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ESG RISK **QUARTERLY**

ECOFACT's briefing for risk experts

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Editorial

Plastics: reduction is the solution, not recycling

The current focus on recycling as a solution to our plastic problem is the result of what academics call **non-market strategies** – using political and social leverage to build and maintain competitive advantage. Consider the **Alliance to End Plastic Waste**, a laudable initiative to which industry players have committed an impressive USD 1.5 billion. However, it would not exist if it did not align with business goals. Firstly, it upholds the legitimacy of plastic as a product. Secondly, the initiative focuses only on improving waste collection and recycling, avoiding critical discussion about plastic substitutes, phaseouts, and product design. Some critics even claim that the overall goal of building a global plastic-recycling industry is to “lock in” our never-ending plastic output.

When I visited the seaside as a child, I used to find seashells. Now I find plastic. I initially became aware of the plastics problem when pictures of plastic in **dead birds** went viral roughly a decade ago, followed by images of the **Great Pacific garbage patch**. **Today, plastic is found everywhere, even in human blood and lung tissue.** If you look at the objects that surround you, most will contain plastic; even paint and flooring materials contain plastic polymers, as do **most fabrics**. The **OECD expects plastic production to triple by 2060**, and while recycling is needed to reduce plastic in the environment, it can't be the solution (see box 1). The only effective way of combating pollution is to reduce the pollutant at its source.

It is no wonder that policymakers are subjecting plastics to greater scrutiny. In addition to actions by **national** and **supranational** regulators, the UN Environment Assembly adopted a **resolution** in 2022, noting that “the rapidly increasing levels of plastic pollution represent a serious environmental problem.” The Assembly also recognizes microplastics as pollutants. UN members aim to negotiate an **international, legally binding** agreement on plastics by 2024.

These regulatory developments present transition risks for the plastics industry – as well as its investors. (There are, however, opportunities to be gained from developing alternative materials.) Plastic's potential impact on human health (see box 2) poses **liability risks** – which are relevant for the **insurance industry**. These liabilities may even exceed claims related to asbestos or smoking, as plastic may affect a larger proportion of the global population in worst-case scenarios. **Plastics are not a recycling problem; they are a pollution problem.**

Olivier Jaeggi

The problem with plastic recycling



Plastics can be made from thousands of different components and often include chemical additives and colorants. Packaging generally consists of inseparable layers of mixed materials, and in other products, plastic parts are usually bonded to other materials. Furthermore, plastic is not inert like glass or metal. It can absorb some of what it contains, potentially making a plastic receptacle toxic (think pesticide containers). Last, but not least, new plastic is cheaper than recycled plastic. These factors make it **practically impossible** to turn plastic waste into a reusable product, with a few exceptions such as PET. As a result, recycling at scale remains uneconomical for products that could be recycled and impossible for all others. New technologies, such as chemical recycling – converting plastic waste into fuel – still need to prove their advantages.

Micro- and nanoplastics are a concern



There are **two rapidly growing sources of microplastics**: primary microplastics are manufactured and added to products (e.g. artificial turf infill, fertilizers, plant protection products, cosmetics, household and industrial cleaners, paints, and varnishes). Secondary microplastics result from the use and disposal of plastic products (e.g. car tires, fibers shed from washing synthetic textiles, shredding processes) or result from larger plastic parts breaking down into smaller and smaller pieces (plastics marketed as “biodegradable” also seem only partly to decompose). Scientists are **finding micro- and nanoplastics everywhere** – even in **blood** and **lung tissue**. These substances have the potential to release harmful chemicals into our bodies. Microplastics are **distributed** by wind and water, and have been found in soil and even **fresh Antarctic snow**. Microplastics barely decompose and therefore accumulate in the environment.

International standards

Updates on cross-sector environmental and social standards that might be relevant as benchmarks for risk assessments.
 Scope: key developments related to the most important international environmental and social standards.

→ Global baseline for sustainability disclosures: ISSB releases its first two standards – IFRS S1 and IFRS S2

The sustainability disclosure standards issued by the International Sustainability Standards Board (ISSB) encompass broad sustainability (IFRS S1) and climate-related metrics (IFRS S2) that communicate “material, decision-useful information” on how the risks and opportunities of climate change affect businesses. The standards are interoperable with the Global Reporting Initiative Standards, which is good news for companies, as it may decrease their reporting burden. Both standards integrate the recommendations of the Task Force on Climate-related Financial Disclosures. Although they are intended to be voluntarily adopted by companies, the goal is for jurisdictions to use the standards as a foundation for mandatory reporting. In addition, the ISSB has published several supporting documents to shed light on the standards’ development process. June 26, 2023

[Read more \(1\)](#) → [Read more \(2\)](#) →



→ OECD expands downstream due diligence recommendations

The OECD has updated its [Guidelines for Multinational Enterprises on Responsible Business Conduct](#) for the first time since 2011. These now include expanded due diligence recommendations. The updated guidelines advise companies to conduct comprehensive due diligence on – and then work to prevent – their potentially adverse impacts on people, society, and the environment. They encourage such assessments across a company’s “business relationships,” supply chains, clients, and investments. The updated guidelines also urge companies to set climate targets that include their own and downstream emissions, and recommend that companies align with international environmental frameworks (e.g. the Paris Agreement and the Kunming-Montreal Biodiversity Framework). In view of increasing sustainability regulation – especially in Europe – civil society organization OECD Watch has [welcomed](#) the changes. June 1, 2023

[Read more](#) →

Open consultations

Our [Policy Outlook database tracks open consultations](#) that are relevant to the wider financial and insurance industries as well as corporate actors. Organizations and governments solicit structured feedback from stakeholders during these events. Interested parties can comment on the materials that are issued to promote dialogue. Please [contact us](#) for more information on open consultations.

Authority	Consultation topic	Deadline for input
International Sustainability Standards Board (ISSB) 	The ISSB is looking for input on its proposal to revise the non-climate-related metrics of the Sustainability Accounting Standards Board standards and taxonomy to ensure that they are more applicable internationally. Read more (for Policy Outlook subscribers) →	August 9, 2023
European Union (EU) 	The EU Commission is accepting feedback on the text of its proposed regulation on the transparency and integrity of environmental, social and governance (ESG) rating activities. Read more (for Policy Outlook subscribers) →	September 2023

Source: ECOFACT's Policy Outlook, a database of in-depth analyses of sustainable finance and corporate responsibility regulatory initiatives across the globe. More information: <https://www.ecofact.com/policyoutlook/>

Spotlight: Plastics – the risks are complicated

A deeper dive into news, issues, or developments that have received significant attention in the past quarter. We also explain why we think the topic is important to your work.

→ In May 2023, 185 investors with USD 1 trillion in assets under management (AUM) issued a **statement** urging companies in the consumer goods and grocery retail sectors to accelerate actions that address the **toxicity** and use of plastics, because efforts have so far been inadequate. Considering that plastic is an indispensable part of all sectors of the economy and human lifestyles in general, this is by no means a simple demand.

This year, for the first time, global environmental reporting platform **CDP** asked 6,743 companies to disclose environmental impacts, reveal perceived business risks, and conduct plastics mapping for “the most problematic plastics production and use.” (Plastics-related disclosure via CDP was requested by investors with USD 136 trillion in AUM.) This further highlights the attention that plastics are receiving, particularly since the Global Plastics Treaty is one step closer to being negotiated.

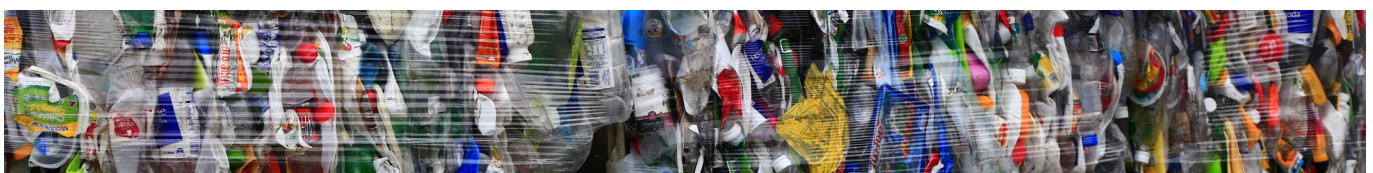
Risks to consider

The scale and pervasiveness of plastic-derived problems might lead one to believe that the sector is considered high risk. Not so, says **Planet Tracker**, whose research revealed that investors and equity markets seem to think the plastics sector is not as risky as other materials sectors, despite investors facing billions of dollars of plastics-related risks.

The **risks** appear to be many:

- **Climate**-related risks
- **Health** risks
- **Policy** and regulatory risks
- **Human rights** risks
- **Economic costs**

Resources for investors		
Title	Source	Description
Turning off the Tap: How the world can end plastic pollution and create a circular economy	United Nations Environment Programme	This report proposes a combination of available solutions and systemic changes needed to tackle the plastics problem. The financial industry has been assigned a central role in driving change and is in a position to align capital flows to support the circular plastics economy.



High-risk sectors

News on risk factors and trends, regulations, and best practices associated with key high-risk sectors.

-  Oil & Gas
-  Mining
-  Forestry
-  Agriculture
-  Utilities
-  Chemicals
-  Other

Risk factor



Studies find that companies' sustainability action has stalled

New research shows that companies are still failing to take action to promote sustainability. Morningstar Sustainalytics has **found** that only 17 percent of companies have set a biodiversity target, and that only 21 percent of companies aim to avoid and reduce their negative impacts on biodiversity. MSCI **notes** that only 19 percent of companies are cutting emissions fast enough to limit global warming to 1.5°C. Similarly, Net Zero Tracker has **reported** that while many companies have made net-zero pledges, most have not set actual net-zero targets, and even fewer have made urgent near-term emissions cuts. Finally, the **Global Slavery Index 2023** shows that 10 million more people have fallen into modern slavery and forced labor since 2018, and that only a handful of countries (Australia and the UK) have adopted meaningful anti-slavery laws in the past five years.

June 11, 2023

Read more (1)



Read more (2)



Read more (3)



Risk factor



Ship tracking exposes illegal fishing and oil transport

Tracking the automatic identification system (AIS) signals of fishing boats and oil tankers can help governments and civil society organizations to find and put a stop to illegal fishing and "dark fleet" operations transporting sanctioned Russian oil. Researchers have **analyzed** data from 28 billion AIS signals to define hot spots and suspicious gaps where fishing boats turn off their AIS transponders so that they can harvest fish beyond international boundaries. Oil tankers can likewise be **tracked** and monitored. The AIS data can even demonstrate "spoofing," whereby dark fleet tankers falsify AIS data while carrying Russian oil in defiance of sanctions. Dark fleets are not illegal. However, if ships break sanctions, they can lose their insurance as well as access to major shipping ports. May 30, 2023

Read more (1)



Read more (2)



Read more (3)



Best practice



Updated deforestation framework for supply chain accountability

The **Accountability Framework** is a core-principles roadmap on deforestation, land conversion, and human rights issues within agricultural and forestry supply chains. The framework and newly revised core principles are designed to help companies in these sectors to set goals for a just transition, take strategic action to achieve those targets within set time frames, and to monitor progress in complying with international norms and the sustainability expectations of leading financial institutions. Operational guidance is available to help apply the core principles to supply chain management, investment portfolios, lending activities, and sustainability initiatives – all with the goal of strengthening ESG performance. April 2023

Read more (1)



Read more (2)



Risk factor



Major corporations fight US crackdowns against toxic "forever chemicals"

Compostable packaging may contain harmful "forever chemicals" linked to health issues. A subgroup of PFAS (perfluoroalkyl and polyfluoroalkyl substances) called "fluorotelomers" can be released and end up in food and drinks, finds a new peer-reviewed **study**. More than 30 US states are considering legislative action, as reported by Safer States, an environmental advocacy group. Minnesota has proposed strict bans on products containing PFAS by 2025. Chipmakers and representatives of the Semiconductor Industry Association, including major players such as Intel, IBM, and Nvidia, have jointly opposed Minnesota's legislation, warning that PFAS chemicals are widely used in electronics manufacturing and that the legislation will result in higher prices for consumers. April 17, 2023

Read more (1)



Read more (2)



High-risk sector controversies

This table shares SIGWATCH data on NGO campaigns and financial institutions' exposure to criticism from NGOs. It also provides ECOFACT-curated links to sector-related controversies from the last quarter as well as our risk rating.

Sector & subsector	Level of controversy Number of NGO campaigning actions per quarter in the last five quarters					FI exposure % share of NGO actions criticizing FIs (SIGWATCH data)	ECOFACT risk rating	Noteworthy news	Sector & subsector	Level of controversy Number of NGO campaigning actions per quarter in the last five quarters					FI exposure % share of NGO actions criticizing FIs (SIGWATCH data)	ECOFACT risk rating	Noteworthy news							
	2022 Q2	2022 Q3	2022 Q4	2023 Q1	2023 Q2					2022 Q2	2022 Q3	2022 Q4	2023 Q1	2023 Q2										
Forestry						5%	Orange	Research shows that certain plantation forest management strategies effectively combat climate change. Read more	Palm oil						1%	Orange	El Niño effects predicted to diminish palm oil production significantly in 2024. Read more							
										9%	Red	World struggling to reduce coal use; coal was the top mining commodity in 2022. Read more	Agriculture						4%	Yellow	Cattle farming and processing in Brazil introduce deforestation to global beef supply chain. Read more			
														3%				Red				Indigenous Peoples worldwide raise alarm on "green colonialism;" transitional-mineral mining is violating their rights. Read more		

ECOFACT risk rating

After weighting the level of controversy associated with each subsector, ECOFACT assigns a risk rating of either **red** (high risk), **orange** (enhanced risk), or **yellow** (moderate risk). The rating reflects our assessment of the degree of reputational risk that financial institutions (FIs) face when investing in the sector.

About SIGWATCH

SIGWATCH scans the messaging of more than 10,000 NGOs around the world every day, identifying active and emerging campaigns and issues, and tracking the criticism (and occasional praise) of corporations and industry sectors. This qualitative and quantitative data offers unique insights into NGO concerns and gives early warning of the problems that companies and investors will have to manage in the months ahead.

Emerging risks

Risks that could be relevant when looking into a company's business model. These issues may not yet be considered highly significant, but they have the potential to be.



Evaluating AI's harms

As artificial intelligence (AI) is rapidly deployed across businesses and sectors, its potential to do harm is also increasing. The Electronic Privacy Information Center (EPIC) **surveyed** the risks of generative AI programs such as ChatGPT and pointed to the "turbocharging" of misinformation, privacy breaches, labor devaluation, entrenched discrimination, and other serious issues concerning intellectual property rights and data security. AI's enormous computing requirements also cause a serious environmental burden: EPIC estimates that training one AI program generates as many carbon emissions as seven people in one year and consumes approximately 700,000 liters of water for server cooling purposes. AI queries also consume up to a **bottle of water** each. To address these risks, EPIC says that countries should legislate privacy, transparency, and anti-discrimination measures regarding AI developments. May 23, 2023

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Seas could rise sooner than expected because land levels lower than previously thought: new study

Rising seas could flood coastal regions faster than previously forecast – due to inaccurate historic elevation measurements. In the past, radar technology was commonly used to measure elevation, however, radar cannot correctly distinguish the distance between treetops and land, which can be 20 meters apart in tropical forests. A recent **study** instead used LiDAR (light detection ranging) technology to reassess elevation, and this approach has led to researchers concluding that a lot of land is not as high as once thought and that more areas are at risk of flooding should the sea level rise by a mere two meters. This also means that many regions probably have even less time to prepare for rising waters, and construction projects in vulnerable areas need to be reassessed, as millions of people could be affected. June 21, 2023

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New risks seen through an insurer's eyes

Every year, the Swiss Re Institute publishes the SONAR report, which is based on "scenario thinking" and consideration of past events to predict, understand, and mitigate emerging risks. The **2023 SONAR report** identifies 13 high-, medium-, and low-impact risk themes alongside the business areas most likely to be affected in the short (less than three years) and medium to long term (more than three years). From the geopolitical polarization of business to anxiety and distraction stemming from social media addictions, SONAR examines risks in the following settings: demographic and social, political and economic, technological and natural environment, and competitive and business. June 14, 2023

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Peer approach

A selection of new sector and issue policies that have recently been adopted or that are receiving attention. This section includes announcements of peer alliances and collaboration.

→ NZIA loses members amid “collusion” claims

The Net-Zero Insurance Alliance (NZIA) lost almost half its members in early 2023. Major insurers, including **Lloyds of London, Munich Re, Tokio Marine, MS&AD Insurance Group**, Grupo Catalana Occidente, **Mapfre**, SOMPO, Allianz, Scor, and AXA (former NZIA chair), have stepped away from the NZIA. As part of the Glasgow Financial Alliance for Net Zero, the NZIA is an organization that encourages insurers to voluntarily decarbonize their portfolios. However, US Republican state attorneys-general have **alleged** that the alliance breaches US anti-trust law and is effectively “colluding” against high-emitting companies or sectors, such as oil and gas. Despite this, the United Nations Environment Programme Finance Initiative, which helped found the NZIA, has **restated** its support for the alliance. May 24, 2023

[Read more \(1\)](#) → [Read more \(2\)](#) →

→ Nordea Asset Management drops chemical giant DuPont over biodiversity impact

Nordea Asset Management (NAM), a sustainability investor, has developed an **exclusion list** covering the banking, insurance, and investment sectors. DuPont is the first company to be blacklisted due solely to biodiversity considerations. NAM's responsible investment list excludes companies engaged in the production or maintenance of weapons or munitions. It also considers revenues from coal mining, thermal coal, oil sands, Arctic drilling, and pornography, as well as biodiversity risk and violations of Indigenous Peoples' rights. Notable entities such as DuPont, Adani Power, BAE Systems, Imperial Oil, Honeywell International, and Petroleos de Venezuela SA have now all been excluded, reflecting the growing trend among responsible investors to avoid involvement with higher-risk companies. May 30, 2023

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→ Sector and issue policies adopted by insurers

This table presents the number of the **nine global systemically important insurers** that have a public policy or guideline for investing in or underwriting for the sectors listed in the left column.

Sector policy	Q2 2023	
	I	U
Agriculture	1	1
Agriculture commodities	2	0
Animal welfare	1	1
Palm oil	3	2
Forestry	2	2
Tobacco	5	3
Fisheries	2	1

Sector policy	Q2 2023	
	I	U
Utilities	1	1
Nuclear power	2	2
Coal-fired power	9	5
Hydropower	1	1
Human rights	7	5
Large-scale resettlement	1	1
Indigenous Peoples' rights	2	1

I = sector-related investment activities have a public policy or guideline

U = sector-related underwriting activities have a public policy or guideline

Policy sector in focus: agrochemicals – pesticides

A discussion that highlights why some financial institutions have developed policies to guide their activities associated with a specific sector or concern.

→ A **report** on global food markets published by the Food and Agriculture Organization (FAO) notes that production has increased in 2023 – which is good news, because a **growing population** means that supply must increase to meet rising demand. However, food systems suffer from persistent vulnerabilities due to **shocks** such as extreme weather, policy changes, and geopolitical friction – there is a pressing need to future-proof agricultural crops.

While the **global biodiversity** crisis has encouraged the discussion of alternative, more **sustainable** methods of producing food, agrochemicals continue to play a critical role in boosting yields, especially in industrial operations. Yearly sales of chemical pesticides in 27 European Union countries is around **350,000 tonnes**, and its use around the world has grown by **20 percent** in the last decade. The FAO **estimates** that 2.7 million tonnes of active ingredients were applied to the world's crops in 2020.

→ What are agrochemicals?



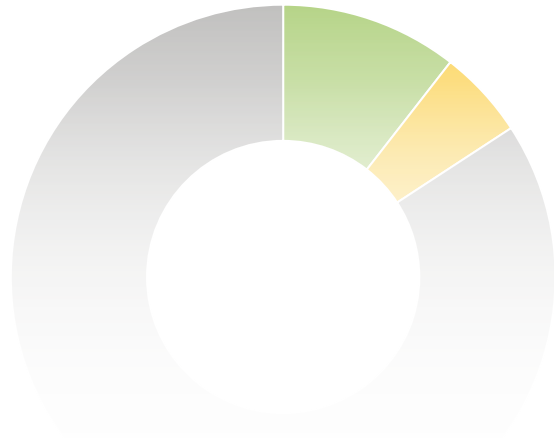
These specialty chemicals are used by the agricultural sector and include fertilizers (providing nutrients to plants), herbicides (controlling plants competing with desired crops), and pesticides (eliminating insects and fungi).

Why we think it matters

Many countries have **banned** certain pesticides, but this does not prevent these chemicals from being sold for use in places that do not impose restrictions, particularly **developing countries**. Because of the concerns described above, countries such as **Canada** and the **European Union** continue to explore more restrictive regulation of pesticides.

Do financial institutions have a chemical-sector investment policy, and, if so, does the policy specifically address agrochemicals?

- Agrochemicals mentioned
- Agrochemicals partially excluded
- No chemical-related policy



*Chart based on data from ECOFACT's **Monitoring Peer Policies**, a comprehensive analysis of environmental and social policies and frameworks of a variety of leading banks and insurers.



New resources

This section highlights tools, databases, and other information that can help you to identify, manage, disclose, and mitigate ESG risks.

→ New resources for climate-risk scenario analysis

The European Insurance and Occupational Pensions Authority has released a free, open-source modeling tool called **CLIMADA-App**, which helps users to cost-effectively understand their risks. It generates detailed exposure, hazard, and risk maps that show the spatial distribution and intensity of climate-related factors. The Bank of International Settlements has published an **executive summary** on how the Network for Greening the Financial System (NGFS) approaches scenario analysis. NGFS shared a **summary** of the feedback it received on its third edition of scenarios. And Climate Interactive's free-to-use **C-ROADS Climate Change Policy Simulator** has been updated to include a new baseline scenario and modified models for the land, forest, and agriculture sectors.

June 23, 2023

Why we think it matters: The European Central Bank's **2022 stress testing** revealed that banks are not meeting the ECB's expectations when it comes to disclosing climate and environmental risks. The Association for Financial Markets in Europe has published a **report** outlining the challenges banks face and made recommendations for improving stress testing.

[Read more \(1\)](#)



[Read more \(2\)](#)



[Read more \(3\)](#)



[Read more \(4\)](#)



[Read more \(5\)](#)



[Read more \(6\)](#)



→ New nature roadmap for insurers

The insurance sector plays a critical role in evaluating nature loss, developing solutions to tackle nature-related risks, promoting the protection and restoration of nature, and working with other industries to value and protect nature. To that end, the University of Cambridge's Institute for Sustainability Leadership has developed a **roadmap** for the insurance sector with the aim of achieving nature-positive underwriting and supporting the transition of the sector's clients toward a sustainable economy. The roadmap identifies solutions and actions for the sector that can be implemented by companies, policymakers, and standard-setters. These include building knowledge and awareness, improved data provision, mandated due diligence, more consistent terminology, and building organizational capacities. The roadmap also highlights best-practice solutions such as the recommendations of the Taskforce on Nature-related Financial Disclosures. April 12, 2023

[Read more](#)



→ Respecting Indigenous rights – actionable due diligence toolkit for institutional investors

Indigenous communities face human rights violations related to activities in the extractive, renewable energy, and agribusiness sectors. AmazonWatch's *Respecting Indigenous Rights* **toolkit** makes the case for considering Indigenous rights as relevant for investors. Aside from mitigating reputational and material financial risks, helping Indigenous communities is also beneficial for the environment. The toolkit consists of two parts: Part A covers fundamental Indigenous rights as currently recognized by international human rights frameworks, and Part B offers practical guidance on implementing due diligence – including identifying and addressing negative effects on Indigenous rights, considering data sources, due diligence questions, and red flags in company practices and policies. April 18, 2023

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Editor in Chief: Jenifer Guillemin **Production:** Kate Haycock, Bronwin Patrickson

Contributors: Bruno Bischoff, Robert Blood, Maria Castillo, Anna Reimann, Nina Reiser, Deborah Thür

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Tel: **+41 58 520 20 00** | info@ecofact.com | www.ecofact.com

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