINDER! Unprocessed data remains just that – data.



05. ESG in Corporate Governance

Good governance is rooted in well-organised Boards consisting of the right balance and diversity in skills, expertise, and experience.

The Board has an integral role to play in ensuring the organisation's ESG strategy aligns with its overarching business plan, taking into account material sustainability risks and opportunities. While individual business areas are responsible for implementing ESG initiatives and practices, the Board's leadership remains central to creating the environment necessary for long-term value creation. Henceforth, their buy-in and endorsement is critical to the success of ESG initiatives.

Corporate Governance within this context pertains to how an organisation is managed and governed regarding Environmental, Social, and Governance considerations. It establishes the groundwork for achieving both the "E" and "S" goals, as poor corporate governance can lead to noncompliance with the organisation's social and environmental pledges. Robust governance is, therefore, critical for ensuring effective management of ESG issues and serves as the cornerstone for which sustainability initiatives can be developed, assessed, and measured.

The World Economic Forum Global Future Council on Transparency and Anti-Corruption have developed a list of considerations pertinent to corporate governance. This list includes, inter alia:

- ⇒ Business Ethics
- ⇒ Board Composition
- ⇒ Incentive Structures
- ⇒ Value Chain Management
- ⇒ Stakeholder Engagement etc.

The Board can be the change enabler within any organisation. To that end, the Board's involvement and commitment to ESG practices are essential for several reasons, including:

01 ESG Strategy

The Board is responsible for defining the company's long-term strategy; incorporating ESG considerations into this strategy is essential for sustainable growth. By incorporating ESG factors into decision-making, the Board can create value for all stakeholders, including shareholders, employees, customers, and communities.

02 Accountability & Transparency

The Board ensures that the company is accountable for its ESG performance. Transparent reporting on ESG metrics is becoming increasingly important to investors, customers, and regulators. The Board plays a pivotal role in ensuring accurate and comprehensive ESG disclosures.

03

Resilience & Adaptability

Companies that incorporate ESG practices are better positioned to adapt to changing market dynamics and societal expectations. The Board's focus on ESG helps the company stay ahead of evolving trends and remain resilient in a rapidly changing business landscape.

04

Stakeholder Engagement

ESG issues often affect a wide range of stakeholders, including employees, customers, suppliers, communities, and investors. The Board's engagement with these stakeholders ensures that their perspectives and concerns are considered, leading to more holistic and responsible decision-making.

For a Board to be effective, certain **governance, controls and communication principles** need to be in place. These can be as simple as receiving high-quality information decks in advance of meetings with well-planned and clearly articulated agendas, or more nuanced like the composition of the Board in terms of experience and expertise, clearly defined roles and responsibilities, communication plan for when a decision is made etc. Furthermore, to ensure that the Board functions effectively, structured Board reviews should take place periodically to stipulate the opportunity to the members of the Board to provide transparent and constructive critiques on how the functioning of the Board can be improved going forward.

A well-organised, well-functioning, and communicative Board can: -

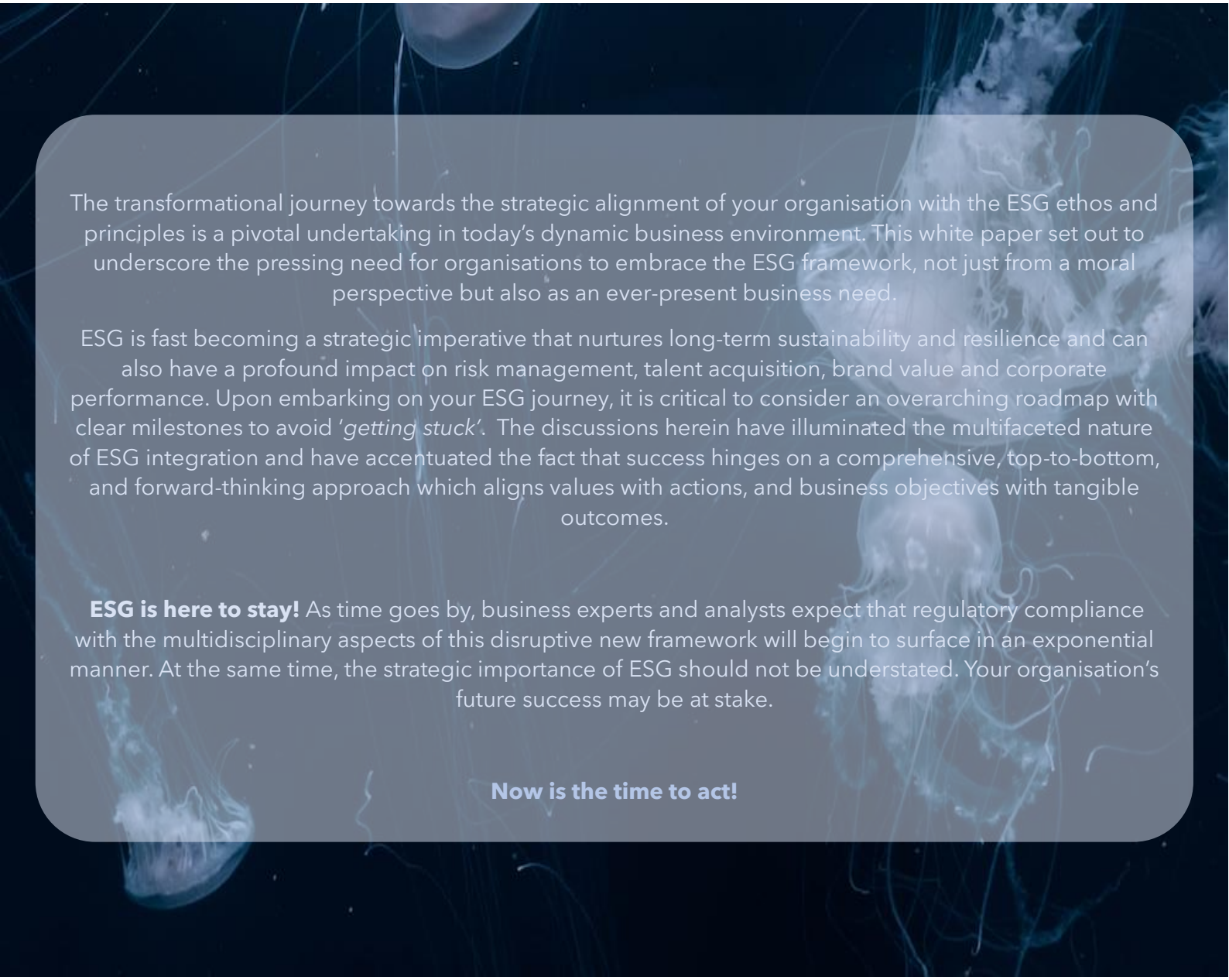
Improve Risk Management – more effective evaluation and assessment of ESG risks as they relate to your organisation, suppliers, and competitors.

Increase Investor Confidence by Better Capital Allocation – better informed decision-making on where and when to allocate capital while enabling greater access to capital i.e., greater transparency attracts investors that prioritise socially and environmentally responsible business practices.

Enhance Strategic Planning – more effective evaluation of risks and opportunities over the short, medium, and long-term.

Enhance Reputation and Stakeholder Engagement – demonstrating commitment to responsible business practices enables organisations to build stronger relationships with customers, employees, and other key stakeholders.

06. Conclusion



The transformational journey towards the strategic alignment of your organisation with the ESG ethos and principles is a pivotal undertaking in today's dynamic business environment. This white paper set out to underscore the pressing need for organisations to embrace the ESG framework, not just from a moral perspective but also as an ever-present business need.

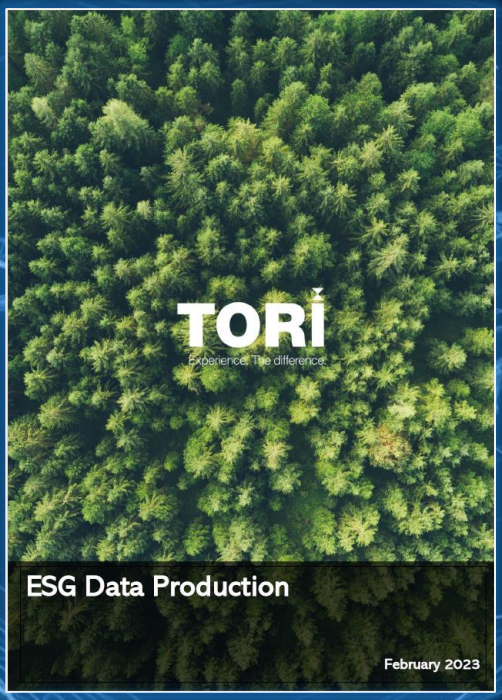
ESG is fast becoming a strategic imperative that nurtures long-term sustainability and resilience and can also have a profound impact on risk management, talent acquisition, brand value and corporate performance. Upon embarking on your ESG journey, it is critical to consider an overarching roadmap with clear milestones to avoid '*getting stuck*'. The discussions herein have illuminated the multifaceted nature of ESG integration and have accentuated the fact that success hinges on a comprehensive, top-to-bottom, and forward-thinking approach which aligns values with actions, and business objectives with tangible outcomes.

ESG is here to stay! As time goes by, business experts and analysts expect that regulatory compliance with the multidisciplinary aspects of this disruptive new framework will begin to surface in an exponential manner. At the same time, the strategic importance of ESG should not be understated. Your organisation's future success may be at stake.

Now is the time to act!

Other TORI Global publications you may find interesting!

01



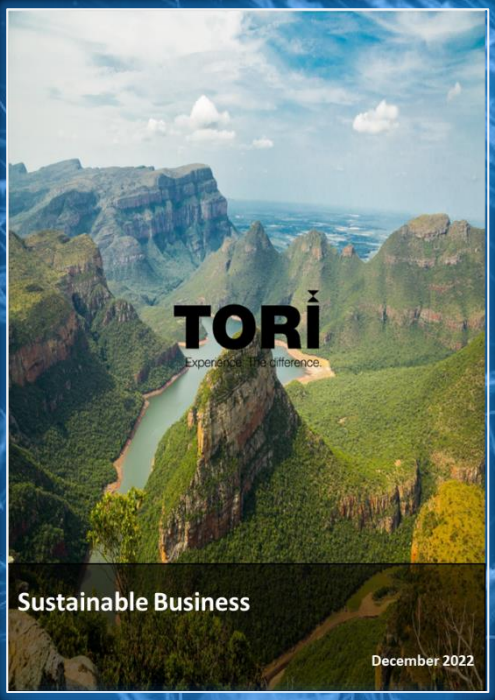
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Type: White Paper

Topic: ESG, Data

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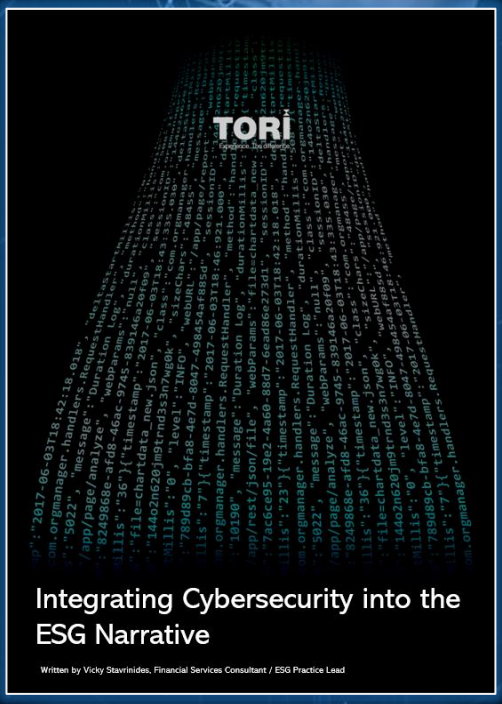
Title: Sustainable Business

Type: Blog Post

Topic: ESG, Business Strategy

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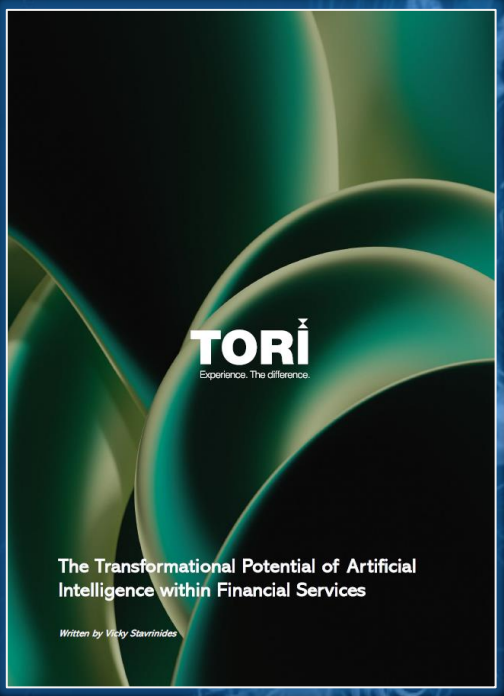
Title: Integrating Cybersecurity into the ESG Narrative

Type: Blog Post

Topic: ESG, Cybersecurity

Link: Click Here

04



Title: The Transformation Potential of AI in Financial Services

Type: White Paper

Topic: AI, Transformation

Link: Click Here



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