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Current Trends and Future Prospects

of ESG Adoption by the Financial Services Industry

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The Key Summary

Balance creation by financial services firms across all three segments in ESG and boosting the transition to greener economy as whole:

Financial services sector is focusing on creating a balance across all three segments in ESG for overall growth: Since all three segments in ESG – Environmental, Social and Governance – are highly interrelated, the financial services sector is aiming to balance their focus on all three segments to gain brand reputation

Crucial role played by the financial services sector in funding the transition to greener economy as a whole: Financial services sector plays a very critical role in funding the transition to net zero and greener economy for all other sectors across the globe, and guiding capital flow to greener sources

Financial services firms increasingly focusing on investing in ESG across their business operations as well as investment strategy:

Financial services sector being more aware of ESG profile across their business operations and their portfolio, investments and underwriting positions: Increasing investor and consumer sentiment shift towards a more responsible society, a sustainable planet, and improved governance is driving the financial services sector to be more aware of the ESG profile of their operations as well as their portfolio, investments and underwriting positions and integrate ESG considerations into their reporting and risk management framework

Overall, **45% of the total respondents in the financial services sector** indicated that they are well progressed in their ESG journey

Financial services firms increasingly focusing on investing in ESG across their business operations as well as investment strategy:

Regulatory pressures across the globe have pushed financial services firms to increase the adoption and advancement in their ESG journey

57% of financial services institutions are engaging in ESG activities for both their own strategy decisions as well as their investment activities

Strong ESG performance results in **lower systemic risk exposure** for the firm, **reducing the cost of capital** and **results in a valuation premium**

Companies with **high ESG ratings** tend to **withstand crisis better** than their competitors

Challenges faced by financial services institutions in adopting ESG practices:

Lack of transparent and consistent data to measure performance on ESG metrics from investments **undermines the credibility of ESG data markets**

Integrating ESG-related activities into financial, credit, investment or risk considerations along with lack of ESG talent and experience is noted as the major challenges, **faced by 34% of the total respondents**

Regulatory challenges, including no defined rules to navigate ESG frameworks for reporting data poses as one of the biggest challenges for the financial services sector

Reviewing data for quality and consistency, as well as reissuing revised data requests to improve data quality are being considered as significant challenges faced by **more than 60% of total respondents**

Firms are increasingly **facing the risk of serious financial and reputational damage**, primarily from greenwashing allegations, if they do not report or disclose their true ESG strategy and adoption

Outsourcing as a good option for finanical services firms to expediate their ESG adoption journey:

88% of the organisations deploy the services of **external consultants** and **outsourcing providers** for their ESG activities

Introduction

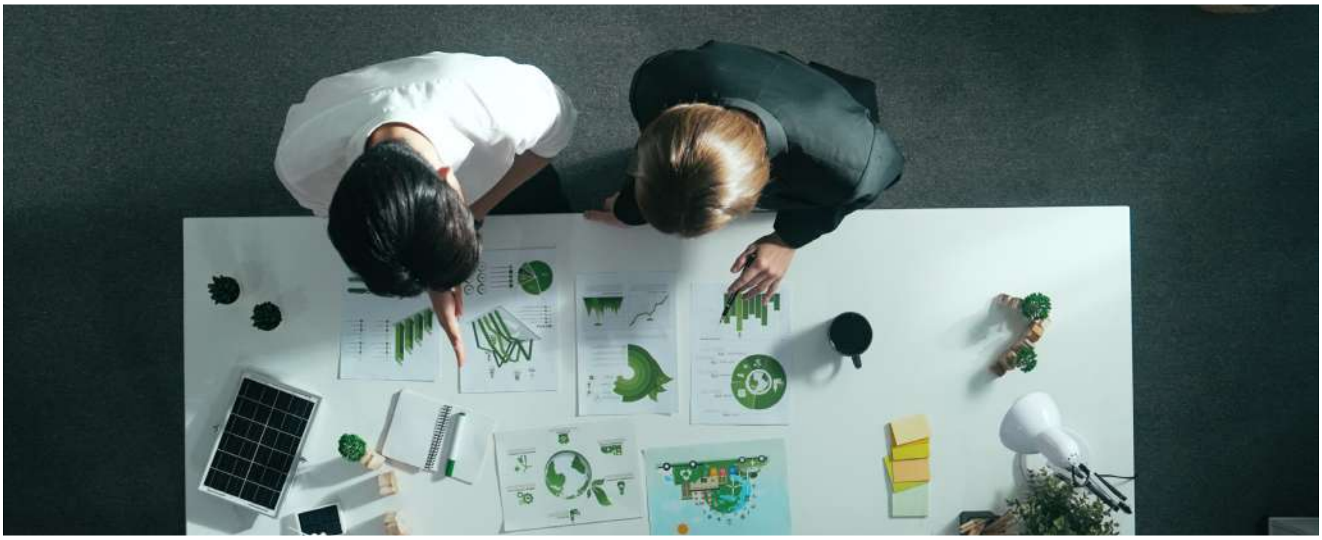
Long gone are the days where the focus of for-profit entities was exclusively on generating shareholder wealth[1]. Beginning in 1970s, the focus gradually changed to have a broader view of for-profit institutional performance to include how these entities were creating value for their employees and the immediate communities where they operated. This was later supplemented by a focus on the impact of institutional practices on the environment. The changes were instigated by several catastrophic events that directed institutional outlook broadly to include several stakeholder groups who are or can affect institutional performance[2]; in addition to modifying governance mechanisms to incorporate and manage ESG practices.

Fast forward couple of decades, with the advent of ISO standards for different aspects of sustainable business practices including social, environmental and governance as well as the growth of reporting standards (e.g., GRI, SASB etc.), complimented by rating agencies (e.g., MSCI, CDP), the institutional focus including that of financial and banking services on ESG gradually became seamlessly integrated with business practices.

Growth of ESG across sectors

The monumental growth of ESG becoming a dedicated practice could be determined by the exponential growth in corporate sustainability reporting (e.g., GRI reporting) from a mere 12% in 1993 to around 80% in 2024[3] (based on global 100 top companies by revenue). In recent years, for-profit institutions have also resorted to disclosing their climate performance as part of a TCFD (now IFRS), CSRD and other guidelines. In the same way, growth in extra-financial reporting regulations (e.g. CSRD, BRSR, King III code etc.) and the need for assurance, have contributed to businesses incorporating ESG as part of their strategic planning, budgeting, governance mechanisms, compensation systems and other management controls (Ghosh et al., 2019[4]).

The business case reasons for incorporating ESG alongside financial decision making are multiple including benefitting from reputational and first mover advantages; managing scarce resources optimally; entering new markets; benefitting from product differentiation; gaining access to socially responsible funds; managing risks; staying competitive; managing talent etc.



Role of the Banking, Financial Services, and Insurance (BFSI) sector towards Corporate Sustainability

The role of the finance industry for fueling such sustainable growth and responsible for-profit institutional practices is paramount. Over the past few years, financial institutions have initiated the incorporation of ESG criteria in their lending practices. This practice allows financial institutions divest from climate/emission sensitive sectors as well as screen investment decisions to ensure funds are lent to those sectors that are likely to adopt sustainable business practices[5 6 7]. Hence, banks will continue to play a significant role in providing transitional capital to help businesses navigate towards sustainable business practices including investing in renewable energy projects, prepare proactively towards climate risk management and contribute towards macro-level net zero commitment. Such green financing practice is not only limited to India but also caters to the global banking industry. The World Bank estimates USD 700-950 billion is needed annually for financing preservation efforts and climate mitigation and adaptation activities[8]. Additionally, financial institutions will continue to play a major role in credit access for marginal communities[9]. In addition, financial institutes also play a pivotal role in offering sustainable indexes (e.g., DJSI) allowing institutional and private investors to invest in sustainable stocks. The socially responsible investment (SRI) fund has also witnessed an exponential growth over the last five years[10 11]. Hence, the BFSI sector is playing a crucial role in funding the transition towards a green economy as a whole.

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[1] *The Origin Of 'The World's Dumbest Idea': Milton Friedman (forbes.com)*
[2] *The Business Student's Guide to Sustainable Management | Principles an (taylorfrancis.com)*
[3] *Global Survey of Sustainability Reporting 2022 - KPMG Singapore*
[4] *Controlling for sustainability strategies: findings from research and directions for the future | Journal of Management Control (springer.com)*
[5] *Firm ESG Practices and the Terms of Bank Lending | SpringerLink*
[6] *ESG-based lending: The next big step in sustainable finance, BFSI News, ET BFSI (indiatimes.com)*
[7] *Screening for ESG Criteria in Lending and Investment Transactions: Chapman and Cutler LLP*
[8] *https://documents1.worldbank.org/curated/en/405891487108066678/pdf/112831-WP-PUBLIC-Introduction-to-Green-Finance.pdf*
[9] *Press Release - Micrometer Q4 FY 22-23.pdf (mfinindia.org)*
[10] *Socially Responsible Funds: The rise and importance of ESG investing in India - CNBC TV18*
[11] *The performance of socially responsible investments: A meta-analysis - Hornuf - 2024 - European Financial Management - Wiley Online Library*

Study Rationale

Given the crucial role of financial institutions in further propagating sustainable business practices, a question naturally arises that requires studying and exploring how these entities manage their own ESG practices (e.g., through strategic integration of ESG, governance mechanisms), the challenges the sector faces in advocating and practicing ESG internally, and the role Acuity Knowledge Partners might play in collaborating with the sectoral players to support them on their ESG journey.

Next, the paper introduces the conceptual framework along with a description of the sample explored. This is followed by our analysis and core findings. We conclude by offering a snapshot of how ESG services at Acuity may guide the sector on the optimal ESG management internally and provide reasonable solutions collaboratively – thereby also fulfilling the SDG goal 17.

Research Question: What is the current state of ESG practices and future prospects associated with the global Banking and Financial Services sectors?

The conceptual framework

The conceptual framework to analyse ESG adoption by the Banking, and Financial Services (BFS) sector across the globe revolved around understanding the progression of financial services firms in their ESG journey and maturity, the route taken by them, the implementation challenges and the benefits they aim to achieve as well as their future plans. While conducting the survey, we focused on analysing the adoption of ESG practices by the BFS sector as well as their future ESG prospects, by studying the following variables:

- If the organizations pertain to any ESG activity, either for their own firm's strategy or investment activities or both, in order to analyse the initiatives taken by the sector. We also analysed if they are more focused on investing in ESG activities for their own organisation's operations or their ESG strategy is inclined towards their investment and portfolio
- Organisational readiness, regulatory compliance and stakeholder engagement to gauge the difficulties faced during the adoption and implementation of ESG strategies in the business
- Benefits identified by the financial services sector in adopting ESG practices including improved risk management, enhanced institutional reputation, improved alignment with stakeholder expectations
- If the financial services institutions have invested in hiring or training an in-house ESG team or have taken external support from consulting / outsourcing firms for their ESG activities
- Future ESG prospects and ESG practices expected to be adopted by the financial services sector over the next 2 years
- Challenges / pain points faced by financial institutions specific to ESG operations, including high implementation costs, finding the right talent, identifying and defining realistic goals as well as appropriate pathways to achieve the defined goals, complexity in integrating ESG metrics with existing systems and lack of clear regulatory guidance
- Benefits of using external support for ESG activities identified by the financial services sectors including cost efficiency, access to experienced ESG talent, expediting the adoption of ESG practices in business operations, amongst others
- Identifying the areas in which BFS firms need external support in their ESG journey and realising their future ESG prospects

Overall study focus

The above parameters facilitated the identification of factors leading to the growth in adoption of ESG in BFS sector, an exploration of the upscaling activities undertaken by the sector, examining the challenges faced by the sector in further adopting ESG and the solutions that are supporting the sector in their sustainability journey.

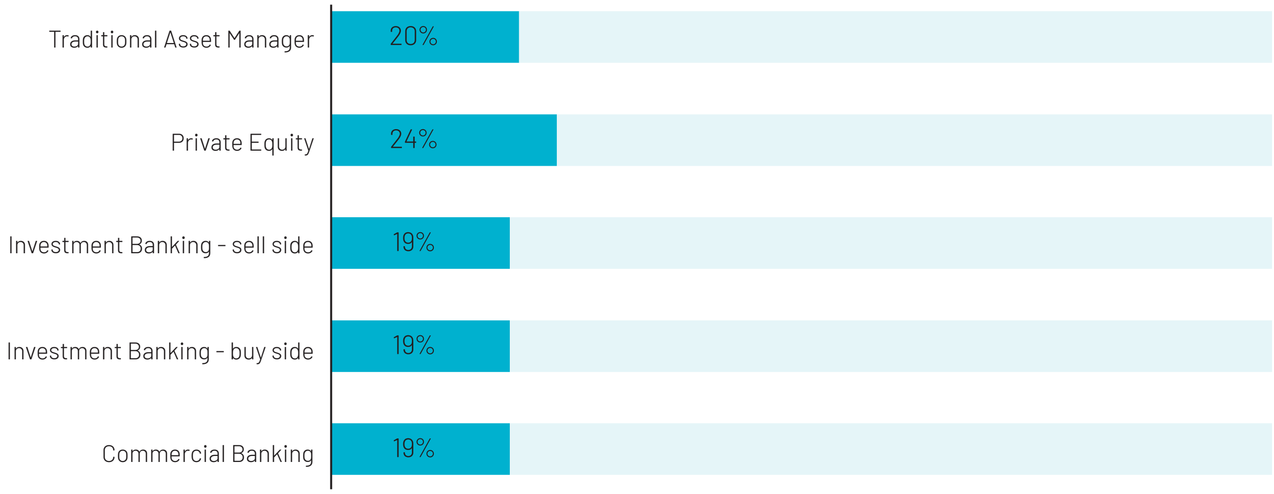
Note on the methodology

In November 2023, Acuity Knowledge Partners surveyed 106 financial services firms across the globe. Respondents were predominantly financial institutions, comprising Private Equity firms (24%), Traditional Asset Managers (20%), Investment Banking – Buy side (19%), Investment Banking – Sell side (19%) and Commercial Banking (19%).

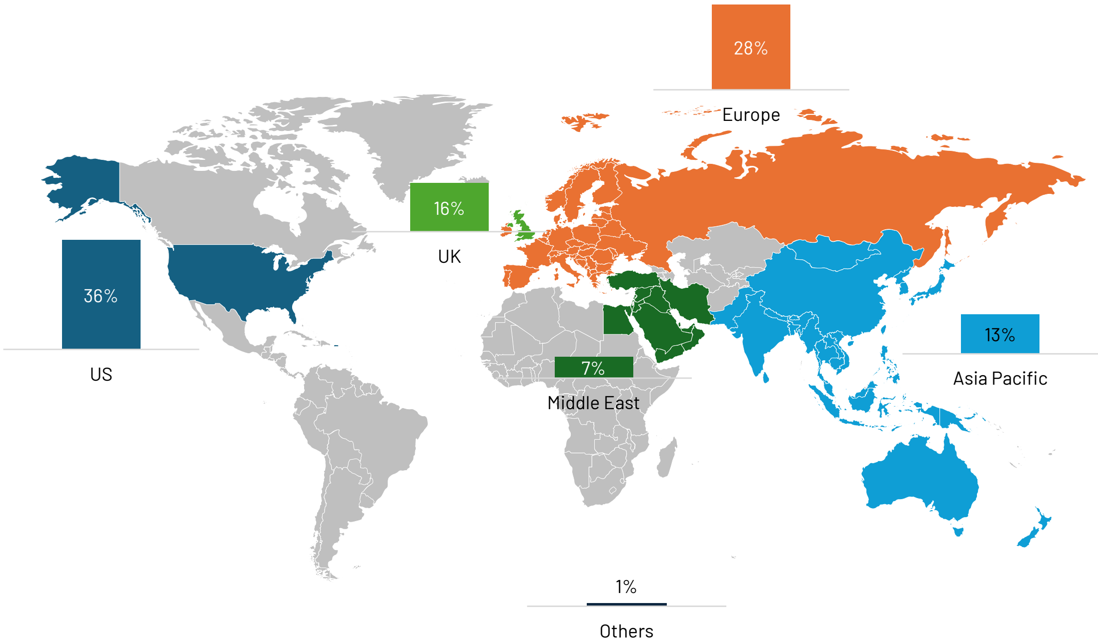
In terms of geographic distribution, 36% respondents were from the United States, 27% from Europe, 16% from the United Kingdom, 13% from Asia Pacific, 7% from the Middle East and 1% from other parts of the world.

Illustrative description of the sample

Respondents – By End Market (n=106)



Respondents – By Geography



Next, we focus on discussing our core findings.

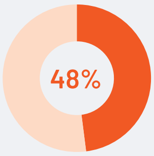
Core Findings and Discussion

DISCUSSION POINT 1: FINANCIAL SERVICES SECTOR BEING MORE AWARE OF ESG PROFILE ACROSS THEIR BUSINESS OPERATIONS AND THEIR PORTFOLIO, INVESTMENTS AND UNDERWRITING POSITIONS:

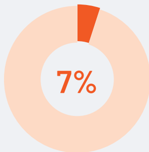
CORE TAKEAWAY 1.1 ESG IN BFSI IS GROWING

ESG advancement in the financial services sector

Advancement in ESG Journey across the Financial Services sector



Companies are growing in their ESG journey.
Developing ESG strategy and related operations.



Companies initiated their ESG journey.
Have some ESG related activities, however, need to explore more clearer way for future strategy.

Majority of the respondents reported to be evolving in their ESG journey, indicating the increased focus of the financial services sector on ESG adoption whilst establishing their 2030 and 2050 carbon emission reduction targets and action plans.

Advancement in ESG Journey across the Financial Services Sector

	Traditional Asset Manager	Private Equity	Investment Banking – sell side	Investment Banking – buy side	Commercial Banking
Well advance in their ESG journey – have a good view of ESG strategy and related operations for the firm and/or their investments	29%	52%	55%	60%	30%
Growing in their ESG journey – developing ESG strategy and related operations	67%	40%	40%	35%	60%
Initiated their ESG journey - have some ESG related activities, however, need to explore more clearer way for future strategy	5%	8%	5%	5%	10%

Financial services firms engaging in ESG activities for their own operations and / or their investment activities

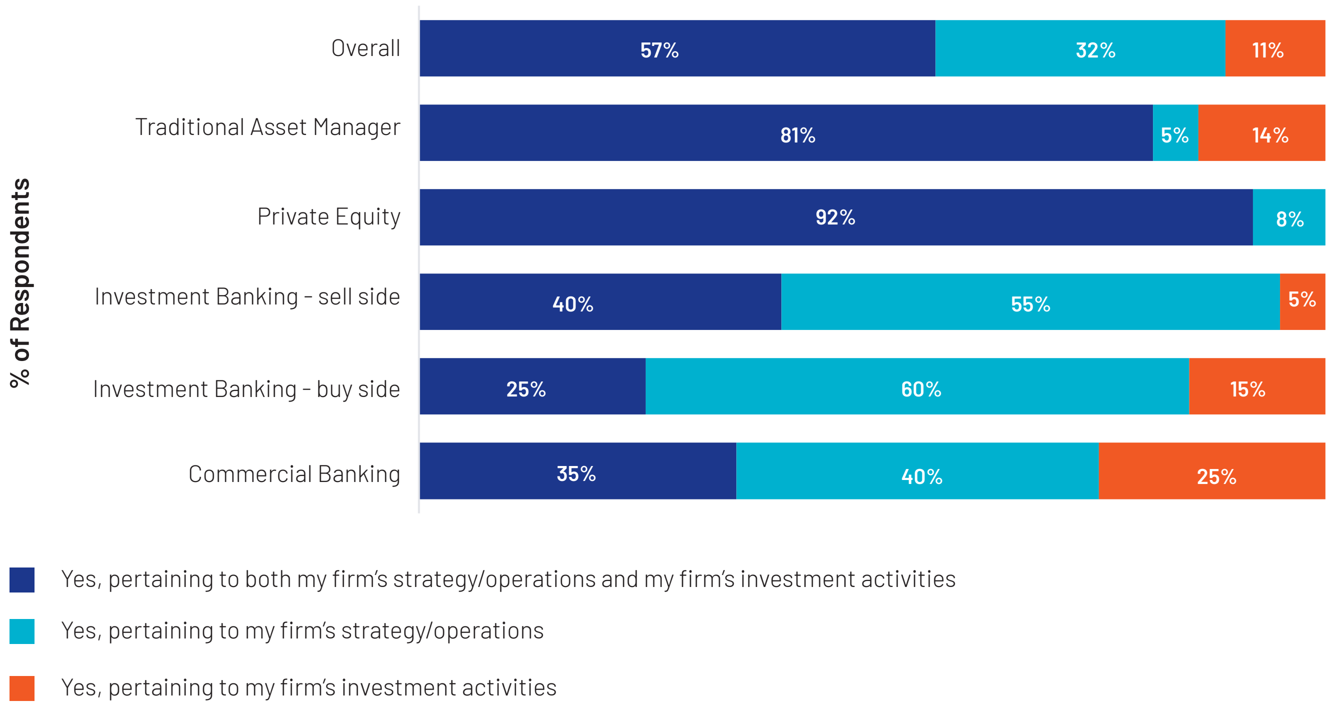
As per the survey responses, our analysis shows **57% of financial services firms** reported to engage in ESG activities for both their own strategy decisions as well as their investments activities.

Financial services sector plays a very critical role in funding the transition to net zero and greener economy for all other sectors across the globe, and guiding capital flow to greener sources as we had noted in the introduction.

Amongst the financial services firms, **92% of Private Equity firms and 81% of Traditional Asset Managers (TAMs)** reported to engage in ESG activities for both their own operations and investment decisions.

Private Equity firms and Traditional Asset Managers recognize the long-term financial benefits of investing in environmentally conscious and socially responsible companies that also allows them to manage long-term risks (e.g., climate change related risks). Limited Partners are demanding transparency and disclosure around ESG activities, putting pressure on General Partners and portfolio companies to adopt sustainable business practices.

The financial services industry recognizes that enterprises with robust ESG performance exhibit lower systemic risk exposure, which in turn reduces the cost of capital for the firm and results in a valuation premium. There is a significant rise in the number of financial institutions that integrate ESG in their decision-making processes globally, and it is expected to increase further.



CORE TAKEAWAY 1.2 SEVERAL STRATEGIES ARE ADOPTED FOR GROWTH IN ESG ADOPTION BY BFSI COMPANIES INCLUDING DEVELOPING AND EXPANDING INTERNAL ESG TEAMS, INVESTMENT IN ESG TECHNOLOGY AND SOFTWARE SUPPORT, HIRING EXTERNAL CONSULTANTS, REFRESHING ESG STRATEGIES AMONGST OTHER.

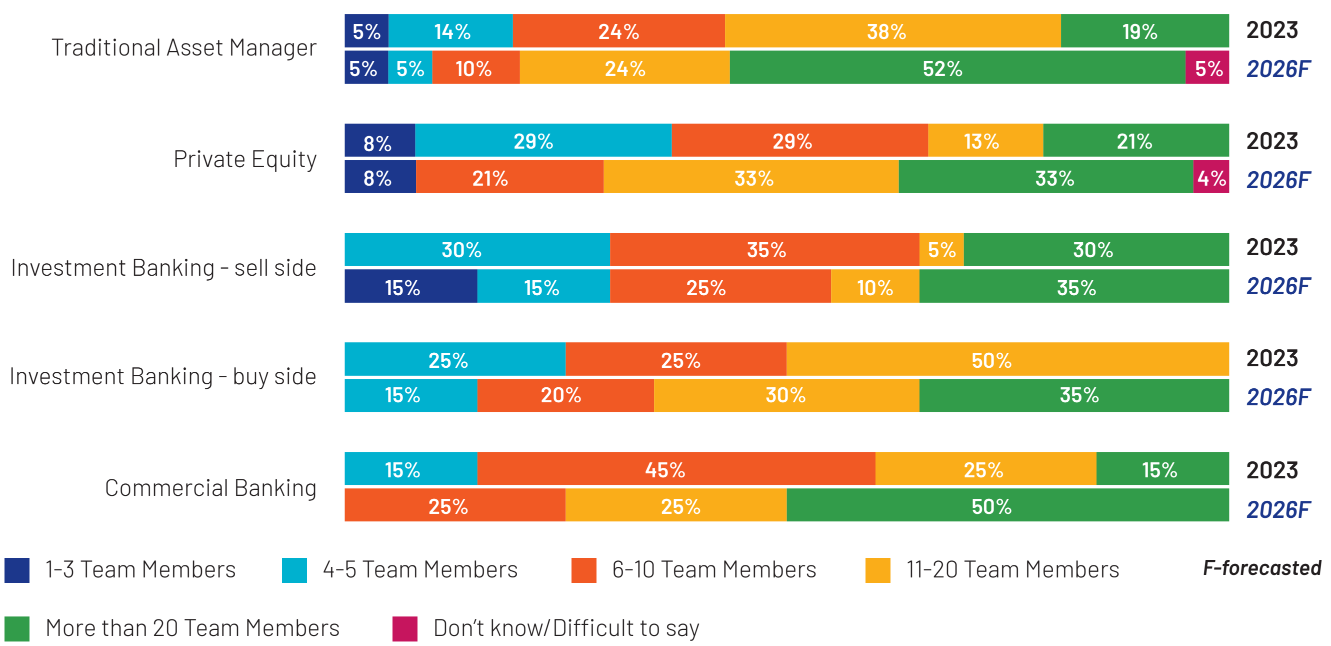
Increasing investment in establishment of dedicated ESG team

Excluding 4% of private equity firms, **all respondents reported to have a dedicated in-house team** that focuses on ESG related activities, with most of the firms expecting the team size to grow to over 20 members in the next three years.

Almost one third of respondents reported to have an average of 6-10 ESG team members: Currently, 31% of total respondents, the highest percentage share, reported to have 6-10 members team dedicated to ESG, followed by 26% confirming a team size of 11-20 team members, and 23% reporting a team size of 4-5 team members.

Expected surge in ESG activity to increase size of dedicated ESG team: 41% of the respondents expect that their team size would grow to more than 20 members in the next three years from current share of 17%, reflecting an increase in efforts in ESG-related resources in the financial services sector.

Dedicated in-house ESG team (Current vs Next 3 years)

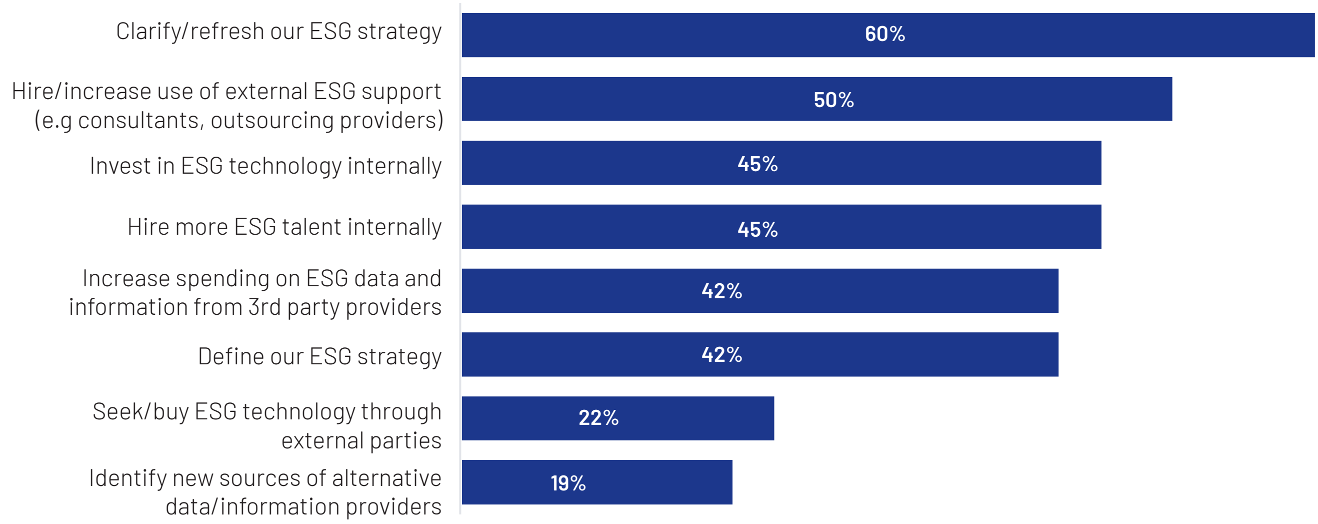


Traditional Asset Manager
With only 19% respondents confirming a team size of over 20 members currently, **52% of participants projected their team size to increase to 20+ by 2026**

Investment Banking - buy side
None of the respondents have a current team size exceeding 20 members, however, **35% anticipate the team size to grow to 20+ members by 2026**

Commercial Banking
Only 15% of respondents have a current team size of 20+ members, and **50% anticipate the team size to grow to 20+ members by 2026**

Focus Areas for ESG activities for next 12-24 months



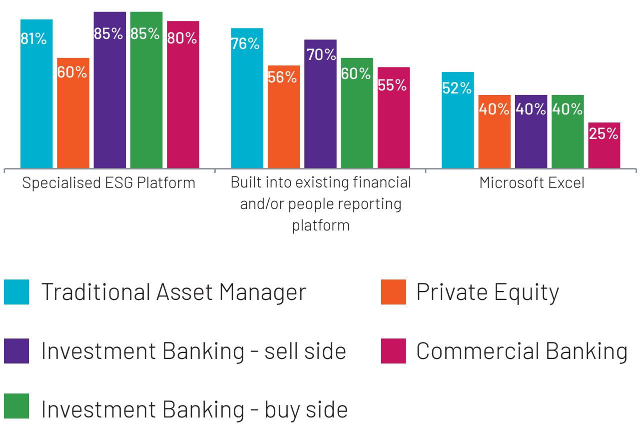
Globally, **refreshing ESG strategy remains one of the top priorities for the financial institutions,** especially in the Investment Banking - sell side and Traditional Asset Management subsector. Companies are aiming for a cost-effective, realistic and scalable ESG data strategy to provide a consistent and coherent approach that covers both internal and external data sources.

Approximately 50% of the respondents highlighted **hiring external ESG support (including consultants, outsourcing providers) to expedite their ESG transition would be a key focus area for them for the next 12-24 months.**

Another focus area of the financial services industry is **investment in ESG technology (e.g., software support as above)**. ESG reporting typically needs the same rigor as financial reporting, and commercially available technology platforms can automate manual tasks of ESG data gathering and reporting. Also, since ESG data management and reporting is metrics-intensive, data accuracy and reliability across the value chain is a key requirement. Hence, it is no surprise that almost half of the financial services respondents reported that they're very likely or somewhat likely to invest in technology and tools to enable more timely and higher-quality disclosure soon.

	Traditional Asset Manager	Private Equity	Investment Banking – sell side	Investment Banking – buy side	Commercial Banking
Clarify/refresh our ESG strategy	71%	40%	90%	60%	45%
Hire more ESG talent internally	62%	44%	40%	40%	40%
Invest in ESG technology internally	38%	52%	55%	35%	45%
Hire/ increased use of external ESG support	48%	44%	55%	55%	50%
Increase spending on ESG data via 3rd party provider	62%	48%	45%	25%	30%
Define our ESG strategy	43%	32%	40%	35%	60%
Seek/buy ESG technology through external parties	33%	12%	20%	35%	10%
Identify new sources of alternative data providers	48%	24%	10%	5%	5%
Others	0%	8%	0%	0%	0%
Do not know	0%	4%	0%	0%	0%

77% of total respondents reported to have **developed a specialized ESG platform** for collecting ESG data, while 63% of the respondents have **integrated ESG reporting into their current financial and/or HR reporting platforms** and 40% cited Excel as their current software tool. Integration of ESG with technology and the financial investment undertaken to develop/ collaborate with technology solutions are further driving the scalability within the sector.



DISCUSSION POINT 2: GROWTH IN COMPLIANCE REQUIREMENTS, NORMS, AND INCREASED OVERSIGHT OF SENIOR LEADERSHIP ARE CONTRIBUTING TO THE GROWTH OF ESG ADOPTION BY THE BFSI SECTOR.

CORE TAKEAWAY 2.1 ADHERENCE TO COMPLIANCE AND NORMS

Regulatory pressures across the globe are acting as a catalyst for financial services firms to adopt and advance in their ESG journey. Financial services firms are now required to develop and disclose their plans to net zero in certain jurisdictions.

Global ESG regulations including Sustainable Finance Disclosure Regulation (SFDR), EU taxonomy alignment, and Task Force on Climate-related Financial Disclosures (TCFD) for non-financial information, are increasingly becoming imperative for companies. In November 2021, the UK government announced at COP26 its plan to make the UK the world's first net zero aligned financial centre.

As highlighted earlier financial services firms realise the significance of integrating ESG into their own business strategy, including their risk and control functions as well as into the regulatory and reporting frameworks. Firms are increasingly facing the risk of serious financial and reputational damage, primarily from greenwashing allegations, if they do not report or disclose accurately their ESG strategies, goals, action plans and overall ESG performance.

CORE TAKEAWAY 2.2: TOP MANAGEMENT ENGAGEMENT IN ESG ACTIVITIES

Sustainability is at the forefront of decision-making and touches all departments, from risk management and compliance to the supply chain and the C-suite: ~61% of the total respondents in the financial service sector confirmed the engagement of CEO / Executive board in ESG endeavors besides having a dedicated in-house ESG team. This reflects the need for an accountable senior executive to assess emerging regulatory requirements and understand the impacts on the business. Leadership also helps to align stakeholders within the company to disclose accurate, material ESG information in a timely manner. This finding is in alignment with previous studies that examined the role of top leadership in stimulating sustainable business practices (Herzig and Ghosh, 2013[12]).

[12] *Managing Responsible and Sustainable Business in the UK | SpringerLink*

DISCUSSION POINT 3: THERE ARE SEVERAL CHALLENGES FACED BY FINANCIAL SERVICES SECTOR IN ESG OPERATIONS AS DISCUSSED BELOW.

Survey respondents reported that they face significant challenges in integrating ESG into their financial, credit, investment and risk disclosures, along with finding the right ESG talent and expertise. Since there is a lack of clarity on linking ESG and strategy, it is difficult for investors to analyse how a company's ESG efforts would affect the cash flow performance of the company. **They all face challenges in collecting accurate data, data quality, data source quality, along with data governance.** Companies want uncomplicated methods to measure long-term value, greater certainty about regulations, and practicable ESG-related frameworks.

Key Challenges faced by financial services sector in ESG operations

As companies are committing to their ESG targets, they are concurrently finding it very hard to find the right ESG talent to advance in their organization' ESG journey. Without the right resources, an organisation's capacity and capabilities towards sustainable business practices may be hampered and remain unrealised.

CORE TAKEAWAY 3.1 PAIN POINTS IN ESG DATA COLLECTION AND REPORTING CYCLE PROCESSES

Reviewing data for quality and consistency, as well as reissuing revised data requests to improve data quality are being considered as significant challenges faced by more than 60% of total respondents. Also, 58% respondents in the financial service firms face a challenge in consolidating ESG data to perform analyis and calculations. ESG data management is a complex task, with data collection being time consuming and resource-intensive.

Since ESG data is sourced from diverse systems across various departments, collating the accurate data is a difficult task, which could result in a disorderly data aggregation pocess that could compromise on the reliability and accuracy of ESG reporting. Many ESG risks are not easily quanitifiable, they are challenging to monitor and manage. Also, adopting new sustainable business strategies may require increased capital expenditure. Shortcomings in the reliability of ESG data have major implications for users. Most obviously, many financial institutions feel that they are unable to rely on a single data provider (e.g., Morningstar, Refinitiv). However, a blended approach based on multiple data vendors not only duplicates external costs, but also necessitates in-house spending to analysis, compare and curate ESG data.

Pain points	% of respondents
Reviewing data received to ensure data quality and consistent responses from others	65%
Reissuing revised data requests to address data quality or consistency concerns	60%
Aggregating / consolidating data received to perform required calculations and figures	58%
Creating data gathering questionnaires/templates for others to complete	51%
Developing analyses and reports (e.g. dashboards, Excel sheets) required for various stakeholders	51%
Reporting back/giving feedback to various stakeholders on the results of your analyses	20%

Disclosure: One of the biggest challenges in ESG reporting according to investors is the lack of transparent and consistent data to measure performance on ESG metrics from investments. Moreover, there is no universal system to validate the authenticity of the data, amidst greenwashing posing a common challenge.

» A classic example is capturing data for scope 3 emissions, where the limitations of underlying disclosure leave data providers heavily reliant on interpretation and proxy metrics.

» Another example is the European Banking Authority's proposal mandating banks to report the Green Asset Ratio (GAR). This in turn requires banks to maintain ESG data for clients at a product/financial instrument level, emphasizing the need for trusted data.

Lack of comparability: The large variation in data sources, methodologies, and criteria utilised by ESG rating agencies contributes to increased skepticism around the usefulness of such ratings attributed to companies across industries. This, in turn, poses challenges for investors seeking to compare ESG ratings reliably. Also, material ESG issues across industries vary, and can be very challenging to compare.

For instance, companies across industries or automotive may give priority to environmental parameters in their ESG strategy, while companies across technology or healthcare may prioritise social parameters in their ESG strategy, and companies in the financial sector may focus on governance parameters. Hence, comparing ESG ratings for companies across different industries may not reflect the actual situation.

There have been controversies that have demonstrated inconsistencies in rating criteria, as well as the risk of ESG rating agencies placing greater/lesser weight on elements of the 'E', 'S' and 'G', when computing ratings. This leads not only to challenges in comparing scores, but also obscures the true rationales behind the ratings given, further inhibiting the ability to verify the data and information provided.

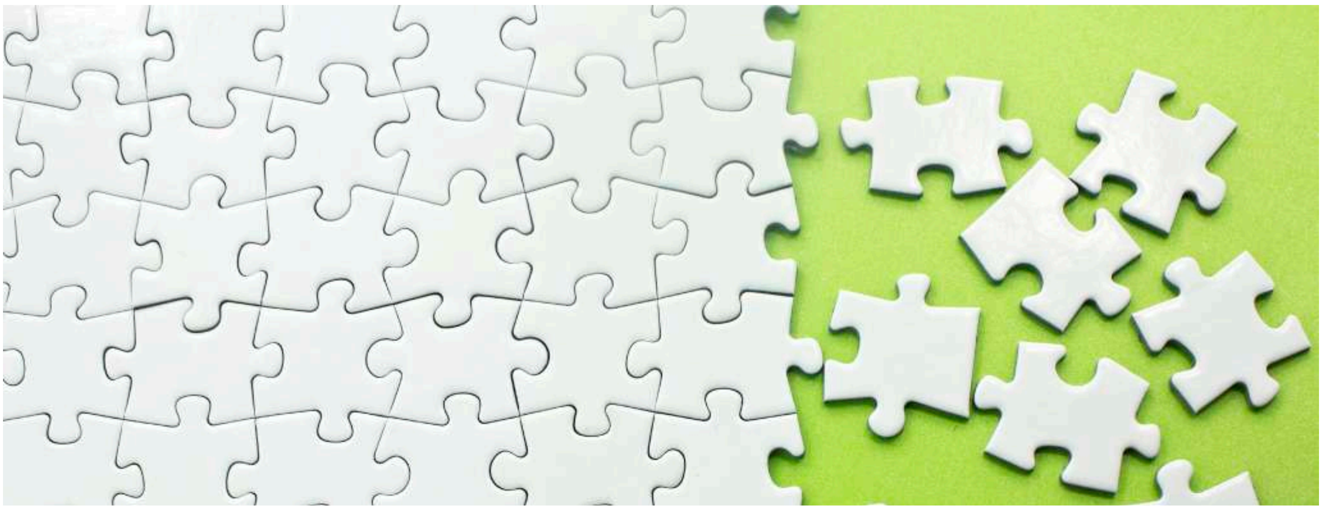
More broadly, the lack of consistency, standardization and independent assurance undermines the credibility of ESG data markets. This is a growing concern, given the increasing costs of compliance failures and the threat from damaging allegations of greenwashing.

Regulatory challenges: While a focus area for the EU has been the 'S' pillar of ESG, for the US, the focus area has been the 'G.' Additionally, guidelines are being made available to navigate the stricter frameworks for reporting data. This makes reporting inefficient, complicating the downstream harmonization and data analysis.

Lack of infrastructure to meet investor-grade reporting requirements: Once a firm works through the challenges of what ESG information to report, they often contend with the challenges of how to effectively collect, manage and produce the information. Both the breadth of ESG data types and the disparate internal and external users of ESG data drive significant reporting complexity.

The process of extracting, cleaning and aggregating data for disclosure is still largely manual—often on multiple spreadsheets—which means that poor-quality data can make its way into reports. We also see those responsible for reporting having trouble referencing the information that ends up in the public domain back to trusted sources. The lack of controls and independent confirmations often result in metrics that are not verified. The growth in technology enabled platforms for ESG integration and superior data management remains at the nascent stage.

Lack of harmonization between jurisdictions, not to mention the incompleteness of crucial taxonomies, can lead to huge inconsistencies in the institutional disclosures that ESG data vendors use to create their scores and ratings.



Challenges faced by financial sector firms	TAM	Private Equity	IB – sell side	IB – buy side	Commercial Banking
Access to reliable, good quality ESG data for public companies					
Access to reliable, good quality ESG data for private companies					
Infrequent data updates					
Capital Positions					
Lack of forward looking ESG data					
Lack of standardized reporting formats					
Difficult to choose relevant regulation/ reporting format					
Meeting the requirements of mandatory reporting & regulations					
Lack of clarity on best practice ESG methodologies (e.g. scoring)					
Integrating ESG into financial, credit, investment or risk considerations					
Lack of ESG talent and experience					
Costs associated with ESG data					
Cost associated with ESG talent					
Have not identified suitable technology solutions for ESG					

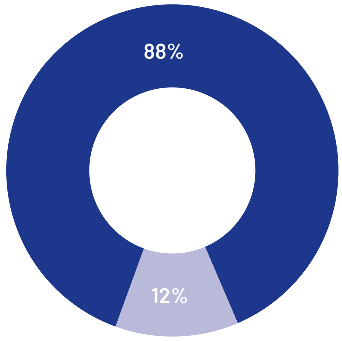
Note: Harvey balls represent indicative weightage for the respective parameters

Low High

DISCUSSION POINT 4: ACTIONS TO OVERCOME CHALLENGES HAVE BEEN IDENTIFIED AS EXPLORED BELOW.

CORE TAKEAWAY 4.1 USAGE OF EXTERNAL SUPPORT BY FINANCIAL SERVICE SECTOR

88% of the respondents
deploy the services of external consultants and outsourcing providers for their ESG activities



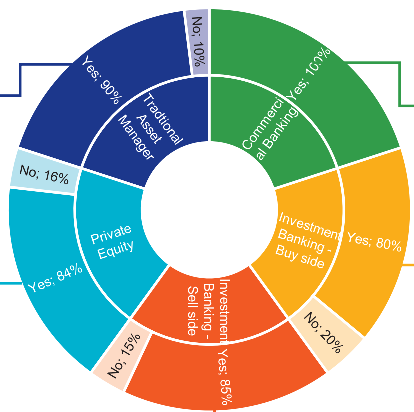
Out of the remaining 12%,
majority are already considering or will be considering using external support in the next three years

The demand for transparency on sustainable and socially responsible practices is increasing rapidly across the financial services sector. The importance of ESG reporting lies in its ability to provide a comprehensive view of an organization's impact on the environment, society as well as its governance policies. Hence, to expedite the process, financial services firms are taking support from experienced ESG professional experts / consultants to develop and implement ESG strategies, for them to not fall behind when compared with their competitors. There is an increasing trend of outsourcing as a strategy for financial services sector to attain their ESG goals. More than **80% of respondents from each sub segment** in the financial services sector reported that they are currently **using an external support including consultancies and/or outsourcing providers** for their ESG activities, either for their firm or for their investments. 100% of Commercial Banking respondents reported to use an external support for their ESG operations, followed by 90% of Traditional Asset Managers reporting the same.

Outsourcing ESG can help financial institutions to focus on their core operations, as well as reduce financial risk and reduce cost in the long term. Financial services firms are increasingly collaborating with ESG consultants to meet their sustainability and ESG objectives in a more effective and efficient manner.

Financial services firms engaging with external consultants in ESG activities for their own operations and / or their investment activities

- 90% respondents of the Traditional Asset Manager suggested outsourcing their ESG activities, mainly due to better quality output and efficiency
- 50% of the other 10% respondents reported their organization will probably consider using external consultant in next three years



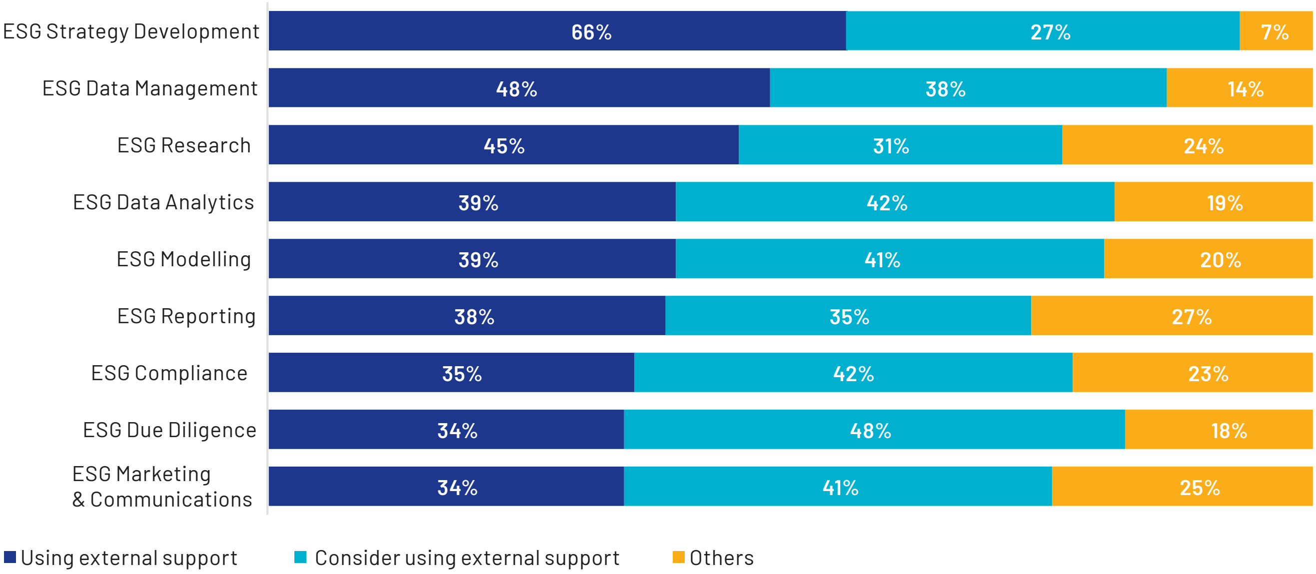
- 100% respondents of the Commercial Banking sector suggested that they outsource their ESG activities
- 70% reported that relevant ESG experience acts as a significant factor of using an external consultant
- 49% of respondents reported to deploy the services of external consults all year around
- Over 40% of the respondents' organisations spend over $1m p.a. on ESG strategy development & ESG data analytics each, with 40% estimating spend to increase by 10-20% in next three years

- 84% respondents of the Private equity sector suggested that they outsource their ESG activities
- Better quality output and Provision of additional capacity serves as the factor for using external consultants
- 62% reported their spend on ESG external support would increase by ~10-20% in the next three years
- 16% respondents reported Lack of ESG relevant expertise in external providers and data privacy concerns as main challenges for not using consultants. However, 75% of their organization would consider the option within next three years

- 80% respondents of the Investment Bank – Buy side sector suggested that they outsource their ESG activities
- Budget constraints, lower ESG related work volume and lack of relevant ESG experience are few pain points due to which 20% respondents do not use external consultants
- 75% of them are sure that their organization won't use or consider using external consultants even in next three years

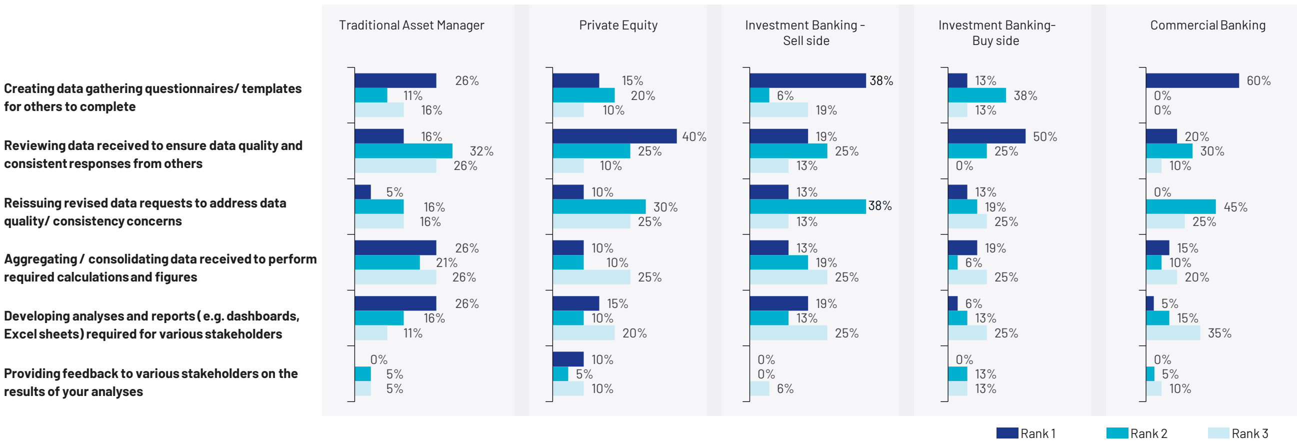
- 85% respondents of the Investment Bank – Sell side sector suggested outsourcing their ESG activities
- The other 15% reported their organization is either considering or will consider using external consultant in next three years

Majority of the financial services respondents are using the support of external consultants and outsourcing provider for their ESG activities, with **66% of the respondents** agreed on using external support **for ESG strategy development** and **27% already considering exploring the support of external consultants** for ESG strategy development.



CORE TAKEAWAY 4.2 PRIORITY AREAS FOR OUTSOURCING SUPPORT

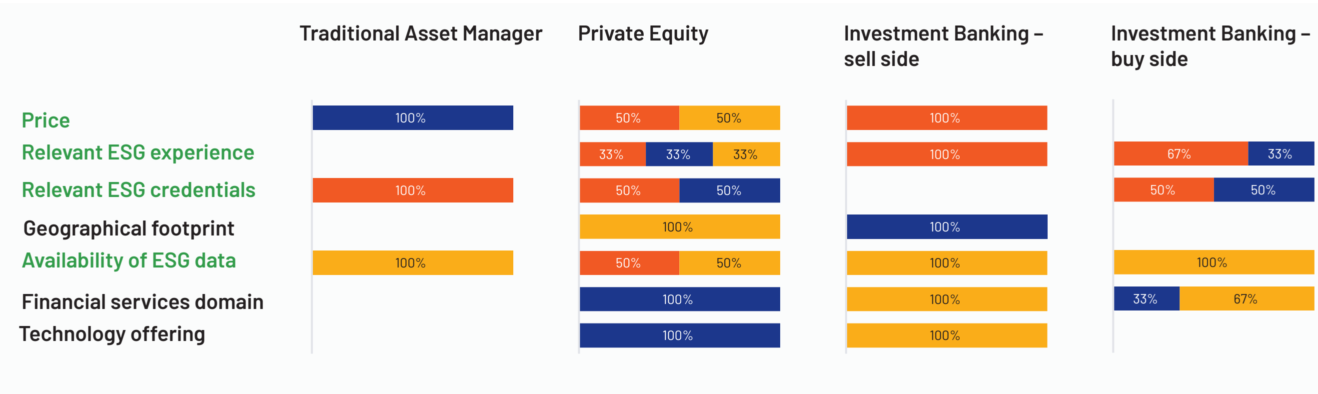
As per the survey, reviewing data received to ensure data quality and consistent responses from others remains the key priority area for outsourcing across the financial services industry, followed by reissuing revised data requests to address data quality or consistency concerns and consolidating data received to perform required calculations.



CORE TAKEAWAY 4.3 FACTORS AND THEIR IMPORTANCE FOR SELECTING AN OUTSOURCING PROVIDER

Relevant ESG experience is the most important factor for selecting an outsourcing provider across the financial services sector markets. Within the end markets, Investment Banking – Buy Side respondents marked relevant ESG experience as the most important factor which is the highest among the end markets. Relevant ESG credentials and price are the other important factors for selecting an outsourcing provider across the end markets.

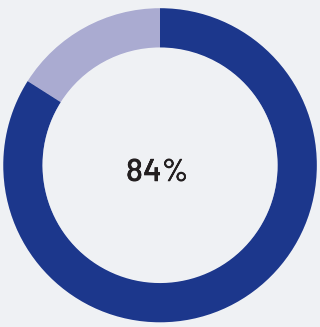
Within the end markets, Investment Banking – Buy Side market respondents marked relevant ESG credentials as the most important factor which is the highest among the end markets, Traditional Asset Managers market respondents marked price as the most important factor which is the highest among the end markets.



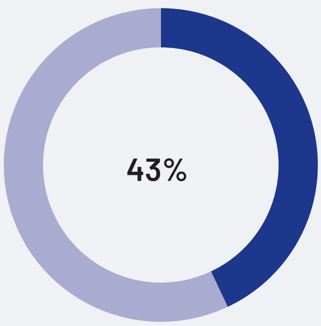
CORE TAKEAWAY 4.4 SOURCING OF ESG DATA FROM EXTERNAL PROVIDERS

Overall, ESG data is collected through key data vendors such as Refinitiv, MorningStar, Bloomberg, MSCI, Moody's, Sustainalytics, FTSE Russell, S&P Global ESG Score, deployed by ~84% of total respondents in the financial services sector.

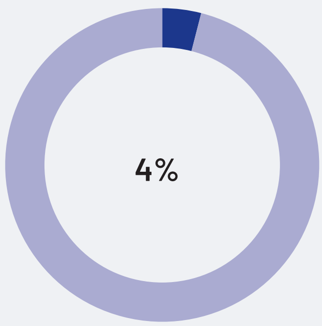
In fact, many larger users of ESG data now have their own ratings teams providing proprietary scores that draw on a range of third-party data sets.



Key ESG data vendors like Refinitiv, MorningStar, Bloomberg, MSCI, Moody's, Sustainalytics, FTSE Russell, S&P Global ESG Score



Other ESG data vendors like Owl Analytics, Richmond Global Sciences, Social Subsidy, ESG Analytics, AI



Do not buy any external ESG data

CORE TAKEAWAY 4.5 BENEFITS OF ENGAGING IN EXTERNAL SUPPORT

Better quality output and increased efficiency are the two of the highest rated benefits offered through using the support of external consultant services which leads the financial services companies to deploy the service of external consultant.

- **Better quality outputs** – **65%**
- **More efficient than using in-house resources** – **57%**
- **Provided 24hr support** – **41%**
- **Provided additional capacity** – **38%**
- **Cost benefits – Lower cost solution vs in house** – **34%**
- **Relevant ESG experience and talent not found in-house** – **34%**
- **Had proprietary ESG data and methodologies** – **30%**
- **Provided more flexibility than in-house resources** – **27%**

Concluding remarks and Acuity's ESG service offerings

Over the past few years, ESG reporting has increasingly become a focal point of regulatory compliance and strategic business considerations within the financial services sector. The pandemic and associated implications on the global economy, combined with climate change and social uncertainty with tensions between various countries, acted as a catalyst to increase the focus of the world on environmental, social and governance issues. The financial services sector is increasingly integrating environmental and social responsibility as well as reducing governance risks in how they operate and invest. **Since all three segments in ESG – Environmental, Social and Governance – are highly interrelated, the financial services sector is aiming to balance their focus on all three segments, to gain market share, improve investor as well as employee confidence, raise more capital as well as enhance brand image.**

This pull factor is reinforced by a strong push from regulation, which continues to actively shape ESG data markets. More institutions are falling within the scope of mandatory European disclosure rules, and emerging regulations in the US, Middle East and Asia continue to stimulate demand in other markets. Asset managers are the heaviest spenders on ESG data, representing 59% of all buyers, followed by insurers and other institutional investors.

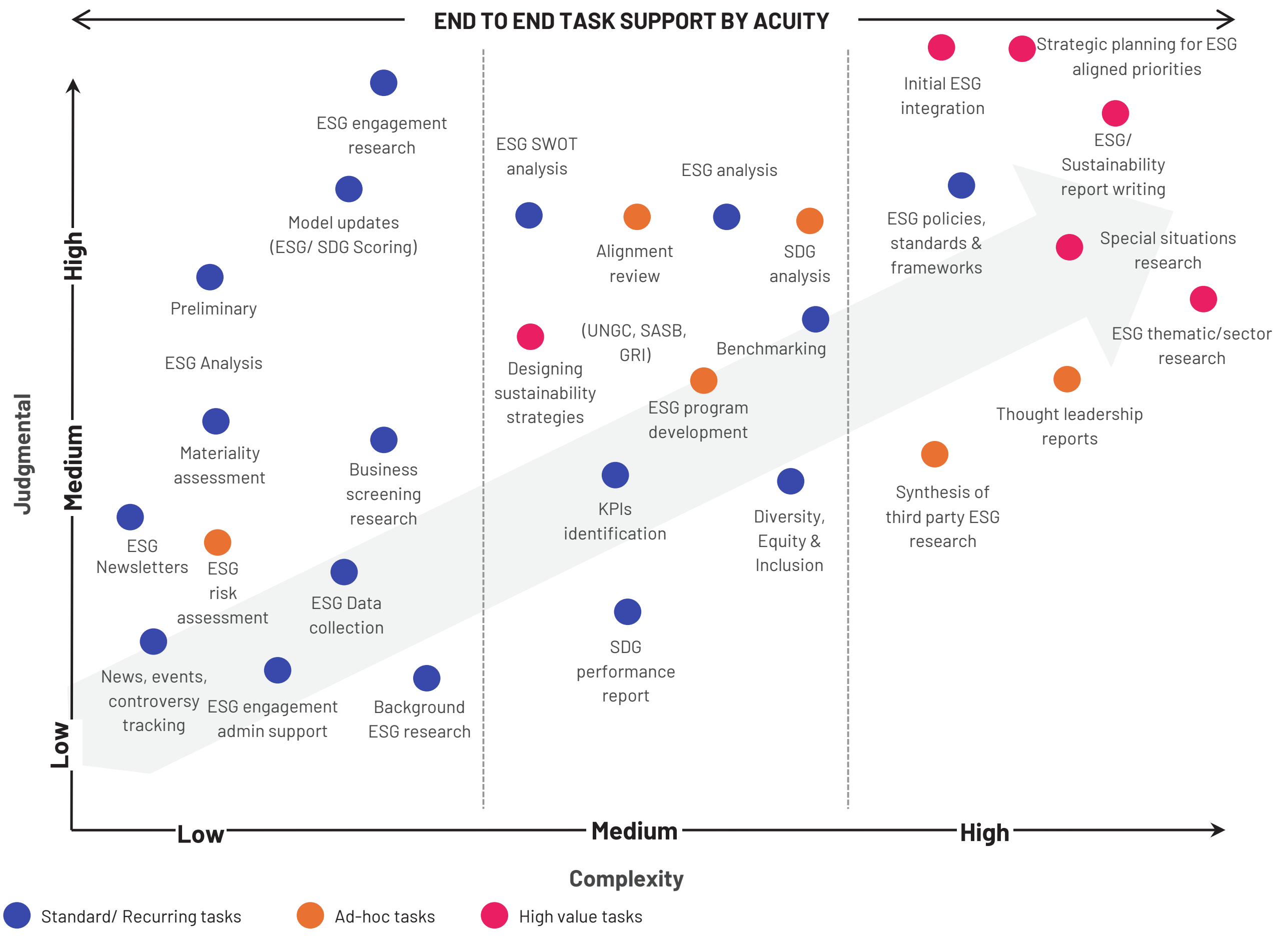
The financial institutions are increasingly focusing on how they can strategically adapt to the new requirements. The sector considers this as an opportunity to leverage innovative technology and explore new partnerships to address major societal issues, enter new markets, and generate profit in collaboration with multiple stakeholder communities while proactively rebuilding trust in institutions. Our analysis indicates that the financial services sector is proactively looking to embed sustainability within their management systems and make it part of their daily decision-making process. This could be gauged considering their commitment in terms of in-house ESG governance teams, their advancements along the path of ESG maturity, their proactive consideration of ESG focus areas for the next 2 years as well as their commitment to engage external support for better integration and management of ESG practices where Acuity Knowledge Partners can be their external support provider. We also identified certain pain-points, challenges and hindrances where Acuity Knowledge Partners may become a part of their extended workforce and offer full-fledged support services as listed below.

How Acuity can support the financial services sector

How Acuity Knowledge Partners can support the financial services sector:

Challenges faced by financial services sector	How Acuity can support
» Difficulty in integrating ESG frameworks into their financial, credit, investment and risk disclosures	» Acuity has experienced ESG professionals that can assist and provide end to end advisory solutions to financial services sector in integrating ESG frameworks
» Difficulty in finding the right ESG talent	» We have the right ESG talents that lay down the ESG goals as well as takes responsibility for the defined plan of action through two business models
» Challenge in collecting accurate data, data quality, data source quality, along with data governance	» Offers practicable ESG-related frameworks as well as data collection templates
» Lack of transparent and consistent data to measure performance on ESG metrics from investments	» Acuity will support clients to develop data capture templates based on frameworks such as GRI, SASB, TCFD. We are also in the process of streamlining data management processes
» Refreshing ESG strategy remains one of the top priorities for the financial institutions	» Offers full-fledged ESG solutions covering strategic ESG management, long term vision and achievable goals
» Access to the right technology and tools to enable more timely and higher-quality disclosure	» Our technical team may support clients with tech enabled, digital tools for efficient ESG data management and disclosure practice
» Disclosure: One of the biggest challenges in ESG reporting according to investors is the lack of transparent and consistent data to measure performance on ESG metrics from investments	» We have dedicated teams to assist our clients develop their ESG reports based on several frameworks
» Lack of comparability	» We have different teams who are experts on certain industries and sectors thereby support sectoral benchmarking and identification of best practices
» Regulatory challenges	» We have experts who have experience and are up to date with reporting requirements like CSRD, BRSR, IFRS etc.

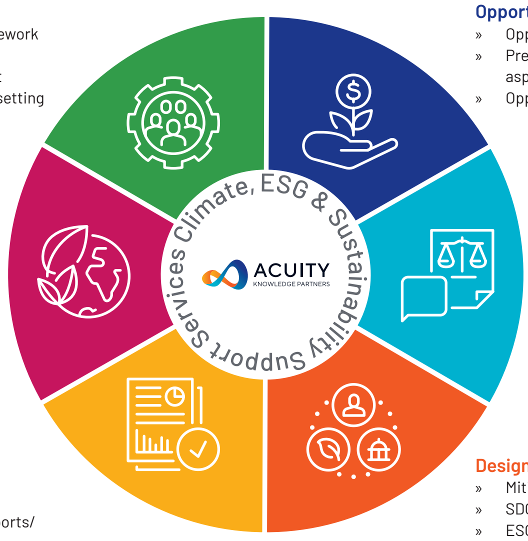
Acuity offers end-to-end task support across the ESG value chain for its clients. Our survey identified the requirements of the financial services sector for the next two years for their journey towards higher ESG maturity. Below, we list our service offerings according to the level of complexity and demonstrate how best we are poised to support the industry in their ESG journey.



Our Suite of ESG Services

Strategy Formulation
- Sustainability management control framework adoption
- ESG maturity and materiality assessment
- ESG KPI identification, analysis & target setting
- ESG roadmap/strategy

Opportunity Assessment
- Opportunity identification
- Pre-investment opportunity screening on ESG aspects
- Opportunity selection and brief profiling



Climate Change
- Physical & Transitional climate risk assessment
- Development of climate related KPIs/Seasonality Model
- Mitigation strategies
- Other support areas

Due Diligence
- ESG due-diligence analysis
- ESG risks & opportunity analysis
- Impact assessment on ESG KPIs
- ESG performance assessment

Reporting and Content
- Sustainability report development
- ESG performance tracking & periodic reports/ branded content
- ESG communication circulars (articles, blogs, newsletters, etc.)
- Whitepapers

Design & Implementation
- Mitigation plans for key material risks
- SDG evaluation and impact
- ESG gap analysis, rating guidance, and response submission
- CDP, TCFD, CSRD, GRI, SASB etc. framework alignment
- ESG training material development

Author

Grateful for all the feedback received from **Shivani Dogra** and **Shankar Shivakumar** during the course of the activity.

Diksha Khanna
Delivery Manager

Diksha has over 7 years of experience on a variety of strategy business consulting and advisory services for corporate clients. Her work predominantly focuses on corporate strategy analysis, industry analysis, market assessment, target screening, competitive benchmarking, pitchbooks, company analysis, due diligence studies, amongst others. She has led and handled multiple teams, managing day to day client engagement, requests as well as involved in strategic planning, delivery and presentation of client deliverables including project scoping, planning and execution for smooth delivery of projects.

Shipra Jain
Delivery Lead

Shipra has over 5 years of experience in strategy research and consulting, having extensive experience in secondary research assignments including industry research, market entry strategy, deep dive company analysis, competitive intelligence, opportunity analysis, lead generation, newsletters, and executive profiles. She has led and handled client across different industries including retail, financial services, and real estate among others, involved in delivery and presentation of client deliverable including project scoping, planning and execution

Akriti Rastogi
Delivery Lead

Akriti has over 6 years of experience in industry research & consulting and has worked on various research projects including industry research, company profiles and competitive intelligence. She is involved in managing projects, including project scoping, identification of research approach methodology, developing strategy frameworks and providing the solutions for client's business needs. She has worked on multiple ad-hoc consulting projects for global clients specializing in market estimation, growth outlook analysis, risk identification, investment flow analysis and opportunity assessment.

Biswaraj Ghosh

Delivery Manager

Dr Biswaraj Ghosh is a key member of Acuity's Corporate and Consulting vertical and oversees project execution and delivery for clients across multiple sectors covering Climate Change, and a range of ESG services. He possesses several functional expertise including solving sustainability-related issues, developing decarbonization strategies, stakeholder engagement, ESG risk assessment, materiality assessment, climate management, sustainability management, target setting, KPI design, etc. through qualitative & quantitative research. He is a Copyright holder (UK and India) for the indigenously developed Sustainability Management Model as part of his PhD thesis. He is also a published author, an international ESG talk show expert and an ESG career mentor. Biswaraj has a PhD in Sustainability Management from Nottingham Trent University, UK; MSc in Corporate Social Responsibility from the University of Nottingham, UK; and a BA (Hons) in Finance, Accounting Management from the University of Nottingham. He is an Ex-Lecturer and Researcher on Corporate Sustainability (UK and Germany).

For more details scan the QR code or visit
www.acuitykp.com

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Acuity Knowledge Partners (Acuity) is a leading provider of bespoke research, analytics and technology solutions to the financial services sector, including asset managers, corporate and investment banks, private equity and venture capital firms, hedge funds and consulting firms. Its global network of over 6,000 analysts and industry experts, combined with proprietary technology, supports more than 600 financial institutions and consulting companies to operate more efficiently and unlock their human capital, driving revenue higher and transforming operations. Acuity is headquartered in London and operates from 10 locations worldwide.

Acuity was established as a separate business from Moody's Corporation in 2019, following its acquisition by Equistone Partners Europe (Equistone). In January 2023, funds advised by global private equity firm Permira acquired a majority stake in the business from Equistone, which remains invested as a minority shareholder.