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Deep Dive

ESG star reporters — Part 2

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This is the second of a two-part series exploring the best and worst examples of ESG reporting. Part 1 focused on why robust standards for ESG reporting are important to combat greenwashing, and on the main blunders we see in ESG reporting. This second part focuses on the some of the better examples of ESG disclosure.

At 9fin, our aim is to make sense of the often fragmented ESG information provided by companies. We use a mixture of technology and expertise to provide transparent and accurate data; as well as clear descriptions when something isn't straightforward.

The below focuses on attributes in company disclosure that are helpful to lenders, using three examples: **Jaguar Land Rover**, **Hannon Armstrong** and **WeBuild**.

Breadth and granularity of information

Given many LevFin issuers do not disclose performance on any ESG metrics, companies with a breadth of data typically correlates to better ESG performance and shows commitment to improvement in this field. Comprehensive reporting also enables lenders to compare and contrast issuers on metrics that matter to them, and to track trends better.

This issue is particularly acute when it comes to diversity and inclusion. From a dataset of 250 leveraged financed issuers, only 4% reported any data on ethnic minorities at the board level, the least reported metric of all, according to 9fin. The gender pay gap was the second least reported metric, with just 9% of companies disclosing that information.

A great example of wide and varied diversity reporting is Hannon Armstrong, a US-based investment company, which reports gender diversity across multiple seniority levels. In addition, it also reports on those who self-identify as racial or ethnic minorities and provide a breakdown of each group, as well as a "Diversity of thought" breakdown, which shows the percentage of the company's leadership team that have degrees outside of business and economics.

The Data Convergence Project, an initiative chaired by CalPERS and Carlyle, recommends LGBTQ breakdowns as an optional metric, while SFDR has no indicators related to the field. As such Hannon Armstrong also goes above and beyond the EU requirements by providing a breakdown across its workforce and at manager level.

Such breakdowns are valuable, particularly in industries that suffer from a dearth of workforce diversity such as technology, a sector of focus for many lenders; however, it should be noted that a number of European countries prohibit the collection of protected-characteristics data, or render it risky in legal terms (in some cases, even if this is done anonymously). Countries in which it is more difficult to gather this data include France, Germany, Denmark, Belgium, Austria and Czechia.

Finally, beyond its wide range of diversity data, Hannon Armstrong gives a breakdown of promoted employees, providing much needed granularity. Seeing data in this light can help make companies accountable for who they promote and confront bias, particularly where there is a disparity between the number of women and minority groups in the company and those that are being promoted.

Full and varied disclosure of environmental impacts is especially important for manufacturing, industrial and construction businesses. For example, WeBuild, a construction and civil engineering business, provides comprehensive waste data and disposal methods and shows its impact on biodiversity by reporting its exposure to protected sites by size and type.

Reporting across multiple years is crucial for lenders to get a full picture of a how a company has improved or worsened over a give time period. 9fin suggest five years is the minimum time period to effectively understand a trend, however given ESG reporting is a somewhat nascent field, information across at least three years is helpful.

Jaguar Land Rover provides GHG emissions data across four years, showing a consistent commitment to reporting, while WeBuild discloses its waste production and disposal and workplace injury metrics across the three most-recent years.

The car manufacturer also offers detail in its CDP report, and discloses both market and location based scope 2 data. The two metrics each have their limitations and focus areas, thus including both helps paint a full picture of emissions.

WeBuild's waste production is split by activity, such as excavation, and it discloses its methods of waste disposal, like landfill. Its disposal data is also separated into hazardous and non-hazardous waste, which is particularly helpful because SFDR outlines principle adverse indicators that include mandatory hazardous waste metrics and an additional non-recycled waste metric.

In comparison to WeBuild, some companies don't disclose their hazardous waste production at all, and others report hazardous or recycled waste as a percentage of an unknown total.

The business also reports injury rates for its direct workforce and subcontractors. This is useful as companies could, for example, outsource their most dangerous work. The business also includes the methodologies behind the formal definitions of both the Lost Time Injury Frequency Rate and Total Recordable Injury Rate which is important as standardisation is low for these metrics. This means that two companies may report what appears to be the same metric but the methodology used to get to them differs. In turn, skewing the performance of one against the other when compared.

Location based data uses an average emissions factor based on geographic location, but it can't account for specific energy providers that use a percentage of renewable energy or other green instruments. Market-based data considers individual energy providers, and can account for renewable energy and other green instruments. However, it's important to note that some instruments aren't appropriate for the use case and not all instruments are regulated meaning that both methodologies are required to properly assess GHG emissions.

External standards and initiatives

Using trusted ESG standards and reporting frameworks is good practice, allowing for better assurance over reporting as well as comparison between companies.

Jaguar Land Rover, for example, reports its emissions and energy consumption using the Carbon Disclosure Project framework (CDP) and has aligned its reporting to requirements set out by the Science Based Target Initiative (SBTi) in order to have its targets verified with the SBTi.

The SBTi is a joint project between the CDP, the United Nations Global Compact and the World Resources Institute, which assists companies in setting sector-relevant and science-based climate change targets. Although the initiative has been criticised for elements of its methodology, and for the sheer quantity and, thus potentially diminished quality of verification, market commentators still suggest the initiative is the leading verifier of emissions targets. Bar carrying out full analysis in conjunction with issuers directly, using SBTi targets could be the best indicator of reputable targets. Look out for a 9fin Educational on the SBTi coming soon.

Getting acquainted with new standards and initiatives is advisable as those standards could well become mandatory or commonplace in the future. For example, biodiversity disclosures are not currently expected at the same level as carbon emissions or climate risks, however the The Task force on Nature-related Financial Disclosures (TNFD) could become more prevalent. Just as reporting based on the Task Force on Climate-related Financial Disclosures is evolving to become a requirement for many firms, especially in the UK, the TNFD could follow.

Additionally, the Carbon Disclosure Project added biodiversity questions to its annual Climate Change questionnaire, which aren't currently included in its scoring, but shows the growing importance of biodiversity as a reporting topic. Some issuers are leading the way on areas of growing importance like biodiversity. For example, WeBuild already measures and reports the types of environmental habitats, such as lakes, that it impacts.

9fin's ESG offering provides subscribers with the data and tools they need to comply with new ESG reporting regulations coming into force later this year under the EU's Sustainable Finance Disclosure Regulation (SFDR). As of December 2022, Financial Market Participants (FMPs) that consider Principle Adverse Impacts (PAIs) on sustainability factors in their investment decisions (all FMPs with 500 employees or more) will have to disclose how each of their financial products consider these impacts. This involves providing information on 14 mandatory PAI data points (the template for the PAI disclosure is given in the RTS Annex I).

Our LevFin ESG dataset currently measures 14 key data points and will soon roll out a total of 25 data points across 740+ European companies and will include all the mandatory SFDR Principle Adverse Impacts (PAIs). To fin out more about our ESG data, please click here.