



#oneshot#3#esgrating



ESG RATING

Use Case : SUSTAINALYTICS

“We consider the feedback we have received on the market for ESG rating and data providers is indicative of an immature but growing market, which, following several years of consolidation, has seen the emergence of a small number of large non-EU headquartered providers,”

Letter to the European Commission, Verena Ross, Chair of ESMA

ESG DATA LANDSCAPE

A diverse ESG Rating Market

Several type of Actors :

- **Generalist Data Providers** (e.g.: Moody's)
- **ESG Data Providers** (e.g. : RepRisk)
- **Data Providers specialized in an E, S or G segment** (e.g. Trucost)

Market consolidation

- **Market consolidation through mergers**
- **European ESG Data providers mainly acquired by US/UK Companies**

The Morningstar logo consists of the word "MORNINGSTAR" in a red, sans-serif font. The letter "O" is stylized as a red circle with a white dot in the center.The Sustainalytics logo features a stylized orange and yellow circular icon on the left, followed by the word "SUSTAINALYTICS" in a bold, black, sans-serif font. Below it, in a smaller font, is the text "a Morningstar company".

Divergence among ESG Ratings

A study from the MIT Sloan «Aggregate Confusion : The Divergence of ESG Ratings» (April 2022) investigates the divergence of ESG Ratings based on data from six prominent ESG Rating agencies.

- **The correlation of ESG Ratings** among the 6 different providers is on average 0.54 (2017 data)

- **The divergence is explained by the measurement (56%), the scope (38%) and weights (6%)**

SUSTAINALYTICS ESG RISK RATING OVERVIEW

Overview of the SUSTAINALYTICS ESG Risk Rating

Coverage

- Approx. 14 000 companies

Source

- 350 Indicators
- 1 300 datapoints

Rating

- ESG Risk Ratings are categorized across five risk levels

Negl	Low	Med	High	Severe
0-10	10-20	20-30	30-40	40-100

- One rating comparable across all subindustries (e.g.: the ESG Rating of an asset manager can be compared to the ESG Rating of an Oil & Gas Company).

An example of ESG Risk Rating

Shell Plc

Industry Group: Oil & Gas Producers

Country/Region: United Kingdom

Identifier: LON:SHEL

Shell is an integrated oil and gas company that explores for, produces, and refines oil around the world. In 2021, it produced 1.7 million barrels of liquids and 8.7 billion cubic feet of natural gas per day. At year-end 2021, reserves stood at 9.2 billion barrels of oil equivalent, 50% of which consisted of liquids. Its production and reserves are in Europe, Asia, Oceania, Africa, and North and South America. The company operates refineries with capacity of 1.8 mmb/d located in the Americas, Asia, Africa, and Europe and sells 15 mtpa of chemicals. Its largest chemical plants, often integrated with its local refineries, are in Central Europe, China, Singapore, and North America.

- Show Less

Full time employees: 82,000

ESG Risk Rating

COMPREHENSIVE ?

37.6 High Risk

Negligible	Low	Medium	High	Severe
0-10	10-20	20-30	30-40	40+

Ranking

Industry Group (1st = lowest risk)

Oil & Gas Producers

69 out of 270

Universe

Global Universe

13447 out of 15613

Last Full Update: Sep 30, 2022 ?

Last Update: Oct 8, 2022 ?



SUSTAINALYTICS ESG RISK RATING SCOPE



TOTAL EXPOSURE : sensitivity or vulnerability to ESG risks

Exposure to ESG Material issues :

- Selection of relevant material issues with regards to the industry and sub-industry level
- Definition of a **BETA** which reflects the deviation from the average exposure to a specific ESG material issue within its subindustry

MANAGEABLE RISK: Material ESG risks that can be managed by policies and initiatives

The manageable risk depends on the «Manageable Risk Factor» **MRF** for a specific material issue (range from 30% to 100%). The MRF depends on : (i) ability of a company to ensure compliance by its employees (e.g. : occupational health and safety), (ii) the effect of outside actors on the ability of a company to manage an issue (e.g. cybersecurity), (iii) the complexity of an issue (e.g. global supply chains), and (iv) the physical limitations on innovation or technology (e.g. airplanes and carbon emissions).

UNAMANGEABLE RISK: which cannot be managed by a company (e.g. : carbon emissions of a company airline)

MANAGED RISK : ESG risks managed by policies and initiatives of the company based on

MANAGEMENT SCORE

MANAGEMENT GAP : gap between the managed risk and the risk that could be managed



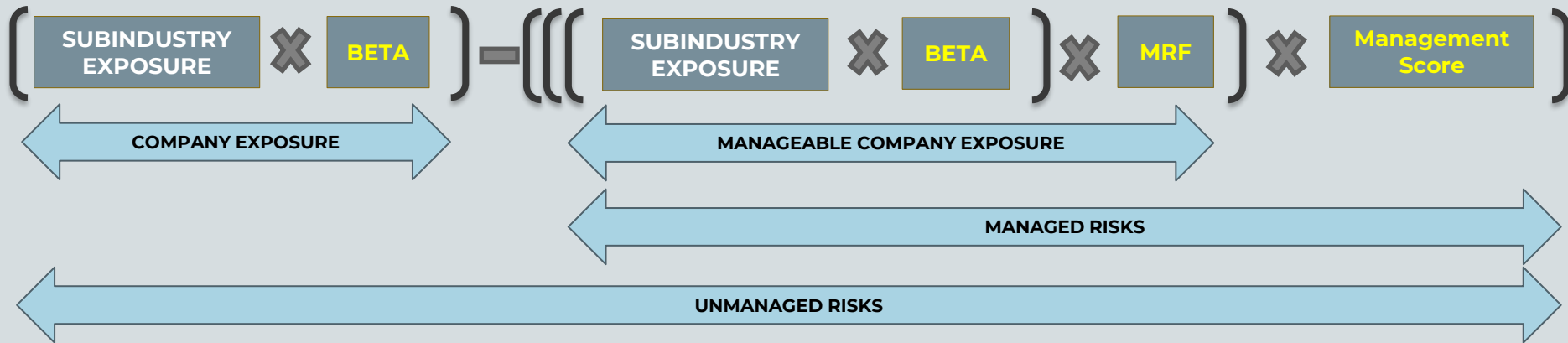
SCOPE OF THE ESG RATING

THE SUSTAINALYTICS ESG RISK RATING CALCULATION

What is a material ESG issue (MEI)?

An issue is considered to be material within the ESG Risk Ratings if its presence or absence in financial reporting is likely to influence the decisions made by a reasonable investor. And to be considered relevant in the ESG Risk Ratings, an issue must have a potentially substantial impact on the economic value of a company

How the score is defined for a material ESG issue?



How the ESG Risk Rating is defined?

The final ESG Risk Ratings score is calculated as the sum of the individual material ESG issues' unmanaged risk scores.



ESG Risk Ratings - Methodology Abstract

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Aggregate Confusion: The Divergence of ESG Ratings*

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Abstract

This paper investigates the divergence of environmental, social, and governance (ESG) ratings based on data from six prominent ESG rating agencies: KLD, Sustainalytics, Moody's ESG (Vigeo-Eiris), S&P Global (RobecoSAM), Refinitiv (Asset4), and MSCI. We document the rating divergence and map the different methodologies onto a common taxonomy of categories. Using this taxonomy, we decompose the divergence into contributions of scope, measurement, and weight. Measurement contributes 56% of the divergence, scope 38%, and weight 6%. Further analyzing the reasons for measurement divergence, we detect a rater effect where a rater's overall view of a firm influences the measurement of specific categories. The results call for greater attention to how the data underlying ESG ratings are generated.

Keywords: Corporate Social Responsibility, Corporate Sustainability, ESG Ratings, Divergence

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