

# Carbon Risk Rating

## Methodology and Research Process

## Carbon Risk Rating

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The Carbon Risk Rating (CRR) provides a sophisticated metric to evaluate how well companies are prepared for a low-carbon economy by looking at how well they manage their climate-related transition risks. The Carbon Risk Rating provides an aggregated score indicating a company's overall climate-related transition risks, using the company-specific risk exposure as a baseline (Carbon Risk Classification) from which a company can take steps toward better alignment with a low carbon economy (Carbon Performance Score).

The **Carbon Risk Classification** assesses a company's exposure to climate-related transition risks by estimating the emission intensity in the company's value chain, based on its industry and business activities. The Carbon Risk Classification considers two elements:

- The **emission-based sector classification**, which assesses the average sector emission intensity along the entire value chain (direct and indirect, i.e., scope 1, 2 and 3 emissions); and
- whether a **company's product and services** portfolio contribute to climate change mitigation, thus creating a positive impact, or rather obstructs climate change mitigation, thus constituting an adverse impact.

The **Carbon Performance Score** evaluates the current carbon-related performance of a company as well as a company's risk management and measures to reduce its carbon intensity in the future, thus addressing both material risk as well as adverse impact. The Carbon Performance Score is based on a combination of quantitative indicators (e.g., current intensity and trend of greenhouse gas emissions), and qualitative indicators (e.g., disclosures on climate change risks and mitigation strategy, emission reduction targets and action plans, etc.).

## Outputs

The **Carbon Risk Rating (CRR)** assesses, on a scale of 0 (Higher transition risk) to 100 (Lower transition risk), how a company deals with industry-specific climate-related transition risks both in its own operations as well as in the supply chain. It allows for the categorization of companies into four groups: Climate Laggards, Climate Medium Performers, Climate Outperformers, and Climate Leaders.

The **Carbon Risk Classification (CRC)** has four risk categories in which a company can fall in, namely High Risk, Medium Risk, Low Risk, and Negligible Risk with a step size of 0.75. A higher value indicates lower risk which means a particular company has a lower baseline risk exposure to climate-related transition risks.

## Research Process

The Carbon Risk Rating is largely derived from ISS STOXX's Climate Solutions emissions data, ISS STOXX's Corporate Rating as well as SDG Solutions Assessment (for more details, please refer to the respective descriptions of those distinct offerings).

While the emission-based sector classification is a qualitative risk value informed by the average sector emissions as provided by ISS STOXX Climate Solutions, the SDG Solutions Assessment is entirely quantitative. This data feeds into the Carbon Risk Classification, whereas the Carbon Performance Score is derived from the Corporate Rating, which uses both quantitative and qualitative data. For more details, e.g., regarding data collection within those solutions, please refer to the respective descriptions.

## Use of Estimated Data

The Carbon Risk Rating relies upon estimated data in some areas.

- The Carbon Risk Classification is derived from the emission-based sector classification and the SDG Solutions Assessment. The former is leveraging average sector emission intensity data that is calculated based on both reported and estimated emissions. In the absence of reported data or if self-reported data is lacking quality, a proprietary approach is applied for estimating GHG emissions to provide a holistic, representative emissions dataset. To check the reliability of self-reported emissions data, ISS STOXX has developed a quantitative rating where, based on a proprietary methodology, a confidence level for the data is determined. If the confidence level of the reported data falls below a certain threshold the issuers data is manually reviewed by analysts and then the data is either accepted or replaced by estimated data.
- Across the covered universe, approximately 70% of data used for the emissions-based sector classification is modelled, mainly pertaining to scope 3 emissions. For the SDG Solutions Assessment, approximately 90% of data is estimated. Analysts are provided with clear guidance to ensure that estimated figures are based on reasonable assumptions with medium to high certainty.
- The Carbon Performance Score is derived from Corporate Rating indicators. For those quantitative indicators that are based on percentage assessments, estimations can be made if no (precise) reported data is available. Analysts are provided with clear guidance on how and in what instances estimations may be made. No estimations are made regarding absolute quantitative data (such as consumption data or intensities).

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