Deloitte.

Environmental, Social, and Governance (ESG): Another CEO imperative

Life sciences companies face distinct challenges with their very visible role in drug pricing and access to medicines, and the pandemic only underscored this focus. During the pandemic, life sciences companies came closer to their purpose—expanding environmental and diversity/inclusion goals and recommitting to social issues and health equity.[1] ESG (environment, social, and governance) at large is growing in importance as investors, partners, communities, customers, and employees increasingly scrutinize the companies they support.[2]

In 2022, ESG performance is expected to come under even more monitoring, and life sciences companies will need to home in on the material factors affecting the sector.[3] Work is also underway for new global ESG standards,[4] and companies will need to determine how best to demonstrate their progress with robust measures and enhanced disclosures.[5]

Materiality, measuring what matters most

Materiality for life sciences

Materiality in ESG defines what is important to stakeholders as well as what is important for business success.[6] Leading material factors for the life sciences sector include:

- Environmental sustainability, making medicines more sustainable and reducing greenhouse gas emissions, in particular, Scope 3 emissions of a company's supply chain[7]
- Drug pricing—balancing the need for innovation with the needs of policymakers[8]—and the broader effect from new ESG regulations[9]
- Access to medicines globally and supporting innovation in medicines and treatments with the greatest need[10]
- Health and race equity, including enhancing diversity in clinical trials[11]
- Diversity in leadership and income equality, including a gender pay gap in scientific research and the pharmaceutical industry[12]

Material issues may sway public perception, ESG ratings, and company valuations,[13] and companies that conduct materiality assessments have been shown to achieve significantly higher disclosure scores.[14] In addition to positive societal impact, companies with strong ESG propositions and materiality may benefit from quantifiable business value.[15]

E, S, and G issues increasingly intertwined

Environmental, social, and governance issues are becoming progressively intertwined. For example, making medicines sustainable protects the environment and has a social impact on the broader access to medicines. As a result, more companies are realizing that ESG metrics and business metrics are inextricably linked.[16]

> At the executive committee, when we review where we are and how we are progressing towards our objectives, we don't look at the ESG metrics separate from everything else, but rather, key elements of our ESG goals are an integral part of the broader set of operational goals and metrics that we review on a regular basis—they contribute to each other. For example, our ability to attract, retain and develop a diverse workforce contributes to our overall success and business results.

***Anat Ashkenazi**, CFO, Eli Lilly and Company*[17]

Transparently tackling ESG challenges with stakeholders

Forward-looking companies should welcome diverse stakeholders and incorporate their perspectives into strategic decision-making to solve ESG challenges. Communicating challenges promotes transparency, and working together with stakeholders may provide:

- A better understanding of the implications of decisions
- Support that minimizes risk
- A social license to act
- More trust and a better reputation[18]

Biopharma companies are often held to an unparalleled standard when it comes to motive and profit, although continued innovation and product availability depend on it. Building trust is a vital pathway to demonstrating the true value that biopharma companies and the rest of the health care system bring to society while also being accountable to shareholders and stakeholders.[19]

While investor relations is available to communicate with shareholders on concerns, Jim Greffet says that a large part of his role, as Head of ESG for Eli Lilly, is determining what is important to stakeholders by having an open door for discussion.[20]

> “The best way to understand what’s on your stakeholders’ minds is to talk to them.”
>
> *Jim Greffet, Head of ESG, Eli Lilly and Company* [21]

Climate disclosure mandates ramping up

The impacts of the environment and climate change are increasingly viewed as a growing financial risk—both in terms of a company’s exposure to impacts as well as their contribution to increased global warming.[22] As more robust data is being sought on environmental issues,[23] climate mandates are ramping up, especially in Asia.[24]

In 2021, New Zealand became one of the first countries to formally legislate the mandatory assessment and reporting of climate change risks by publicly listed companies, banks, investors, and insurers.[25] The Securities and Exchange Board of India rolled out a series of rules in 2021,[26] and Thailand’s SEC (Securities and Exchange Commission) will soon require companies to annually disclose ESG impacts and policies, including the level of greenhouse gases emitted.[27]

Non-financial ESG reporting is further along in the European Union, but the first set of reporting standards—the Commission’s proposal for a Corporate Sustainability Reporting Directive (CSRD)—is expected in October 2022.[28] In the United States, the SEC recently proposed new rules to standardize climate-related disclosures for US-listed companies.[29]

Growing focus on Scope 3 emissions

Investors are particularly interested in "Scope 3" disclosures—greenhouse gas emissions (GHG) that also include a company's suppliers and other partners. Under the US SEC's new proposed rules, registrants would be required to disclose Scope 3 GHG emissions, if material or if the registrant has set a GHG emissions target or goal that includes Scope 3 emissions. The proposed rules would provide a safe harbor for liability from Scope 3 emissions disclosure and an exemption from the Scope 3 emissions disclosure requirement for smaller reporting companies.[30] Digital solutions for measurement and optimization (that include Scope 3) are a core component of a successful Net Zero strategy.

Some life sciences companies are setting ambitious Scope 3 targets led by AstraZeneca (see figure 1).[31] In addition to its long-term target, AstraZeneca commits to reducing absolute scope 3 GHG emissions from fuel and energy related activities, upstream leased assets and downstream leased assets—80% by FY2030; from use of sold products—95% by 2030; and from upstream transportation and distribution, waste generated in operations, business travel, employee commuting and end of life treatment of sold products—46% by FY2030. All commitments are from a 2019 base year. AstraZeneca also commits to science-based targets by FY2025 for 95% of its suppliers by spend covering purchased goods/services and capital goods, and 50% of its suppliers by spend covering upstream transportation and distribution and business travel.[32]

Figure 1: Life sciences companies' absolute Scope 3 GHG Net-Zero commitments

Company	Target	Target Year	Base Year	Notes
AstraZeneca	90% reduction	2045	2019	Long-term target in addition to other shorter-term targets
Illumina, Inc.	46% reduction	2030	2019	From purchased goods and services, capital goods, upstream transportation and distribution, business travel, employee commuting and investments
Novartis	35% reduction	2030	2016	
Merck & Co., Inc.	30% reduction	2030	2019	Target boundary includes biogenic emissions and removals from bioenergy feedstocks
Pfizer Inc.	10% reduction 64% reduction	2025 2025	2019	10% from upstream transportation and distribution 64% of its suppliers by spend covering purchased goods & services Target boundary includes biogenic emissions and removals from bioenergy feedstocks
Johnson & Johnson	20% reduction	2030	2016	Target boundary includes biogenic emissions and removals from bioenergy feedstocks
GlaxoSmithKline	16% reduction	2030	2017	
Takeda	15% reduction	2025	2018	Through educating and influencing suppliers[33] and commits 67% of its suppliers by emissions covering purchased goods and services, capital goods and upstream transportation and distribution will have science-based targets by 2024
Sanofi	14% reduction	2030	2019	Target boundary includes biogenic emissions and removals from bioenergy feedstocks

Source:Science-Based Targets Initiative, 2021.

Broader effects on the supply chain and drug pricing

Additional costs are typically involved with meeting ESG criteria, and changes may have an effect on pharmaceutical pricing policies. Drug pricing is increasingly becoming a broader ESG topic, cutting across corporate governance, the investment community, and global access to medicines. But new ESG requirements may focus on the degree of influence a supplier has within the supply chain beyond Scope 3 greenhouse gas emissions.[34]

For example, the recently approved Supply Chain Due Diligence Act in Germany introduces new obligations for German companies with regard to protecting human rights in supply chains globally. The entire supply chain, from the extraction of raw materials to the delivery to customers, is covered by the new act—which will apply to companies with at least 3,000 employees in Germany in 2023, and those with at least 1,000 employees in 2024.[35]

Statutory health insurance funds in Germany are also introducing ethical considerations into pharmaceutical supply contracts. One tender for the supply of five antibiotics was part of the discount contract system that included a number of ESG conditions—including protections for workers' rights and environmental standards. Those with higher environmental standards had a better opportunity to win the contracts, while in the past, the main criteria was price.[36]

Collectively making medicines sustainable

The non-profit Sustainable Medicines Partnership (SMP) endeavors to bring the biopharma industry together on a single initiative—reducing waste in medicines. The biopharma industry produces 4.5 trillion medicines annually—and many are never used. For example, US$37 billion in medicines are lost every year due to failures in cold chain logistics alone.[37]

Another reason for waste is shelf life given to a medicine is typically based on the information available when it went through the approval process. But it may actually be twice as long before it is no longer effective.[38]

> "I saw the magnitude of the problem as well as the opportunities to deal with it. I wanted action"
>
> *Dr. Nazneen Rahman, Founder, YewMaker and Sustainable Medicines Partnership, Non-executive Director, AstraZeneca*[39]

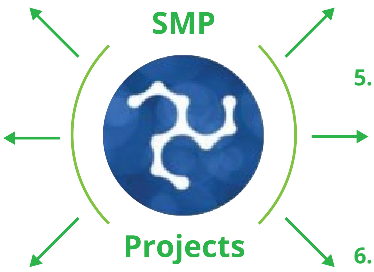
SMP is a four-year program designed to deliver evidence-based, scalable, and sustainable solutions that address six pillars to make medicines sustainable (see figure 2).[40] The organization is not only looking to rally the biopharma industry, but also collaborating with the 'Big 4', the NHS, health care, the medicines supply chain and packaging, government bodies, academia, researchers, designers, entrepreneurs, and patient groups.[41]

Figure 2: 6 pillars of the Sustainable Medicines Partnership

1. Transparent environmental impact
- Carbon footprint based on C02e not expenditure
- Practical, comparative tools & metrics
- Incentivised disclosure and reduction

2. End-to-end traceability
- Track sourcing, production, use and disposal
- Immutable record with integrated C02e
- Responsible, resilient, agile supply chain

3. Long shelf life
- Shelf life based on stability not approval timing
- Cost-effective, scalable shelf life extension process
- Standardised, simplified, incentivised



4. Digital patient information
- Digital by default, accessible to all
- Improved patient experience and adherence
- Substantial decrease in C02e and costs

5. Every dose used
- Quality assured, pre-expiry meds as standard
- Uncollected prescriptions
- Integrated with equitable access programs

6. Recyclable packaging
- Take-back packaging as standard
- Safe, cost-effective alternatives to incineration
- Reduce single-use with closed loop recycling

Source: Deloitte analysis

Improving access to medicines

Overall, pharmaceutical companies are making incremental progress in improving access to medicines globally and supporting innovation for treatments with the greatest need.[42] But the impact of these ESG factors was clearly highlighted by the pandemic.[43]

According to the Access to Medicines Foundation, 5 billion people have access to medicines, but there are 2 billion people to go.[44] The Access to Medicines Index is a tool designed to drive change in the pharma industry by tracking its progress.[45] The Foundation's new strategic direction for 2022-2026 expands the range of companies and healthcare sectors to mobilize in the fight against health care inequality.[46]

2021 Access to Medicines Index results

The 2021 Index analyzed how the world's top 20 pharmaceutical companies addressed access to medicine in 106 low- and middle-income (LMIC) countries for 82 diseases, conditions, and pathogens (see figure 3).[47] Companies were measured and ranked overall and in individual categories for:

- Governance of access
- Research & development
- Product delivery[48]

Of the 20 companies analyzed in 2021, GlaxoSmithKline (GSK) took first place overall as well as first place in the governance of access and research and development categories. GSK leads governance due to its clear access-to-medicine strategy embedded in its overall corporate strategy and CEO remuneration tied to access objectives. In R&D, GSK is undertaking 22% of the total number of priority R&D projects, followed by Johnson & Johnson with 13.6%.[49]

Novartis was the first to begin mainstreaming access planning across its pipeline[50] and attained first place for product delivery in the 2021 index, leading consistently across all access strategies.[51] In 2021, 8 companies adopted processes to systematically address access to medicine for all new products, and 12 out of 20 make access to medicines a direct board level responsibility. Sanofi was recognized for its approach to access strategies for supranationally procured products (procured through international organizations like The Global Fund).[52]

> "Large research-based pharmaceutical companies have a critical role to play in preparing for the next pandemic. While academic groups and small biotechs can pioneer new research ideas, big companies are essential in ensuring rapid development and access."

Access to Medicines Foundation[53]

Figure 3 :Access to Medicines Index 2021, top 20 pharma companies

Source: "Access to Medicine Index 2021," Access to Medicine Foundation, 2021.

Taking actions to improve access performance

Pfizer's performance in planning for access improved from previous years, helping the company move into a top 5 overall position for the 2021 Index.[54] Some actions Pfizer took to improve access include:

- Expanding access planning during development from vaccines to all products
- Launching a Global Pricing and Access Strategy that requires access planning for all products to commence two years pre-launch
- Sharing many IP assets with third-party researchers, e.g. for malaria and TB via research institutions and via the COVID-19 Therapeutics Accelerator
- Completing a sustainability bond whose proceeds are used for social (e.g. for COVID-19 and AMR Action Fund)and environmental projects[55]
- Reaching nearly 700,000 patients in 2020 through its ex-US patient assistance programs, some of whom may not have otherwise been reached through traditional commercial channels[56]
- Linking CEO remuneration to access performance.[57]

The Methodology Report for the 2022 Access to Medicines Index lays out the metrics by which companies will be assessed this coming year.[58] A greater weight will be put on R&D in 2022, focusing on indicators that measure outcomes, rather than polices and processes.[59] The 2021 Access to Medicines Index found that despite major gaps in the pediatric drugs pipeline, only 6% of R&D projects targeted children under 12 years of age.[60]

Leading health equity

Strategies for enhancing diversity in clinical trials

A material factor for life sciences under the social umbrella, or "S" in ESG", is diversity in clinical trials. COVID-19 brought existing social inequalities to the fore, and ensuring clinical trials better reflect patient populations will expand access to potentially life-saving therapies, build trust, and promote innovation.[61]

In the report, ***Five Key Strategies for Enhancing Diversity in Clinical Trials***, the Pharmaceutical Research and Manufacturers of America (PhRMA) and the Deloitte US Center for Health Solutions (CFHS) outline five critical strategies for enhancing diversity in clinical trials during the research and development of new medicines.[62]

- **Create a network of clinical trial sites in underserved communities.** Establish research sites in locations where potential participants already receive care, including non-traditional locations such as community health centers and pharmacies.
- **Develop a racially and ethnically diverse pool of investigators and staff.** These key community ambassadors can ensure that trials are culturally competent and mindful of unconscious/implicit bias.
- **Establish long-term relationships and invest in the community.** Prioritize long-term and sustainable community building efforts, like investing in health education or supporting the next generation of diverse health practitioners and investigators.
- **Engage the community in conversations.** Sponsors should communicate and work toward shared understanding with the community and seek input into the elements of design that might impact community members' ability to participate.
- **Provide sustainable support and standardized platforms.** Build a data infrastructure that leverages real world data and includes baseline measurements to improve data on race and ethnicity.[63]

A community-based clinical trial infrastructure may be the most effective way to sustainably accomplish the goals of enhancing access to clinical trials and promoting health equity. Shifting the paradigm will likely require substantial cross-stakeholder commitment and collaboration.[64]

Principles of health equity for medtech

Medtech makes the technologies and tests that are responsible for the accurate diagnosis of disease and improved patient outcomes. AdvaMed (Advanced Medical Technology Association) is a global trade association advancing the interests of the medtech industry and is working to ensure the industry is doing its part to mitigate the adverse impacts of health disparities among people and communities of color.[65]

AdvaMed's board-created and board-approved set of principles are designed to guide the industry in addressing racial health disparities. The principles call on industry to:

- **Promote inclusion and equity and health care.** Promoting unbiased treatment of patients likely requires partnerships to educate the industry and others on identifying, acknowledging, and addressing bias.
- **Partner in education with stakeholders.** Outreach to, and partnership with, clinicians to educate them regarding disparate trends in patient care, including access technologies.
- **Advocate for and facilitate patient access to innovative technology.** Develop and disseminate materials for use by patients, providers, and facilities.
- **Promote research equity in the medtech industry.** Require engagement and partnership with other caregivers and groups to bridge the gap, and promote the need for, involvement in studies and research to include more diversity among investigators.[66]

Health equity is covered extensively in Deloitte's 2022 Global Health Care Sector Outlook.[67]

Advancing diversity and women in leadership

Women appointed CEOs globally rose to 13% in 1H 2021, compared to 6% in the previous 6-month period.[69] In the Fortune 500, there were 41 women CEOs in 2021, an all-time record, but just 8.1% of the total.[70] In the Fortune Global 500, women accounted for 23% of the chief executives in 2021, including 6 women of color, also an all-time high.[71] As of January 2022, women hold 31 (6.2%) of CEO positions at S&P 500 companies.[72] Women of color hold only 1 percent of CEO positions across the Fortune 1000.[73]

Some notable new CEO appointments in 2021 for Life Sciences and Health Care include: Karen Lynch, CVS Health (the $268 billion health care giant is now the largest company ever to be run by a female chief executive); Roz Brewer, Walgreens Boots Alliance (the only Black woman currently running a Fortune 500 company); Reshma Kewalramani, Vertex Pharmaceuticals,[74] and Tan Sin Yin (Jessica Tan), co-CEO, Ping An Insurance.[75]

China capitalizes on digital platforms for health equity

For decades, China has strived to achieve health equity nationwide. During the pandemic, with many outpatient clinics closed and medical supplies low, patients with non-COVID-19 symptoms were among the hardest hit groups. Digital health care proved to be a promising solution to this issue, and the pandemic accelerated the development of many digital health platforms, including WeDoctor and Alibaba Health. These platforms facilitated online health care consultations and the delivery of medicine from health care institutions to patients—providing more accessibility. Digital accessibility was also encouraged in rural regions, where more patients delayed treatments than in urban areas.[68]

> We're seeing more intentionality. We're seeing a focus on women of color. And we're seeing a recognition that diversity and women in leadership is even more important.

Lorraine Hariton, CEO, gender equality organization Catalyst[76]

Research shows that efficiency gains from having a larger female representation in firm leadership can be quite large.[77] Women CEOs exhibited a different leadership style than men during the COVID-19 crisis—leaning toward empathy, adaptability, accountability, and diversity.

Women's more positive communication style scored higher for words expressing trust and anticipation, according to S&P Global.[78] They report that female CFOs are more profitable and have produced superior stock price performance compared to the market average. Women may be the most underutilized source of growth.[79]

According to the Women Business Collaborator, there are 10 accelerators for advancing women to the CEO role:

1. Recognize women's experience, talent and acumen to be CEO Leaders
2. Generate board support for women in the pipeline
3. Create shareholder and stakeholder value
4. Sponsor and advocate for women leaders
5. Include diverse women
6. Celebrate and affirm the men who are building pipelines
7. Use successful Women CEO role models as examples and advocates
8. Pay equal or better compensation
9. Search Firms to include women in their slates
10. Join and support women's organizations focused on position, pay and power for all women[80]

There is also a gender pay gap that needs to be addressed in the overall scientific research community and pharmaceutical industry.[81] A significant imbalance between genders was found by the British Gender Pay Gap Report.[82] It is interesting to note that GSK, the leader in access to medicines, had no gap in distribution of pay—and also appointed the first female to CEO of a leading pharma company, Emma Walmsley in 2016.[83]

In 2022, companies are expected to face continuing external pressures from institutional investors, activist shareholders, potential employees, and customers to increase the representation of women on corporate boards, in C-suite positions, and across executive leadership, as well as equal compensation and mobility for women and people of color.[84] If life sciences companies are to be truly understanding of the diverse patient population they seek to serve, executive and board members should also be truly representative.[85]

ESG ratings and raising levels of public trust

More than 150 ESG ratings and data providers

Rating agencies and data providers are useful tools for measuring an organization's positive or negative impact on ESG issues. But the sheer number of firms to consider—each using its own methodology—is often a challenge.[86]

There are at least 600 products from more than 150 organizations providing ESG data to corporations and asset managers. Leaders in the field include MSCI, Sustainalytics, ISS ESG, Bloomberg, and S&P Global (TRUCOST). Some data providers are specific to industries—like the Access to Medicines Index.[87] Chinese ratings providers come from many diverse viewpoints, ranging from traditional index/data providers, fintech companies, asset managers/owners and academic/non-profit institutions to consulting companies.[88]

As a result, rankings from the many data firms assessing ESG performance vary.[89] Novartis, an ESG leader in the sector, publishes its performance ratings provided by various agencies (see figure 4).[90]

Figure 4: Novartis performance ratings across ESG ratings providers, updated January 2022

Agency	Rating	Current	Previous	Industry perspective
Access to Medicine Index[1]	Score	4.18 ▲	3.2	2 / 20
CDP[2]	Climate score	B ▼	A-	Management band B/B-[9]
	Water score	A- ▼	A	Leadership band A/A-[9]
FTSE4Good[2]	ESG score	4 ▼	4.7	n/a[10]
ISS ESG[2,3]	ESG score	B ▶	B	4 / 473
MSCI[2,4]	ESG score	A ▶	A	Best rated peers: AAA (3 PharmaCos), AA (10 PharmaCos)
	MSCI Global Compact	Pass ▲	Watchlist	
	Controversy[7]	3 ▲	1	
S&P Global[2,5]	ESG score	83 ▲	73	5 / 91 in Pharmaceuticals (97th percentile)
Sustainalytics[2,6]	Risk score	17 ▲	21	1 / 432 in Pharmaceutical subindustry group[11]
	Controversy level	3 ▶	3	

1. Published every 2nd year. Result shown shows 2020/20218 scores 2. 2021/2020 scores 3. Published every 2nd year. Updated December 2021. 4. Updated December 2021 5. Updated December 22, 2021. Novartis has been a DJSI World member since 2022 6. Updated April 2021 7. 0-10 scale, 0 being most severe controversy 8. Leadership as defined by rating agencies 9. Climate: Novartis received a B (Management band), same as the Biotech & pharma sector average, Water: Novartis received a A-(Leadership band), higher than the Biotech & pharma sector average 10. Novartis is in the top 5 Pharmaceuticals 11. Pharmaceuticals subindustry group.

Source: Novartis, January 2022.

> ESG is central to the Novartis strategy and is critical to delivering on our purpose to reimagine medicine to improve and extend people's lives. Looking ahead, we are renewing our focus on our ESG material topics, redoubling our efforts on improving access to medicines and accelerating our journey toward a zero-carbon future.

Vas Narasimhan, CEO, Novartis[91]

Bridging the ESG perception/reality gap

There is an overuse of cliches in ESG reporting, and stakeholders expect to see evidence of action, not empty words.[92] However, despite actions, more than 90% of 250 public companies studied by data company RepTrak have a perception/reality gap between public opinion and ESG actions/ratings.[93] With this gap, a company may be judged more harshly in a crisis scenario,[94] and the pandemic demonstrated the importance of anticipating and managing risk.[95]

To mitigate this risk, biopharma companies might consider working together on specific ESG initiatives to build more trust and raise public opinion of the industry[96]—especially since biopharma ranks as one of the least trusted industries according to many consumer polls.[97] While public opinion improved during the pandemic, recent Deloitte research found the lowest levels of trust for biopharma to be in the United States and the highest in India.[98]

Preparing for new global standards

A significant challenge—for ratings' agencies, asset managers, and companies themselves—is that ESG information is not reported in a standardized way.[101] The IFRSF (International Financial Reporting Standards Foundation) formed the International Sustainability Standards Board (ISSB) to provide the global financial markets with high-quality disclosures on climate and other sustainability issues. Consolidation of several standard-setters is expected by June 2022, with the release of the first batch of climate-related disclosure standards.[102]

The World Economic Forum's International Business Council welcomes the arrival of the new IFRSF standards that the IFRSF has indicated[103] and suggests companies consider its Stakeholder Capitalism Metrics framework to prepare.[104] Life sciences companies should not wait for mandates and can begin by:

- Identifying the metrics most relevant to their own company's strategy and stakeholders as well as those relevant to the life sciences sector[105]
- Identifying a full list of individuals and groups whose interests are affected or could be affected by its company's activities[106]
- Monitoring and evaluating how new and existing third-party relationships impact the company's ESG priorities
- Collaborating across the ecosystem to simplify data collection, synthesis, and reporting
- Looking for ways to transform business models and innovate solutions to move toward goals
- Communicating the company's ESG vision and strategy early to win support[107]

Financial vs non-financial ESG communications

Sustainability reporting is expected to be a trusted, credible, and relevant resource for stakeholders–making a clear link between financial and non-financial information.[99] Some companies may create problems by repurposing technical financial investor information into other public communications geared to a less technical audience. While at times this may be a matter of resources, life sciences companies should consider the effects on public perception, and opt for more authentic messaging targeted to each specific audience.[100]

Gathering data for better ESG reporting

It is important that corporations measure and report on the results of their ESG efforts to live up to the purpose set for the enterprise. This enhances integrity and authenticity of the environmental and social goals.[108] Selective reporting that does not connect narrative information and financial information can lead to greenwashing.[109] The temptation can be great for being seen as ethical, as this may drive profitability. But the risks remain, even if unintentional, with bad data and communications.[110]

Watchdogs are analyzing ESG reports, questioning the substance of companies' pledges and looking for evidence of greenwashing.[111] By utilizing better data and analytics, companies can have a more systematic, quantitative, objective, and financially relevant approach to key ESG issues—providing ESG reporting with data integrity.[112]

Demonstrating performance for ESG reporting starts with:

- Knowing what needs to be collected
- Knowing who needs to be involved in the process
- Knowing where the data is in the business
- Developing a robust, future-proof data collection process[113]

In addition to data management, Deloitte research finds that organizations could likely improve the efficiency and effectiveness of ESG reporting processes with an integrated and automated platform approach. Strong governance and internal controls in ESG measurement and disclosure are part of establishing a comprehensive strategy for integrating ESG considerations into business processes.[114]

> As a board member, it's also my responsibility to ensure that ESG reporting is not a marketing exercise but one that transparently lays out a set of goals that leadership is measuring its performance against.

Jamere Jackson, CFO of AutoZone, Audit Committee Chair, Eli Lilly and Company[115]

Investor focus on ESG reporting

ESG now accounts for 10% of global fund assets, and 2021 was a record year for investment. US$649 billion poured into ESG-focused funds worldwide thru 30 November 2021, up from US$285 billion in 2019.[116] Experts say US$4 of every US$10 moving into global equity funds is being diverted to ESG funds.[117] From the US$6.1 trillion held in ESG funds, 59% is held in Europe, Middle East, and Africa, according to Refinitiv Lipper Research.[118]

While inflows in European ESG funds decreased in 2021, this was more than offset by rising flows into US and Asian ESG funds. In China, RMB 250 billion (US$39.3 billion) was invested in ESG funds through Q3 2021,[119]and the number of funds surged to 48—close to the total of the previous 5 years.[120]

Foreign investors in Chinese assets have to meet their fund domicile standards on ESG when investing in China, which is driving improved reporting by Chinese firms.[121] Researchers studied a novel dataset that showed ESG performance in China positively associated with the short-term cumulative returns of CSI 300 stocks around the COVID-19 crisis. They concluded that investors may interpret ESG performance as a signal of future stock performance and/or risk mitigation in times of crisis.[122]

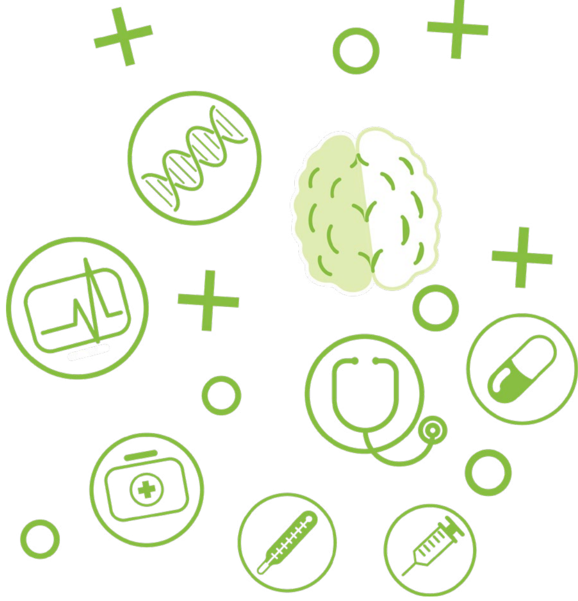
Investors are looking for demonstrative ESG reporting to compare a company's ESG risks and opportunities to their business strategy, operations, and financials.[123] In 2022, as the velocity of ESG investments rise[124] and investor focus on ESG practices grows, more board members are considering whether ESG measures should be incorporated into executive incentive plans to hold management accountable for ESG results.[125] ESG is expected to remain front and center for 2022.[126]

New sustainability-linked bonds (SLB) tied to climate, access to medicines, biodiversity

Since Novartis became the first pharma to create an SLB in 2020, SLBs have become a growing trend.[127] In November 2021, a global pharma manufacturer linked both climate and access to medicine targets to an SLB. Their US$5 billion bond is the largest of its kind from any sector and the first issued by a generic medicines company. They are committing to access to medicine targets with a 150% increase in both the number of registrations and products provided through access programs in LMICs.[128]

In addition to access to medicines and other ESG concerns, part of Eli Lilly's sustainability bond is tied to a specific category addressing terrestrial and aquatic biodiversity conservation—using their skills in genetic engineering and recombinant technology to avoid testing on animals. Since 7 out of 8 manufacturing plants have transitioned, there is larger effect on the environment and conservation. For example, by eliminating testing on horseshoe crabs, an endangered species, Eli Lilly also protects the birds that feed on the crab's eggs.[129]

In 2022, companies can expect more scrutiny for SLBs. While SLBs are linked to Key Performance Indicators (KPIs), there are no standards. Penalties for missing KPIs are often less serious. Another issue is that the maturity date of the bond and the measurement of the KPIs often coincide, potentially enabling the issuer to redeem early if KPIs are going to be missed.[130]



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