THEME ARTICLE

Implications of COP26 and ESG

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The outcome document, known as the Glasgow Climate Pact, calls on 197 countries to report their progress towards more climate ambition next year, at COP27, set to take place in Egypt. A number of participants felt disappointed because of softening of the language of the declaration. The language of the earlier draft "the phase-out of unabated coal power and of inefficient subsidies for fossil fuels" was softened. The language in the final draft was toned down to "phase down" coal use. India was credited to have demonstrated diplomatic acumen in achieving this change.

The UN Secretary General summed up the outcome of COP26 at Glasgow in following words, "The approved texts are a compromise. They reflect the interests, the conditions, the contradictions and the state of political will in the world today. They took important steps, but unfortunately the collective political win was not enough to overcome some deep contradictions. We must accelerate actions to keep the 1.5 deg goal alive. We are still knocking on the door of climate catastrophe. It is time to go into emergency mode or our chance of reaching net zero will itself to zero. I reaffirm my conviction that we must end fossil fuels subsidies. Phase out coal. Put a price on carbon. Build resilience of vulnerable communities against the here and now impacts of climate change. And make good on the $ 100 Billion climate finance commitment to support developing countries. We did not achieve these goals at the conference. But we have some building blocks for program". His concern was clear.

Key COP26 Achievements

The COP26 outcome document, however, reflected commitments to end deforestation; to drastically reduce methane emissions; and to mobilize private finance around net zero. The text also reaffirmed resolve towards the 1.5 degree goal; boost climate finance for adaptation; recognized the need to strengthen support for vulnerable countries suffering from irreparable climate damage. At COP26, parties built a bridge between good intentions and measurable actions.

Private Sector Engagement

The private sector also showed strong engagement with nearly 500 global financial services firms agreeing to align $ 130 trillion – some 40 per cent of the world's financial assets – with the goals set out in the Paris Agreement, including limiting global warming to 1.5 degrees Celsius.

Cut Emissions from Methane and Coal

There was also a methane pledge, led by the United States and the European Union, by which more than 100 countries agreed to cut emissions of this greenhouse gas by 2030. Meanwhile, more than 40 countries – including major coal-users such as Poland, Vietnam and Chile – agreed to shift away from coal, one of the biggest generators of CO_2 emissions.

US – China Pledge for Climate Cooperation

Also, in a surprise for many, the United States and China pledged to boost climate cooperation over the next decade. In a joint declaration they said they had agreed to take steps on a range of issues, including methane emissions, transition to clean energy and decarbonisation. They also reiterated their commitment to keep the 1.5C goal alive.

Green Transport

Regarding green transport, more than 100 national governments, cities, states and major car companies signed the Glasgow Declaration on Zero-Emission Cars and Vansto end the sale of internal combustion engines by 2035 in leading markets, and by 2040 worldwide. At least 13 nations also committed to end the sale of fossil fuel powered heavy duty vehicles by 2040.

Beyond Oil and Gas Alliance

Many 'smaller' but equally inspiring commitments were including one by 11 countries which created the Beyond Oil and Gas Alliance (BOGA). Ireland, France, Denmark, and Costa Rica among others, as well as some subnational governments, launched this first-of-its kind alliance to set an end date for national oil and gas exploration and extraction.

On the thorny issue of financing from developed countries in support of climate action in developing countries, the text emphasizes the need to mobilize climate finance "from all sources to reach the level needed to achieve the goals of Paris Agreement. Private businesses have to play a more crucial role.

India's Stand

The Prime Minister of India presented five nectar elements, 'Panchamrit', to deal with the challenge of climate change, as follows:

First: India will take its non-fossil energy capacity to 500 GW by 2030.

Second: India will meet 50 percent of its energy requirements from renewable energy by 2030.

Third: India will reduce the total projected carbon emissions by one billion tonnes from now till 2030.

Fourth: By 2030, India will reduce the carbon intensity of its economy by less than 45 percent.

And fifth: By the year 2070, India will achieve the target of Net Zero.

These 'Panchamrits' will be an unprecedented contribution of India to climate action.

The Prime Minister also, presented the concept of one word – LIFE – which means Lifestyle for Environment. What is needed today is mindful and deliberate utilization, instead of mindless and destructive consumption and he advised the path that is best covered by ESG.

ESG Agenda and Rating

Climate change discussion has given ESG a greater push. As businesses have come center-stage to achieve Net Zero Target, ESG concept and implementation has become important. ESG issues continue to integrate with strategic business imperatives. The pandemic and climate change have highlighted the importance of sustainable and resilient business models to support the economic recovery, basing on insightful reporting to provide stakeholders with a clear understanding of models, while making informed investments and taking other related decisions. Investors and bankers are having expectations on ESG disclosures, and companies are expected to have systems and data based information to ensure authenticity.

ESG Rating Agencies have important role. An important issue is "How can the data of Rating Agencies be rated." Whether they are using the latest data or not is a key issue. They have to correlate hundreds of data points. Successful agencies will be those remaining ahead of the curve. Rating of different agencies will seldom converge and comparisons with other agencies is not an option. Benchmarking becomes difficult. Though SEBI is expecting top 1000 companies to submit 'Business Responsibility and Sustainability Report (BRSR)' to report annual sustainability progress. It is expected that about 200 top companies will create their own system and manpower. Their reports will be true and factual. A large number of software companies will also mushroom to support other 800 companies prepare their reports. The validity or reliability will be difficult to ascertain. Each of the software companies will write their algorithm and create their models. So the output will be constrained by their models and the data points used by them.

India Ratings and Research (Ind-Ra) has announced the launch of its integrated disclosure that show how environmental, social and governance factors impact individual credit rating decisions. These disclosures will be part of rating action commentaries (RACs) for all entities having listed securities whose ratings will be assigned or reviewed effective 1 January 2022. It will be based on total 14 comprehensive ESG sub-factors considered a part of this disclosure: 5 of these are environment related; 5 are social related and 4 are governance related. Environmental factors include: Greenhouse gas emission/air quality; energy and fuel management, water and waste water treatment; waste and hazardous materials; and exposure to environmental impacts. Social factors include: community relations and social access; customer welfare, product safety, data security; labour relations and practices; employee well-being; and exposure to social impacts. Governance factors include: operational execution; governance structure; group structure; and financial transparency.

Rating of companies for their ESG involvement may become a significant factor in decision making.

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