

# Unigestion **ESG SCORE**

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March 2023

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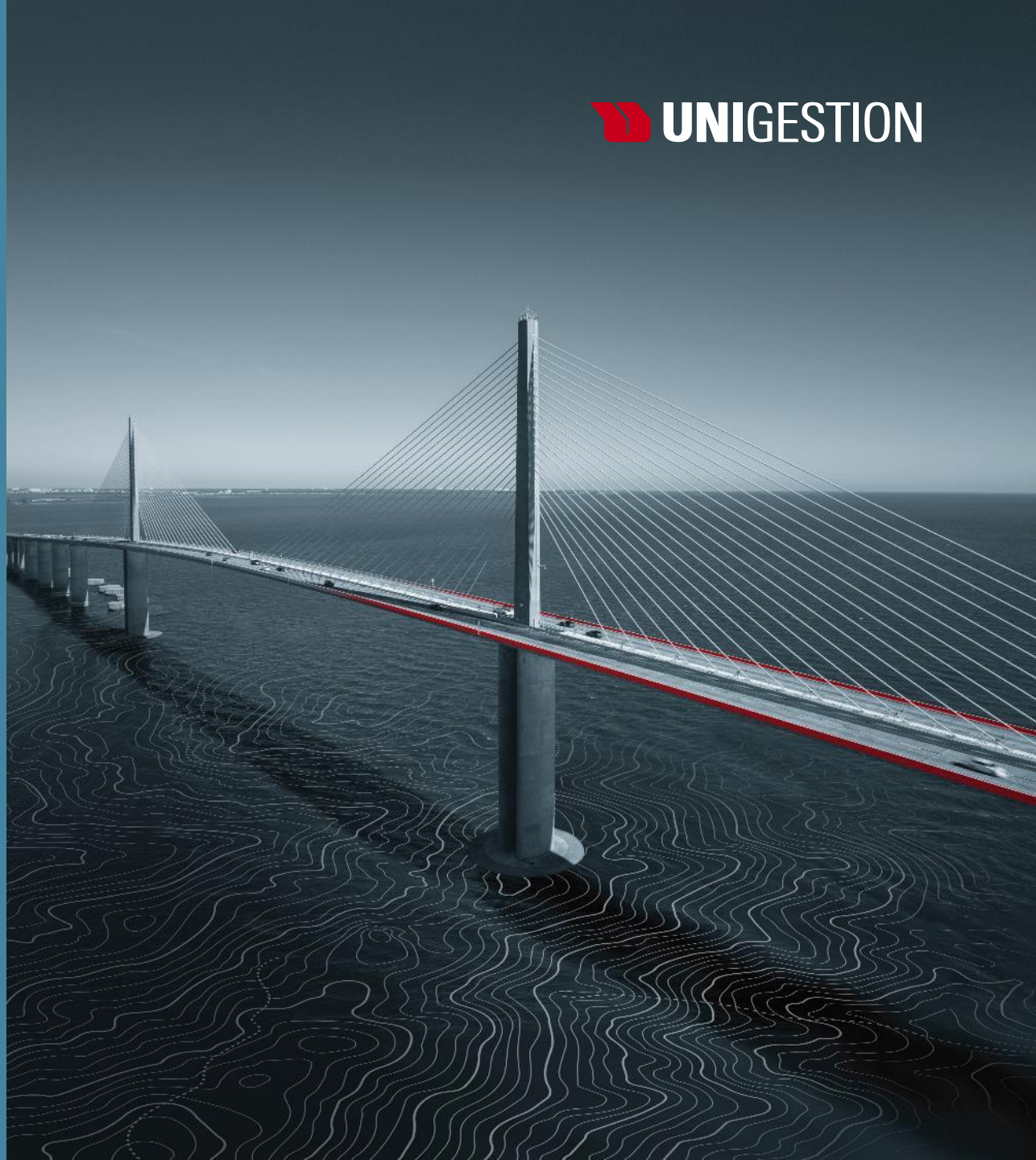
# EXECUTIVE SUMMARY

- ▶ Follows proprietary methodology informed by the widely recognised sustainability accounting standards of Sustainability Accounting Standards Board (SASB)
- ▶ Takes into account the financial materiality of ESG issues
- ▶ Measures the proportion of a company's exposure towards ESG risks that are effectively managed
- ▶ Can be disaggregated into E, S and G components
- ▶ ESG score is between 0 and 100, where 100 is best



# Company-Level ESG Score

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# SUSTAINABILITY ACCOUNTING STANDARDS BOARD (SASB)

*The Sustainability Accounting Standards Board (SASB) is an independent non-profit, whose mission is to develop and disseminate sustainability accounting standards that help public corporations disclose material, decision-useful information to investors. That mission is accomplished through a rigorous process that includes evidence-based research and broad, balanced stakeholder participation.*

**Idea: just as IASB & GAAP are used as reporting standards for financial statements, SASB establishes industry specific ESG disclosure standards. These standards are voluntary.**

Guiding Principles:

1. Global applicability
2. **Financial materiality**
3. Approach to standard setting
  - Industry specific
  - Evidence based
  - Market informed



SASB's emphasis on **financial materiality** is what sets it apart from other sustainability reporting standards.

Source: SASB



# SASB MATERIALITY MAP

- ▶ **26** sustainability-related business issues, or **General Issue Categories** (GICs), which are grouped into **5 dimensions**: Environment, Social Capital, Human Capital, Business Model & Innovation and Leadership & Governance.
- ▶ A set of reporting/rating metrics or **Accounting Metrics** (AMs) for each GIC. These can be more than one AM per GIC.
- ▶ SASB standards inform which GICs are financially material for a company in a given SASB industry and the relevant metrics used for our ESG assessment.
- ▶ SASB classification comprises **11 Sectors** and **77 Industries**, where sectors are close to GICS1 and industries to GICS2 or GICS3.

Source: SASB



# ESG SCORE CONSTRUCTION

## Top Down

- ▶ Our ESG view is based on measuring the proportion of a company's exposure to ESG risks that are effectively managed.
- ▶ ESG risk exposure score is at subindustry level (close to GICS4).
- ▶ Management of ESG risk is scored using SASB's standards, which allows us to calculate the proficiency of a company at managing their ESG risks.
- ▶ For simplicity, we refer to this as ESG Risk Score.

$$UNG\ ESG\ Score = 100 - exposure * \left( 1 - \frac{ESG\ Risk\ Score}{100} \right)$$

$$ESG\ Risk\ Score = w_E * E * cv_E + w_S * S * cv_S + w_G * G * cv_G$$

E, S and G are dimension scores

cv is the controversy adjustment

w is the weight of dimension in the ESG Risk Score



# ESG SCORE CONSTRUCTION

## Bottom up

**Step 1:** We compute a General Issue Category (GIC) score for the company for each material GIC, using relevant in-house indicators. SASB standards inform which GICs are financially material for a company, based on its SASB industry.

**Step 2:** GIC scores are combined into 5 SASB dimensions: Environment, Social Capital, Human Capital, Business Model & Innovation and Leadership & Governance.

**Step 3:** 5 SASB dimensions are grouped into Environment, Social and Governance dimensions and penalised by corresponding controversies

**Step 4:** E, S and G dimensions are combined into an ESG Risk Score

**Step 5:** ESG Risk score is combined with subindustry level ESG risk exposure to give final Unigestion ESG score







# STEP 1: CALCULATING GIC SCORES

## Example: Oil & Gas Exploration & Production, calculating Air Quality GIC Score

- ▶ SASB standards inform which general issues are material for a company in Oil & Gas Exploration & Production industry
- ▶ We choose metrics closest to those stipulated by SASB and take their arithmetic average to compute a GIC score

Dimension	Material General Issue Category (GIC)	Account Metrics
Environment	<ol style="list-style-type: none"> <li>1. GHG Emissions</li> <li>2. Air Quality </li> <li>3. Waste &amp; Hazardous Materials Management</li> <li>4. Ecological Impacts</li> </ol>	Air emissions of the following pollutants: NOx (excluding N2O), SOx, volatile organic compounds (VOCs) and particulate matter (PM10)
Social Capital	Human Rights & Community Relations	<b>Unigestion Metrics</b> <ul style="list-style-type: none"> <li>▶ Nitrogen oxide emissions</li> <li>▶ Sulfur dioxide emissions</li> <li>▶ VOC emissions</li> </ul>  <p>Air Quality Score is the arithmetic average of the Unigestion Metrics, rescaled to a score from 0 to 100, where 100 is best</p>
Human Capital	Employee Health & Safety	
Business Model & Innovation	Business Model Resilience	
Leadership & Governance	<ol style="list-style-type: none"> <li>1. Business Ethics</li> <li>2. Management of the Legal &amp; Regulatory Environment</li> <li>3. Waste &amp; Hazardous Materials Management</li> <li>4. Critical Incident Risk Management</li> </ol>	

Source: Unigestion, SASB



# STEP 2: CALCULATING SASB DIMENSION SCORES

## Example: Commercial Banks

- ▶ If SASB considers any dimension to be financially immaterial for a given industry, we substitute it with a proxy.
- ▶ Proxies are constructed using all available metrics relevant to the SASB dimension topic.

Dimension	Material General Issue Category (GIC)	
Environment	None	→ Substitute with Environment proxy
Social Capital	<ol style="list-style-type: none"> <li>1. Data Security</li> <li>2. Access &amp; Affordability</li> <li>3. Selling Practices &amp; Product Labelling</li> </ol>	
Human Capital	None	→ Substitute with Human Capital proxy
Business Model & Innovation	Product Design & Lifecycle Management	
Leadership & Governance	<ol style="list-style-type: none"> <li>1. Business Ethics</li> <li>2. Systemic Risk Management</li> </ol>	

$$SASB\ Dimension\ Score = \frac{1}{n} \sum_{i=0}^n x_i$$

$n$  is number of Material GICs in a given dimension  
 $x_i$  is the  $i$ th GIC score in a given dimension

Source: Unigestion, SASB



# STEPS 3–4: SASB DIMENSION GROUPING & ESG RISK SCORE CALCULATION

## Example: Building Products & Furnishings

- ▶ Weight of SASB dimension is determined by the proportion of material GICs attributed to the dimension
- ▶ Controversy adjustment is applied at the ESG dimension level

ESG Dimension	SASB Dimension	Material GIC	# Material GICs	
Environment (E)	Environment (E)	Energy Management	1	
Social (S)	Social Capital (SC)	Product Quality & Safety	1	
	Human Capital (HC)	None	1	→ Substitute with Human Capital proxy, which counts as 1 GIC
Governance (G)	Business Model & Innovation (BMI)	1. Product & Lifecycle Management 2. Supply Chain Management	2	
	Leadership & Governance (LG)	None	1	→ Substitute with Leadership & Governance proxy, which counts as 1 GIC
			Total: 6	

$$ESG Risk Score = w_E * E * cv_E + w_S * S * cv_S + w_G * G * cv_G =$$

$$= \frac{n_E}{N} * E * cv_E + \left( \frac{n_{HC}}{N} * HC + \frac{n_{SC}}{N} * SC \right) * cv_S + \left( \frac{n_{BMI}}{N} * BMI + \frac{n_{LG}}{N} * LG \right) * cv_G$$

n is the number of material GICs per SASB dimension (in the example  $n_E=1, n_{HC}=1, n_{SC}=1, n_{BMI}=2, n_{LG}=1$ )

N is the total number of material GICs (in the example  $E=6$ )

Source: Unigestion, SASB



# CONTROVERSY ADJUSTMENT

Controversies are applied at the ESG dimension level:

- ▶ **Environment:** Operations Incidents, and Product & Service Incidents
- ▶ **Social:** Customer Incidents, and Society & Community Incidents, Employee Incidents
- ▶ **Governance:** Social Supply Chain Incidents, and Environmental Supply Chain Incidents, Business Ethics Incidents, Governance Incidents, and Public Policy

There are 5 levels of controversy, from 1 to 5, with 5 being the most severe. Each level deducts a certain percentage off the dimension's score:

Controversy Severity	Penalty
1 (Marginal Impact)	2.5%
2 (Low Impact)	5%
3 (Medium Impact)	7.5%
4 (High Impact)	20%
5 (Severe Impact)	30%

$$\text{Controversy Adjustment} = (1 - \sum_{i=0}^5 c_i)$$

Source: Sustainalytics, Unigestion





# MANAGEMENT DECISION SETUP

- ▶ **Decision 1:** Excluding non-covered companies (Bottom-up/Signal)
- ▶ **Decision 2:** Excluding worst-in-class: Companies with ESG score below 60 of the universe with negative trend (Bottom-up/Signal) (ESG scores are 0-100, 100 being the best)
  - Trend definition: average short term (6 months) score compared to average long term (24 months) score

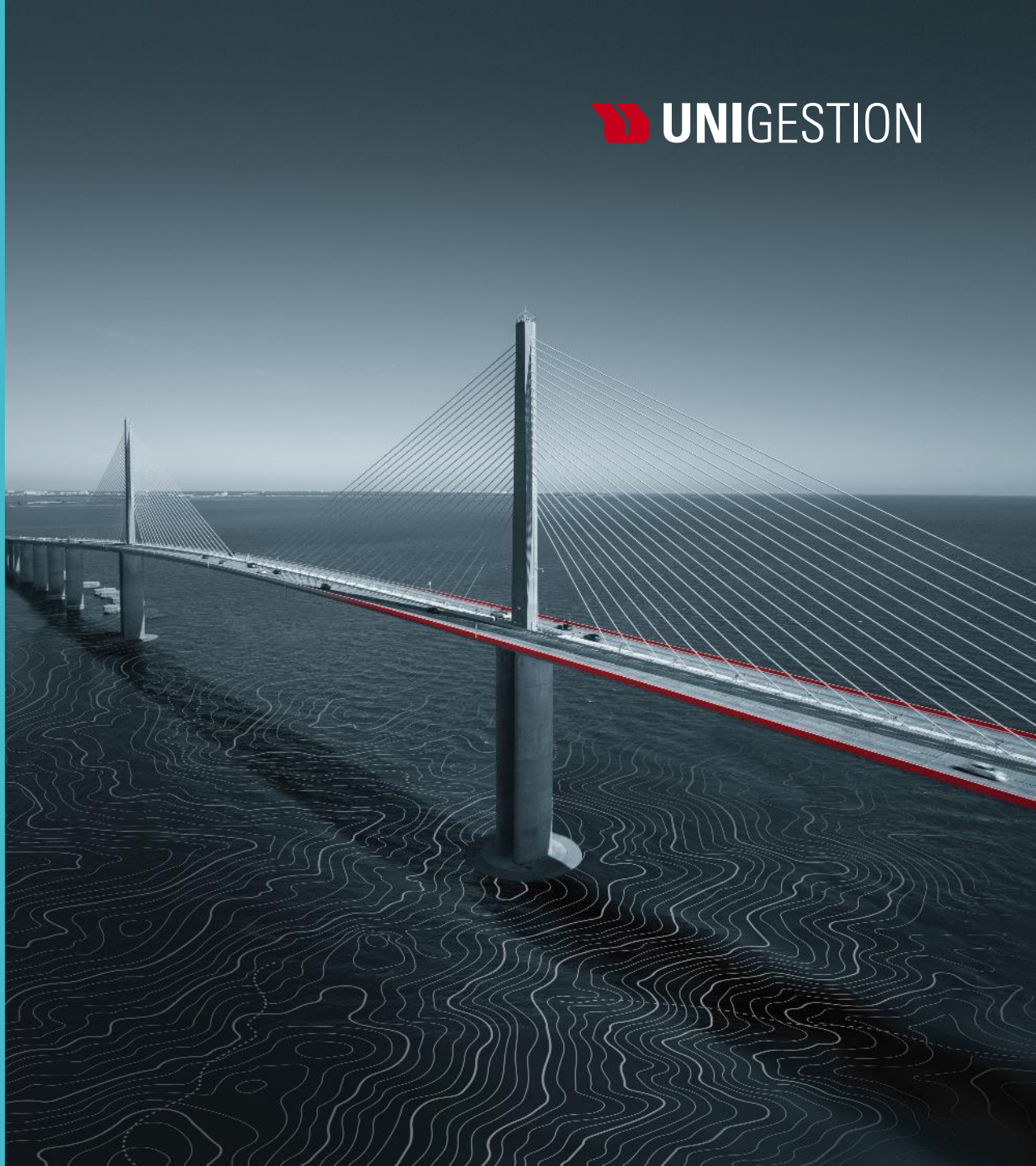
	Point 1	Point 2	Trend
<b>Definition</b>	$\frac{1}{6} \sum_{i=0}^6 ESG_{(T-i M)}$	$\frac{1}{24} \sum_{i=0}^{24} ESG_{(T-i M)}$	Point 1 – Point 2

- ▶ **Decision 3:** Overall portfolio ESG score higher than the index whose worst quintile has been excluded, based on ESG score rank over the investment universe. (Top-down)



# Sovereign ESG Score

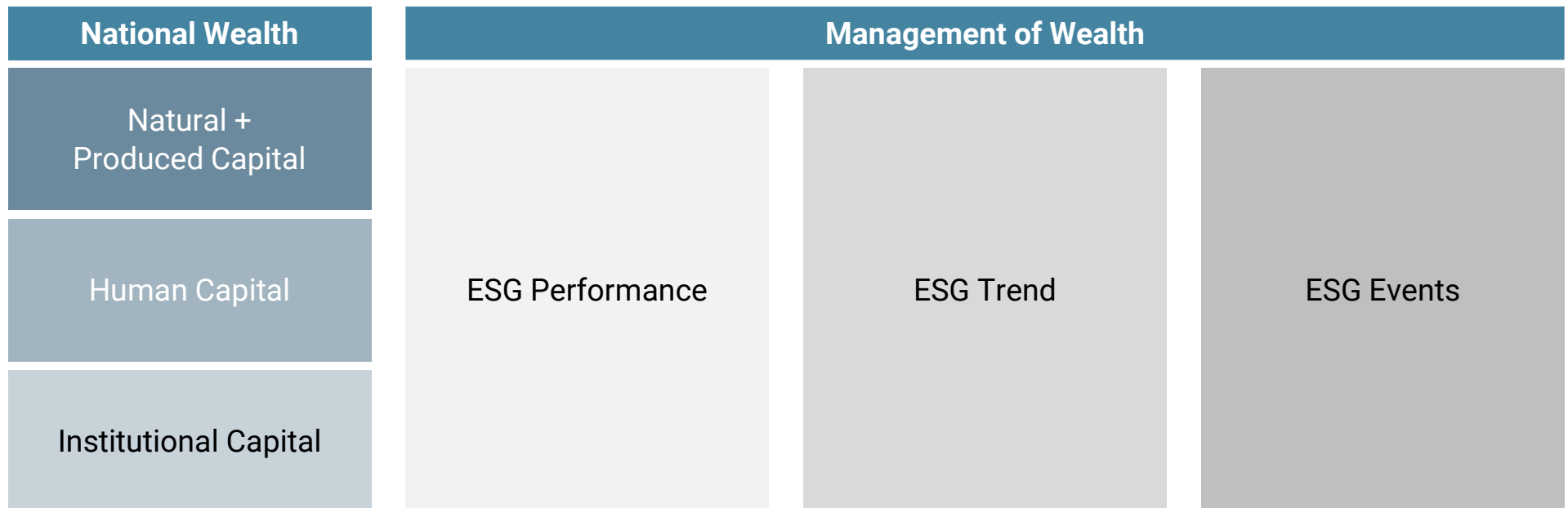
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# ESG RISK SCORE

## ► ESG Rating Components

The rating measures national wealth comprised of natural and produced capital, human capital, and institutional capital, and a country's ability to utilize and manage these capitals in an effective and sustainable manner determined by its ESG performance, ESG trends and ESG events. The aggregate score includes a wealth score and an ESG risk factors score corresponding to these two components



Sources: Unigestion, Sustainalytics





# NATIONAL WEALTH

- ▶ **Natural and Produced Capital**

The portion of natural resources, including assets like forests, water, fish stocks, minerals, biodiversity and land, that a country utilizes for its economic activity. Produced Capital includes infrastructure, machinery, etc that is produced through the economic activity of a country.

- ▶ **Human Capital**

Includes the stock of knowledge and skills among economic participants.

- ▶ **Institutional Capital**

The social and institutional infrastructure that enables the productive functioning of a society and economy. Institutional Capital is assessed to account for 15% of a nation's wealth generated from natural, physical and human capital.

# MANAGEMENT OF WEALTH

- ▶ **ESG Performance**

Country's performance with regards to key ESG indicators

- ▶ **Trends**

The evolution of ESG performance over past five years

- ▶ **Events**

Include a material incident that can have a negative impact on the wealth of the nation and/or how it is being managed. In a way it is similar to controversies for companies.

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