GO GREEN OR ELSE

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Environmental, social, and governance (ESG) matters have been making headway in the nearly all sectors of the economy, including banking. As a driving force in the global economy, banks play a crucial role in promoting sustainable development and responsible investing. However, are all sectors and the society equally ready - not just for ESG-related trends but, above all, for the upcoming attendant regulations and requirements?

A HANDFUL OF FACTS

According to the Green Finance in Poland report for 2022 by PwC, all the banks surveyed have integrated elements of sustainable finance into their products; and over 80 percent have included such elements in their business strategy and administration processes. Moreover, 15 of the 16 banks surveyed reported plans to expand their sustainable finance product ranges in 2023.

In recent years, banks have recognized that their activities and investments may have a significant influence on the environment and society. In ensuring that these impacts are positive and sustainable, it is critical to maintain long-term customer loyalty, investor trust, and sustained growth. Furthermore, it is increasingly clear that ESG principles now form an integral part of sound risk management practices and are essential to the resilience and profitability of banking operations.

A recent research on how the general public in Poland is aware of ESG, entitled Mediality of ESG. Report 2020-2022, from the ESG Institute and the XBW Ignacy Krasicki Foundation, unveils a different reality, showing that 85 percent of the Polish society has never come across the term ESG before.

While businesses fare better in understanding ESG, there still remains room for improvement. According to the Survey of Sustainability Reporting, published by KPMG in Poland in January this year, only 44 percent of the surveyed companies identify and report ESG factors that significantly affect the company's value and business model.

Notwithstanding the fact that this data only constitutes potted statistics on the issue, it may be argued that it clearly reveals how differently ESG matters are perceived by various market players, moving the largest companies away from Poland's leading financial institutions, and leaving the general public completely behind.

ARE THEY READY?

The EU legislation is and will largely remain one of the main factors affecting the awareness of business in challenges and benefits of ESG. An important step in that field was taken on January 5, 2023 when the Corporate Sustainability Reporting Directive entered into force. It aims to modernize and consolidate the rules on the disclosure of environmental and social information companies are under. According to the directive, along with big companies, SMEs listed on regular markets, will now be additionally required to report on sustainability. This will bring around 50,000 companies under the sway of the new regulations.

It is worth noting that the winds of change in ESG are now affecting the companies obliged to provide non-financial reporting under specific legal regulations, and are about to impact the entire economy. This is mainly because the entities obliged to submit ESG reports will have to demonstrate that their suppliers, contractors and the materials they use meet various criteria, not least eco-friendly ones.

Another example of abroad application of ESG regulations in the EU is the adoption by the European Parliament on March 14, 2023 of a project amending Directive 2010/31/EU on the energy performance of buildings (EPBD).

The proposed amendment aims to significantly reduce greenhouse gas emissions and energy consumption in the EU construction sector by 2030 and to make it climate-neutral by 2050. Under the draft directive, from 2028 onward, all new buildings should be emission-free, while buildings owned or occupied by public authorities should achieve it two years earlier. According to the EPBD directive amendment project: "The fact that buildings are responsible for greenhouse gas emissions even before their operational lifetime is the consequence of the carbon already embedded within all building materials. An increase in the use of sustainably and locally sourced nature-based building materials (...) has the potential to substitute for more carbon intensive materials and to store carbon in the built environment via the use of wood-based materials".

It is clear that, sooner or later, almost all market participants will be obliged to follow ESG requirements, even if not directly, they will have to follow the expectations of their contractors and financial institutions, in particular the banks.

THE BENEFITS

Contrary to the notion that the ESG regulations amount to nothing more than a legal burden, they will bring long-term benefits for the business sector. First, the companies will either have to report ESG compliance or will prefer to intensify cooperation with those contractors who show greater care for sustainable development. That is why more and more companies emphasize the necessity to comply with ESG standards not only in their own structures but also in relation to their business partners.

The same applies to investors who believe that entities operating on ESG principles bring higher return rates in the long run, and, which perhaps has become much more important recently, are better able to cope with crises. With this, sustainable funds are gaining in importance. As predicted by Bloomberg Market Intelligence, the value of ESG assets may reach USD 50 trillion globally by 2025.

Finally, the ESG principles enjoy wide public interest and have direct impact on the reputation of entrepreneurs. Needless to say, the attitude of a given company in ESG is important not only when it comes to the perception of a given brand by its consumers but also by its potential employees who increasingly pay attention to the ethical dimension of their employers.

GREEN UNTRUTHS

One of the risks associated with implementing ESG principles is 'greenwashing'. Although there is no legal definition in either Polish or EU legal acts, 'greenwashing' should be understood as a mis-leading commercial practice based on seeking to impart the false impression that a given product or service has positive impact on the environment.

In 2023, greenwashing has found increasing reflection in the activities of lawmaking bodies. The main example

supporting this trend is the proposed Green Claims Directive, whereby the EU wants to take decisive action to protect consumers against greenwashing scams.
A similar approach can be observed in the financial sector for which the European Supervisory Authorities have published a Call for Evidence to ferret out potential greenwashing practices in the whole EU financial sector. A progress report is expected by the end of May 2023 and a final report by the end of May 2024. In parallel, the European Securities and Markets Authority is deep in consultations on funds' names using ESG or sustainability-related terms, to prevent misleading practices and said it will issue its final guidelines by Q3 2023.

ACT NOW OR PAY LATER

The implementation of ESG principles across a variety of economic sectors, in particular through EU regulations, is inevitable. The areas to which these regulations will soon apply means that literally everyone, sooner rather than later, will have to comply with them. It is clear that preparing for these changes as soon as possible will pay off in the long run.