

Biggest Energy Transition Risks Lie in Policy and Data Realms, Say Fixed-Income Asset Manager ESG Leads in Ratings' Spring ESG Leadership Council

What are the biggest risks in energy transition faced by institutional fixed-income investors?

Inconsistent policies globally as well as consistency and depth of data, according to the results of a poll of the senior heads of sustainability at buy-side investment firms at the Spring ESG Leadership Council, organized by S&P Global Ratings' Americas Market Outreach team.

More specifically, these ESG leaders cite "Different policies to help facilitate the transition to carbon-neutral by sector and country" and availability of "Asset-level data to understand multinational exposures with operations exposed to various climate change regulations" as equally important top concerns. Other risks include forecasting of carbon taxes and emissions trading schemes, and measuring the impact of transition plans, according to these leaders, who have direct oversight into the ESG processes at their firms.

The ESG Leadership Council was organized in two parts: (1) An analytical update led by the Americas Head of Market Outreach and (2) an investor discussion update, led by the Global Heads of Sustainable Finance Business and Innovation at S&P Global Ratings and ESG Product Innovation and Analytics with S&P Global Sustainable1, the company's new ESG and sustainability organization.

Ratings' Sustainable Finance team members discussed with the investors a key emerging topic in sustainable finance: Biodiversity and the impact on businesses of nature loss. They also shared views on physical risk in credit analysis and briefed participants on the planned ESG Indicators, along with a refresher on the longstanding surveillance of material ESG factors in credit ratings.

S&P's ESG Leadership Councils, like its Investor Councils and sector-focused Roundtables, are organized around topics and questions of most interest to the investors participating. Topics discussed at this session included:

- Whether the "G" of ESG in credit ratings is viewed through the bondholder lens or more broadly: some management actions may not be viewed as good governance practices by minority equity holders, but bondholders may benefit.
- The introduction of ESG indicators, including current plans for calibration and rollout across sectors as opposed to a sector-by-sector approach.
- The tensions for asset owners who support the energy transition away from carbon-emitting sources by owning renewable energy securities but face higher risks and capital charges for doing so.

- A discussion of investor firms' strategies on investment in polluting industries: whether to withdraw from those industries or continue to invest in and engage with companies in support of their energy transition.
- Impact reporting, and the expectation that investors' institutional clients will soon start demanding this of fund managers.
- Factoring physical risks into public finance ratings and why similarly rated issuers can have very different physical risks.
- The data gap that exists between more-widely-reported and measured "E" factors versus "S" and "G" factors.

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