EMERGING SUSTAINABILITY ISSUES IN BUSINESS: A STUDY OF THE INTERFACE BETWEEN ENVIRONMENTAL, SOCIAL, GOVERNANCE VARIABLES AND BUSINESS WITH SPECIAL REFERENCE TO INDIAN CORPORATE SECTOR

ABSTRACT

The role of business enterprises has become extremely fundamental and critical for the growth of sustainable business and sustainable development as a whole. The business world, particularly in the west is in the process of baptizing itself to a newer paradigm of sustainability. The term 'sustainability' being highly varied and expansive in nature, the present study proxies it using environmental, social and governance (ESG) factors for the purpose. These situational factors previously considered as non-financial, hence unimportant, are persistently posing challenges to business. The challenge not only remains in strategizing to combat the fast changing scenario but in converting these risks into newer business opportunities to generate wealth for the stakeholders. However, the impact is causal. Increased operations through business activities might also have a direct and indirect impact on the environmental and society as a whole. Thus, for the betterment of global environment, society and business, ESG impacts need to be monitored, measured and managed. However, the process makes sense if and only if these new opportunities emanating from ESG activities prove material to business i.e. ESG factors add significant value to investments. The present research explores this proposition, first by conducting a global study wherein 100 academic papers dealing with the interlinkage between ESG factors and financial performance of business entities are selected using Cochrane methodology across different geographical domains over a time period of 1990-2015 and analyzed through meta-analysis. The idea was not only to assess the relationship between two sets of variables but also to decipher the impact of different control variables on the relationship. The results emphasize on the positive impact of ESG factors on business performance. Secondly, the results are tested in the Indian scenario by considering 31 firms from BSE-100 which constituted the sample group selected through a process of screening based on publication of sustainability reports using G3 and G3.1 guidelines and the rest 69 firms constituting the control group, over a time period of 2011-2015. The results indicated that different ESG dimensions have dissimilar impacts on financial performance of firms. Environmental disclosures were found to have a positively significant impact on P/E ratio of firms. However, the study establishes a weak but negative impact of environmental disclosures on RONW, Tobins'Q and market liquidity.

More importantly, corporate governance disclosures were found to have a profound and positive impact both on intrinsic value addition indicators RONW, ROCE and market value addition indicator Tobins'Q. The results obtained are in sync with the arguments of legitimacy theory which states that a socially responsible firm has more legitimacy and more firm value.

To ensure that ESG factors are fully operative, pre-existence of a market is required that acknowledges such typically non-financial issues as impacting variables. Thus, to assess the market maturity of ESG factors, primary surveys are conducted with institutional investors aka fund managers, investment bankers and company executives to comprehend their levels of perception and awareness related to the same. Collating the results of the survey, the study embarks upon the growing concern and consciousness among market participants in terms of sustainable business. However in terms of implementation, efforts are still in a nascent stage. The study highlights existing disparity between perception of the senior sustainability officials of companies and actual efforts undertaken. The trend is more or less the same in case of institutional investors, wherein their perception about ESG is high considering composite Likert scores calculated on the basis of perception based questions, the appropriateness of which is tested through a Cronbach's alpha. However, efforts are underutilized.

The last objective of the study pertains to financing ESG efforts undertaken by the business sector. None of the non-market approaches ensure a perennial source of finance to sustainability efforts due to non-pricing or mis-pricing of ESG factors. The study argues that if the market is ready to pay a premium, a self-sustaining financing mechanism can be generated to finance and contain sustainability efforts. However, presence of asymmetric information between investors and companies dampens the actual pricing of these factors. Effective pricing can be achieved only with the help of market forces subject to certain conditions viz. maintaining the existing growth rate of the firm, reinvesting a part of the company's net profits in undertaking ESG investment, integrating ESG factors in the mission, vision and statement of the company, minimizing informational asymmetries through signaling, exploring sustainable investment choices in both the debt and real estate markets and an affirmative role on the part of policy makers and market regulators is essential in driving demand for sustainable products.