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Environmental, Social, And Governance (ESG) Evaluation

XYZ Cement Co. Ltd.

Executive Summary

XYZ Cement Co. Ltd. (XYZ) is one of the largest cement producers in the world, with operations mainly based in ABC Country. XYZ's products include cement, clinker, aggregate, and concrete. The company is also expanding business operations to Southeast Asia and other regions.

The company's ESG Evaluation score of 64 mainly reflects high sector-related ESG risk exposure. On the other hand, as the industry leader in ABC, the company's strong initiatives and leadership in environmental protection and efficient energy consumption amid the country's ongoing supply-side reform supports its environmental assessment. The final score also reflects XYZ's strong customer satisfaction, strong engagement in community activities, and satisfactory management and governance. Stronger controls for production safety and water management could further improve its overall ESG Profile.

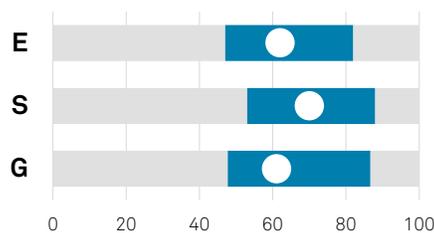
The company had three ESG incidents related to water quality management, production safety and cyber in recent years, which have caused regulatory fines and casualties. We do not expect these incidents to have a material impact on XYZ's financial performance, but we do expect the company to increase expenditures to prevent these incidents from happening going forward.

No material score adjustments for General Factors were made.

Entity	XYZ Cement Co. Ltd.
Location (HQ)	ABC Country
Primary Operation Location(s)	ABC Country
Publication date	April 11, 2019
Primary Contact	
Secondary Contact	

Profile Score

64/100



Preparedness Opinion

Adequate

Awareness:	Good
Assessment:	Good
Action:	Good
Culture:	Good
Decision-making:	Excellent

ESG Evaluation



A higher score indicates better sustainability

Company-specific attainable and actual scores

Component Scores

Environmental Performance			Social Performance			Governance Standards		
Sector/Region Risk Level		32/50	Sector/Region Risk Level		38/50	Sector/Region Risk Level		22/35
 Greenhouse Gases	Good		 Workforce & Diversity	Good		 Structure & Oversight	Good	
 Waste	Good		 Safety Management	Lagging		 Code & Values	Good	
 Water	Good		 Customer Engagement	Strong		 Transparency & Reporting	Good	
 Land Use	Good		 Communities	Strong		 Cyber Risks & Systems	Good	
 General Factors (optional)	None		 General Factors (optional)	None		 General Factors (optional)	None	
E Profile (30%)		62	S Profile (30%)		70	G Profile (40%)		61

ESG Profile (incl. any adjustments)

64/100

Preparedness Summary

We view XYZ's preparedness as Adequate. In our view, XYZ is aware of the impact of its operations on climate change and environmental pollution, especially as the government tightens environmental protection controls and public scrutiny intensifies. The company has strengthened environmental standards and developed energy recycling and conservation technologies. We expect the integration of an ESG culture to continue and to further improve throughout the company's reporting ranks and business operations. We expect the company to continue to lead the industry in terms of technological upgrades, increasing environmental standards, and efficient energy consumption.

Preparedness Opinion

Adequate

ESG Evaluation

ESG Profile	64/100
Preparedness Opinion	Adequate (No impact)
Further Adjustment (if any)	0

64/100

ESG Profile

64/100

Overview

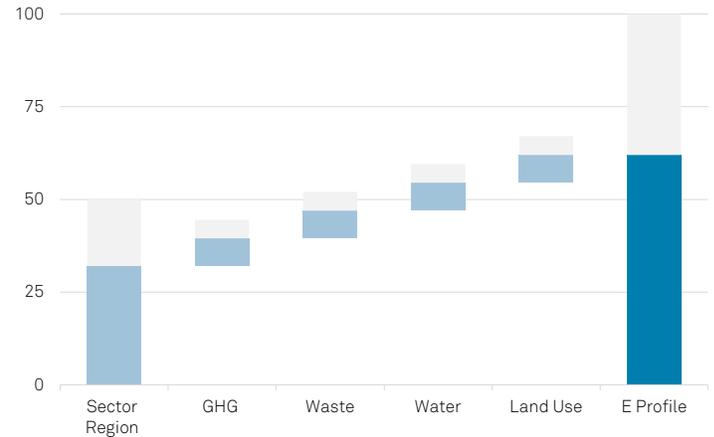
XYZ's Environmental Profile is typical of its sector. Only Scope 1 greenhouse gas (GHG) emissions are tracked, but this is the most material scope for cement producers. The company has relevant policies in place and complies with common conventions. The company has also tried to mitigate its exposures by developing or testing new technologies. There are biodiversity and land use risk exposures in the quarry supply chain and XYZ is committed to mitigating these risks by focusing on how suppliers of limestone manage these risks. XYZ is not going above and beyond what is typical of the sector, but should its activities improve we may adjust our scores upwards.

XYZ's Social Profile has strengths and weaknesses. The company has strong customer engagement, has become a leading cement provider with customers in the region, and can satisfy large demand quantities. XYZ has strong ties to the communities in which it operates, which are driven top-down as the company is state-owned. Community support is necessary because the company operates in an industry with high safety risks. Unfortunately, a recent explosion occurred that resulted in deaths. As a result, although safety conditions have been improving, the company scores as Lagging for safety management. If the company's new risk management improves safety metrics over time, we could revise our score to Good from Lagging.

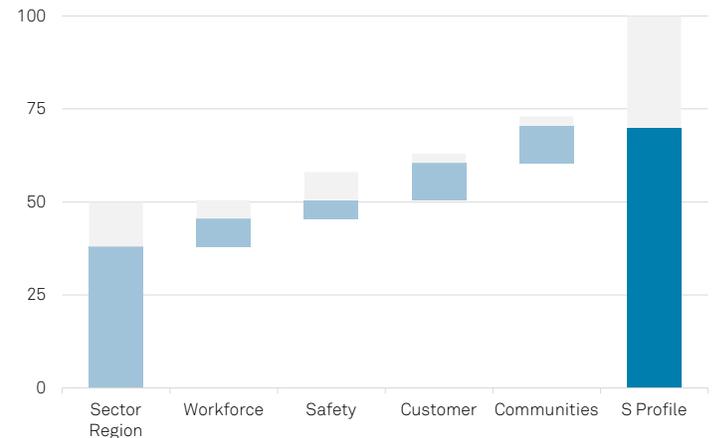
XYZ follows governance standards that are typical for the region. It has independent board members and relevant policies and committees. The company is state-owned and local government still has a relatively strong influence, which could cause potential governance risks. The Transparency and Reporting score is Good and the company discloses its code and values with commitments to the environment and diversity.

■ Component score (incl. adjustments) ■ Potential score ■ Profile score

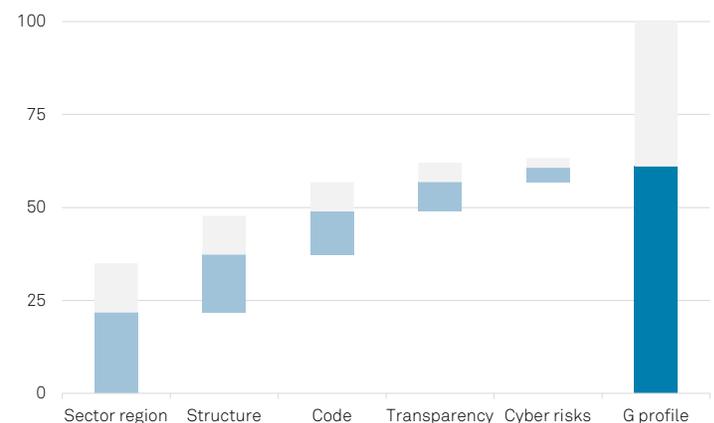
Environmental Profile (30%)



Social Profile (30%)



Governance Profile (40%)



Environmental Factor Analysis



Greenhouse Gas Emissions

Good

- Emissions policies in place and strictly complies with applicable regulations and laws. The company racks Scope 1 carbon intensity but not Scope 2 and 3; Scope 1 carbon intensity has been declining.
- Management has increased funding to upgrade energy efficiency technologies to reduce carbon intensity levels. As a result, the company has developed or used various pollution prevention technologies, including carbon capture and storage technology, desulfurization technology, selective catalytic reduction, selective non-catalytic reduction, dedust technology, and biofuel systems.
- If we do not observe material improvement in disclosure standards or track record of reducing carbon intensity, we may lower the score.



Waste

Good

- The company has waste policies in place to ensure better waste treatment and recycling. As a result, amount of waste processed has increased dramatically in recent years.
- XYZ uses cement kiln co-processing method to process hazardous waste, which can be used in cement production as well.
- The company has developed waste heat power generation to recycle waste energy and indirectly reduce energy consumption and carbon emissions.



Water

Good

- Water management policies in place to ensure better water use. Water intensity declined by 20% in 2018.
- Developed waste water treatment system to enhance water recycling.
- The company has set up mechanisms that regularly monitor water quality at production sites.
- ▲ ESG event of water pollution occurred at one production site. However, we believe the company's water management is satisfactory because the incident is an individual case. The company conducted a thorough review of other sites and found no such situations at other sites. The company has improved water management since.



Land Use

Good

- Complies with Convention on Biological Diversity & Green Mining Treaty.
- Demonstrated commitment to conserve biodiversity in limestone mining operations.
- Committed to improving utilization of mined limestone resources.
- Minimizes impact on adjacent environment and animal species.
- ABC country has relatively high biodiversity risk, but the company has strong policies in place to prevent such risks.



General Factors <None>

- We have not made any adjustments to the final Environmental Profile.

Social Factor Analysis



Workforce & Diversity

Good

- The company has demonstrated commitment to ensure diversity. Fairly diverse workforce relative to regional peers in terms of gender, ethnicity, and age.
- Turnover is low and the vast majority of staff are full-time employees with satisfactory benefits. The company has an improved compensation plan, which considerably increased financial benefits to retain top talent. Leave policies are comparable to regional peers but could be improved.
- Representation of women in senior management is low relative to that of the overall workforce.



Safety Management

Lagging

- Established safety policies and safety departments to guide production and review implementation. The number of safety incidents has been declining.
- Organizes safety trainings and rewards outstanding individuals to enhance safe production mindset.
- △ An explosion occurred once at a mining site and caused casualties. The company conducted a thorough review of other sites. Safety conditions have improved since.
- We have a conservative view until the company demonstrates stronger and longer safety track record.



Customer Engagement

Strong

- No. 1 regional cement brand, with strong customer loyalty. Cement products are used in major infrastructure projects.
- Strong product quality and able to deliver large quantities of products to meet demand.
- No evidence of customer complaints, data privacy breaches, or product quality incidents.



Communities

Strong

- Strong awareness of community responsibility since the company a state-owned enterprise.
- Proactively engages in community activities, including donations, nursing home visits, and poverty elimination.
- Community activities are not only in ABC country, but also across the region.



General Factors <None>

- We have not made any adjustments to the final Social Profile.

Governance Factor Analysis



Structure & Oversight

Good

- The board consists of independent board members and a committee structure, which ensures satisfactory governance structure and oversight. However, as the controlling shareholder, local government still has a relatively strong influence, which could cause potential governance risks.
- Anti-corruption and external audit rotation policies are in place. However, some policies (including whistle-blowing, political donations, and cyber security) are missing or not publically disclosed.
- There is no board member with formal ESG responsibility, no employee representation on the remuneration committee, and no tracking of the gender pay gap.



Code & Values

Good

- XYZ has good standards for setting a code of conduct for its employees. It conducts training, tests, seminars to ensure employees understand the code
- No indication of tracking the pay gap between the CEO and average employees or between genders. However, we do not believe the pay gap is significant between senior management and workers.
- Nevertheless, XYZ has a clear purpose and value statement with response to its environmental values and commitment to diversity.



Transparency & Reporting

Good

- XYZ's reporting practices and transparency have relatively low risk and serve to enhance the overall governance scores. In addition to reporting and disclosing information, XYZ publishes an annual corporate social responsibility (CSR) report and tracks relevant information that is critical in assessing its profiles.
- Still room for improvement as the ESG-related figures or metrics could be more specific in the CSR reports.



Cyber Risks & Systems

Good

- We view cyber risk as not materially important to the company's operations, although this could change in the future.
- ▲ Recently a ransomware attack occurred that was highly publicized. The company found the attack within a day and did not suffer significant losses. We anticipate the company will step up its security measures; however if it stagnates its risk management in light of this event, then we may change our score to Lagging from Good.



General Factors <None>

- We have not made any adjustments to the final Governance Profile.

Preparedness Opinion

Preparedness	Low	Emerging	Adequate	Strong	Best-in-class
Awareness	Developing	Good	Excellent		
Assessment	Developing	Good	Excellent		
Action	Developing	Good	Excellent		
Culture	Developing	Good	Excellent		
Decision-Making	Developing	Good	Excellent		

Summary Opinion

We view XYZ's preparedness as Adequate. XYZ's emerging and strategic risks relate primarily to environmental risks associated with its current profile, and political mandates from the government to address these over the next 10-15 years. The company is aware of the long-term impact of its business operations on the environment. The company's strategic plan aligns with the country's long-term sustainable development strategy, which could minimize the long-term risks. The company has increased capital expenditures in research and development for environmental protection and energy saving to achieve those aims. However, compared to global peers, we do not believe the company has best-in-class preparedness performance.

Awareness	Developing	Good	Excellent

In our view, the company is aware of the long-term risks and opportunities it faces going forward. Environmental protection, reducing business cyclicality, and concentration have been identified as the company's top priorities. Expanding into new markets could raise up different risk profiles that the company will need to navigate. These risks are frequently discussed at top executive meetings. Apart from being aware of risks, the company has also identified opportunities, which are to broaden product offerings and enlarge geographical reach to help itself navigate an uncertain future. The company conducts regular reviews with external sources to validate the long-term risks and opportunities, and monitors technological developments that could disrupt its ability to deliver on its strategic objectives.

Assessment	Developing	Good	Excellent

The company applies various analytical methods, including scenario analysis and stress testing, in its strategic and financial planning process to explore the potential impact of various factors. The company tests assumptions including economic growth, cement demand and prices, technological advancements in production, and the geopolitical risks associated with geographic expansion. The scenario process and outcomes enable the company to determine its future business strategy, allocate funding for capital expenditures, and facilitate financial management. The company also stress tests itself to analyze the financial buffer in potential extreme market downturns and other tail risk events.

Action

Developing

Good

Excellent

We believe the company has taken effective and responsive actions to mitigate short- and long-term risks in the past and will likely continue on the same path. Even though the industry is currently at a peak, the company has formulated long-term strategic plans to diversify product offerings and geographical reach to mitigate risks from the country's economic slowdown. The company has also increased investments in technological development to mitigate environmental risk. That being said, we do not believe the company is excellent in this regard because their strategic plans lack specific and quantifiable objectives.

Culture

Developing

Good

Excellent

Commitment to and importance of environmental protection and long-term thinking is embedded in the company's corporate culture. The company realizes that the workforce needs to support long-term thinking in order to remain competitive over the coming years. The board is responsible for regularly reviewing environmental performance and diversification, with key performance indicators closely linked to those objectives. Board meetings constantly include discussions around environmental protection and the company's future offerings. We do not view the culture as excellent because the culture is yet to be embedded throughout the entire reporting structure. In our view, mid-level management and general staff still need improvement in this regard to execute on strategy and navigate potential disruptions.

Decision-making

Developing

Good

Excellent

We view the company's decision-making as excellent because their business and financial decisions align with long-term strategies, and the board has enough flexibility and experience to navigate risks and opportunities. The company aims to further increase capital expenditures to enhance technological development, especially in environmental protection, which will likely strengthen its business model. The company has also stepped up overseas acquisitions to broaden geographical reach to mitigate potential concentration risk. As a result, we have observed improvement in technologies and intensity metrics. We expect the trend to continue going forward.

Sector/Region Risk

Primary Sector(s)	Building Materials
Primary Operating Region(s)	Hypothetical

Sector Risk Summary

Environmental exposure

Building material companies are very exposed to GHG emissions and waste risks. Cement and other heavy-side building materials companies typically need to crush and move raw materials to produce their end-products, which may require a lot of fuel and create waste and pollution. The cement industry, together with steel, ammonia, and ethylene, produce about half of total CO₂ emissions in the industrial sector. Most large cement players, particularly in EMEA, are committed to reducing carbon emissions in line with the Paris Climate Agreement, mainly through greater usage of alternative fuels and raw materials to reduce the clinker ratio. We believe more of a cement company's capital expenditures will be for energy efficiency and compliance with environmental regulations. Building materials companies may also be exposed to climate-related risks (storms, harsh winters, etc.), which can interrupt local operations and damage equipment. Climate changes also shape needs for building materials and consumer behavior, and can make companies adapt their product offerings.

Social exposure

Social risks in the building material industry are less relevant than environmental risk. Companies typically track and manage incidents and have specific programs to educate their work forces, resulting into a low safety management risk, particularly in developed countries. Consumer behavior is becoming a key driver due to greater demand for green products and accelerating innovation rates. Additionally, population growth, urbanization, and rising living standards provide opportunities for medium to long-term growth, but building materials will need to adapt their product offerings to evolving population needs.

Regional Risk Summary

We have included our regional risk summary for Argentina. Much of the workforce remains in the informal sector of the economy and poverty has been rising. The country's regulations and tax code impose heavy compliance costs for businesses, and encourage informality and tax evasion. The rule of law suffers from corruption in public agencies, as well as politicization of administrative and sometimes judicial decisions. Nevertheless, a new anti-corruption law was adopted in 2018 (Law 27.401) to address this issue, and corporate governance standards in the country seem to be improving. The recent launch of a new corporate governance-focused segment on the Buenos Aires Stock Exchange and an update to the Corporate Governance Code due before summer 2019 are positive steps. The governance segment will follow the same voluntary basis of the Brazilian Novo Mercado. The revised Code will now cover important new topics such as gender diversity on boards and will operate on a comply-or-explain model for listed companies.

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