How Companies Can Improve their Investor Rating Scores on ESG

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As investors increasingly push to assess companies' Environmental, Social and Governance (ESG) performance, our publicly traded clients and potential clients often ask us how they can improve their investor rating scores. This question is more complicated than it seems. We recently analyzed six ESG frameworks and distilled the trends and most effective approaches to provide some simple guidance to companies just starting their ESG journeys.

Start with Materiality

Investors want to know that a company has diligently assessed the issues that will have the greatest impact on its finances and business continuity. Thus, our first recommendation is to complete a simple materiality analysis if at all possible. Every company and industry has its own set of material issues[1]. Ideally, each company determines what is material to its business based on its sector, culture, values, stakeholders, and business model. SustainabilityNext helps companies with the materiality assessment process by using available research gleaned from expert frameworks, peer benchmarking, and robust stakeholder engagement. A company has the best chance of improving its ESG performance—and ultimately its investor rating scores—by tailoring its ESG strategy and metrics to specific material issues.

Our Research

Many of our clients—and in particular those just starting their ESG journeys with few or no resources to conduct a materiality assessment— desire a simpler approach to investor ratings. In response, we have analyzed the topics that are most frequently covered in rating agency questionnaires and investor-based reporting frameworks.

[1] *According to the Global Reporting Initiative (GRI), a material topic is one that "reflects a reporting organization's significant economic, environmental and social impacts or that substantively influences the assessments and decisions of stakeholders."*

The following sections and charts compare information from the reporting frameworks of six investor-focused entities that are most frequently used or referenced by our corporate clients: SASB, MSCI, ISS, Sustainalytics, Vigeo-Eiris, and BlackRock. All of these frameworks also focus on investors, in contrast with other frameworks that may have a wider target audience. See the methodology section and references for more information on how we conducted our research.

What Does SustainabilityNext Research Say?

The "top 10 topics" chart below shows that environmental and social issues are fairly evenly covered by investor surveys and requests for information.

Table I: Top 10 Overall Topics

Topics on this list were included in all six frameworks.

Topic	Category
Emissions (GHG)	Environmental
Emissions (other air emissions)	Environmental
Energy	Environmental
Waste	Environmental
Labor management and practices	Social
Occupational health and safety	Social
Employee benefits and retention	Social
Employee training and education	Social
Diversity and inclusion	Social
Supply chain	Environmental/Social

ENVIRONMENTAL TOPICS

On the environmental side, emissions of greenhouse gases (GHGs) and other substances are consistently among the key topics of interest to investors. Beyond the six entities we studied, other reporting platforms such as CDP (previously known as the Carbon Disclosure Project) and Task Force on Climate-related Financial Disclosures (TCFD) focus almost exclusively on greenhouse gas emissions and climate risk disclosures. Investors ask most often for metrics on emissions totals, the amount of reduction, and the emissions intensity of companies' products and services.

Energy use is closely linked to GHG emissions. With a clear focus on companies' bottom line, investors want to see metrics that demonstrate increased energy efficiency and a movement toward decarbonizing energy sources.

For many companies at the beginning of their ESG journeys, focusing on environmental issues makes sense because projects that reduce energy, emissions or waste often produce clear and tangible financial ROI. Also, environmental projects typically yield straightforward metrics to show progress.

Click here to learn more about some of the concrete environmental impacts our clients have achieved.

Table II: Environment

Topic	Framework Frequency
Emissions (GHG)	6/6
Emissions (other air emissions)	6/6
Energy	6/6
Waste	6/6
Supply chain*	6/6
Climate risk	5/6
Materials	4/6
Water	4/6

**included in both Environmental and Social list*

SOCIAL TOPICS

Although data on the benefits of pursuing social issues has been slower to develop, investors are starting to pay more attention to this area. Our research shows that investors are scoring companies on their labor management practices and overall work environment, including health and safety, training and education, and diversity and inclusion. Investors are expecting companies to establish policies against the use of child labor and forced labor as well as policies and management systems that promote workforce diversity and inclusion and that keep workers safe and healthy. In most cases, investors are expecting measurable goals and milestones.

In our work with companies over the past seven years, we have seen businesses struggle with programs and key performance indicators (KPIs) in many of these social areas. As a result, companies often receive low social scores from investor rating agencies.

Some companies have implemented initiatives but have not yet set measurable targets. Other companies might be unwilling or unable to disclose metrics in their sustainability/ESG reports; this is often the case with regard to health and safety. In some areas, such as diversity, equity and inclusion (D, E & I), businesses recognize that they need to address a set of issues—often as a result of employee surveys—but struggle to build consensus internally on what these programs should look like or which data to track. D, E & I has emerged as a major issue amid the growing Black Lives Matter movement and recent data highlighting the lack of diversity in corporate leadership. As a result, companies are reevaluating their role in perpetuating racism both internally and externally. Going forward, we hope to help companies develop practices and metrics that address the root causes of these issues.

Although the topic of managing supply chains in environmentally and socially responsible ways is on our overall "top 10" list, we see many companies struggling to determine how they should tackle these objectives and what to disclose. Human-rights issues and climate-related natural disasters have plagued major supply chains around the globe for years, and now a global health pandemic is further disrupting supply chains. Even so, many of our clients face challenges convincing internal stakeholders to take action, such as by investing in programs that will allow the company to manage supply chains in more environmentally sound and socially responsible ways.

Table III: Social

Topic	Framework Frequency
Labor management and practices	6/6
Occupational health and safety	6/6
Diversity and inclusion	6/6
Employee benefits and retention	6/6
Employee training and education	6/6
Supply chain*	6/6
Non-discrimination	5/6
Public policy/political contributions	5/6
Customer health and safety	5/6
Local communities	4/6
Marketing and labeling	4/6
Customer privacy	4/6

**included in both Environmental and Social list*

GOVERNANCE TOPICS

While no governance issues made our overall "top 10" list, several appeared in 5 out of 6 frameworks.

Investors remain interested in whether a company has a board committee focused on corporate social responsibility, as well as in the composition of the board as it relates to various diversity aspects such as race, gender, age, and professional experience and skills. We also see that investors have been looking at linkages between remuneration and compensation policies and processes and ESG or other non-financial targets, as well as transparency around payment philosophy and performance.

Table IV: Governance

Topic	Framework Frequency
Governance structure and composition	5/6
Anti-corruption	5/6
Remuneration/compensation policies and process	5/6
Grievance mechanisms	4/6
Board ESG role/responsibility	4/6
Conflicts of interest	4/6
Anti-competitivebehavior	4/6
Tax Approach, Governance, and Disclosure/Transparency	4/6

Where are We Headed?

Since the beginning of the global health pandemic in early 2020, many questions have arisen about whether investors will continue to focus on ESG issues as we fall into an economic recession. Experts ranging from UBS to CitiBank to Blackrock echo a resounding "yes." In fact, most investor representatives tell us that ESG issues will become more important. The data are starting to show that companies with robust ESG strategies and metrics are more resilient and have fared better during this crisis.

The pandemic has brought inequities in remuneration and pay policies to the forefront as low-wage, front-line workers are furloughed or fired while CEOs receive bonuses. Companies' health and safety and training practices are also under greater scrutiny. In addition, racial equity issues that have surfaced as a result of both COVID-19 and the Black Lives Matter movement will likely become increasingly important as investors assess whether companies are well-positioned for the future.

Conclusion

Companies across all industries are likely to be asked about a number of key topics by investors who are engaging on ESG. While we strongly urge every company to conduct its own materiality assessment and research to determine the right set of material issues and metrics to disclose, our "top 10" topics can serve as a starting point alongside the list of key governance topics. We are interested in seeing how future investor surveys and questionnaires will reflect the new reality brought about by COVID-19 and the social justice movements sweeping the globe.

Methodology and References

Our research included reviewing investor frameworks, surveys, and guidance to understand which topics were of interest to which investor entity. We then calculated the number of times a topic or indicator appeared across multiple frameworks and surveys. Totals for each topic were ranked to determine which topics appeared most often.

Table V: ESG Frameworks and Surveys Analyzed

Name	Type of Framework	Description and/or link to referenced material
SASB	Voluntary disclosure[1]	Materiality Map, Standards
MSCI	Rating agency[2]	MSCI ESG Ratings Methodology
ISS	Rating agency	Environmental & Social Key Issues, Governance Tech Doc
Sustainalytics	Rating agency	Industry-Specific Questionnaire
Vigeo-Eiris	Rating agency	Industry-Specific Questionnaire
BlackRock	Investor[3]	BlackRock does not have a survey or questionnaire but provides guidance on its primary interests at Investment Stewardship Engagement Priorities

We recognize that these entities do not play the same exact role in the ESG investing and rating world, and that they might have widely divergent methodologies for measuring and weighting these issues for their assessment of corporate ESG factors. Because some of our analysis is based on industry-specific questionnaires, it might not represent a complete picture of the included rating agencies. Also, BlackRock has no public scoring or rating system but does publish guidelines for topics upon which it engages companies in its portfolio.

[1] *Voluntary disclosures are guidance frameworks that provide recommended reporting topics and metrics to assist companies determine how to best prioritize and communicate ESG topics that are relevant to their business. Disclosure topics can be related to both financial and non-financial performance.*

[2] *Rating agencies are third-party data aggregators. Companies are assessed based on publicly available information, such annual filings, sustainability reports, company websites, publicly available company policies, and media sources. The data may be made public or made available exclusively for the company.*

[3] *Investors are companies such as asset managers who invest on behalf of others and engage directly with companies.*

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