ERM SUSTAINABILITY INSTITUTE

Sustainability Trends

QUARTERLY OUTLOOK

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A critical moment for climate action

The moment for accelerated climate action is now as emissions continue to rise and countries prepare to assess what is likely limited progress against their emissions targets at COP28. Still, progress elsewhere in the form of expanding carbon pricing and corporate climate disclosure mandates offer hope that ambition and action will converge.

The energy transition at an inflection point

- The pathway to achieve net zero emissions by 2050 and no more than a 1.5°C temperature rise is narrowing. The International Energy Agency's (IEA's) latest Net Zero Roadmap found global energy sector emissions rose to a record high in 2022. At the same time, the IEA projects energy sector emissions will peak this decade as clean energy growth reduces fossil fuel demand. More work is required, with the IEA forecasting that renewable energy needs to triple by 2030 to keep net zero by 2050 in reach.
- The upcoming COP28 climate summit in Dubai will aim to accelerate climate progress. Attendees will assess the first Global Stocktake of countries' progress toward achieving their Paris-aligned emissions targets. Additionally, COP28's Emirati organizers will push for countries to commit to tripling renewable energy capacity by 2030 (as the IEA Net Zero Roadmap calls for) and a mid-century phase down of unabated fossil fuel use, which is seen as too slow by many, including the European Union.

Carbon pricing schemes gather momentum

- Twenty-three percent of global greenhouse gas emissions now fall under carbon pricing schemes, compared to only five percent in 2010. Growth looks set to continue with countries like Indonesia and Japan expected to enact new schemes.
- Outside of more traditional schemes, this month the European Union began requiring companies to collect data on their products' embedded emissions in preparation for the 2026 enactment of its Carbon Border Adjustment Mechanism, which will add a carbon price to imported products. Adding this cost to a previously unpriced externality will put further pressure on companies to reduce their emissions.

The corporate climate disclosure landscape continues to evolve

Corporate climate-related reporting requirements continue to emerge across geographies. Starting in 2024, Australia will mandate its largest companies and financial institutions to report on their climate-related governance, strategy, risks and opportunities, and metrics. Across the Pacific, California will require companies operating in the state with revenues of greater than $1 billion to report their Scope 1, 2, and 3 emissions starting in 2026, and require companies with revenues greater than $500 million to report their climate-related financial risks starting the same year.

Whether companies have the expertise to appropriately address emerging reporting requirements remains to be seen. One recent survey of Board members found that 48 percent report missing the necessary skills and expertise needed to address climate-related issues. Other companies are struggling to find and keep workers because of their climate impact. For example, oil and gas companies in the U.S. are grappling with a hiring shortage due to falling enrollments in petroleum engineering programs stemming in part from prospective students' climate change concerns.

The dynamic corporate nature landscape

The release of the Taskforce on Nature-related Financial Disclosures' (TNFD) final recommendations, which establish a new formula for nature-related disclosure, comes at a time when companies' existing disclosure efforts languish. However, other areas of corporate nature action are much more dynamic as coalitions form to help companies reduce their nature-related impacts.

Nature-related disclosure, defined

- The Taskforce on Nature-related Financial Disclosures (TNFD) released its final recommendations at NYC Climate Week 2023. The recommendations lay the groundwork for expanded nature-related disclosure by outlining a set of 14 disclosures covering governance, strategy, risks and impact management, and metrics and targets. The recommendations align with existing standards such as the Task Force on Climate-related Financial Disclosures and the International Sustainability Standards Board, as well as global biodiversity goals like those in the Kunming-Montreal Global Biodiversity Framework.

Slow corporate nature progress receives catalysts

- The launch of the TNFD disclosure recommendations will help the many companies that do not yet report on nature. The World Benchmarking Alliance's 2023 Nature Benchmark found that only two percent of the world's 350 largest food and agricultural companies assess and disclose their nature-related impacts and dependencies and that zero (!) adequately address them.
- Beyond the TNFD, other nature-related support for companies is emerging. In November 2023, Business for Nature will launch the It's Now for Nature campaign, which will include guidance on how companies can develop a nature strategy and contribute to halting and reversing nature loss by 2030, while institutional investors with more than $23 trillion in assets under management recently launched Nature Action 100. Nature Action 100 will

accelerate corporate ambition and action on nature by engaging companies and developing nature-related sector pathways and action plans.

- Some companies' are accelerating nature progress. Nineteen leading consumer companies committed to the recently launched Deforestation-Free Call to Action for Leather, which aims to achieve deforestation free bovine leather supply chains by 2030. Other companies are focused on reforestation. Unilever's Dove brand recently announced its Nature Regeneration Project to restore 123,00 acres of rainforest in Southeast Asia over the next five years by partnering with communities in forest frontier areas to promote sustainable natural resources management.

Human rights challenges broaden

While conventional human rights issues like child and forced labor continue to confound companies, a new strain of challenges are also emerging as climate change threatens worker health and conflict in the Middle East has companies walking a public relations tight rope.

Past and present human rights issues challenge companies

- After an internal review, Citigroup announced that the historical companies that compose its present-day form benefited from slavery in the U.S. While the bank did not find any indication that these companies directly purchased or sold people, they did confirm that they benefited from financial transactions with individuals and entities that did.
- Current human-rights issues have also been on the minds of companies. In August 2023, H&M announced it was withdrawing from Myanmar over concerns about human rights abuses in the country's garment sector. H&M's move followed a Business & Human Rights Resource Centre report that found a significant rise in alleged human rights abuses following the 2021 military coup in the southeast Asian country.
- The war between Israel and Hamas present companies with complicated human rights questions. Some, like a group of global venture capital firms, are expressing their support for Israel and its technology community. Others expressed dismay over comments made about the conflict and acted as a result. For example, numerous tech leaders dropped out of Europe's largest tech conference after its co-founder and CEO (who has since resigned) shared that he believed Israel committed war crimes in its response to Hamas' attack, while companies who support Israel's right to respond and defend itself are deeply concerned over the humanitarian crisis and civilian casualties in Gaza.

Worries about working conditions

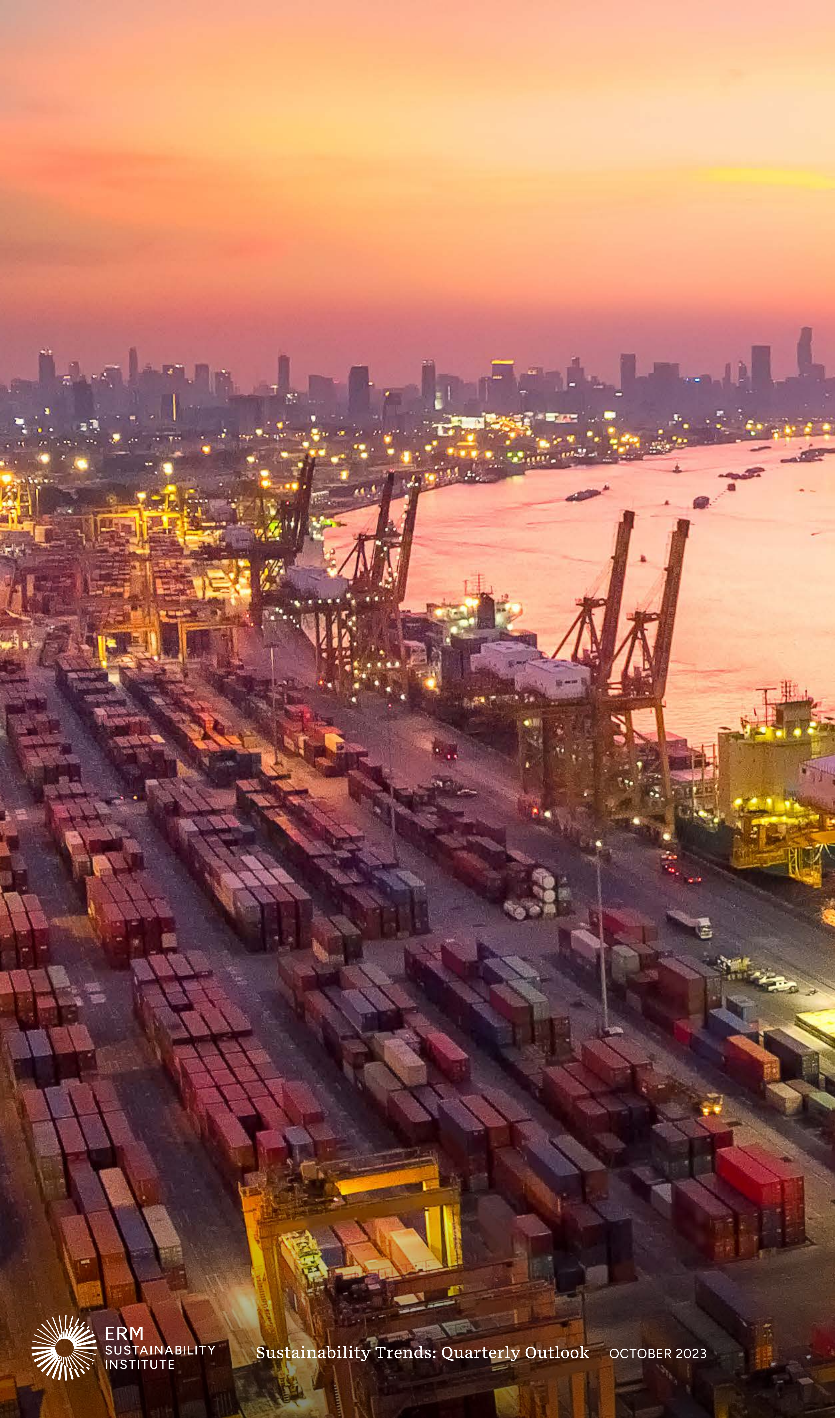
- After a New York Times Magazine investigation found that major U.S. food companies like Perdue Farms are employing children as young as 12 in slaughterhouses, the U.S. Department of Labor announced it was opening an investigation into the companies in an effort to eliminate domestic child labor.
- The question of who works has broad economic implications. In India, female workforce participation has declined since 2000, threatening a $734 billion GDP boost that an 11 percent increase in female workforce participation by 2030 would generate. The opposite is true in the U.S., where

female workforce participation has broken out of a pandemic slump to help boost the developed world's strongest economy.

- For workers with no choice but to work outside, the northern hemisphere's hottest summer on record turned uncomfortable jobs into potentially lethal ones. Numerous Italian workers doing physical labor outside died this summer in record heat, highlighting stark disparities between office and outdoor work. In the Middle East, inequalities generate risk, as migrant workers there lack the legal protections afforded to full citizens and face acute and chronic illnesses as a result.

Workforce diversity headwinds

- In the aftermath of George Floyd's 2020 death, many U.S. companies promised to hire and support more minority employees and, according to a September 2023 analysis, many organizations fulfilled those commitments. At S&P 100 companies in 2021, 94 percent of 323,094 new jobs went to people of color, with diversity increasing across all rungs of the corporate ladder.
- Despite progress, new challenges could derail future efforts. In the first corporate earnings season after the Supreme Court overturned affirmative action in university admission processes, diversity, equity, and inclusion mentions on Russell 3000 company earning calls decreased 54 percent from the previous year. A growing number of lawsuits inspired by the Supreme Court ruling challenging corporate diversity programs is likely one contributing factor.



Sustainable supply chains in focus

After years of supply chain disruptions, companies turn to sustainable and socially responsible solutions to increase their resiliency to external shocks. Resiliency, both to climate change and policy and regulation, is also inspiring companies to develop innovative ways to reduce their supply chain emissions.

As supply chain challenges mount, companies seek sustainable solutions

- Since the start of the COVID-19 pandemic, supply chains have been snarled by one incident after another. Though the impacts of lockdowns and heightened demand for consumer products have dissipated, climate change is increasingly complicating supply chains. At the end of September, the Panama Canal Authority reduced the number of daily ship crossings to limit the effects of a serious drought that is lowering water levels in the canal. Similarly, after a summer of low water levels on the Rhine, shipping traffic on the river was again reduced in early October 2023 after another period of dry weather.
- Spiraling supply chain issues have companies thinking sustainability. A July 2023 survey of global corporate procurement leaders found that ESG factors are their number two priority given the long-term supply chain resilience benefits they generate. This goes beyond environmental issues: socially responsible supply chain management is gaining traction. In September, Telos, a social supply chain-focused initiative launched with leading companies in Europe, the Middle East, and Africa as members. The initiative's efforts center on its Buy Social campaign, which introduces companies to socially responsible suppliers, trains them on how to engage with these suppliers, and supports their reporting efforts to track spending and impact.

Efforts to tackle supply chain emissions quicken

- Companies must reduce their Scope 3 emissions. The UK's Tesco, for example, recently announced plans to reduce its forest- and agriculture-related supply chain emissions by 39 percent by 2032 from a 2019 baseline by pursuing deforestation-free animal feed sources and utilizing low-carbon fertilizer, among other strategies. In Mexico, Grupo Bimbo recently linked a green bond to its success in meeting its Scope 3 emissions reduction goals, making it the first Latin America company to tie Scope 3 emissions to a green finance instrument.

- Shipping emissions make up a considerable portion of corporate Scope 3 emissions, a fact not lost on the global shipping industry, which in July agreed to achieve net zero emissions by 2050, along with interim targets for 2030 and 2040. Maersk, one of the companies likely to be most involved in making net zero shipping possible, announced in June that it would retrofit one of its ships so that it could sail on green methanol. The company followed this announcement by launching its first ship able to sail on green methanol or traditional fuels; the ship will emit 100 tons of CO_2 less per day than diesel-fueled ships.