ESG Credit Factors | A Deeper Dive

Nov. 17, 2021

This article does not constitute a rating action.

S&P Global Ratings

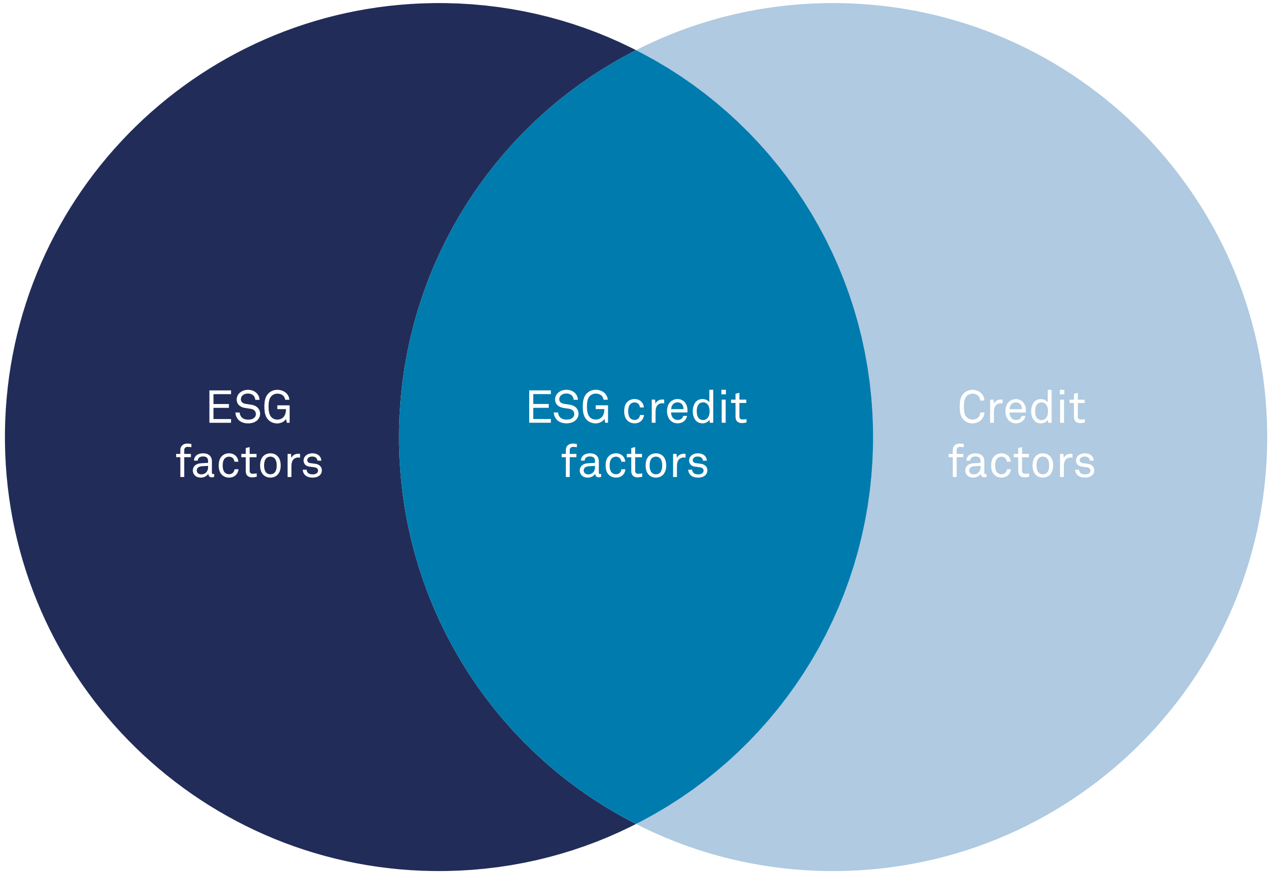
What Are **ESG Credit Factors?**

Here we provide descriptions of key environmental, social, and governance (ESG) factors that have affected creditworthiness or may influence future creditworthiness.

As described in our "Criteria - Environmental, Social, And Governance Principles In Credit Ratings," published Oct. 10, 2021, ESG factors may or may not materially influence our credit analysis. **ESG credit factors** are those ESG factors that can materially influence the creditworthiness of a rated entity or issue and for which we have sufficient visibility and certainty to include in our credit rating analysis. ESG credit factors can have a negative or positive impact on creditworthiness, depending on whether they represent a risk or an opportunity, for example, regulatory or reputational risks.

These factor descriptions may evolve over time and are not meant to be static or exhaustive; rather, they provide additional context for our current analysis of ESG factors within the framework of our credit ratings and methodologies. They do not introduce new analytical approaches, rather, they provide additional transparency for our criteria.

The Intersection Of ESG And Credit



- ESG factors typically incorporate an entity's effect on and impact from the natural and social environment and the quality of its governance.
- ESG credit factors are those ESG factors that can materially influence the creditworthiness of a rated entity or issue and for which we have sufficient visibility and certainty to include in our credit rating analysis.
- Importantly, not all ESG factors materially influence creditworthiness, and thus credit ratings.

Source: S&P Global Ratings.

Why Are We Providing Additional Disclosure Of ESG Credit Factors?

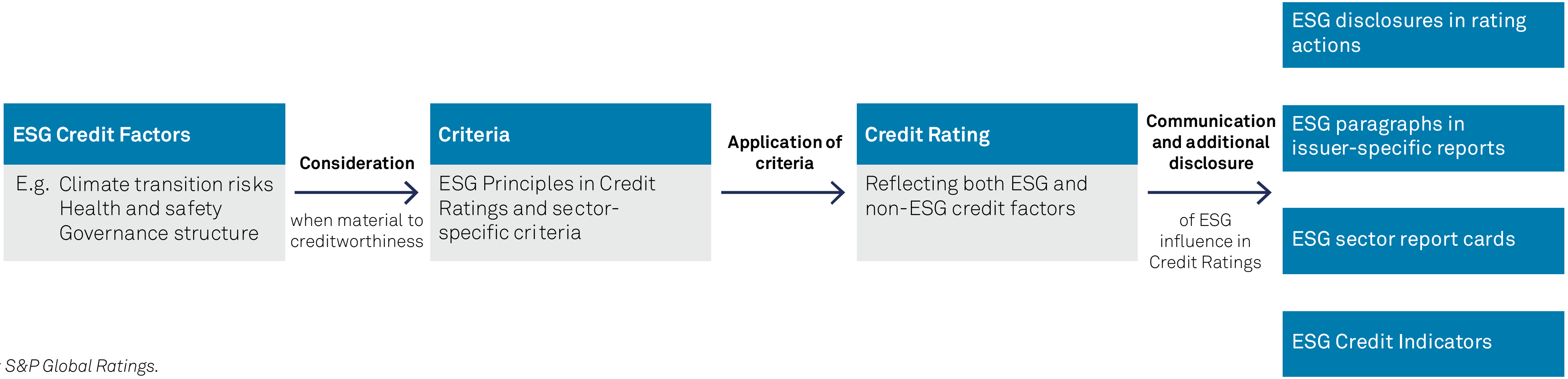
These descriptions of ESG Credit Factors:

– Provide consistency across sectors when discussing ESG factors, with examples listed in our criteria

– Support disclosure when a rating action is driven by ESG considerations

– Illustrate how ESG factors may influence our credit rating analysis

– Add transparency and clarity on ESG credit factors to guide our discussions with issuers and investors



Source: S&P Global Ratings.

Environmental

The Environmental dimension describes how private and public entities interact with, influence, and respond to changes in the physical environment. Environmental analysis considers entities' exposure to physical and transition risks and how they preserve or deplete natural capital. The environmental perspective can include the positive and negative environmental impacts and dependencies generated in the provision of goods and services, when relevant to our credit rating opinion (for information on how we analyze these factors see "Criteria For ESG Principles In Credit Ratings," published Oct. 11, 2021).

We identify the following Environmental credit factors: Climate Transition Risk, Physical Risk, Natural Capital, Waste And Pollution, and Other Environmental Factors.

Climate Transition Risk

Climate Transition Risk considers the implications of the world's transition to a low carbon and greener economy through a reduction in greenhouse gas emissions, shifts in public sentiment and consumer demand, changes in climate policy or legislation, or technological advancements which could lead to significant swings in demand and costs for or development of certain products and services.

Physical Risk

Physical Risk associated with the environment can be characterized by events such as wildfires, floods, droughts, or hurricanes; or, exemplified by longer-term shifts in climate patterns such as increasing temperatures, rising sea levels, or increased weather variability. Physical risks also include other natural disasters that are not always climate-related such as earthquakes.

Natural Capital

Natural Capital can be defined as the sum of the stock of renewable and non-renewable resources available in the world. This is made up of elements which include plants, animals, soils, minerals, water, and air. Biodiversity is a feature of living natural capital.

Waste And Pollution

Waste And Pollution includes issues related to all waste products, wastewater and other pollutants, and air emissions other than greenhouse gas emissions. Waste And Pollution can be considered an element of Natural Capital.

Social

The Social dimension describes how private and public entities manage and are affected by health and safety and how they develop, use, and preserve their human and social capital to secure their social license to operate or mandate to govern. The social perspective can include positive and negative social impacts and dependencies generated in the provision of goods and services, when relevant to our credit rating opinion (for information on how we analyze these factors see "Criteria For ESG Principles In Credit Ratings," published Oct. 11, 2021).

We identify the following Social credit factors: Health And Safety, Social Capital, Human Capital, and Other Social Factors.

Health And Safety

Health And Safety includes considerations such as risks and opportunities incurred across the life cycle of a product or service, or those associated with adherence to relevant health and safety regulations and voluntary codes; occupational health and safety, public health and safety issues, plus pandemics, wars, and conflicts. Health And Safety may be considered an element of either Social Capital (Public Health And Safety) or Human Capital (Employee Health And Safety).

Social Capital

Social Capital includes considerations such as risks and opportunities related to how entities treat and respond to consumers, citizens, and communities through providing responsible, affordable products and services, including data privacy and security. Social capital factors can involve responses to socioeconomic and demographic issues.

Human Capital

Human Capital includes considerations such as an entity's approach to treating employees through employment practices (hiring, recruitment, remuneration, development, retention, and related practices), and the working conditions it provides, including labor relations and employee health and safety. Human capital management throughout the value chain may materially influence credit through reputational impacts.

Governance

The Governance dimension describes the organization and impact of decision-making at all levels of private and public entities. Governance considers the system of rules, procedures, statutory frameworks, and practices by which entities are directed and controlled, how they make decisions, comply with the law, and weigh and communicate the interests of the entity with stakeholders. This includes how the entity manages strategic risks and opportunities to navigate potential disruptions (for information on how we analyze these factors see "Criteria For ESG Principles In Credit Ratings," published Oct. 11, 2021).

We identify the following Governance credit factors: Governance Structure, Risk Management, Culture And Oversight, Transparency And Reporting, and Other Governance Factors.

Governance Structure

Governance Structure refers to how an entity is set up to make decisions that weigh the interests of its stakeholders. The independence, composition, and effectiveness of decision-making bodies and the institutional setups of sovereign and local governments may be key considerations. This also may include turnover, skill sets, and key person risk associated with the management structure.

Risk Management, Culture, And Oversight

Risk Management, Culture, And Oversight refers to how an entity makes and executes decisions or policies. This may include an entity's effectiveness in identifying, monitoring, selecting, and mitigating the risks it takes, and the extent to which these risks are contained within the entity's risk appetite. This factor may also consider alignment of the entity's culture to strategic vision and the entity's ability to set and achieve strategic goals within its capabilities.

Transparency And Reporting

Transparency And Reporting considers the extent to which stakeholders have ready access to all relevant information about an entity, including its audited financial reports. This may include the quality, reliability, frequency, and timeliness of the entity's information disclosure and the standards of its jurisdiction.

Analytical Contacts

Dennis Sugrue
Insurance Ratings
+44-20-7176-7056
dennis.sugrue@spglobal.com

Emmanuel Volland
Financial Institutions Ratings
+33-14-420-6696
emmanuel.volland@spglobal.com

Gregg Lemos-Stein
Corporate Ratings
+1-212-438-1809
Gregg.lemos-stein@spglobal.com

Karl Nietvelt
Infrastructure Ratings
+33-14-420-6751
karl.nietvelt@spglobal.com

Nicole Delz Lynch
Corporate Ratings
+1-212-438-7846
nicole.lynch@spglobal.com

Pierre Georges
Infrastructure Ratings
+33-14-420-6735
pierre.georges@spglobal.com

Nora Wittstruck
U.S. Public Finance Ratings
+1-212-438-8589
nora.wittstruck@spglobal.com

Sarah Sullivant
Sovereign/IPF Ratings
+1-415-371-5051
sarah.sullivant@spglobal.com

Kate Scanlin
Structured Finance Ratings
+1-212-438-2002
kate.scanlin@spglobal.com

Matthew Mitchell
Structured Finance Ratings
+33 (0)6 17 23 72 88
matthew.mitchell@spglobal.com

spglobal.com/ratings

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