

# MSCI ESG Ratings

## ASX ISSUER METHODOLOGY WEBINAR

Morgan Ellis & Aaron Wei

September 2021



# Introducing MSCI ESG Research

First ESG provider to assess companies based on industry financial materiality<sup>1</sup>

**270+**  
ESG  
analysts<sup>2</sup>  
(400+ FTE)

**14,000**  
issuers in  
ESG Ratings  
coverage

**1,500+**  
ESG equity &  
fixed income  
indexes use MSCI  
ESG Research  
ratings and data

**1,700+**  
clients



<sup>1</sup> Through our legacy companies KLD, Innovest, IRRG, and GMI Ratings. ESG Ratings dating back to 1999.

<sup>2</sup> Source: MSCI ESG Research as of March 2021. Includes full time employees, employees of foreign affiliates providing investment advisory services to MSCI ESG Research LLC, and global allocated staff performing non-investment advisory tasks.

\* Representative office for business development.



**MSCI**

**The Independent Research in Responsible Investment Survey**

MSCI voted **Best Firm for SRI Research, Corporate Governance and Sustainability Indexes** for the fourth consecutive year

**WINNER**

MSCI

**2020 ESG Trends project: What are the big challenges for the new decade?**

2019  
2018  
2017  
2016/2015

ESG research report of the Year

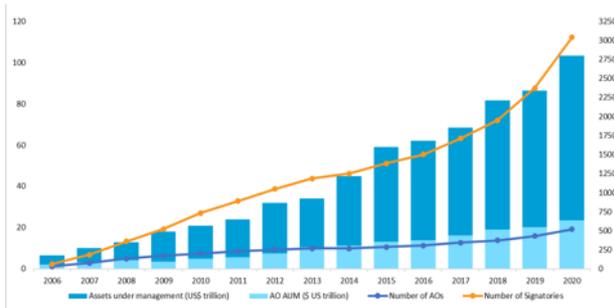
# Why ESG?

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# ESG investing is growing dramatically...why now?

**UN PRI\* Has Grown to Over 3,000 signatories in managing over \$100 trillion in AUM**



**99% CAGR in ETF AUM Tracking MSCI ESG Indexes since 2013**



## HERE'S WHY:

**1** Investors have become less tolerant of corporate ESG incidents

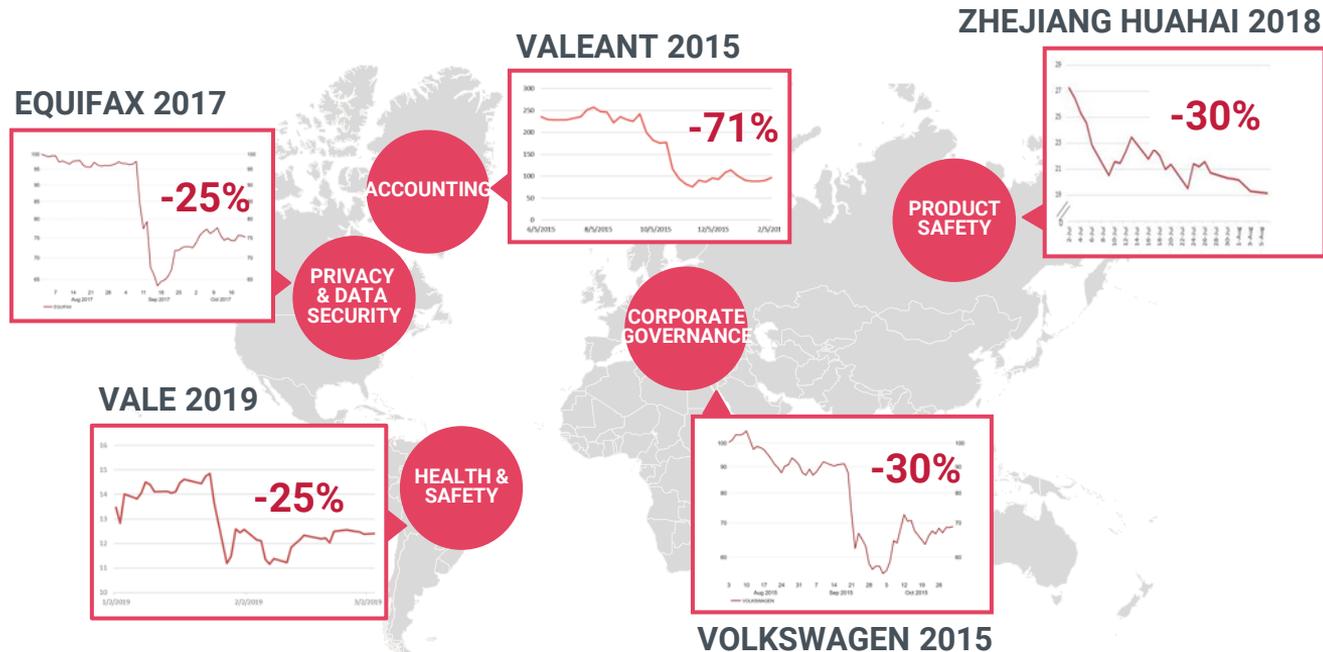
**2** Investors demonstrating willingness to act

**3** Greater understanding of ESG's influence on risk and return

**4** Technology and ESG Ratings data enhancements

# ESG incidents and stock price movements

30 years ago, Exxon's stock price barely moved when Exxon Valdez spilled 11mm gallons of oil on the Alaskan shore.\* Today, with social media allowing for immediate, global communication of issues, investors are making companies accountable for their actions.



Examples only for illustrative purposes, not indicative of future performance or necessarily representative of broader market reactions.

Information Classification: GENERAL

# ESG leaders have demonstrated increased sophistication across their organizations

## Asset owners

PENSION FUNDS

CONSULTANTS

INSURANCE

ENDOWMENTS & FOUNDATIONS

CIO OFFICE

FUND SELECTION

FINANCIAL ADVISORS

RETAIL

## Asset management

FUNDAMENTAL EQUITY

Other / product

Other / product

EMERGING

FUNDAMENTAL FIXED INCOME

ESG SPECIALIST

RISK MANAGEMENT

ACTIVE FUND

QUANT

STEWARDSHIP & GOVERNANCE

COMPLIANCE

PASSIVE FUND & ETP

Asset Managers are moving beyond fundamental equity and **integrating ESG into fixed income and quantitative** strategies with growing sophistication

**Largest consultants** are **incorporating ESG** dimensions into manager selection in reaction to Asset Owner requests

**Engagement** is becoming an important tool for improving company performance and returns

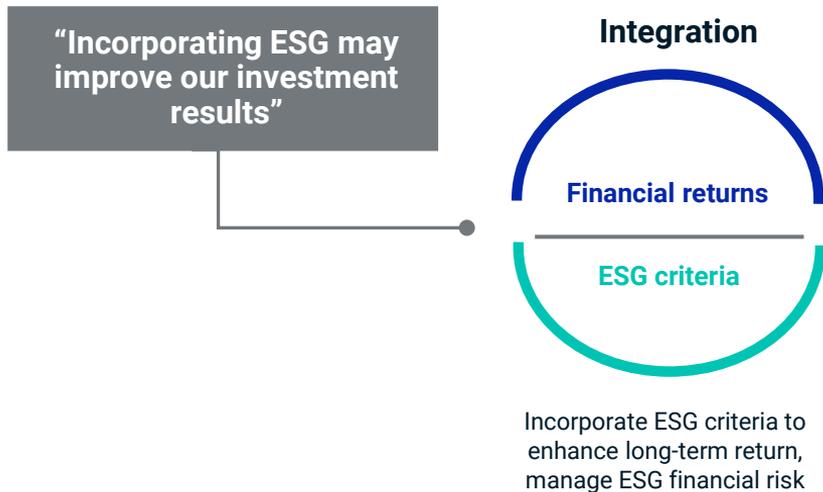
Risk teams are increasingly **systematically reporting** on ESG risk

Demand for active and passive **ESG Funds across asset classes** for total portfolio exposures

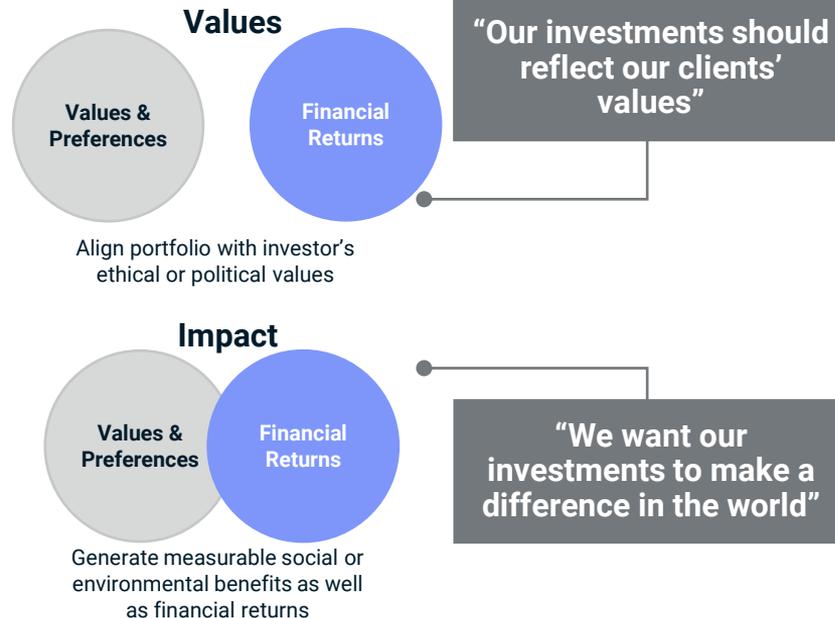
# Understanding the most common ESG objectives

Incorporating ESG into investment strategy or creating products typically starts with understanding client objectives, which may combine elements of managing long-term risk, reflecting values and positive impact.

## Investment Objectives



## Individual Objectives



# What are MSCI ESG Ratings?

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# What are ESG Ratings?

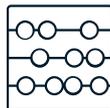
MSCI ESG Ratings aim to measure a company's **resilience to long-term, financially relevant ESG risks**

To do this we measure:

**Robustness of governance controls**, the foundation of good risk management



BOARD



ACCOUNTING



OWNERSHIP AND CONTROL



EXECUTIVE PAY

Exposure to **long-term systematic risk** factors



CLIMATE CHANGE



WATER SCARCITY



DATA SECURITY



DEMOGRAPHIC SHIFTS

**Management quality & ability to limit surprised and event risks**



ACCIDENTS



FRAUD



SHUTDOWNS



STRIKES

# Key research questions

1

## Q: How is the company governed?

How do governance structures impede / enable it to be a long-term steward of capital?

**A:** Analyze ownership structure, board, incentives and behavior.



2

## Q: What risks does the company face?

How exposed is its business model to relevant short-, medium- and long-term ESG risks?

**A:** Map company operations to an extensive proprietary database of ESG risk factors.



3

## Q: What does the company say?

What is its strategy for managing these risks? What measures has it put in place?

**A:** Benchmark company disclosures and policies vs. industry peers.



4

## Q: What does the company do?

What evidence do we see that these risks are being managed? What is its track record?

**A:** Evaluate alternative data from sources outside the company.

# Governance assessment for all companies

## Detailed analysis of:

- Shareholders and management alignment
- Relationship of governance structures, events, and corporate behavior
- Local market standards
- Business ethics policies and corruption risk
- Tax controversies



### Board

Size, director election standards, tenure and gender diversity  
Assessment of financial, industry and risk management expertise



### Pay

Robust data on CEO pay. Analysis of pay for performance link.  
Assessment of compensation committee independence



### Ownership and Control

Ownership structure, shareholder rights and key takeover defenses  
Major owners and insider holdings



### Accounting

Audit committee structure and fees paid to outside auditors. Transparency metrics tied to revenue, expense recognition, asset-liability valuation



### Business Ethics

Oversight and management of business ethics issues, involvement in business ethics controversies, and exposure to corruption risks



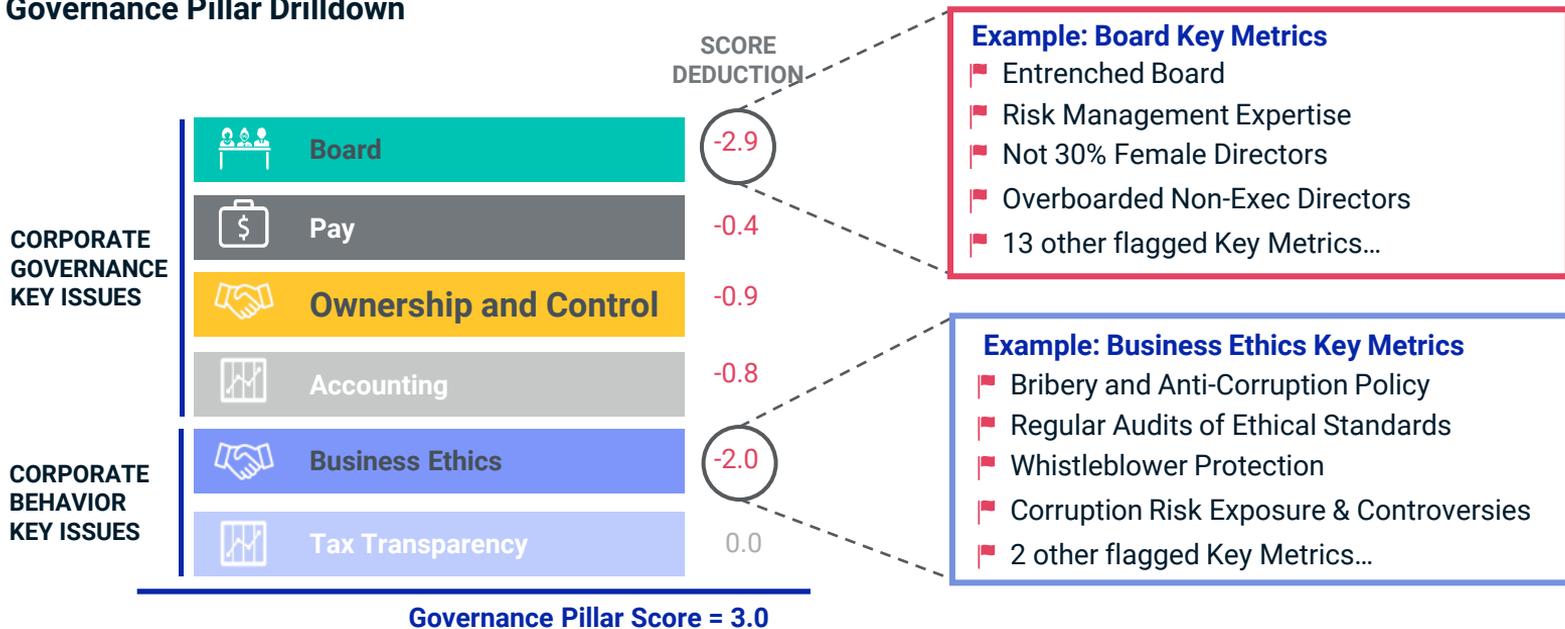
### Tax Transparency

Estimated corporate tax gap and involvement in tax-related controversies

# How is Governance assessed?

- Corporate Behavior and Corporate Governance are **assessed for all companies**
- **Key Metrics correspond to score deductions** from the Governance Pillar Score

## Example of Governance Pillar Drilldown



Governance Pillar Score = 10 – Total Score Deductions

Source: MSCI ESG Research as of March 2021

# MSCI ESG Rating model key issues

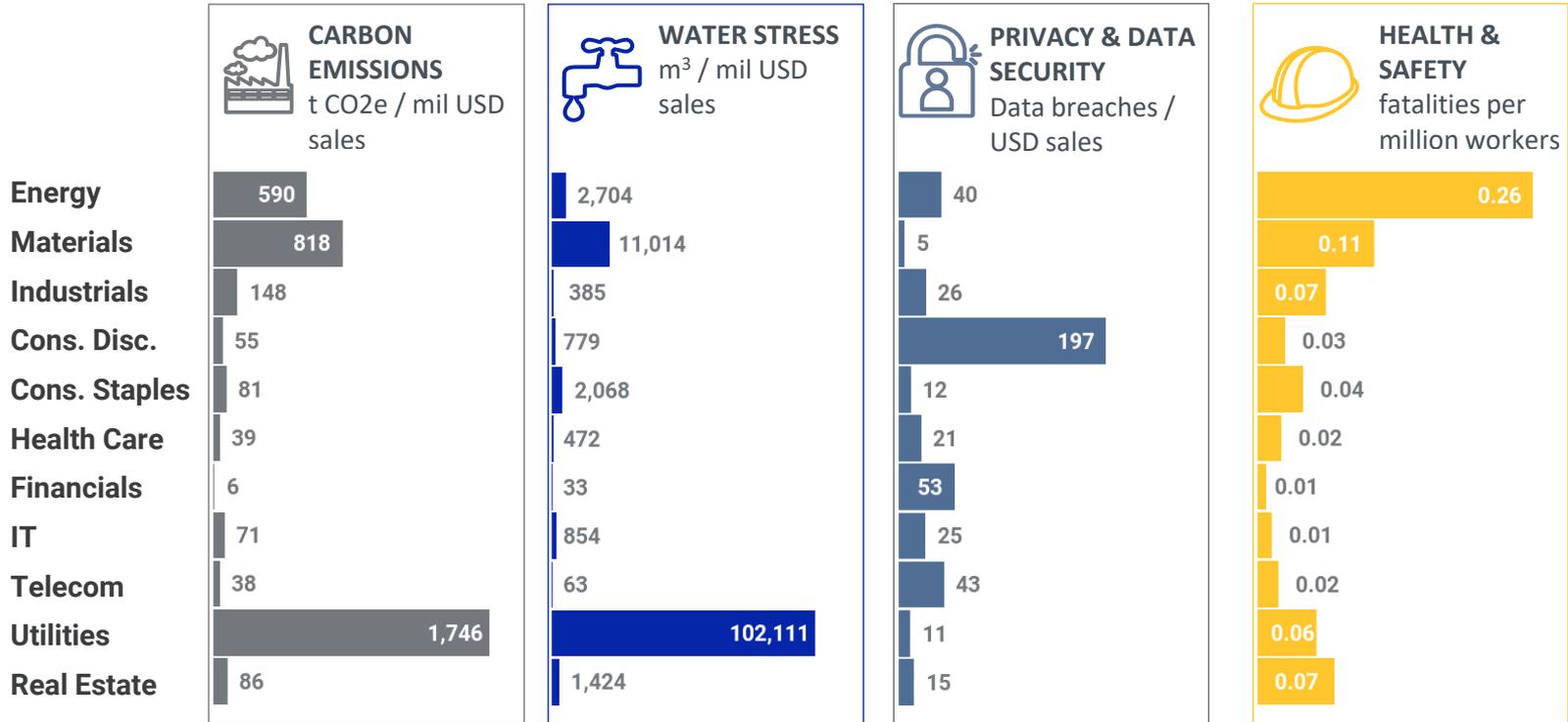
Example: Soft Drinks Sub-Industry

MSCI ESG Score									
ENVIRONMENT PILLAR				SOCIAL PILLAR				GOVERNANCE PILLAR	
Climate Change	Natural Capital	Pollution & Waste	Env. Opportunities	Human Capital	Product Liability	Stakeholder Opposition	Social Opportunities	Corporate Governance	Corporate Behavior
Carbon Emissions	Water Stress	Toxic Emissions & Waste	Clean Tech	Labor Management	Product Safety & Quality	Controversial Sourcing	Access to Communication	Board	Business Ethics
Product Carbon Footprint	Biodiversity & Land Use	Packaging Material & Waste	Green Building	Health & Safety	Consumer Financial Protection	Community Relations	Access to Finance	Pay	Tax Transparency
Financing Environmental Impact	Raw Material Sourcing	Electronic Waste	Renewable Energy	Human Capital Development	Privacy & Data Security		Access to Health Care	Ownership	
Climate Change Vulnerability				Supply Chain Labor Standards	Responsible Investment		Opportunities in Nutrition & Health	Accounting	
					Insuring Health & Demographic Risk				
					Chemical Safety				

  **Soft Drink Sub-Industry: e.g. Coca-Cola**

  **Universal key issues applicable to all industries**

# Environmental and social risks are industry-specific

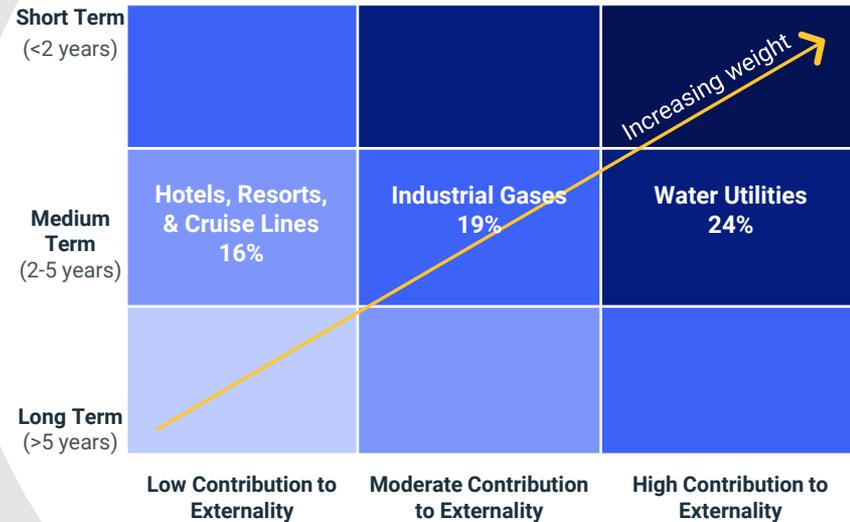


Sources: Carbon emissions and freshwater withdrawal intensities based on sample of 3,823 and 1,633 companies, respectively as of March 2, 2020. Percentage of companies with active bribery and ethics controversies is based on the number of companies with ongoing bribery & fraud controversies in the MSCI ACWI Investable Market Index (IMI) as of March 2, 2020. Fatalities per million workers calculated based on three-year average fatality rates from the Census of Occupational Injuries (US Bureau of Labor Statistics). Data breach intensity calculated based on three-year average of the number data breaches by sector (Verizon Data Breach Investigations Report) and business segments for companies in the MSCI ACWI Index as of March 2, 2020.

# Setting key issue weights

## Key issue weights are based on:

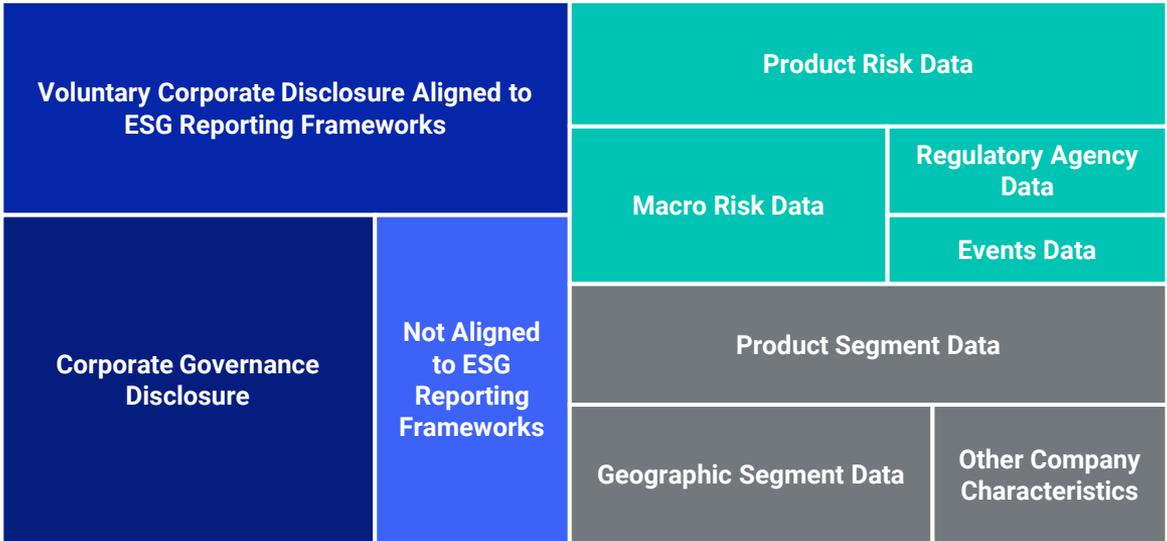
- Industry's contribution to externality vs. other industries
- Time horizon of risk factor for that industry
- Number and significance of other issues assessed
- Minimum 33% weight applied to the Governance Pillar, based on standard time horizon and impact for Corporate Behavior and Corporate Governance



# Source of data inputs into MSCI ESG Ratings, sized by % of contribution

● Company-reported ESG information
 ● Information from other sources
 ● Company characteristics

Most standardized
Least standardized



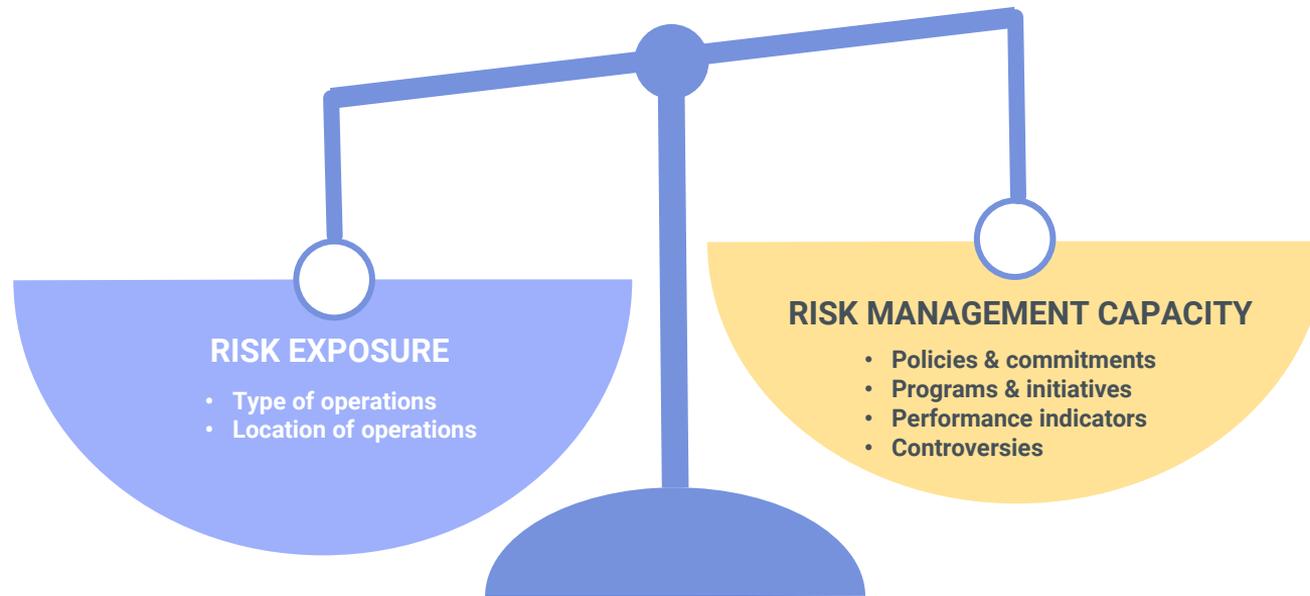
## Data Processing

- ▶ Acquire data
- ▶ Fill data gaps with proxies and estimates
- ▶ Standardize data

## Modelling

- ▶ Convert to quantifiable assessment
- ▶ Aggregate model components
- ▶ Apply weights

# Measuring ESG risk exposure



**EVALUATE RISK MANAGEMENT STRATEGY  
IN THE CONTEXT OF RISK EXPOSURE**

# How MSCI ESG Research assesses company risk management practices

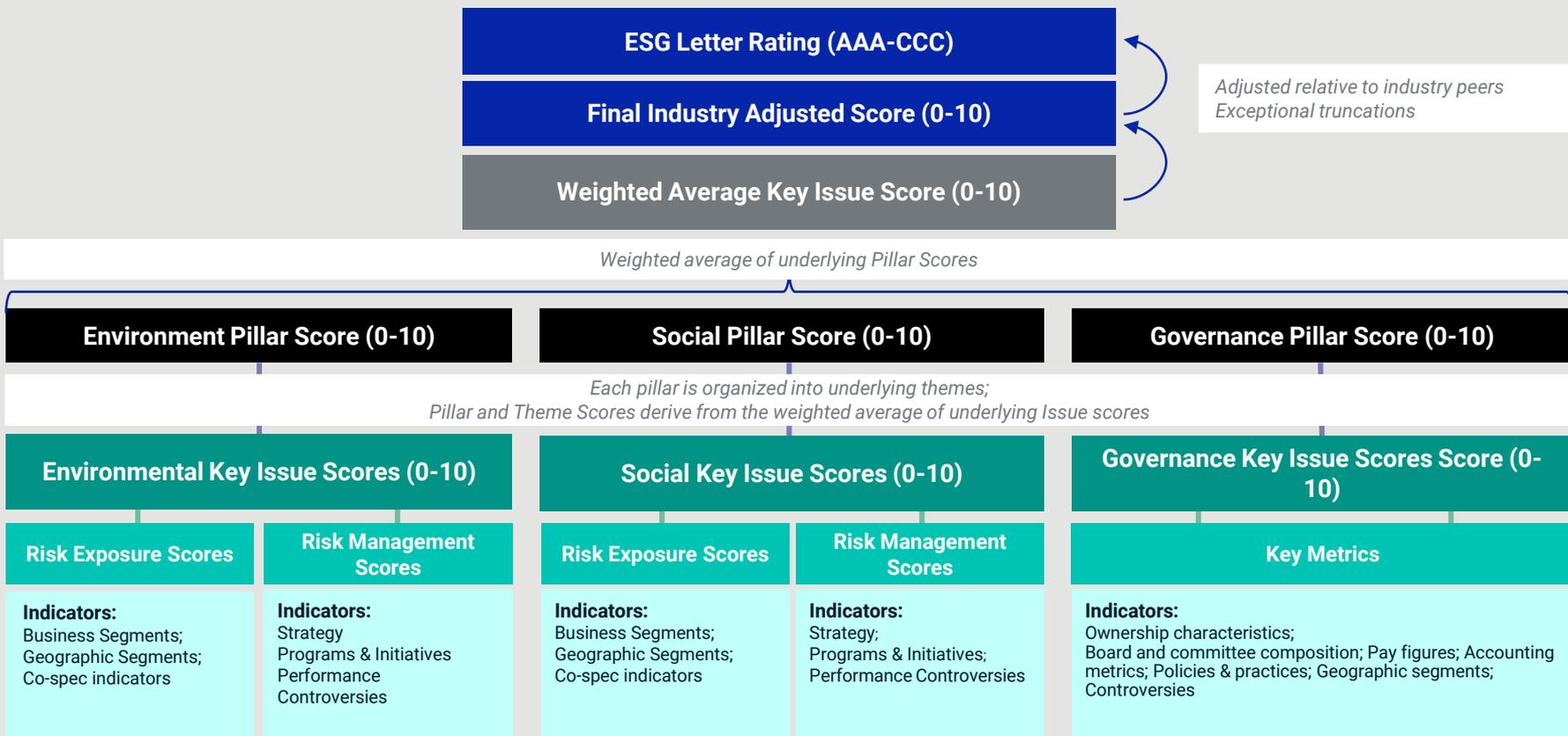
	EXAMPLE METRIC	COMPANY 1	COMPANY 2
PRACTICES	Oversight of Water Management	Board-level Committee BEST PRACTICE 	No evidence of oversight WORST PRACTICE 
	Water Reduction Target	5% annual reduction in water intensity BEST PRACTICE 	No evidence of target WORST PRACTICE 
	<b>Practices Score</b>	<b>8.5/10</b>	<b>2.0/10</b>
PERFORMANCE	Water Intensity vs. Industry Peers	21,450 m3/mil USD sales 2.1x industry average	7,150 m3/mil USD sales 0.7x industry average
	Water Intensity Trend	+2.1% CAGR (2016-2019)	-7.8% CAGR (2016-2019)
	<b>Performance Score</b>	<b>3.5/10</b>	<b>8.0/10</b>
CONTROVERSIES	Severity of Ongoing Controversies	No ongoing controversies	One <b>Severe</b> Controversy
	<b>Controversy Deduction</b>	<b>0.0</b>	<b>-2.5</b>
<b>MANAGEMENT SCORE</b>	<b>Average (Practices, Performance) - Controversies</b>	<b>6.0 / 10</b>	<b>2.5 / 10</b>

How strong are the company's programs and policies?

How effective are its programs and policies?

Do ongoing controversies indicate potential lapses in oversight?

# How the scores roll up to the final ESG Rating

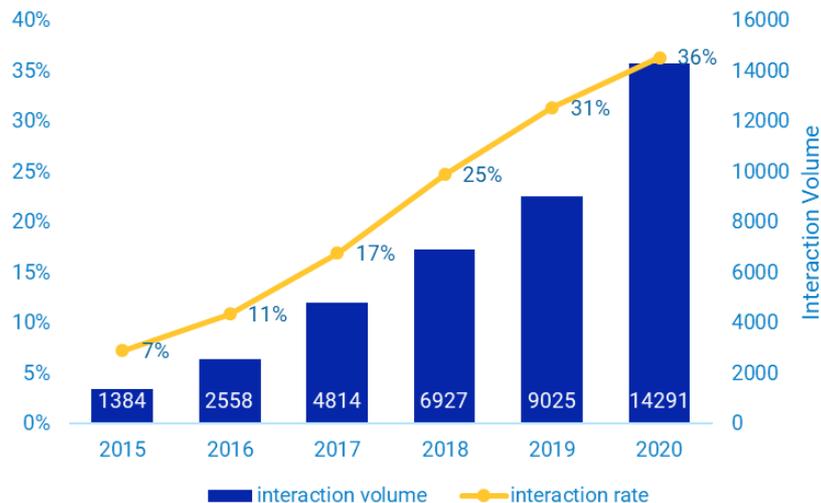


# How to Interact with MSCI

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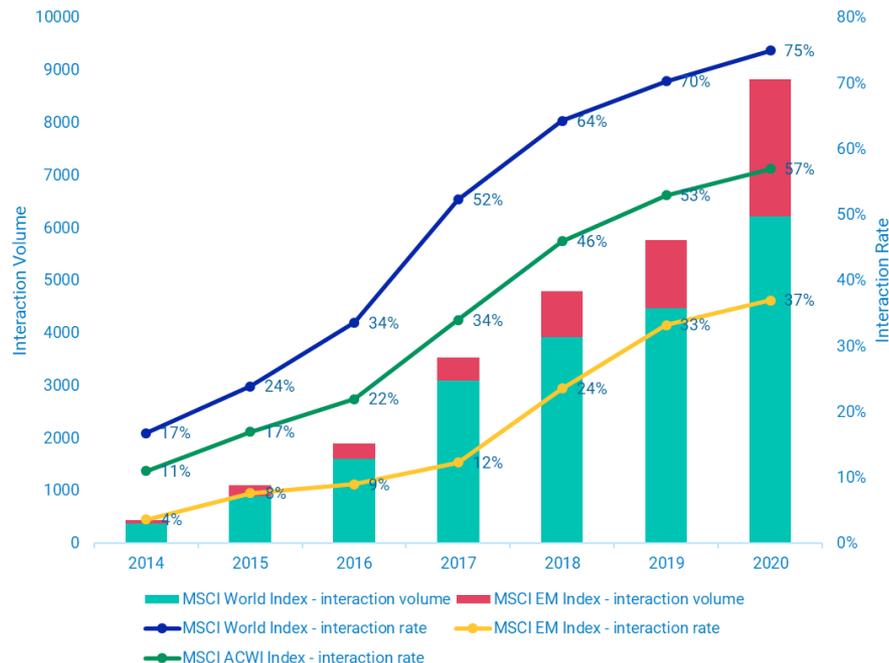
# Issuer Awareness of ESG Continues to Rise

## MSCI ACWI Investible Markets Index



Source: MSCI ESG Research LLC

## MSCI World Index vs. MSCI EM Index



\*Interaction volume includes any inbound communication from an issuer via E-mail, phone call, and queries or feedback submitted via the Issuer Communications Portal.

# Australia Issuer Interactions

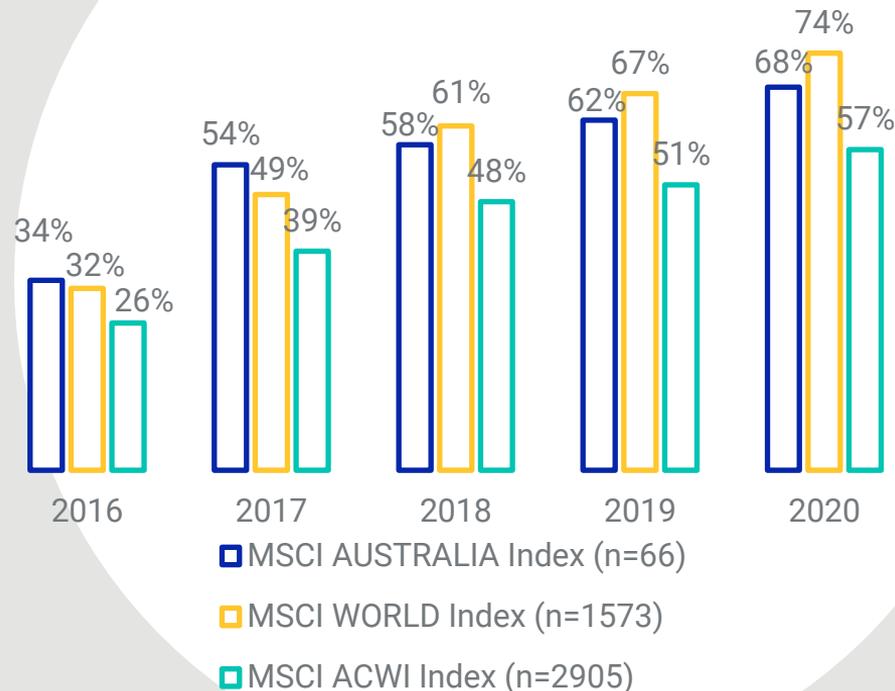
**Insights:** Australian issuers, part of the MSCI Australia Index have been steadily increasing interactions with MSCI.

Australia issued legislations<sup>1</sup> on mandatory disclosure of social and environmental information back in 2001, and energy and emissions reporting<sup>2</sup> in 2007 (amendments to this act are made annually). Australian Securities Exchange issued rules<sup>3</sup> that require disclosure on corporate governance since 2003.

## Most Active Issuers in recent two years

Issuer	Number of Interactions
Evolution Mining	34
Medibank Private	23
Origin	21
AGL	19
QBE	17
BHP	14
CBA	12
Rio Tinto	11
Mirvac	10
Scentre	10

## Issuer interaction trend



Source: MSCI ESG Research LLC, as of April 20, 2021

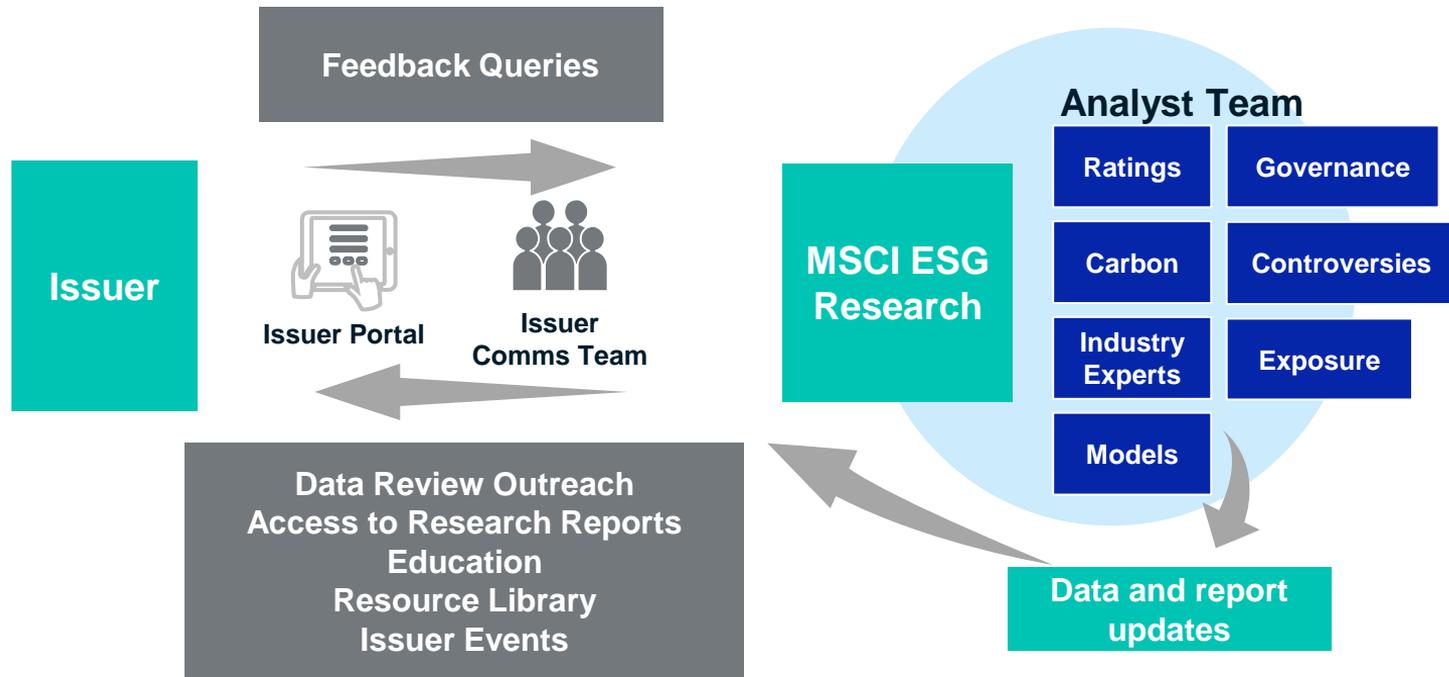
Interaction rate is the % of companies in the relevant MSCI Index that have reached out in the given year. The most active issuers are those who interacted with MSCI Issuer Communications team most frequently in recent two years.

<sup>1</sup> This Act requires the disclosure of social and environmental information on companies filing director's reports. The Corporations Act 2001. Australia Government. Last modified on Apr.4, 2021. [Source](#)

<sup>2</sup> National Greenhouse and Energy Reporting Act 2007. Australia Government. [Source](#)

<sup>3</sup> Australia Securities Exchange (ASX) Listing Rules. ASX. 2003. [Source](#)

# Typical Issuer Interaction



# Engage With Us Through Our Dedicated Issuer Portal

Our [ESG Issuer portal](#) allows companies to access their ESG Research reports at any time and make changes to their designated contact.

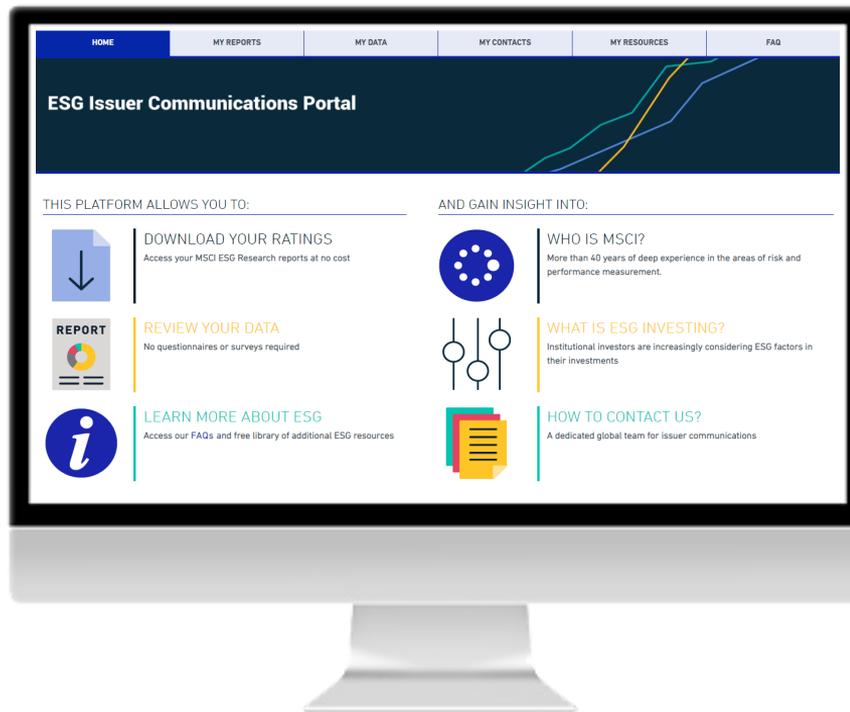
This is also where you submit feedback **at any time**.

## Additional resources

- [Issuer Portal User Guide](#)
- [www.msci.com/resources-for-issuers](http://www.msci.com/resources-for-issuers)
- [Apply to use your ESG Ratings badge](#)

## Contact us

- [esgissuercomm@msci.com](mailto:esgissuercomm@msci.com)



# Engage with us through the Issuer Communications Portal



Login to the ICP

<https://esgicp.msci.com/>

Navigation Tab

ESG Issuer Communications Portal

THIS PLATFORM ALLOWS YOU TO: GAIN INSIGHT INTO:

MSCI

LOG OUT

HELP GUIDE DATA VERIFICATION FORM - [...]

ESG Ratings	Carbon	ESG Controversies	Exposure	Governance Metrics	Screening Research	Racial Diversity	SFDR
Water Stress	Opportunities in Clean Tech	Labor Management	Human Capital Development	Privacy & Data Security	Corruption & Instability	Other Labor Metrics	Corporate Behavior

- + Weight
- + Practices
- + Performance

Submit

IMPORTANT: Please ensure that you have reviewed all relevant data prior to submitting comments. While we welcome feedback at any time. In order to avoid any confusion while processing your feedback, we kindly request that you refrain from providing additional comments until all previous submissions have been reviewed and resolved.

# Digital Data Verification Form

## Data Review Efficiency

- Standardized and consistent feedback format
- Includes only company-verifiable data
- Data pre-filled; not a survey!

Extent of certification to a widely accepted product safety / quality standard (e.g. HACCP, ISO 9001, or equivalent)

### MSCI Value

Most (over 80%) owned facilities are certified to widely accepted standards

### Issuer Value

Most (over 80%) owned facilities are certified to widely accepted standards

Most (over 80%) owned facilities are certified to widely accepted standards

Some (over 20% and below 80%) owned facilities are certified to widely accepted standards

There is some evidence of certification

Few (less than 20%) owned facilities are certified to widely accepted standards

Company intends to pursue widely accepted certification of owned facilities

No evidence

Practices

Supply chain and sourcing

Membership in recognized industry-wide partnership(s) on supply chain/contractor risk evaluation and mitigation Not disclosed

Conducts supplier training on quality assurance

Frequency of supplier training Training is on an ad hoc as-needed basis or

Scope of supplier training Some suppliers

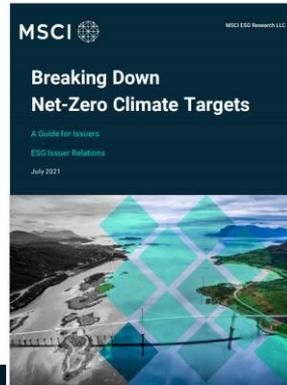
## Metric Transparency

- Better understand MSCI ESG Research assessment criteria
- Submit feedback with public evidence

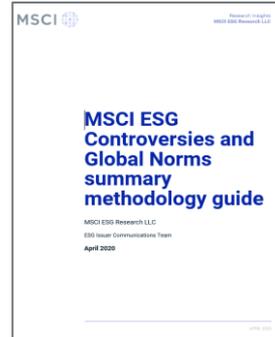
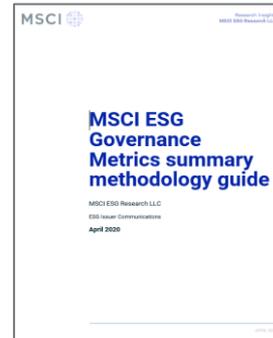
# Additional resources available through the portal

- Visit the “My Resources” tab for access to on-demand webinars, methodology and more

## FAQs and ‘How To’ Guides



## Summary Methodology Guides



## What goes into an ESG Rating?



## [Watch the MSCI ESG Ratings video](#)

### ALSO:

- Webinar recordings
- Relevant ESG thought leadership content from MSCI ESG Research
- And more!

# Our ESG Issuer Communications Commitment



## Independence

- No advisory or consulting



## Consistency

- Systematic outreach to issuers
- Standard data review process



## Traceability

- Use of publicly available data
- No confidential information



## Transparency

- Issuer access to data and own reports at no cost
- Record of all interactions



*For all inquiries related to your company's ESG data and assessments, the ESG Issuer Communication team is your main point of contact.*

*Get in touch:*

*[esgissuercomm@msci.com](mailto:esgissuercomm@msci.com)*

**Q&A**

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