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Exploring Environmental, Social, and Governance (ESG) Score Variations Across Industries

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Abstract

Sustainability reporting is the disclosure and presentation of Environmental, Social and Governance (ESG) aspects in business. Environmental, Social, and Governance (ESG) factors are increasingly important in today's business world as they are regarded as critical indicators of a company's sustainability. All the stakeholders (investors, shareholders, creditors, government and customers) have considered the ESG as a prime factor for sustainable development. Most important measure of sustainability is ESG score. The study aims to compare the ESG score of listed companies across seven major industries. Seven major industries identified for this study were Fast Moving Consumer Goods (FMCG), IT, Financial services, Automobile, Bank, pharma and Energy. ESG scores published by CRISIL were taken for this study for the financial year 2021-22 which includes both overall ESG scores and the scores of each of its three specific dimensions (environmental, social, and governance). Mean and standard deviations were used for this study to analyse ESG scores. We find that IT sector had highest mean and minimum variation in the overall ESG score. Among these seven industries, Automobile sector emerged as the least sustainable sector based overall ESG and followed by FMCG and Pharma. In the Environmental Score, we find that Banking sector was the leader followed by IT and financial Services. Automobile is the least sustainable sector based on Environmental score. In case of social aspect, more sustainable sector was bank with highest mean of social score. The least sustainable sector was automobile followed by FMCG and financial services based on mean of social score. Based on governance scores, the IT sector was the most sustainable sector with highest mean. Following the IT sector, the banking and financial services sectors were also highly sustainable. The least sustainable sectors were energy and automobile. Another finding of this that ESG scores are significantly different across seven industries.

Keywords: ESG (Environmental Social & Governance), Sustainability, Sustainability reporting

Introduction

Sustainability reporting is the disclosure and presentation of Environmental, Social and Governance (ESG) aspects in business. Environmental, Social, and Governance (ESG) factors are increasingly important in today's business world as they are regarded as critical indicators of a company's sustainability. All the stakeholders (investors, shareholders, creditors, government and customers) have considered the ESG as a prime factor for sustainable development. Due to the pressure of international orgnisations like UN, companies are more focused on sustainability reporting. Different methods and measures have been used by companies for reporting the sustainability. Most widely used framework for sustainability reporting is GRI (Global Reporting Initiative). Remaining frameworks are issued by Sustainability Accounting Standard Board, Carbon Disclosure Project and TCFED.

In India, SEBI has introduced framework in the name of BRSR (Business Responsibility and Sustainability Reporting) in 2021, this is the extension of previous framework BRR (Business Responsibility Reporting). Starting from financial year 2021-22, the top thousand listed companies have the option to voluntarily submit the BRSR (Business Responsibility and Sustainability Reporting). But in the financial year 2022-23 onwards, it will be mandatory for them to submit it. Companies' Sustainability reporting is based on three core areas (Environment, Social and Governance) of business operations which impact not only the business itself but also society as a whole. All the frameworks of sustainability reporting include both quantitative and qualitative indicators of business. The main purposes of sustainability reporting are accountability, transparency, and stakeholders' engagement. Sector-wise analysis is very essential for comparing across sectors.

ESG score is the best quantitative measure for Comparing the sustainability practices of different industries. ESG scores have become an important measure for analysing a company' s sustainability practices, which have a direct impact on long-term value creation. ESG scores have an impact on company's goodwill and brand equity, as well as influencing consumer perception and purchase decisions of consumers (Chatterji and Toffel,2019). Consumers have favorable perception on companies with strong ESG credentials. This will lead to brand loyalty and competitive advantage. ESG score shows the company's performance in addressing environmental impact, social responsibility, and corporate governance issues, meeting the expectations of investors, consumers, regulators, and employees. (Lins et al., 2017). Regulatory bodies around the world are making sustainability reporting compulsorily for listed companies (Rasheed et al., 2021).

The calculation of ESG scores are based on both qualitative analysis and quantitative data (Khan et al.,2016). Combining the different qualitative variables presents challenges in developing standardised methodologies for ESG evaluation (Luo & Kanuri, 2020). Improving the data reliability and comparability are the main challenges for researchers in the area of ESG (Environmental, social and governance). ESG score has a positive correlation with stock return and profitability of a company (Dhailiwal et al., 2014). But this relationship may vary across industries due to sector specific factors (Bassen et al., 2019). Different industries have different concerns in the area of environmental, social ang governance. The aim of this study is to compare the ESG score across the seven major industry sectors.

Literature Review

Adhering to the prescribed ESG standards has become a prerequisite for accessing capital market (Boesso & Kumar 2020). They also highlighted the ESG integration is no longer a concern but has become central to banking operations. They also suggested that banks are responding by embedding ESG factors into their strategic frameworks, which influences decision-making processes and risk management strategies. Chatterji and Toffel (2019) studied how companies react to being publicly rated by examining the mechanisms through which these ratings influence firm actions, particularly in terms of improving social and environmental performance. provide valuable insights into the strategic responses of firms to external ratings, emphasizing the role of ratings as both a motivator for improvement and a potential source of symbolic compliance.

Clark et al (2020) make a compelling case that sustainability is not just a moral imperative but also a financial one. Their study showed the importance of integrating ESG factors into corporate and investment strategies to achieve long-term financial outperformance. Dhaliwal, Li, Tsang, and Yang's (2014) investigated the relationship between voluntary nonfinancial disclosure, particularly Corporate Social Responsibility (CSR) reporting, and the cost of equity capital. They also provided the robust evidence that voluntary nonfinancial disclosure, through the initiation of CSR reporting, can lower a firm's cost of equity capital. This finding underscores the importance of transparency and the strategic role of CSR activities in financial markets.

García-Sánchez et al (2021) showed the mediating role of CSR in linking sustainability practices to financial outcomes, focusing on whether sustainable practices directly impact a firm's financial performance or if this relationship is mediated by CSR activities. Gond et al. (2019) studied the intricate relationships between management control systems (MCS), environmental, social, and governance (ESG) objectives, and dynamic capabilities in organizations. The paper provided a theoretical framework to understand how MCS can be configured to balance the demands of contingencies and ESG goals while fostering dynamic capabilities.

ESG Performance and Stock Returns: A Comparative Study of Emerging and Developed Markets" by Grewal et al (2022): This paper showed the relationship between Environmental, Social, and Governance (ESG) performance and stock returns across emerging and developed markets. Main objective of this study was to compare how ESG performance impacts stock returns in Emerging and Developed Markets. It also highlighted the need for improved ESG reporting and standards in emerging markets to enhance the reliability of ESG data. Khan et al (2016) titled Corporate Sustainability: First Evidence on Materiality, provided evidence that the financial market reacts more favourably to sustainability disclosures when they are material to the firm's industry or operations. The main finding of this paper is that investors value sustainability information relevant to the company's specific context. The study concluded that materiality is a key factor in effective corporate sustainability reporting and that focusing on material issues can lead to improved financial performance and stakeholder communication.

The paper by Lee et al (2020) studied the relationship between corporate sustainability performance and Environmental, Social, and Governance (ESG) disclosure in Korea. The main finding of this study was that higher corporate sustainability performance is positively associated with the quality of ESG disclosures. Lins et al (2017) titled "Social Capital, Trust, and Firm Performance: The Value of Corporate Social Responsibility During the Financial Crisis" investigated the impact of corporate social responsibility (CSR) on firm performance during periods of financial instability. The study focused on the relationship between CSR and firm performance, particularly during the 2008 financial crisis. The study suggested that CSR can provide firms with a competitive advantage during economic downturns by enhancing trust and social capital. This can lead to better performance outcomes when compared to firms that do not engage in CSR. The paper by Luo and Kanuri (2020) examined the role of ESG (Environmental, Social, and Governance) ratings in predicting corporate social responsibility (CSR) outcomes. Specifically, they analysed the MSCI ESG ratings and their effectiveness in forecasting a company's CSR practices. The findings contributed to the ongoing discussion about the role of ESG ratings in investment and corporate governance.

Methods

The study aims to compare the ESG score of listed companies across seven major industries. Seven major industries identified for this study were Fast Moving Consumer Goods (FMCG), IT, Financial services, Automobile, Bank, pharma and Energy. ESG scores published by CRISIL were taken for this study for the financial year 2021-22 which includes both overall ESG scores and the scores of each of its three specific dimensions (environmental, social, and governance). CRISIL (Credit Rating Information Services of India Ltd) is an Indian credit rating agency and is also a subsidiary of American company S & P Global. 315 companies were selected from above mentioned industries. For calculating the ESG score of companies. CRISIL used more than 600 Key Performance Indicators (KPI) of 1000 companies.

The calculation is based on publicly available information from company website, SEBI, annual reports published by companies as well as ESG data from reliable sources such as industry associations and government agencies. This includes both quantitative and qualitative disclosures. To determine overall ESG score for a company, weights are given to Environment (35%), Social (25%) and Governance (40%) attributes. Governance has been assigned the highest weightage due to the assumption that good governance practices is the cornerstone for environment and social agenda of any company. ESG score published by CRISIL is in between 0 to 100. To know the best sector among the seven sectors, statistical measures like mean and standard deviations were used. In order to understand the significant associations between groups, one way -ANOVA test was conducted.

Results

We analyse the ESG scores of companies from seven sectors. The following table shows the number of companies under seven industries.

Table 1: Number of companies under seven Industries

Industry	No of Companies
Pharma	62
FMCG	41
IT	48
Financial Services	32
Automobile	54
Bank	34
Energy	44
Total	315

Source: CRISIL

First, we analyse the overall ESG scores across industries. Mean and standard deviations are the statistical measures used for this analysis.

Table 2: Overall ESG mean and standard deviation

Industry	Overall ESG (Mean)	Overall ESG (SD)
Pharma	52.30	6.67
FMCG	51.75	5.46
IT	71.52	4.70
Financial Services	53.71	6.72
Automobile	46.81	4.89
Bank	60.79	4.94
Energy	61.86	5.20

The above table showed that IT sector had highest mean and minimum variation in the overall ESG score. Among these seven industries, Automobile sector emerged as the least sustainable sector based overall ESG and followed by FMCG and Pharma. Apart from the overall ESG score, Individual ESG scores of three specific dimensions of Environment, Social and Governance were also analysed. Table no 3 mentioned about ESG score of Environment dimension.

Table 3: ESG mean and standard deviation of Environment Dimension

Industry	Mean	SD
Pharma	36.08	12.04
FMCG	38.53	8.05
IT	48.95	13.36
Financial Services	42.25	7.56
Automobile	30.76	8.55
Bank	54.82	5.94
Energy	32.94	10.44

Source: CRISIL

Based on Environment Score, Banking sector was the leader followed by IT and financial Services. Automobile is the least sustainable sector based on Environment score. Other less sustainable sectors were energy, Pharma and FMCG.

The next dimension of sustainability is the social aspect. The following table showed the ESG score of social dimensions.

Table 4: ESG mean and standard deviation of Social Dimension

Industry	Mean	SD
Pharma	51.79	8.02
FMCG	43.84	8.30
IT	52.12	9.49
Financial Services	47.00	9.34
Automobile	38.42	7.63
Bank	54.02	4.78
Energy	49.61	11.45

Source: CRISIL

More sustainable sector was bank with highest mean of social score. Other sustainable sectors were IT and Pharma after the banking sector. The least sustainable sector was automobile followed by FMCG and financial services based on mean of social score

The last aspect of ESG was Governance. The following table shows the governance score of seven industries.

Table 5: Mean and Standard deviation of Governance Dimension

Industry	Mean	SD
Pharma	67.08	4.10
FMCG	68.30	4.54
IT	71.14	4.73
Financial Services	69.45	7.37
Automobile	66.32	3.68
Bank	69.97	7.62
Energy	63.58	2.95

Source: CRISIL

Based on governance scores, the IT sector was the most sustainable sector with highest mean. Following the IT sector, the banking and financial services sectors were also highly sustainable. The least sustainable sectors were energy and automobile.

Impact of industry specific factors affecting the sustainability of different industries (Bassen et al., 2019). So, it is relevant to test the significant difference across seven industries. One way ANOVA is used to test the following hypothesis

H1: ESG scores are significantly different across the seven industries

Table 6: ANOVA

Source of Variation	SS	DF	MS	F	P-value
Between Groups	20044.45	6	3340.741	107.1366	**2.26E-72**
Within Groups	9604.075	308	31.18206		
Total	29648.52				

The p-value is less than the significance level of .05, hence concluded that ESG scores are significantly different across seven industries. Therefore, it can be inferred that industry has a significant effect on ESG score.

Discussions

This study focuses on the impact of sustainability reporting across different industries. ESG score is the best single measure to study the sustainability of companies. Overall ESG score and specific scores of Environmental, Social and Governance were used in this study. Mean and standard deviations were used for this study to analyse ESG scores. IT sector had highest mean and minimum variation in the overall ESG score. Among these seven industries, Automobile sector emerged as the least sustainable sector based overall ESG and followed by FMCG and Pharma.

In the Environment Score, we find that Banking sector was the leader followed by IT and financial Services. Automobile is the least sustainable sector based on Environment score. Other less sustainable sectors were energy, Pharma and FMCG. In case of social case, more sustainable sector was bank with highest mean of social score. Other sustainable sectors were IT and Pharma after the banking sector. The least sustainable sector was automobile followed by FMCG and financial services based on mean of social score. Based on governance scores, the IT sector was the most sustainable sector with highest mean. Following the IT sector, the banking and financial services sectors were also highly sustainable. The least sustainable sectors were energy and automobile. Another finding of this that ESG scores are significantly different across seven industries.

Conclusion

This study contributes to an understanding of sustainability reporting of companies and impact on different industries. 315 companies were selected from seven major industries.IT sector has a highest ESG score under, Environment, Governance and overall ESG score. The least sustainable industries were automobile energy. Among three dimensions of ESG, Governance had the highest score and Environment had the Least score. ESG score significantly different across industries. Industry has an impact on sustainability reporting. Companies should focus on Environment dimension of ESG as the least Environment score. Automobile, Pharma and Energy companies should give more importance to sustainability. All the companies irrespective of the sectors should work more on sustainability because the average ESG score of the companies far from 100.

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