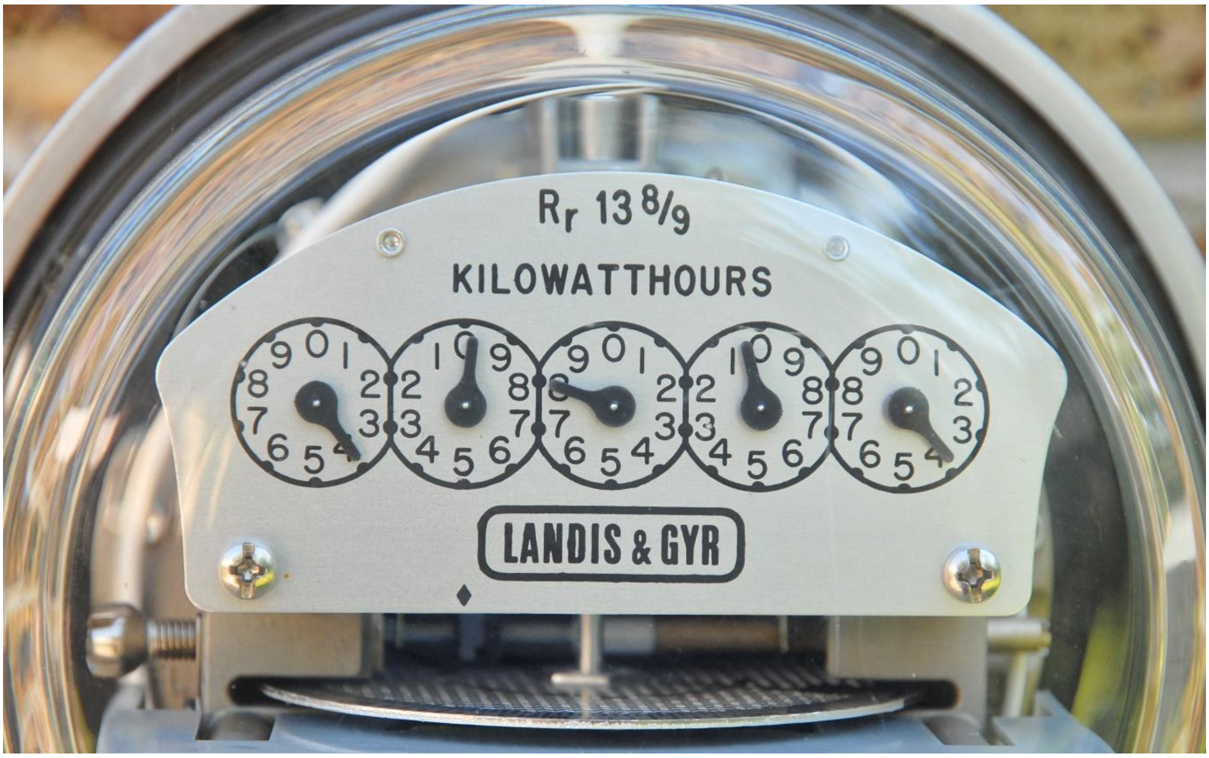


Impact Cubed

WHY DOES HAVING A GREAT IMPACT MODEL IMPROVE CARBON ESTIMATES?

If you've been to our website recently, you'll have seen a short read on what "impact" means to us.

It started in 2008, when our quant team got interested in ESG data and wanted to understand a company's impact on society and the planet. To do that, we needed to measure how well the company is managed and governed, but also what products and services it sells. What the team found was that the ESG scores were not fit for their purpose so they began to build tech-powered ESG models that provide objective, factual data.

Building a better impact model

The keystone in Impact Cubed's model is the way we measure the impact of the products and services companies' sell.

First, we created an industry classification system that splits the global economy into 2,300 business activities. (Conventional ESG data models have fewer than 200 business activities.)

Each of these business activities were mapped to the United Nations' Sustainable Development Goals (SDGs). Then, we built a model to quantify the countries where companies generate their revenues, because some impacts are regional rather than global. So for every company, we look at every regional revenue stream (and there can be many for diversified companies), classify each in a systematic way, and tag it as positive, neutral, or negative social or environmental good as defined by the SDGs.

This detailed quantitative approach allows us to ask better questions about companies and be more accurate about measuring impact.

What does a better impact model have to do with carbon emission estimates?

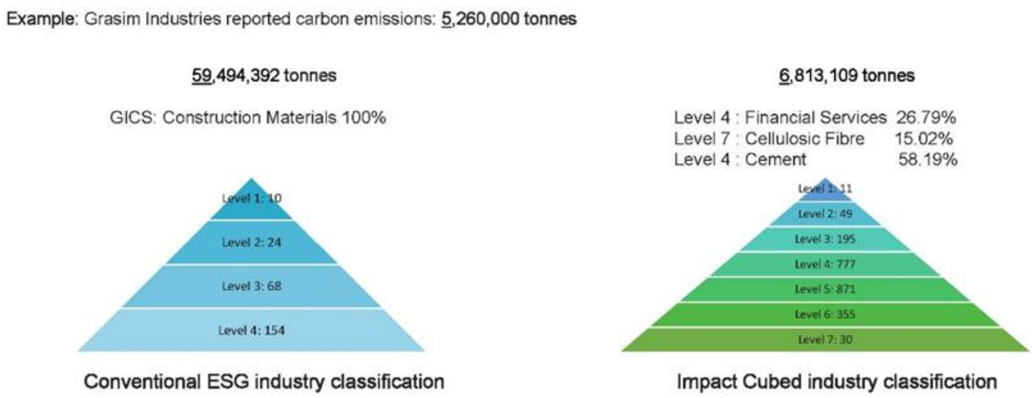
One of the big challenges with ESG data is the disclosure cliff, as we have written about before. Impact Cubed covers securities issued by 40,000+ companies. With the exception of the world's largest businesses, most companies don't disclose emissions data. In fact, fewer than 8,000 of those 40,000+ have quantitative disclosures of their carbon emissions.

This means that until companies start reporting on their carbon emissions, ESG-minded investors will need to use an estimated value. After all, if a company does not disclose it doesn't mean it has zero carbon emissions! For now, estimating carbon emissions is the order of the day so smart ESG investors are ones that know how important it is to ask about estimation models.

How do carbon estimates compare between conventional ESG industry models and Impact Cubed's highly detailed 2,300 region-sector classification? We selected Grasim Industries, which has diverse business lines, as a case study example.

The conventional ESG approach uses GICS level 4 classifications that divide business activities into 154 categories. Using this approach, Grasim is classified as construction materials, which has a very high industry average carbon emission rate. The conventional ESG approach yields a carbon estimate of 59 million tonnes, over 10 times higher than the actual 5.3 million tonnes disclosed by Grasim.

On the other hand, Impact Cubed's model accounts for all of Grasim's business activities mapped to a much more detailed and precise industry sectors: financial services, cellulosic fibre, and cement. Financial services and cellulosic fibre have much lower carbon emissions than cement production. The overall result? A much closer estimation of reality, 6.8 million tonnes.



Why investors benefit

A great impact model does a better job estimating carbon emissions, but it has other benefits as well.

For investors looking to find alpha based on company's business activities, the very detailed region-sector model provides better insight. For example, some investors believe that companies with products aligned to a low-carbon economy will be future winners. Having a more granular list of business activities helps in culling potential winners and losers. Our model can also spot, for example, companies generating revenue from high-polluting activities in countries with proposed environmental taxes or policies.

When it comes to aligning investments with investors' interests in environmental or social matters, a very detailed region-sector model means a manager can create more customized and personalized portfolios. For example, our model classifies 85 business activities as being environmentally or socially harmful, as defined by the SDGs. The conventional ESG industry approach flags 10 to 15 business activities. Managers are forced to take a broad-brush approach to including or excluding securities to align with investor interests.

The next time you are evaluating ESG data providers and trying to sort out substance over marketing fluff, ask how many sectors they use in their estimation model and whether they take all regional revenues into account. Your clients will be glad you did.

For a demo on Impact Cubed's industry leading ESG and impact models, please get in touch at info@impact-cubed.

Want to know more? You can find all of our short reads here.

ABOUT IMPACT CUBED

Impact Cubed provides ESG analytics and investment solutions for building more sustainable portfolios with greater impact. It combines an award-winning approach to integrating impact into risk and return with technology-enhanced portfolio design and management. The outcome is a seamless approach to customised sustainable investing.

You can find out more about our data and portfolio models at www.impact-cubed.com and if you would like to contact us at info@impact-cubed.com we would be happy to hear from you.

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