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ESG trends in 2023

Key ESG areas to keep a watch on this year

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What you need to know about ESG in 2023

2023 is shaping up to be a year where organisations continue to evolve their ESG and sustainability priorities. For some, it's business as usual; for others, it'll be a year of change and disruption. Regardless of where you're at on your ESG journey, there are five key areas to keep a watch on this year:

1. An increasing focus on ethics and integrity
2. Prioritising supply chain security, resilience and transparency
3. Transitioning workforces
4. First Nations inclusion and empowerment
5. A dynamic political landscape with expanding regulatory changes

PwC Australia's ESG experts have explored these themes in detail, providing insights that may shape or affirm your ESG focus this year.

1. An increasing focus on ethics and integrity

At a glance

ESG ambition and targets are growing, but ambition needs to be translated into quality actions.

Consumers, investors, employees and regulators are increasingly on the lookout for false or misleading ESG claims.

The consequences of greenwashing are rising – in terms of reputation, business performance and legal penalties.

Transparency builds trust, so accurate disclosure is key.

In an era of greater scepticism and distrust, the ESG performance of the public and private sectors is under ever-increasing scrutiny.

Consumers, shareholders, investors, employees and broader stakeholder groups will keep raising the bar for ESG performance. And customers are putting their money where their values lie. More than 60% of people[1] are basing their purchasing behaviours on sustainability and ethical criteria, and this is growing by 10% each year. They're also prepared to pay more for ethically sourced, sustainably made products.

Recent research by PwC Australia showed that in FY22, 49% of the ASX200 disclosed a net-zero target, a 13% increase on FY21, but that there is still significant work to be done on transition plans and Board upskilling. This year, many more corporates and other organisations will increase their ESG ambitions and disclosures in line with growing community expectations – and we expect to see them extend their focus beyond net zero to also include broader environmental impacts and the important social and ethical principles intrinsic to a holistic ESG program.

ESG is also increasingly impacting investment and capital strategies, and that is going to continue to rise in importance this year. Investors and their stakeholders now expect transparency of ESG information to measure and compare performance.

There's increasing investor appetite to tackle sustainability issues that span multiple but closely linked sustainability themes (such as sponsoring a 'just transition' to a low-carbon economy) and we expect strong investor demand for reliable data-backed analysis to inform their ESG investment decisions. Data and technology, including analytics tools, are becoming central to investor decisions.

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Targets are a great start, but consumers and investors are increasingly demanding that organisations 'walk the talk' and translate their ambitions, rhetoric and targets into meaningful action. We expect to see a much greater focus this year placed on progress rather than intentions, and alignment of business performance with stated claims.

After all, strong ESG performance is good for everyone – and it's good for business. Companies that lead in ESG are attracting premiums in sales and mergers, and are magnets for investment and financing.

Rising costs of greenwashing

As stated commitments rise, so too must transparency. Consumers, investors, employees and regulators are becoming ever more alert to false or exaggerated ESG claims. And where there's greenwashing, there'll be consequences: brand damage, ongoing scrutiny from regulators, and the risk of fines and litigation.[3] Investors, too, are becoming more discerning about the ESG status of their investments, and will be watching carefully and quick to divest.

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Quality of action, transparency of claims

As well as demanding greater translation of ambition to action and genuine transparency, consumers and investors will also be asking about the quality of ESG actions. Scrutiny of the quality of carbon credits,[6] for example, is likely to intensify with consideration of whether these credits are leading to genuine abatement.

Getting on the front foot with detailed, accurate reporting will help deliver a brand advantage and protect against greenwashing.

Consumers, investors and regulators understand that sustainability journeys take time. Rather than overstating progress, we recommend that organisations focus on increasing the transparency around the steps they are taking within their own operations and in their supply chains, demonstrate how they're translating ambition into action, and back up any ESG claims through reputable reporting frameworks and third-party assurance.

2. Prioritising supply chain security, resilience and transparency

At a glance

Geopolitics and COVID-19 have upended the status quo for supply chains and spurred a shift to sovereign manufacturing.

Supply chains can be a source of operational and reputational risk, but can also offer new opportunities for efficiencies, innovation and ESG improvements.

Scrutiny on supply chains will continue to grow in 2023 as the public seeks more understanding of the full product journey.

Expectations are growing for reporting and reducing scope 3 emissions – so it's time to get started.

Nothing has exposed our dependencies on global supply chains quite like COVID-19 and the war in Ukraine – and these factors will still be with us throughout 2023 and beyond. A key focus for government and business this year is ensuring secure, reliable and high-performing suppliers.

With greater control and transparency of supply chains comes more capacity to manage a range of risks: operational, commercial and reputational. And that means greater competitiveness and resilience for businesses. Looking closely at how suppliers are progressing on their ESG journeys brings potential to up sustainability all along the chain – and to embed new innovations, technologies, efficiencies and circularity.

We predict a growing focus on supply chain sustainability, transparency, resilience, cybersecurity and technological innovation. We also anticipate significant shifts in global supply chains along with efforts to secure greater sovereignty of supply chains for essential goods.

Supply chains continue to come under greater scrutiny from consumers and investors – from emissions and environmental impacts through to labour and governance practices. Sustainability in supply chains will be a key criterion for investment decisions[11] over the next decade as investors increasingly seek evidence of integrity, circularity, and alignment with frameworks such as the Equator Principles[12] and UN Sustainable Development Goals.[13]

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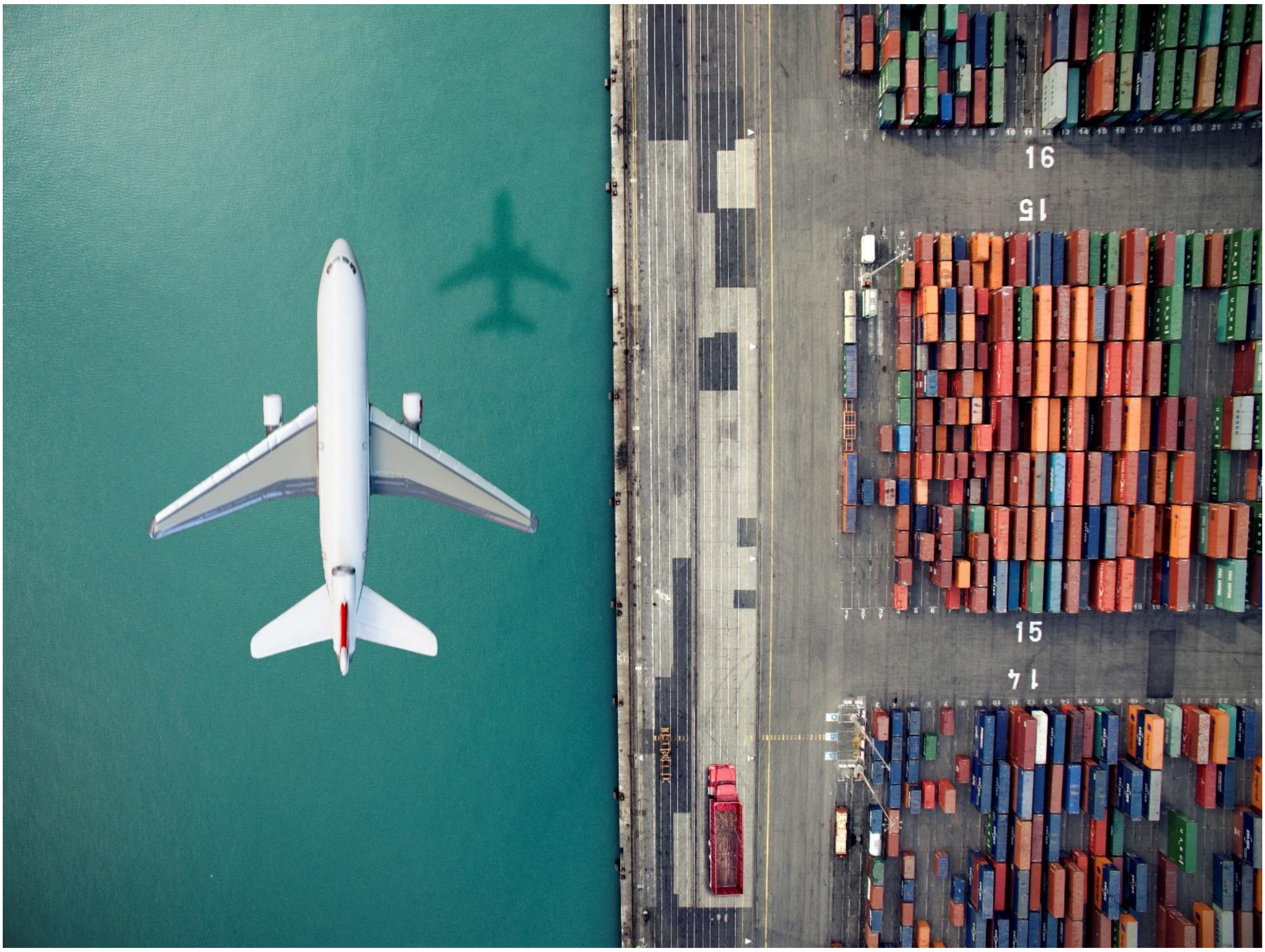

Getting to grips with scope 3 emissions

In 2023, we anticipate that the demand for reporting of scope 3 emissions will rise, as will expectations to reduce them – a challenging area for many. These are the emissions produced by all the parties involved in an organisation's supply chain. According to a 2021 report of 8,000 companies,[15] emissions in supply chains were as much as 11 times greater than in business operations. Moving towards lower carbon supply chains is a critical priority in any organisation's attempt to reduce its overall footprint.

Supply chain security in cyberspace

When considering supply chains, cybersecurity needs to be on the agenda. Digital transformation helps supply chains deal better with disruptions, but is also providing cybercriminals with ever-increasing opportunities.

To build greater resilience to future shocks and strengthen ESG performance, this is a great year to focus on supply chains. We recommend that organisations take a deep dive into their supply chain strengths and vulnerabilities, and start to build the skills and gather the data that will soon be called for.

3. Transitioning workforces

At a glance

More workers, new skills and training pathways will be needed to deliver and power the clean energy transition.

The transition to net zero must be a 'just transition' for workforces and communities affected by major industrial shifts.

Strong ESG credentials will help attract and retain talent.

Any true shift to be a sustainable organisation will require consideration of organisational structure as well as culture and behaviours.

Over the coming years, we anticipate that the already strong focus on labour and skills will intensify as our industries transition to a net zero economy and face into ever-evolving climate and societal concerns.

Large structural shifts in sectors such as mining and energy will add to the disruptions in workforces and working practices experienced through COVID, and the ongoing adjustments workers are having to make as advanced technologies and digitisation transform the way we work.

The past few years have highlighted the impacts of change on workers, and underline how critical a resilient, engaged workforce is to an organisation's performance. As part of ESG performance, businesses will be expected to demonstrate that they value their personnel and ensure fair treatment and conditions, not only for those they're directly responsible for, but also across their supply chains. With a tight labour market and stalled skilled migration, workers will be in high demand in the 'war for talent', and will vote with their feet.

Where organisations are looking to transform and put sustainability at their core, in addition to structural changes, employee upskilling and sustainability programs, they'll also need to prioritise organisational culture and behaviours. This involves a deep understanding of cultural realities, setting clear cultural aspirations that support sustainability, and driving behavioural change.

New jobs, more workers

As the clean energy transition gathers pace, new skills will be needed in many areas of the economy.

It's no surprise, then, that as green economy jobs multiply, the recruitment pressures on companies will increase – especially in filling skilled roles. Already, many renewable energy companies are finding that job candidates lack the experience or qualifications[21] required to take up the opportunities available.

Training will be crucial to skill up the workforce, especially given that an estimated 59% of the job opportunities[22] in the energy transition between 2025 and 2050 are expected to be higher skilled roles such as technicians and trade workers, professionals and managers.

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A ‘just transition’

While jobs boom in the renewables sector,[27] many workers and communities connected with waning industries, such as fossil fuels, will be affected. For an inclusive and equitable energy transition, business and government will need to work together to create meaningful and timely jobs for displaced workers, support redeployment and retraining, and maintain economic opportunity and activity in affected regional communities. Transitional implications for workers, sectors, communities and regions will need to be managed, including proactively upskilling and reskilling, providing support for SME partners and suppliers, and integrating social metrics into reporting and disclosure around net zero.

Critically, the end goal in ESG is not just net zero, but a thriving, socially just, sustainable future. Although there will be impacts to be managed, there will also be vast opportunities to engage in the jobs of the future – for current workers, for communities, and for our children as they complete their studies and enter the workforce. Workforce planning needs action now, coupled with a long-term and inclusive view, regular skills audits to guide upskilling and focus recruitment, and greater encouragement of broad workplace diversity.

In future, we expect to see increasing awareness and engagement of all employees with ESG as a ‘whole of company’ challenge. With more workers starting to choose employers that match their values, and even taking to ‘climate quitting[28]’, organisations with strong ESG performance will have the upper hand in attracting and retaining talent. We recommend strong action this year to embed ESG in all functions of the business and incorporate it into business values and culture.

For an inclusive and equitable energy transition, business and government will need to work together to create meaningful and timely jobs for displaced workers of waning industries, support redeployment and retraining, and maintain economic opportunity and activity in affected regional communities.

4. First Nations inclusion and empowerment

At a glance

In late 2023, the referendum on an Indigenous Voice to Parliament will be a focal point on the journey for constitutional recognition for First Nations peoples.

There is a great opportunity for First Nations participation in the booming clean energy sector through employment, procurement and new ownership models (including co-investment/co-ownership from First Nations groups).

Businesses should consider stepping up their efforts in applying a First Nations lens to commercial activity.

Expectations are rising for organisations to consider these issues as a part of business as usual, and to be mindful of the social value that can be generated with key stakeholders as a result.

A critical part of any organisation's ESG performance should be its relationships with diverse First Nations communities.

None of these things are a matter for government alone. Business has a major role to play in ensuring appropriate consultation and inclusion, ethical practices, and support for First Nations businesses and workers.

Trust, respect and mutual benefits

Where trusted relationships can be formed, and respect demonstrated, there is a very significant opportunity for proponents to partner with First Nations groups across the country for mutual, long- term benefit including employment and procurement.

We anticipate that with heightened focus across the nation on First Nations inclusion, businesses will increasingly be expected to ensure decisions are made with free, prior and informed consent. With an abundance of capital available, we're anticipating a marked shift from 'doing no harm' to increased inclusion, which will feature co-investment and co-ownership for mutually beneficial economic outcomes.

The benefits of greater inclusion of First Nations people and perspectives will flow both ways.

Businesses who lead in this area will be best placed to achieve greater social licence and trust, attract and retain the best talent, and be able to take advantage of new commercial opportunities and advantageous partnerships. We recommend that organisations take meaningful action in 2023 to improve outcomes for everyone and to get ready for policy changes that may flow in coming years.

5. A dynamic political landscape with expanding regulatory changes

At a glance

Global crises have spurred governments to respond, but there's a risk of a race for green subsidies

We've seen government and regulatory interventions in the energy sector in 2022 and there's a lot more we can expect ahead.

With recent changes to the safeguard mechanism, high emitters should be on the hunt for greater emissions reductions.

It's time to get ready for ESG reporting in line with international standards.

With the ESG challenge an urgent global priority, we're seeing continual, rapid changes in policy and regulation in Australia and internationally. In 2023, governments are responding swiftly to the changing geopolitical landscape to safeguard their nations' energy security, stabilise and strengthen supply chains, and capitalise on the opportunities of the energy transition.

Green subsidies overseas have ripples for local projects

Some of these responses, such as the USA's Inflation Reduction Act[32] (IRA), could spark a global race for green subsidies. The IRA mobilises US$369 billion in support for domestic energy production and manufacturing, creating enormous power to attract clean energy businesses, investment, talent and materials. Other jurisdictions are becoming concerned about what this might mean for their own clean energy ambitions.

The EU has responded with a Green Deal Industrial Plan[33] and Critical Raw Minerals Act[34] to safeguard its clean energy industry and maintain progress towards net zero. And, in Australia, a growing number of business leaders and advocates are urging the government to consider its own measures[35] to boost the strength of our clean energy industry and support the viability[36] of an Australian green hydrogen export industry. Already the impact of the IRA is being felt in the changing economics of the export hydrogen market, which is stymieing Australian projects[37] with some choosing the US as their preferred location over Australia.

> In this dynamic regulatory and policy landscape, it will be advantageous to do more than simply maintaining a watching brief. Organisations that clarify their perspectives, strategies and plans, and consider their potential alternatives, will be best placed if rapid adjustments are needed.

Get ready for reporting

In 2023, we will see momentum grow towards standardised ESG reporting. The International Sustainability Standards Board (ISSB) is forging ahead with finalising international standards for sustainability and climate reporting. Meanwhile, Governments have released a consultation paper on the development of a climate-related financial disclosure framework for companies and financial institutions[44], with plans to phase in mandatory sustainability and ESG reporting requirements for large entities from 2024.

The current proposal will require companies to collect, assess and report annual data and disclosures including:

- overarching climate risk governance and assessment – consistent initially with the Taskforce on Climate-Related Financial Disclosures[45], which will ultimately transition to the IFRS Foundation's[46] new International Sustainability Standards Board (ISSB) sustainability reporting standards[47] set to be released in 2023 and effective in 202448
- material climate and sustainability risks – assessed and disclosed using, at a minimum, financial materiality principles
- scope 1, 2 & 3 greenhouse gas emissions.

We expect that the fast-paced and dynamic state of the regulatory environment will continue for some time. This is the time to be alert to changes and to step up internal readiness to report on ESG in line with international standards. Early preparation will make adjustment quicker and easier when new requirements come into force.

To learn more, read our recent report on ESG reporting trends.

What does this all mean for business?

There’s a lot to get one’s head around when it comes to ESG matters and pursuing sustainability ambitions.

Bringing yourself up to speed on the trends most likely to impact your organisation is vital. Preparedness and upskilling can’t be overstated.

If you’d like to explore the impact of any of these trends on your organisation, please reach out to one of PwC Australia’s ESG and sustainability experts.

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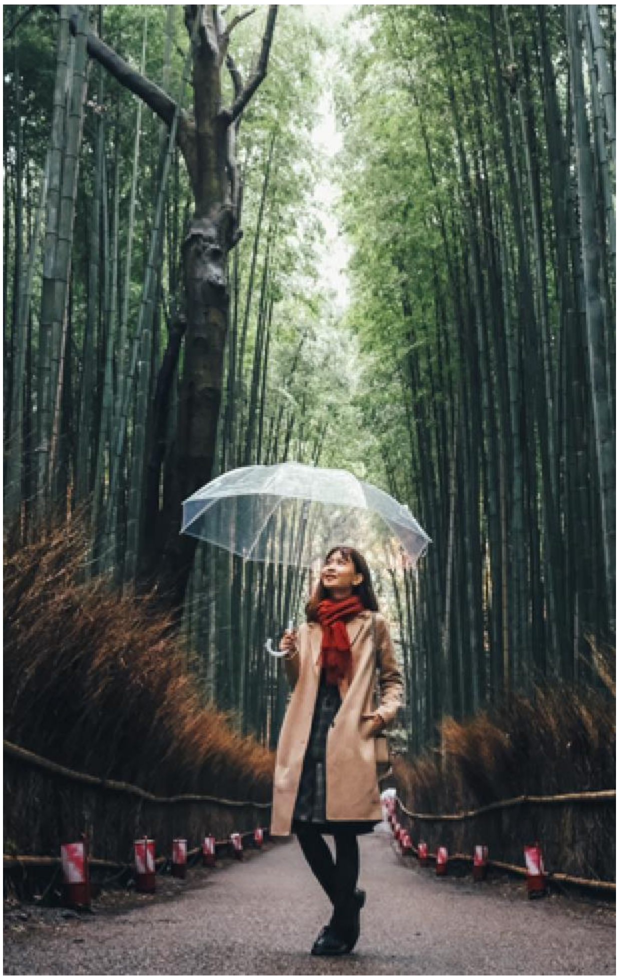

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Australian Securities and Investments Commission (ASIC)

Australian Cyber Security Centre

Australian Climate Leaders Coalition (CLC)

Critical Minerals Office

IFRS Foundation

International Sustainability Standards Board

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