ESG Ratings Service report

April-June 2022

A report by EIU

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Contact us

LONDON

Economist Intelligence
20 Cabot Square, London E14 4QW,
United Kingdom
Tel: +44 (0)20 7576 8000
e-mail: london@eiu.com

NEW YORK

Economist Intelligence
750 Third Ave, 5th Floor,
New York NY 10017, United States
Tel: +1 212 541 0500
e-mail: americas@eiu.com

HONG KONG

Economist Intelligence
1301 Cityplaza Four 12 Taikoo Wan Road Taikoo Shing, Hong Kong
Tel: + 852 2585 3888
e-mail: asia@eiu.com

GURGAON

Economist Intelligence
Skootr Spaces, Unit No. 1 12th Floor, Tower B,
Building No. 9 DLF Cyber City, Phase - III Gurgaon - 122002 Haryana,
India
Tel: +91 124 6409486
e-mail: asia@eiu.com

DUBAI

Economist Intelligence
PO Box No - 450056, Office No - 1301A Aurora
Tower Dubai Media City Dubai,
United Arab Emirates
Tel: +971 4 4463 147
e-mail: mea@eiu.com

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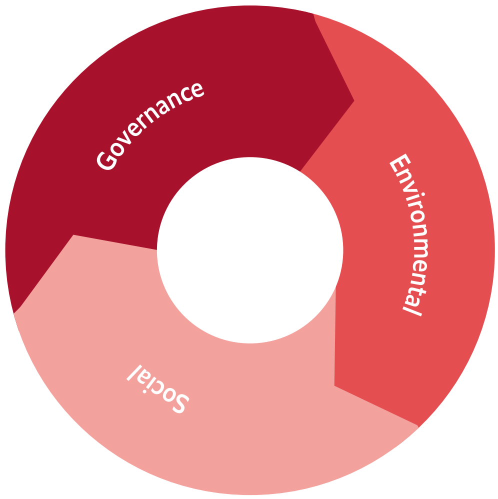
ESG ratings review: Environmental performance improving, but decarbonisation faces risks

- The top of EIU's ESG rankings changed little during the second quarter of 2022, with Europe, Australia and New Zealand continuing to dominate. Japan managed to break into the top 20 (rising from 23rd place to 20th), mainly owing to a stronger performance in our Decarbonisation category, driven by improvements in the Responsible production and consumption indicator. Although Japan has long had an impressive plastic recycling rate, the enactment of the Plastic Resource Circulation Act earlier this year mandates that businesses reduce the usage of disposable plastics items and promote the recycling of plastic waste.
- China's already weak ESG profile deteriorated, dragging the country into the bottom fifth of our overall ESG rankings (falling from 116th place to 121st). Although the UN reported that other countries expanded their protected land area significantly, this metric remained static for China. Additionally, China's governance score also deteriorated during the quarter, primarily owing to the onerous restrictions imposed on the populace in an attempt to enforce its zero-covid policy.
- The Environment pillar was the main driver of improvements in our ESG ratings in the second quarter. This was the result of broad-based improvements in our Environmental Stewardship category, mainly due to larger estimates from the UN with regard to the area of protected land in many countries. However, we expect Decarbonisation scores to deteriorate over the remainder of 2022 and in 2023 as a result of the global energy crisis.
- This quarter's edition of EIU's ESG ratings includes changes to three of the 90 indicators that make up the scoring model. All three changes were to indicators in the Environmental pillar of the ratings. Indicators were added for measuring Deforestation Area, Species Covered By Protected Areas and Renewable Energy Regulation in a country. To make way for these three new indicators, we removed from the ratings model indicators for Threatened Mammal Species, Ecosystem Vitality and Climate Action.

To measure the impact that actors in a country have on sustainability, the overall ESG assessment considers nine categories, equally balanced across the three pillars: environmental, social and governance.

- Electoral process and pluralism
- Functioning of government
- Corporate governance

- Labour conditions
- Equality rights
- Civil rights



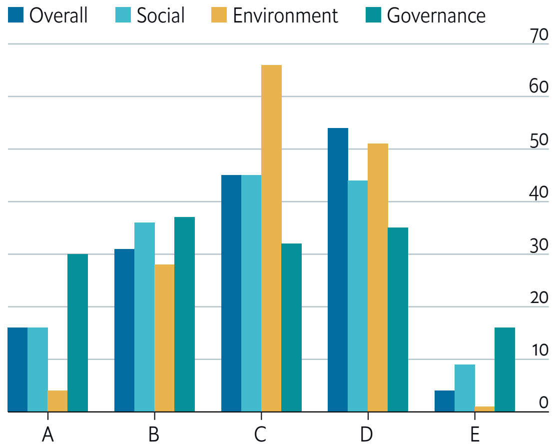
- Decarbonisation
- Environmental stewardship
- Water and waste management

The performance of countries in our ESG ratings deteriorated slightly in the second quarter. On the upside, 16 of the 150 countries covered by the ratings remain rated as A. Moreover, Jamaica moved up from a C to a B rating, taking the total number of B ratings to 31. However, three countries (Rwanda, Kyrgyzstan and the UAE) slid from a C to a D rating.

From a thematic perspective, the Environment pillar was the main driver of change in our ESG ratings last quarter. Within the Environmental pillar, 11 countries moved into a different ratings band, compared with seven in the Social pillar and four in the Governance pillar. Countries including Mali, Burkina Faso and Sierra Leone made significant gains in the Environment pillar, mainly

Few strong performers in the environment pillar

(ESG scores by country rating A-E)



Source: EIU.

Biggest movers in Q2 2022

	Q1 2022	Q2 2022	Ranking places gained/lost
Benin	113	100	13
Mali	122	112	10
Kazakhstan	121	112	9
Belarus	120	112	8
Moldova	76	70	6
Ghana	66	61	5
Liberia	99	94	5
Burkina Faso	113	108	5
Algeria	129	124	5
Pakistan	128	124	4
Slovenia	19	23	-4
Namibia	44	48	-4
Uganda	108	112	-4
Albania	53	58	-5
UAE	92	97	-5
China	116	121	-5
Jordan	96	102	-6
Kuwait	98	104	-6
Lebanon	108	117	-9
Eswatini	101	117	-16

Source: EIU

owing to improved performance in our Decarbonisation and Environmental Stewardship categories.

From a geographic perspective, all of the top ten gainers in the ESG rankings were emerging markets, although none of these ten countries ended up in the top 50. The most significant climbers were Benin and Mali, although neither country broke into the top 100. Ghana is the highest ranked of these ten countries, having moved up from 66th to 61st place.

There was little change at the top of our ESG rankings, with Europe, Australia and New Zealand continuing to dominate. However, Japan managed to break into the top 20 (rising from 23rd to 20th), mainly owing to a strong performance in the Decarbonisation category.

ESG rankings: top ten countries

	Q1 2022	Q2 2022	Ranking places gained
Denmark	1	1	0
Finland	2	2	0
New Zealand	3	3	0
Sweden	4	4	0
Norway	6	4	2
Ireland	5	6	-1
Luxembourg	6	7	-1
Switzerland	6	8	-2
Netherlands	9	9	0
UK	9	10	-1

Source: EIU

ESG rankings: bottom ten countries

	Q1 2022	Q2 2022	Ranking places gained
Djibouti	139	141	-2
Chad	143	141	2
Venezuela	144	141	3
Laos	141	144	-3
Congo (Democratic Republic)	145	145	0
Iraq	146	146	0
Myanmar	147	147	0
Yemen	148	148	0
Iran	149	149	0
Sudan	150	150	0

Source: EIU

Environmental performance has improved, for now

Ratings revisions were more common in our Environment pillar than in the Social and Governance pillars. Out of the 150 countries rated, 11 moved into a different rating band for Environment (six moved up and five went down). Our Environmental Stewardship category was a significant driver of these ratings changes owing to an extensive update by the UN to some of the data underpinning our model. Specifically, four indicators that measure the extent to which environmentally sensitive areas in a country are legally protected (Protected land, Protected freshwater, Protected forest area and Protected marine territorial waters) were both updated and revised. Despite these ratings changes, Environment remains the worst-performing of the three pillars in our ESG ratings, with only four countries (Denmark, Estonia, Latvia and Lithuania) receiving an A rating, compared with 16 countries in the Social and 20 countries in the Governance pillars.

Looking ahead to the remainder of 2022 and 2023, we expect Decarbonisation scores to deteriorate for most countries as a result of the global energy crisis. Disruptions in global energy markets caused by the pandemic and the war in Ukraine have forced governments in the developed and the developing world alike to shift their focus from the energy transition to short-term energy security. This shift is diverting some resources from renewables to fossil fuels, aided by the returns on offer from the spike in commodity prices.

For instance, the European Commission's REPowerEU, released in May, plans to wean the bloc off energy imports from Russia, partly by allowing for a more gradual phase-out of coal-powered electricity generation in the EU than previously anticipated. Germany's government, which includes The Greens environmentalist party, has approved an increase in coal usage in order to build up gas reserves for the winter. China's government is also trying to reduce record power prices by encouraging a massive ramp-up in coal production. It has approved three new coal mining projects in early 2022, as well as permitting the construction of five new coal power plants. By contrast, permits for large projects remained largely frozen in 2021 owing to emissions concerns.

Looking beyond 2023, however, the global energy crisis will probably accelerate public and private investment into renewables in order to speed up the transition away from fossil fuels, at least in developed economies. Renewable energy power generation will be seen as an attractive way of reducing exposure to volatility in global fossil-fuel supplies and prices. For instance, the EU's REPowerEU plan anticipates an extra US$221bn in investment into renewable energy generation between 2022 and 2027 as a result of reduced oil and gas imports from Russia. The Commission aims to increase the share of renewable energy in the EU's energy mix to 45% by 2030, up from the previous target of 40%.

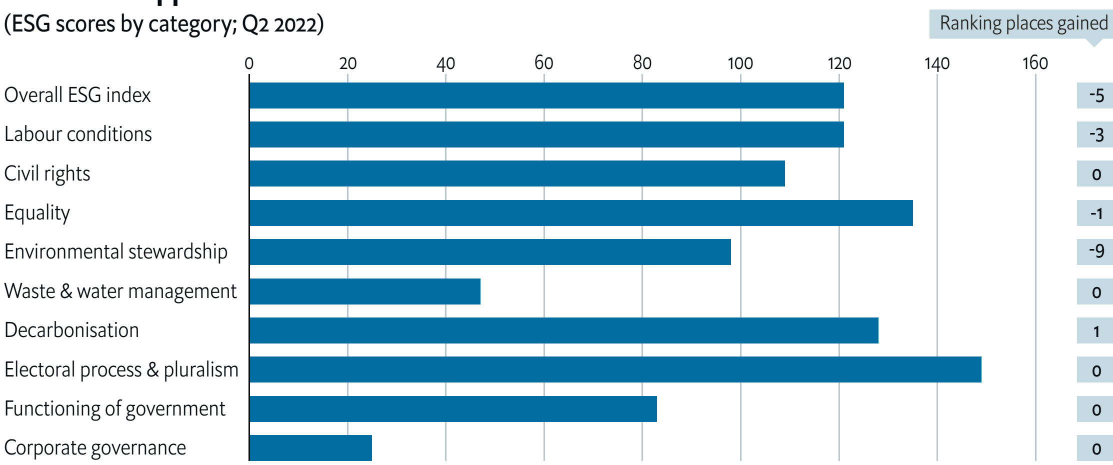
Environmental Stewardship improves as protected land area rises

Our overall score for the Environmental stewardship category has improved owing to an increase in protected land area in countries across the world. According to the UN's *Protected Planet Report 2020*, between 2010 and 2020 nearly 82% of countries had raised their share of both designated protected areas and geographical areas protected through Other Effective Area-based Conservation Measures (OECM). OECM is a conservation definition that refers to a geographically defined area, distinct from a protected area, where positive long-term conservation outcomes are still being achieved. This amounts to an increase of more than 21m square km, which means that 42% of the world's protected areas were added over the past decade. As at May 2021 more than 28m square km of coastal waters and more than 22m square km of land and inland water systems were within protected areas and OECMs.

China's underperformance worsens

China's already weak ESG profile deteriorated in the second quarter, dragging the country into the bottom-fifth of our overall ESG rankings (down from 116th to 121st). China's rank deteriorated in all three pillars, falling from 97th place to 109th for Environmental, from 122nd to 126th for Social and from 103rd to 106th for Governance. The particularly large slide in China's ranking for Environment was mainly due to a lower ranking in the Environmental Stewardship category (from 89th to 98th). New data from the UN revealed significant expansion of protected land for many other countries, while the area of protected land in China remained stable. The slow pace of improvement in China's Environmental Stewardship profile also resulted in the country being downgraded in the Environmental Stewardship Trend component of this category.

China has slipped backwards on ESG
(ESG scores by category; Q2 2022)



Source: EIU.

China's Governance profile also deteriorated in January-March, mainly owing to a poorer score for Excessive Executive Power. China's zero-covid policy has resulted in significant restrictions on civil liberties since the start of 2022, with a return to the severe lockdown measures last seen in early 2020. Although Shanghai's lockdown has now been lifted, as at mid-June 2022 around one-third of China's population, mostly in the biggest population centres, were still required to show nucleic acid results in order to use public transport or enter public facilities. We expect the government to continue with its zero-covid strategy into 2023, which means that the country's Governance scores will remain low.

Japan moves up the rankings on Decarbonisation gains

Japan rose from 34th to 13th in our ranking for Responsible Consumption and Production, which is an indicator in our Decarbonisation category based on the UN's assessment of a country's progress towards Goal #12 of the Sustainable Development Goals ("Ensure sustainable consumption and production patterns"). This improvement has been supported by reductions in production-based nitrogen and sulphur dioxide emissions and a decline in non-recycled municipal solid waste.

The country has long sported an enviable plastics recycling rate of 85%. The Plastic Resource Circulation Act, enacted in April this year, urges manufacturers to consider recyclability in the design of all their products and packaging, and requires major hotels and convenience stores to charge customers for disposable plastic items such as single-use bags, plates and cutlery, and to only offer items made from at least 60% recycled or biodegradable materials.

New indicators included this quarter

In constructing our rating system, EIU and the wider Economist Group aim to use indicators that are mutually exclusive and collectively exhaustive (MECE)—that is, that answer a fundamental question as completely as possible, without overemphasising one aspect of the measurement. For this reason, we use an unweighted model and the same number of indicators over time. The balance of indicators within our ESG ratings is extremely important.

We are continually testing new data sources to find ways to improve our ESG rankings. We will occasionally substitute data sources in our model when we believe that we have found a better or more reliable metric. Typically, this occurs when either: (a) newly available data provide a superior measure of some aspect of ESG compared with the data source that we are currently using; or (b) we decide that an existing indicator is inadequate and exchange it for an alternative, pre-existing data source.

This quarter's edition of our ESG rankings includes changes to three of the 90 indicators that make up the scoring model. All three changes were to indicators in the Environmental pillar of the ratings.

1. Pillar - Environment
Category - Environmental Stewardship
Indicator - Deforestation

- For indicator Ind-EE05, we substituted in a new measure of Deforestation Area, which now complements the pre-existing measure of Deforestation Growth (Ind-EE13). Whereas Deforestation Growth measures the percentage change in the area of naturally regenerating forest over the previous five years, Deforestation Area measures the absolute area of deforestation in a country. We made this change to highlight countries where even small percentage changes in forest area have a globally significant impact. This approach underlines how countries including Brazil, the Democratic Republic of the Congo and Indonesia are experiencing exceptional absolute levels of deforestation, despite only suffering relatively small percentage changes in forest area.

- To make way for the Deforestation Area indicator, we removed the Threatened Mammal Species indicator from the ratings. The ratings already contain one measure of Endangered Species (Ind-EE09), which is based on the Red List Index (RLI) from the International Union for Conservation of Nature and Natural Resources. We decided that a second measure of local threatened species was superfluous.

2. Pillar - Environment
Category - Environmental Stewardship
Indicator - Species covered by protected areas

- The Environmental Stewardship category contains four measures of how much of the ecologically sensitive land area in a country is legally protected. The Environmental Stewardship category already measures the percentage of freshwater (Ind-EE04), forest (Ind-EE06), marine waters (Ind-EE07) and sites deemed important for terrestrial biodiversity (Ind-EE03) that are legally protected in a country. In the second quarter of 2022 we added an indicator measuring Species Covered By Protected Areas (Ind-EE08). Based on the Map Of Life's Species Protection Index (SPI), this metric measures how effectively conservation areas conserve habitat and support the health and survival of species and their populations.
- To make way for the Species Covered By Protected Areas indicator, we removed Ecosystem Vitality from the ratings. This indicator was based on Yale University's Ecosystem Vitality Index, which is part of the university's Environmental Protection Index. The Ecosystem Vitality Index is a broad measure of environmental conditions in a country that overlap with other metrics in our ESG ratings. As we prefer to use indicators that are specific to a particular aspect of ESG, the general Ecosystem Vitality score was a prime candidate for replacement.

3. Pillar - Environment
Category - Decarbonisation
Indicator - Renewable energy regulation

- We added a measure of Renewable Energy Regulation (Ind-ED08) to the Decarbonisation category of the Environment pillar. This indicator is based on the World Bank's Regulation Indicators For Sustainable Energy (RISE) data. We believe that the inclusion of this metric strengthens the coverage of "energy transition" within the Decarbonisation category. The Decarbonisation category now has five indicators broadly measuring a country's energy transition. These are: Renewable energy capacity growth (Ind-ED01), Renewable energy share (Ind-ED02), Low-carbon transition exposure (Ind-ED07), Renewable energy regulation (Ind-ED08) and Responsible consumption and production (Ind-ED09).
- To make way for the Renewable Energy Regulation indicator, we removed the indicator Climate Action from the Decarbonisation category. Climate Action was a measure of a country's performance against goal 13 of the UN's Sustainable Development Goals, namely "Take urgent action to combat climate change and its impacts". This metric overlapped with many of the other indicators in the Decarbonisation category. As we prefer to choose indicators that are fairly specific to a particular aspect of ESG, Climate Action was a prime candidate for replacement.

Update on key ESG legislation: Q2 2022

US (proposal, May 2022)

The Securities and Exchange Commission (SEC) has proposed amendments to the Investment Advisers Act of 1940, requiring advisers to disclose information on how they incorporate ESG into their advice. The amendment would create three categories of ESG investment strategies:
integration (where ESG is one factor among several);
focused (where ESG is a major factor); and
impact (where enhancing ESG is the investment priority).

US (legislation, effective June 2022)

The Uyghur Forced Labor Prevention Act, signed December 2021, prevents the entry of goods manufactured in the Xinjiang province of China. The only exception to this rule would be if the Commissioner of US Customs and Border Protection ruled that such products were not produced using forced labour.

Singapore (proposal, May 2022)

Following a consultation period, the Green Finance Industry Taskforce (GFIT) has proposed a GFIT Taxonomy for Singapore-based financial institutions to encourage investment in sustainable activities.

China (legislation, effective February 2022)

China's Ministry of Ecology and Environment (MEE) has mandated that certain organisations must make environmental disclosures annually starting from February this year. The rules apply to listed companies and bond issuers that were penalised for environmental reasons in the previous year, as well as organisations that discharge a significant amount of pollutants. The rules are part of the MEE's efforts to implement the Plan for the Reform of the Legal Disclosure System of Environmental Information that it issued in May 2021.

EU (legislation, effective January 2022)

The EU's Taxonomy Regulation came into effect from January this year, outlining technical criteria and disclosure requirements for ESG monitoring. The European Central Bank (ECB) and the European Securities and Markets Authority (ESMA) will now require certain institutions to undergo regular climate-related stress tests.

EU (agreement, effective January 2023)

In June the EU reached a provisional political agreement on adopting the Corporate Sustainability Reporting Directive, which will become effective for large companies in the EU by 2023.

Germany (legislation, effective 2023)

Germany's Supply Chain Act (Lieferkettensorgfaltspflichtengesetz), approved in June 2021, obliges all companies with German registration to monitor their supply chains for compliance with environmental standards and to avoid human rights violations. The legislation comes into effect on January 1st 2023 for companies with more than 3,000 employees, or in January 2024 for those with more than 1,000 employees.

Environmental
Transition policies face energy security headwinds

Key takeaway: Our ESG ratings highlight that decarbonisation is a weak point for many countries, including otherwise strong ESG performers such as Canada, Australia and Norway. In this article, we assess how high progress towards decarbonisation in these and many other countries will slow in 2022 owing to concerns over energy security.

Europe| World| Industry| Highlights| Energy| Energy policy

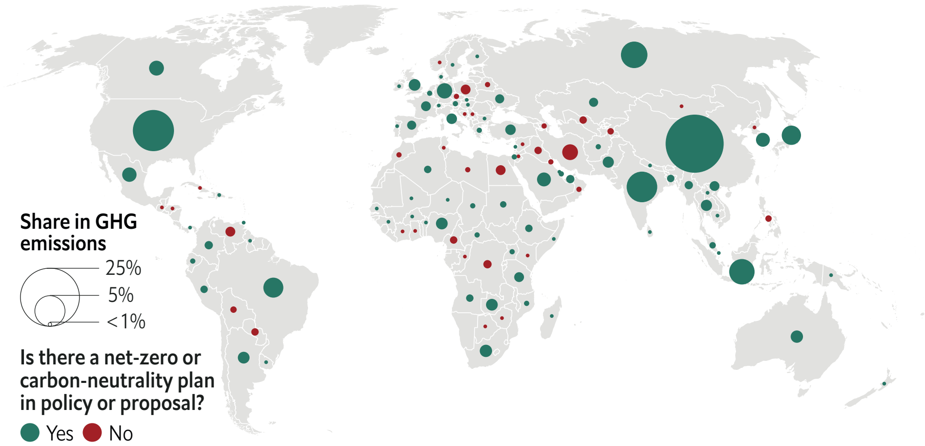
April 12th 2022

- **Energy transition is expected to retain a central role in energy policy, but concerns over energy security amid the war in Ukraine risk delaying decarbonisation efforts.**
- **High energy costs and supply uncertainties have prompted some governments to scale back climate goals and to shift the policy focus towards ensuring energy security.**
- **High commodity and capital costs will add to the challenges related to energy transition and will have a significant impact on developing countries in particular.**
- **Recent IPCC reports have highlighted the need to adapt to climate disasters, and where mitigation efforts are falling short of climate goals, adding to the list of areas in need of policy and investment support.**
- **Country peculiarities in terms of development and fossil-fuel resources would determine the focus of energy policy in the foreseeable future.**

The transition to a clean energy economy has been a fundamental long-term dynamic for the global energy industry in the past few years. Energy-related emissions, predominantly from fossil fuel combustion, account for about 90% of global total carbon dioxide (CO_2) emissions. Energy transition to low-carbon sources retains the central role in policies to tackle climate change, but recent global incidents have thrown up challenges.

About 140 countries globally have announced some sort of net-zero or carbon neutrality target, although with varied timelines, covering almost 90% of global emissions. Substantially increasing renewables in the energy mix, which requires massive investments, is a central goal in most of those commitments. Such targets require action now, but can only yield benefits in future years. This often means that seemingly more pressing economic concerns, such as high energy costs, take precedence.

Net-zero targets cover about 90% of global emissions
(share in global greenhouse gas emissions)



Sources: Net Zero Tracker; Climate Action Tracker; EIU.

Disruptions in the global energy markets caused by the pandemic and the war in Ukraine have uncovered major risks as governments, in the developed and the developing world alike, are shifting their focus from the energy transition to short-term energy security. A focus on the latter would lead to diverting some resources from renewables to fossil fuels.

Recent events lead to a shift in policy emphasis

To reduce dependence on a single source, the EU's REPowerEU plan targets completely abandoning Russian gas by 2030, substituting it with liquefied natural gas (LNG), in addition to a continued adoption of renewables and energy efficiency. Increasing LNG imports will require massive investments in developing new regasification terminals required to receive LNG, and possibly funding liquefaction terminals in exporting countries to secure long-term supply guarantees.

ETS price has bounced back but remains below pre-invasion levels
(ETS futures price, €/mt of CO_2)

Sources: ICE; EIU.

Although the EU policy does not dilute the importance of moving away from fossil fuels, the policy effort required to strengthen energy security could delay decarbonisation and curtail investment in clean energy. Carbon prices on the EU emissions trading scheme (ETS) have dropped dramatically and remain below pre-invasion levels, as an indication of market sentiment for an expected delay in Europe's decarbonisation drive.

At its annual legislative meetings held in March 2022 China suggested that it was taking a flexible approach to its carbon emissions and energy-saving goals set under its 14th five-year plan framework. The country delayed its deadline of "peak carbon use" in the steel sector from 2025 to 2030, and indicated plans to increase domestic coal mining capacity, despite efforts in recent years to reduce coal consumption. These changes reflect a re-prioritisation of near-term growth prospects, amid an economic environment clouded by the prolonged effects of the pandemic, disruptions caused by the war and stress in the domestic property market. The softening approach highlights the acknowledgment of challenges in achieving ambitious climate goals while ensuring energy security and economic growth.

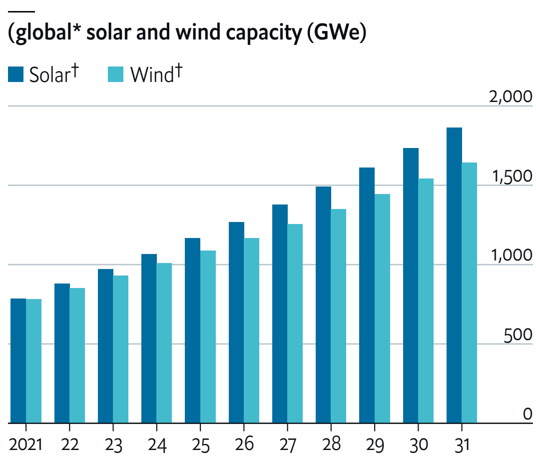
Despite the recent challenges, we believe that in the long-run the two goals of energy transition and energy security could converge, as renewables are increasingly viewed as a secure, abundant and affordable source of energy. Such a convergence in policy thinking is more likely in fossil-fuel importers such as Europe, Japan and China, but may face higher resistance in countries such as the US, Canada and Australia, which may find it attractive to double down on their domestic hydrocarbon reserves.

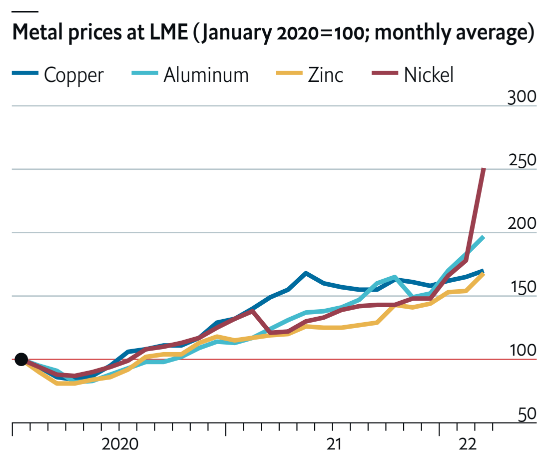
Market fundamentals as dampener

Furthermore, the war in Ukraine has caused a steep rise in the prices of many base metals such as copper and zinc, which are important inputs in solar and wind farms. Prices of nickel and lithium, which are used in batteries, have also climbed since the invasion. Affordable battery technology is crucial for decarbonising the auto sector and supporting a renewables-based power system, which is characterised by intermittent generation due to weather-related factors.

Long-term purchase contracts may insulate manufacturers from cost pressures in the short term,

High commodity prices will hinder energy transition



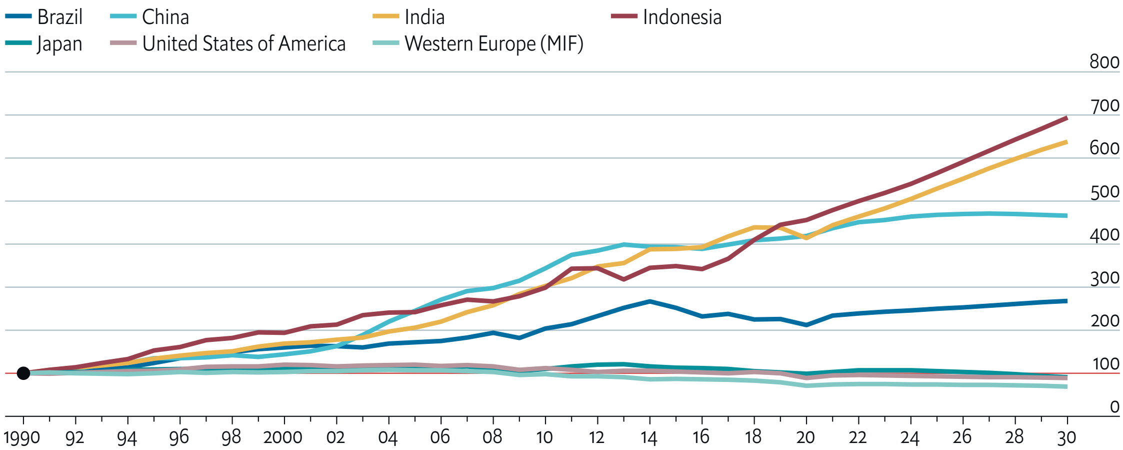


Sources: IEA; World Bank; EIU. *Aggregate of 68 countries covered by EIU service. †2022-2031 values are EIU forecasts but elevated prices of these metals for an extended period will make the transition costlier, potentially causing higher resistance to abandoning dirty fossil fuels.

On the financial side, central banks moving to a monetary tightening cycle will discourage investment capital for development or scaling of nascent technologies such as carbon capture and green hydrogen, which are necessary for expediting the transition process.

From an international perspective, these trends would constrict the availability of financial support from the developed world to facilitate the energy transition in emerging economies—support that has already fallen short of pledges. As a result, emerging economies will continue to invest in fossil-fuel power generation in order to cater for economic and population growth, widening disparities in the energy transition between developed and developing countries.

Emissions trajectory widens between the developed and developing world
(total CO_2 emissions from fuel combustion; 1900=100)



Sources: IEA; EIU.
*2022-30 values are EIU forecasts.

IPCC rings the warning bell

Amid the recent events, which have major implications for the global energy industry (and its transition), the Intergovernmental Panel on Climate Change (IPCC) has called for greater efforts to tackle climate change effectively. Recent reports from IPCC have highlighted the need to undertake massive investments to adapt to natural disasters, and the apparent gap between ambition and the reality of emissions reduction.

Short-term energy security concerns are already posing a challenge to effective mitigation. Meanwhile, climate-related natural disasters are becoming increasingly commonplace, creating further policy dilemmas for developing countries in terms of allocation of funds earmarked for mitigation, notably to support developing countries.

The interlinked issues of ensuring energy security and decarbonisation of the energy system will remain a variable in energy policy in the years to come. The convergence (or lack thereof) of the two issues will be shaped by country-specific conditions. Developed economies that have only minimal fossil-fuel reserves, such as in Europe or Japan, would be keen to switch to a clean energy system quickly, while their fossil-fuel-rich peers in North America and Australasia would take a steadier policy approach to energy transition, which may result in stronger support for fossil fuels. In developing economies such as India and China, policy will be balanced between development priorities and climate pledges. Fossil fuels will continue to dominate their energy mix, with an expected impact on investment in renewables due to the current risk scenario.

War and monetary tightening will constrict climate finance

Key takeaway: Countries with significant public funding for decarbonisation of their economies, such as Germany, Norway and the UK, tend to score highly in the Decarbonisation category of our ESG ratings. Public funding will become an even more important driver of progress towards the energy transition in 2022 and 2023 as the tightening of global monetary policy limits the role that private capital is able to play in major investments.

Asia| Europe| Economy| Long-term outlook| Long-term trends

May 18th 2022

- **Public funding and higher energy costs will drive innovation in the energy transition. However, this will be counteracted in part by higher interest rates depressing private funding, and increased public spending on more urgent cost-of-living concerns.**
- **Government support for new technologies such as hydrogen and carbon capture is increasing, but the scaling of existing technologies will be slowed by higher materials costs.**
- **Venture capital is showing signs of slowing, as are more traditional forms of lending to the private sector. This is likely to have a negative effect on green finance more broadly.**
- **The impact on developing countries will be particularly acute because funding for their energy transition primarily comes from aid budgets, which will be stressed.**

The Russia-Ukraine war has had a profound impact on the energy transition, primarily through increased prices of hydrocarbons, particularly oil and natural gas. Many analysts have seen this as a boon to the energy transition, but in addition to the headwinds in the real economy that the green energy sector faces, the climate financing landscape will be changed by the war. This will have significant impacts on what, as well as where, new projects will receive funding.

Implementation is harder, innovation is easier

Globally, governments have seen the war in Ukraine as a wake-up call to invest in alternative sources of energy, including both fossil fuels and renewables. In the short term most countries are working to increase the sourcing of oil and natural gas to make up for the lost capacity from Russia. In the medium term, however, there is divergence in strategy. Countries, such as the US and Australia, with substantial domestic hydrocarbons sectors are investing in greater oil and gas extraction. However, for governments such as the EU, Japan and the UK, this primarily means a focus on renewable energy. As the region most exposed to a potential cut-off of Russian hydrocarbon exports (either by Russian action, or as part of expanded sanctions), the EU has announced the speeding-up of the rollout of and permitting processes for renewable energy deployment and increased investment in hydrogen and biomethane technologies. Similarly, the UK has accelerated the permitting process for modular nuclear reactors and offshore wind, and has directed more investment to hydrogen and carbon capture. Public funding and financial incentives for the energy transition are likely to increase in these jurisdictions. However, new financial commitments have been slow to materialise, with documents such as the UK energy strategy and the European Commission's RePowerEU initiative outlining changes in emphasis of existing funds, rather than making any new funding available. At the same time, new public oil and natural-gas investment has increased in response to meeting the immediate demand, keeping these sectors competitive for longer.

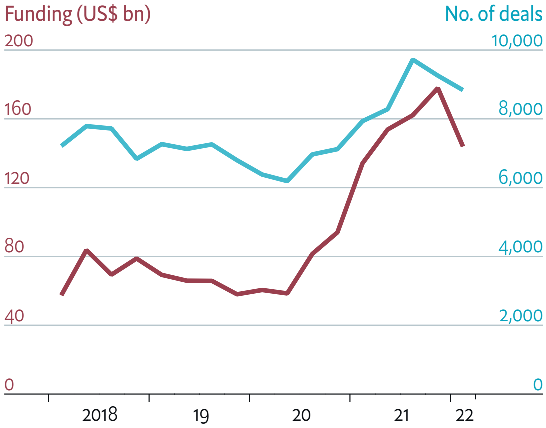
In addition, although the soaring prices of hydrocarbons have incentivised an accelerated shift to renewables in the medium term, the invasion has raised the absolute cost of scaling renewable technologies as well. Important input materials in solar and wind projects, and especially in electric-vehicle batteries, have increased in cost. Without increased public funding, this change in cost will, on the margin, shift green investment spending away from the rollout of existing renewable technologies and towards innovation and piloting new technologies, which are less materials intensive. This push towards innovation is concentrated in hydrogen and carbon capture and storage (CCS) technologies. These technologies, although still unproven at scale, are becoming closer to being economically viable, and bodies such as the International Energy Agency (IEA) and the UN Intergovernmental Panel on Climate Change (IPCC) have in recent reports identified both hydrogen and CCS as necessary components of the green transition. As these technologies appear closer to bearing fruit, investment in this sector will become more attractive to governments and investors.

Despite greater public attention, private money faces new hurdles

Public-sector support will also probably have to take on a greater share of the energy transition, as private funding is likely to face headwinds. After years of loose monetary policy, the monetary tightening cycle begun by the Federal Reserve (the US central bank), the Bank of England (the UK's central bank) and other global central banks is beginning to depress the pool of capital available for green investment, while making higher-risk or lower-yield green investments less attractive on the margin. The returns to green finance compared with more traditional investments are difficult to parse, as many of the funds are provided by investors explicitly looking for green investment.

However, there are already signs of slowing in the private financing market. For example, the supply of overall venture-capital funding declined in the first quarter of 2022 following expansion throughout the pandemic. This decline supports our existing forecast that the overall pool of credit extended to the private sector in North America, western Europe and Asia, the biggest sources of green investment, will largely stagnate in 2022, following growth in 2020 and 2021. The impact of monetary tightening on green finance is likely to be less extreme than in other sectors such as information and communications technology, owing to the dedicated pool of green investors and continued public-sector interest. However, this slowdown will limit the pool of private green finance available in the coming years.

Tightening cycle is hitting venture capital
(global venture capital funding and deals by quarter)



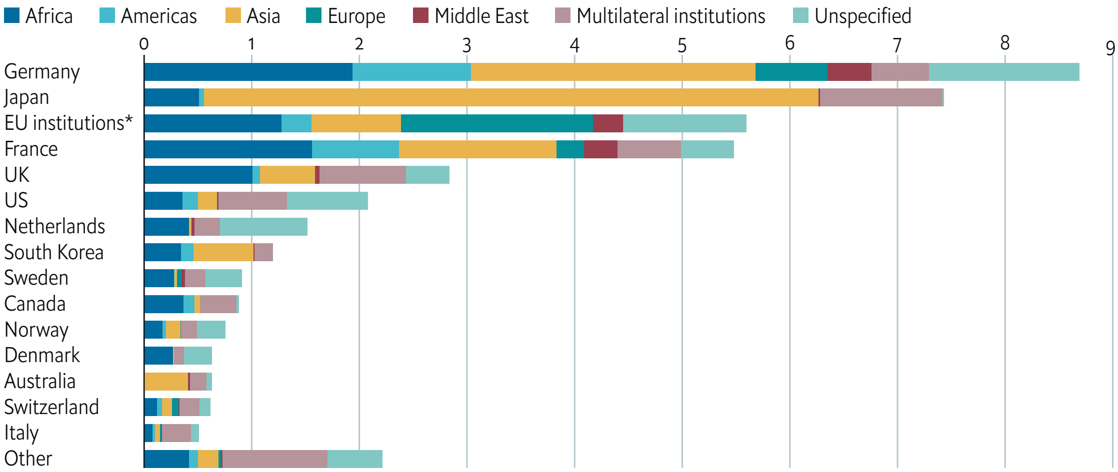
Source: CB Insights.

At the same time, the market for green financing is beginning to mature, with the EU taxonomy of green investments having come into force at the beginning of the year. The taxonomy sets stricter standards for what projects can be designated as green or sustainable. Theoretically, the change in taxonomy will only target projects that do not achieve meaningful impacts on decarbonisation, so the direct negative effect on the energy transition will be minor. However, the higher compliance and due-diligence costs are still likely to limit the growth of the pool of green investments on the margin, particularly in a funding environment that is already becoming more difficult in other ways. The current crisis has also solidified a political consensus within the EU that will allow natural-gas projects to be considered sustainable in certain circumstances.

Divide between advanced and developing countries will widen

Higher costs, tighter public budgets and monetary tightening will exacerbate the divergence between developing and advanced economies in financing the energy transition. In advanced economies the impact of higher construction and private financing costs is likely to be counteracted by greater direct public funding and a head start on basic investment in the energy transition. However, in developing countries, much of the energy transition is funded by international aid from advanced economies.

Europe, Japan and UK provide most climate aid
(total climate aid provided by country, 2019; US$ bn)



Source: OECD.

*Excluding European Investment Bank)

The war will stretch these aid budgets in three ways. First, donor countries will come under pressure to freeze, if not cut, their aid budgets to tackle the domestic cost-of-living crisis as well as increase defence spending. Multilateral institutions are similarly likely to refocus on more urgent priorities as their existing commitments go less far given higher input costs. The World Bank, for example, has announced that it is working to mobilise US$50bn in financing for crises stemming from Russia's invasion of Ukraine, including food and energy insecurity. Most of the largest donor countries will be facing significant cost-of-living and inflationary pressures, and are unlikely to be in a position to expand, and may even contract, aid provision.

Second, existing projects supporting the energy transition in developing countries will not extend as far, owing to the increased input costs. As a result, even if aid funding is maintained at existing nominal levels, the gap between what is needed and what will be provided by aid will continue to grow. Finally, developing countries themselves are likely to come under increased domestic pressure around basic food and energy security issues, and will be less likely to prioritise energy transition projects. Developing countries have also emphasised the need for greater financing for adaptation funding, in addition to funding for decarbonisation, as the impacts of climate change become more real. In addition to aid funding, other sources of funding will be similarly constrained—mobilising private finance was already a harder sell in developing countries.

Policy push for coal in China

World| Industry| Highlights| Energy| Coal

Key takeaway: China performs poorly in the Environmental pillar of our ESG ratings, including with respect to the country's energy transition, ranking at just 143rd place in our Decarbonisation category, for example. An increased focus by the Chinese government on energy security will boost the country's consumption of coal in the near term, preventing any significant improvement in China's Decarbonisation rank in 2022 or 2023.

May 13th 2022

- **Recent policy directives from China under the 14th Five Year Plan (FYP) for energy 2021-25 stress the need to continue using coal in the country's energy system.**
- **EIU has pushed back its forecast of peak coal consumption in China to 2027-28, from an earlier expectation of 2025. We expect consumption to peak at 3.6bn tonnes of coal equivalent.**
- **The government faces a dilemma between ensuring short-term energy security and achieving targeted cuts in emissions.**
- **China's emissions will see a temporary bump as more coal is consumed, but the plans do not permanently undermine the country's climate goals.**
- **In future, coal power is likely to be used as a back-up to support a renewables-based power system, particularly in emergency situations.**

China has pledged to phase down the use of coal, but recent policy pronouncements have scaled back its ambitions, raising concerns about continued carbon emissions. In March 2022, China's National Development and Reform Commission (NDRC), the state economic planner, and the National Energy Administration (NEA), the state energy regulator, jointly published the 14th FYP for energy with an objective to accelerate the development of a "modern energy system". The document underlined the importance of coal to China's energy system and in ensuring its "basic energy needs". A similar policy tone was conveyed at the annual "two-sessions" legislative meeting held in the same month, where President Xi Jinping said that coal would remain the "mainstay" of China's energy needs.

The recent policy push to coal comes as the task of balancing climate action against energy security and economic growth becomes increasingly difficult globally in an uncertain environment marked with tight energy markets and geopolitical tensions. China also experienced an energy crisis in 2021, when several provinces were exposed to power shortages that affected economic activity. The shortages were driven by a surge in coal prices, a sharp increase in electricity demand, as well as aggressive compliance with energy intensity targets set out by the government.

China boosts coal production and projects

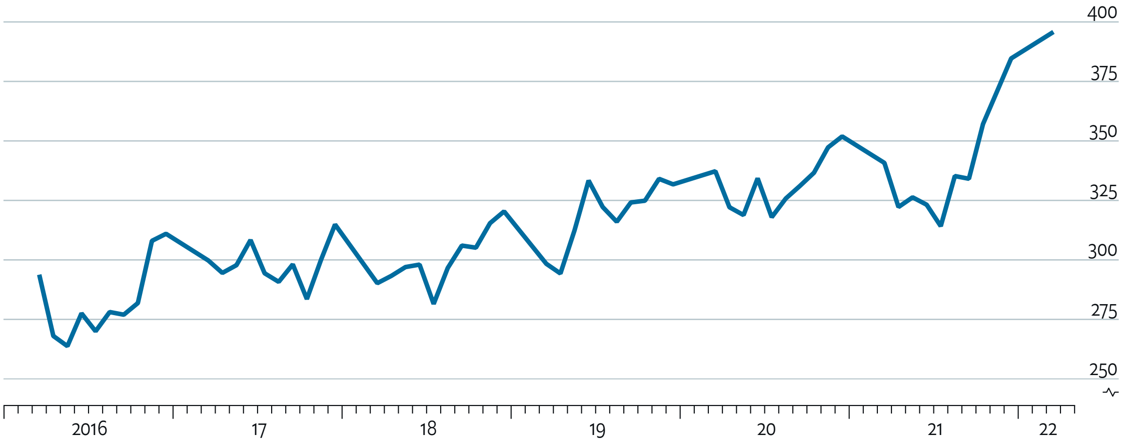
The government responded to the power shortages by calling for a massive ramp up in coal production in the final months of 2021. Higher production continued in the first quarter of 2022 reaching close to

1,082m tonnes, a 13% increase from the same period last year. The NDRC also approved three new coal mining projects in early 2022, with a capacity to produce 19m tonnes of coal a year. Furthermore, five new coal power plants with a combined capacity of 7.3 GW were approved for construction in the first few weeks of 2022. By contrast, in 2021 permits for large projects had remained largely frozen owing to emissions concerns.

In late April the Ministry of Finance announced a cut to import tariffs on coal to zero from May 2022 until March 2023 in a bid to secure additional overseas supply, which provided for 8% of total consumption in 2021. However, imports are not expected to play a major role in ensuring supply in 2022, as international coal prices remain at record levels as a result of the war in Ukraine. Consumers would opt for domestically sourced coal as its production remains high all throughout the year.

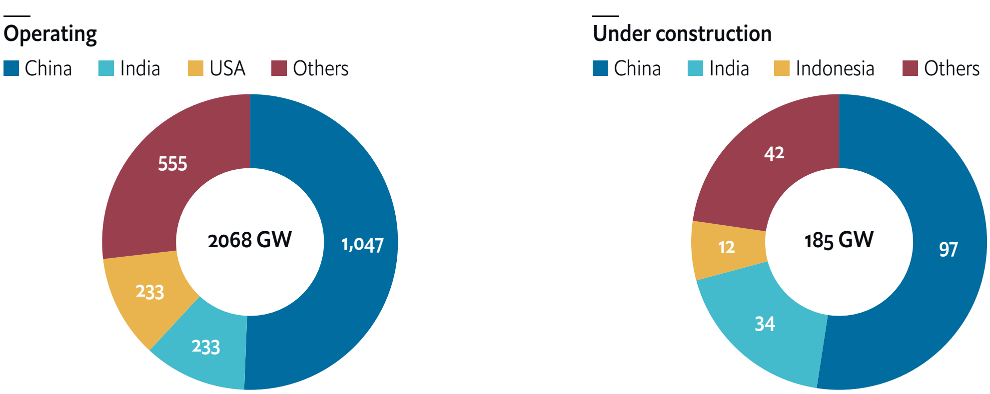
The policy push towards coal highlights China's reliance on the carbon-intensive fuel, with its large reserves making coal a fall-back option in times of crisis.

Coal production in China remains high since Q4 2021
(monthly coal production; m tonnes)



Sources: National Bureau of Statistics; EIU.

China adds to its coal-fired electricity capacity
(top 3 countries and others; as at end 2021)



Sources: Global Coal Plant Tracker; EIU.

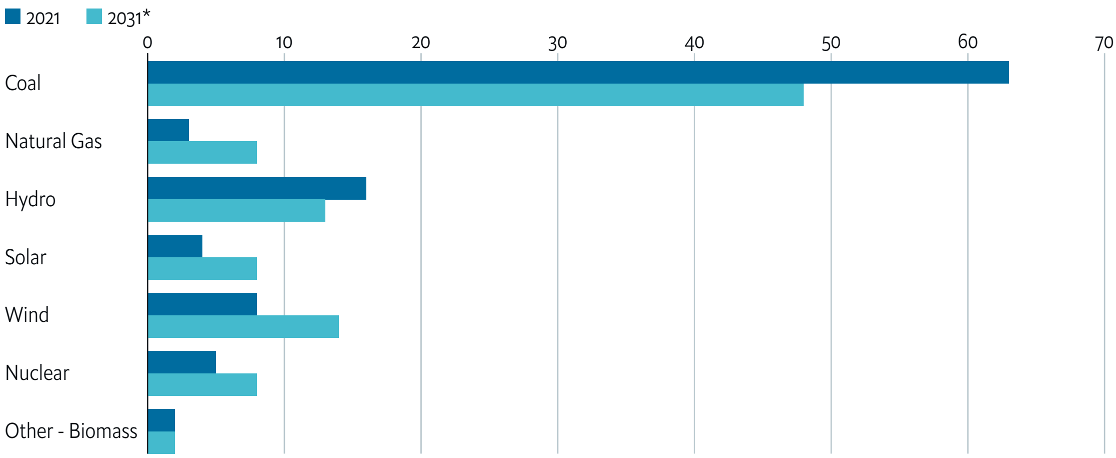
However, the government directives have emphasised the need for 'efficient' and 'clean' use of coal and other fossil fuels. Most of the coal power plants that are under construction or coming online are high-efficiency, meaning they are less carbon intensive than their older counterparts. Moreover, newer coal power plants in China are geared more towards providing flexible peaking services to a grid intended to be dependent on solar and wind power, where generation fluctuates depending on weather conditions.

It is likely that coal plants in China would act as a support to a renewables-based power system in future, operating below peak capacity in normal times and boosted only in emergency situations. A broad-based retirement of coal plants would occur at a stage where sufficient storage capacity has been deployed to manage fluctuations in renewables generation. The existing transmission infrastructure, which is more suited to coal power, would also need to be overhauled.

Climate targets remain achievable but insufficient

Coal burning accounts for the bulk of China's carbon emissions and support to the fuel would certainly extend the timeline for its targeted emissions cuts. Nevertheless, the recent pivot does not indicate a major long-term policy shift away from cleaning the energy system and reducing emissions. Although emissions are likely to bump upwards in the short term, a significant build-up of renewables capacity will keep China on track with its climate goals. The country is expected to add about 766 GW of solar and wind power capacity in 2021-30, with total capacity reaching 1,300 GW by 2030. This would be 100 GW more than the official target. The share of non-fossil-fuel sources in power generation will increase from 32% in 2021 to 42% in 2030, while that of coal will fall from 63% to 48%.

Cleaner fuels will gain at the cost of coal in China
(share in electricity generation; %)



Sources: IEA; EIU.

*EIU forecast.

The concern, however, is that China's current emissions targets, as submitted under its revised nationally determined contributions at the COP26 climate-change summit, are insufficient to keep global temperatures from rising above the 1.5°C threshold. Any pushback on emissions control from the world's largest emitter would make that task even more difficult.

Social
Social media regulation goes beyond freedom of speech

Key takeaway: Regulation of social media will become an increasingly important aspect of a country's ESG profile, mainly via the Social pillar. The era of self-regulation by social media companies is ending, with multiple jurisdictions, including the EU, the US, the UK, Canada, Singapore or Chile, looking to introduce regulation. The most successful outcomes are likely to emerge in countries that adopt a co-operative approach between social media firms and government.
World| Telecommunications| Next-generation technologies| Google
April 29th 2022

- **The internet, not the tech companies, is the public square**
- **Tech companies want to drive engagement, not create a balanced marketplace of ideas**
- **Regulators want to ensure what is illegal offline is illegal online, but are also looking at regulating tech companies as opposed to the content itself**
- **This is ultimately about who decides between tech companies and nation-states**

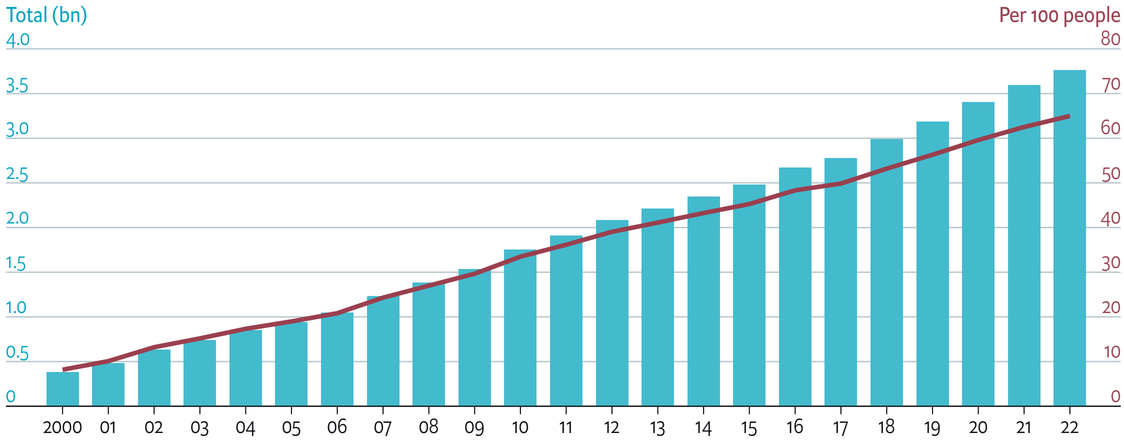
With Elon Musk acquiring Twitter, and former US President Barack Obama discussing the impact of social media on democracy, issues related to free speech, content and Big Tech companies have again come to the forefront of public debate. The planned deal also points to the important relationship between nation-states and Big Tech companies, which can be fraught given differing attitudes to free speech. What works in the US may not work in Europe or China.

What is the public square?

Proponents of free speech argue that Twitter, Facebook or YouTube are the public square, and should therefore include every kind of speech. However, this confuses the channel (the internet) with the platform (Twitter, Facebook or YouTube); the internet is the public square, and the companies operating on it are private entities. They need to offer services within a framework of publicly accepted norms, but the channel and not the platform is the marketplace for ideas.

The number of internet users has multiplied by ten since 2000, and these users can choose which particular service to use, even if network effects create winners and losers. In the same way, the internet allows for new companies to be created every day, should someone decide to do so. This is why the debate on internet governance models, between the current Western-backed multi-stakeholder model (open, decentralised and industry-led), and the cyber-sovereignty alternative (closed, centralised and country-led) proposed by China and Russia, is so critical, as the latter would require governments to approve the creation of new platforms on the internet.

Global internet users: a ten-fold increase since 2000
(global internet users)



Source: EIU.

Big Tech companies have specific business models

The larger tech companies are commercial enterprises which are not there to provide balance. Instead their business model, underpinned by advertising which makes the service free to users, favours a specific type of content, which drives greater engagement. This in turn can drive greater enragement, as the way these platforms work can put users in filter bubbles (where previous behaviour influences what can be seen) and can increase confirmation bias (searching for the evidence confirming previous beliefs).

It has also led companies to introduce their own regulation. This was to improve safety for users on their platforms, so that they would keep coming back, but mostly to appease their main revenue source, the advertisers. Many brands do not want their products to be next to content they would consider harmful or dangerous, even if the content is legal, and tech companies have taken explicit steps to make sure it did not happen, as a way to protect their bottom line.

What to moderate?

This era of self-regulation is now over, with multiple jurisdictions, including the EU, US, UK, Canada, Singapore or Chile looking to introduce regulation. The idea is to make what is illegal offline illegal online, but what is illegal is not uniform globally. For example, denying the Holocaust is illegal in France or Germany, but not in the US, and these rules will drive the growing regionalisation of the online world, instead of the global but US-led (as most Big Tech companies are American) approach that has been in place until now.

However, a growing number of countries are looking to introduce regulation against harmful or hateful content, or misinformation, which are not in themselves illegal; the latter has especially been focused on following Russia's invasion of Ukraine. This raises the difficult question of how to regulate content that is not illegal by law, which remains more difficult for governments to do because of the potential accusation of censorship. This is why the onus is starting to move away from regulating content in itself, and regulating the companies instead. This could mean making platforms responsible for the content that they publish, removing the broad immunity that Section 230 has given them in the US (by not making them liable for content published by their users) or regulating how content can spread, either by opening up the algorithms that are responsible for what is seen by users or reducing its virality to limit reach.

Power and decision-making

Ultimately, this is about the relationship between Big Tech companies and nation-states. Someone will need to make a decision in the end (and not making a decision is still deciding), so who decides and who is legitimate to decide are the two critical questions. Tech companies have looked to encroach on what had traditionally been the competencies of nations-states, such as money (Meta looking to launch its own currency), security (Apple going ahead with full encryption) and even content (Donald Trump being banned while still serving as US president). This leads to three potential relationships between the two entities.

- Replacement, where tech companies replace nation-states as the way to articulate the global order. This is very unlikely, but not far from the ambitions of some tech leaders, including Elon Musk.
- Co-optation, where nation-states retain complete control over tech companies, as has been the case in China or Russia recently.
- Co-operation, where the two entities continue to work with each other, respecting each other's boundaries and sometimes collaborating on some key issues.

The latter is the most likely, and content moderation provides an example, as much of the regulation will require tech companies to do most of the work under the supervision of public bodies. With a greater focus on sovereignty and regulation, nation-states have regained some control over tech companies, but the tension will continue as technology becomes increasingly important as a strategic priority.

How a US abortion ruling could affect healthcare

United States of America| Politics| Recent developments| Healthcare| Healthcare provision

Key takeaway: Landmark rulings by national judiciaries on civil rights issues can affect a country's ESG profile. If the US Supreme Court rules in favour of a Mississippi law restricting abortions later in 2022, this could lower the US score in the Civil Rights category of the Social pillar in our ESG ratings.

May 19th 2022

- **This summer the US Supreme Court is likely to rule in favour of a Mississippi law restricting abortions.**
- **Such a decision would overturn the precedent set in the 1973 Roe v Wade case, which gave federal abortion rights to all women in the US.**
- **Multiple states will proceed with bans or restrictions on abortion. This will have repercussions for US healthcare providers and insurers, forcing them to adjust their policies.**
- **Bans will also have implications for the welfare and health of women and children, particularly in states with poor social safety nets.**

In early May 2022 Politico, a US news outlet, leaked a document showing that a majority of the justices on the US Supreme Court supported a Mississippi state law that bans abortions after 15 weeks of pregnancy. A positive ruling, if confirmed in late June or July, would overturn a previous decision made by the Supreme Court under the 1973 Roe v Wade case, which gave federal abortion rights to all women across the country until the 24th week.

Endorsement of the Mississippi law will prompt many other states to introduce new laws, with some (mostly Republican) states restricting abortions and others (mostly Democrat-led) confirming abortion rights. These laws will affect women across the US and increase the country's political polarisation. They will also affect the policies of individual healthcare providers, health insurers and other companies in relation to abortion coverage. If abortion restrictions coincide with weak social safety nets in many states, there could also be other health implications for women and children.

States will respond quickly to a decision

According to the Guttmacher Institute, a US research body, 31 states have passed legislation that would ban or restrict abortions, including 13 with specific "trigger laws" if Roe v Wade is overturned. These restrictions range from bans after 15 weeks of pregnancy to those banning abortion after six weeks or fewer (as in Texas and Mississippi). By contrast, about 16 states and the District of Columbia have legislation that would preserve the right to abortion even if federal rights were curtailed.

Bringing in new restrictions on abortion would put the US in a small group of countries that have curtailed abortion rights in recent years, including Poland. Far more countries are moving in the direction of liberalisation. However, the US federal rights are unusually liberal in allowing abortion on request up to 24 weeks. Most other wealthy countries have an earlier cut-off for on-demand terminations, although they allow late abortions in exceptional circumstances, such as a threat to the mother's health.

There is a small chance that the final Supreme Court ruling, expected in late June, may be softer than the leak suggests. However, this appears unlikely; the former US president, Donald Trump, appointed three conservative judges to the Supreme Court during his time in office, in the hope of influencing future decisions. Any ruling against Roe v Wade may also be challenged in the future, although there is no guarantee that this would result in it being overturned.

Women and companies will face difficult decisions

If more states have restrictive abortion laws, women wishing to terminate a pregnancy will have to travel to other states to have an abortion. This will further fuel social inequalities, given that it will be easier for higher-income women to travel and pay for terminations. Insurance coverage for abortion is already patchy across the US. Legislation from 1976 prohibits the use of federal funding for abortion, except in cases of rape, danger to the life of the woman, or incest. Abortion is not included within Medicaid, the federal health insurance fund for low-income families. However, some states have included abortion coverage in their own Medicaid plans, and six states require abortion coverage in private health insurance plans. In anti-abortion states, insurance coverage is likely to become illegal even for out-of-state terminations, and companies will have to abide by that decision.

Since news of the draft opinion was leaked, some private companies have stated that they will cover travel costs associated with seeking an abortion, if new restrictions kick in. Starbucks, Amazon, Microsoft and Apple are among those offering reimbursement. However, direct help with the medical cost of terminations is likely to be outlawed in many anti-abortion states. Even in pro-choice states, such provisions will only help those with jobs, furthering inequalities. Many women with lower incomes (including teenagers), or without family support, might either opt for illegal abortions or to have the baby.

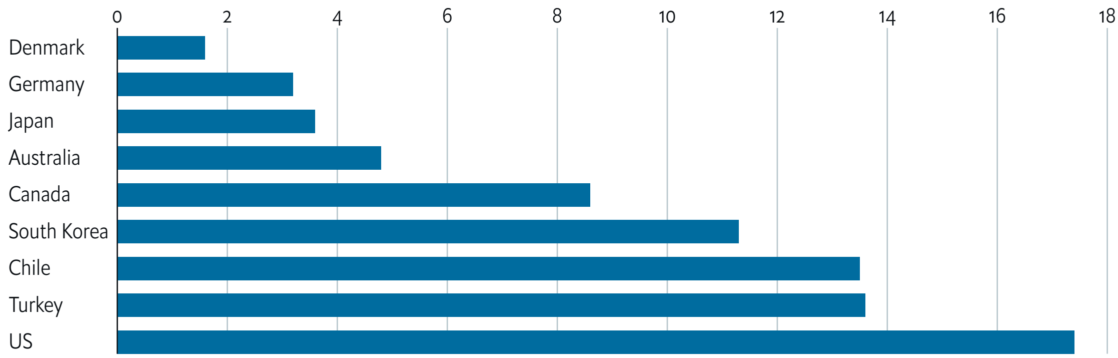
Lack of social safety nets

The US already has the highest maternal mortality rate among high-income countries, according to the Commonwealth Fund, a private US health foundation. In part this is caused by obesity, but it is also due to a shortage of maternity providers, especially midwives, and the lack of access to comprehensive postpartum support. Many women skip prenatal and other check-ups due to the high cost of healthcare in the US. Proponents of women's rights argue that this could become an increasing problem if abortions are banned. Ideally any bans should be accompanied by measures to ensure better healthcare for expecting and new mothers. However, data from the US Census Bureau suggests that many of the states poised to restrict abortion have relatively low per capita spending on welfare.

Currently Medicaid covers the delivery of the baby, but its coverage of prenatal and postpartum periods is spotty. Full coverage for mothers covers only the first two months after giving birth. Although states have an option to extend this to a full year after birth, many women fall through the cracks. Illinois is the first state in the country to have legislation (passed in 2021) that extends full Medicaid plan benefits to mothers for one year after giving birth. US legislation also requires only unpaid maternity leave after the birth of a child. Many women covered by Medicaid return to work quickly, compared with those under private health insurance in the US.

There are also fears that an increase in unwanted pregnancies will lead to greater child poverty. About 16% of all children in the US live in poverty. There have been attempts made to improve the welfare safety net for children. Under the American rescue plan passed in March 2021, from July to December 2021, the child tax credit was expanded and payments were made monthly (instead of annually). According to a study published by Columbia University in January 2022, this reduced child poverty by 30%. Despite this, states such as Texas have actually reduced the amount that they spend annually on basic assistance, even while banning abortion.

The US has the highest maternal mortality rate among high-income countries
(maternal mortality rate per 100,000 live births; 2018)



Source: OECD, EIU.

Proposed constitution could expand Chilean workers' rights

Key takeaway: Working conditions are a central component of the Social pillar in our ESG ratings. Chile is debating whether to strengthen rights to collective bargaining in its constitution, which could boost the country's ranking of 61st in the Labour Conditions category of our Social pillar. Labour Conditions is the weakest category in Chile's Social pillar, for which the country ranks 32nd overall.

Chile| Economy| Forecast| Policy trends

May 3rd 2022

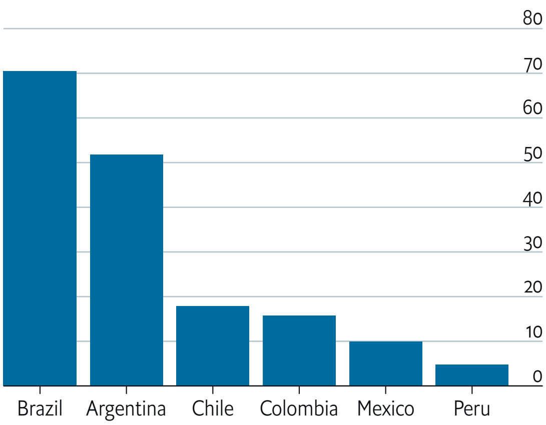
What's happened?

Chile's constituent assembly has approved articles that would expand workers' rights for inclusion in the proposed constitution. If the new text receives public backing in an exit referendum (which is still our baseline forecast), these articles would significantly alter labour relations, for instance by increasing the scope for collective bargaining and allowing unions to participate in firms' decisions-making processes.

Why does it matter?

The president, Gabriel Boric, has made strengthening the power of organised labour a major plank of his government's proposed economic and social reforms. The articles approved by the constituent assembly reflect the government's policy priorities, and we anticipate that the enabling laws that would regulate the enumerated constitutional rights would favour organised labour. One article would allow workers to broaden the scope of collective bargaining to include branch- and sector-level negotiations, as well as negotiations within a territory (negotiations currently occur at the firm level). Chilean labour relations would therefore come to resemble those in Argentina and Uruguay, where sector-level negotiations are the norm; however, these types of agreements would increase labour market rigidities and harm small and medium-sized firms, as larger firms are likely to be able to pay higher wages.

Collective bargaining in Latin America's largest economies
(share of employees covered by a collective agreement*)



Sources: ILOSTAT; EIU. *Using latest available data.

The constituent assembly also approved an article that states that "workers, through their unions, have the right to participate in the decisions of the company". The ambiguity of the approved text has caused significant concern among the business community, as it leaves it up to the legislature to determine how participation by the unions would be regulated. We would expect the Boric administration to try to introduce the kind of regulations that feature in its policy platform, which include guaranteeing that union representatives are on the board of large firms (what constitutes a large firm is unclear) and that the boards achieve gender parity.

Although it is not our core forecast, even if the proposed constitution were rejected in the exit referendum, we would expect the Boric administration to pursue labour reforms to expand the scope of collective bargaining, increase worker representation on boards, reduce the working week from 45 to 40 hours and raise the minimum salary from Ps350,000 to Ps500,000 by the end of Mr Boric's term. Congress is currently considering a proposal to raise the minimum salary to Ps400,000 by August.

What next?

Uncertainty regarding the consequences of the proposed constitutional reform for labour regulations will further weigh on the business environment and firms' investment decisions, keeping growth below potential in 2022-23. There is also a significant risk that policy uncertainty may be prolonged, affecting investment over the medium term.

UN debates Sri Lanka's human rights record

Sri Lanka| Politics| Forecast| International relations

Key takeaway: EIU's in-house team of country analysts is able to assign scores to countries for subjective criteria such as civil rights and human rights abuses that would otherwise be difficult to quantify in an ESG rating. In the case of Sri Lanka, our analysts take into account criticism by bodies such as the UN and the EU when scoring the country's Social and Governance pillars.

March 28th 2022

What's happened?

The Ukraine crisis appears to have spared Sri Lanka stringent criticism of its human rights record by the UN Human Rights Council (UNHRC) when the latter met in February-March. However, the Archbishop of Colombo, Cardinal Malcolm Ranjith, took the extraordinary step of participating in a debate to call on the international community and the UN to help bring justice for the 270 foreigners and locals killed in a jihadi terror attack on churches and hotels on Easter Sunday in 2019. His comments follow a report on Sri Lanka's recent record presented to the UNHRC by the UN High Commissioner for Human Rights, Michelle Bachelet; the report called on Sri Lanka's government to make public its final report of the Commission of Inquiry into the Easter Sunday terrorist bombings, which has not been released in full.

Why does it matter?

In the last decade the UNHRC has passed several resolutions urging Sri Lanka to hold accountability trials and inquiries into allegations of violations of international human rights and humanitarian laws and possible war crimes committed by both sides in the country's 26-year-old war with the separatist Tamil minority, which ended in May 2009 with the defeat of the Tamil secessionists.

The government rejected a UNHRC resolution calling for foreign judges and prosecutors to participate in post-war accountability trials, but it promised to set up domestic mechanisms for the purpose and also to go ahead with reconciliation between the ethnic groups involved in the conflict. The government asked for "space and time" to do so. However, little has happened to bring human rights violators before the law or to initiate real reconciliation.

Meanwhile the government has relied heavily on a 40-year-old Prevention of Terrorism Act, which was intended to be a temporary law, to arrest and detain political opponents and harass civil rights and human rights activists, journalists and others who have little or nothing to do with terrorism.

What next?

Sri Lanka emerged largely unscathed from the latest UNHRC session because there was no resolution on which to vote. However, the situation will be vastly different when the UNHRC gathers for meetings in September. About 15 UN experts have already issued a statement urging Sri Lanka's government to abolish the Prevention of Terrorism law. The law has also been criticised by the EU, which has urged Sri Lanka's government to abolish it and adhere to other international conventions.

Governance
The Philippines under a Marcos presidency

Philippines| Politics| Forecast| Election watch

Key takeaway: Although there is some overlap between the indicators used to measure a country's Social and Governance profiles in our ESG ratings, there are often significant divergences in the overall scores for these pillars. For instance, the Philippines ranks 52nd in our Governance pillar, boosted by an inclusive electoral process. However, the Philippines ranks 80th in our Social pillar, dragged down by lower scores for civil rights, equality and labour conditions. Our country analysts expect broad scoring continuity following a victory for Ferdinand "Bongbong" Marcos Jr in the Philippines' May presidential election, which ended the term of his predecessor, Rodrigo Duterte.

May 6th 2022

- **Ferdinand "Bongbong" Marcos Jr, the front-runner in the presidential race, is ideologically aligned with the incumbent president, Rodrigo Duterte. This shared stance suggests that an agenda of continuity rather than change will take hold after the elections.**
- **Domestically, Mr Marcos will not deviate significantly from his predecessor's core stance in favour of market liberalisation and hardline security policy. In terms of foreign policy, the ongoing rebalance towards the US will continue.**
- **The biggest risk to Mr Marcos's presidency will be the execution of his policy agenda, which is likely to be stymied by a lack of political expertise.**
- **An ineffective and corrupt administration would be a worst-case scenario for investors.**

The Philippines will hold a presidential election on May 9th to elect the successor to the incumbent, Rodrigo Duterte, who has served a full six-year term and is constitutionally ineligible for re-election. EIU continues to expect Mr Marcos to win by a healthy margin and become the next president.

Having established a convincing lead early in the campaign, Mr Marcos has mostly avoided media engagements and debates, and has disclosed little of his vision for the country in substantive policy terms. Based on his previous record as a senator and his political alignment with Mr Duterte for much of the latter's presidency, Mr Marcos is likely to pursue a broadly similar policy course, albeit with his own touch.

Continuity without the bombastic rhetoric

Effectively running as a continuity candidate in the ongoing campaign, Mr Marcos's abiding conservative views and previous defence of some of Mr Duterte's more controversial policies suggest that things will not change drastically under his presidency. Although the previously cordial relationship between Mr Marcos and Mr Duterte has cooled in recent months, Mr Marcos remains ideologically close to Mr Duterte, as made evident by the fact that Sara Duterte, the daughter of the incumbent president, has opted to contest the vice-presidency as Mr Marcos's running mate.

Mr Marcos has maintained a consistently wide lead to the eve of the election

Candidate	Polling range, Apr 2022
Ferdinand Marcos Jr	53-64%
Leni Robredo	20-25%
Isko Moreno	5-10%
Manny Pacquiao	5-7%

Sources: aggregates of polling data; EIU.

Considering Mr Duterte's enduring popularity throughout his six-year term, despite the covid-19 pandemic and strong international criticism, Mr Marcos has few incentives to eschew this proven recipe for success by a fellow right-leaning conservative. That said, Mr Marcos, the son of a former long-serving president and the current head of a powerful, enduring political dynasty, will be his own person and will not give sway to Mr Duterte, despite his daughter's likely election as vice-president.

Beyond the immediate priority of responding to the pandemic and rising inflationary pressure, through the continued implementation of relief measures, an administration led by Mr Marcos will maintain the broadly pro-market policy agenda set by his predecessor. The Philippines has been able to register consistently healthy economic growth on average for over a decade as a result of this ongoing and gradual liberalisation.

In concrete terms, this means that Mr Marcos will continue to embrace the three key pillars of infrastructure upgrade, tax incentives for businesses and the removal of investment barriers. However, there could be a subtle shift in the focus or scope for some of these initiatives, based on the new president's preferences. This could include the attachment of increased importance to digital and nuclear energy infrastructure, compared with conventional transport projects under Mr Duterte's "Build, Build, Build" initiative.

Hopes for the strengthening of liberal democratic norms and less confrontational domestic security policy are likely to be dashed under Mr Marcos. As a conservative on security issues, he has defended Mr Duterte's controversial "war on drugs" against allegations of widespread human-rights abuses and expressed strong support for fighting the communist insurgency. He, like Mr Duterte, has been the target of scathing criticism from the liberal-leaning media, which has faced an increasingly hostile landscape in recent years amid threats of lawsuits and violence. The country's poor ranking for media freedom is unlikely to improve in the foreseeable future.

The most noticeable difference under a Marcos presidency in the coming months will probably be an absence of bombastic and belligerent rhetoric, which Mr Duterte has frequently employed against his perceived domestic and international critics. While not changing much of the substance of the policy agenda, a more civil oratorical style could help to cool the temperature over controversial aspects of the government's programme, such as the war on drugs.

Marcos's policy agenda will remain broadly similar to Duterte's

Policy area	Continuity/departure from Duterte presidency	Examples
Economics	Continue on a pro-market course, but with possible tweaks	Focus on infrastructure could see greater attention given to digitalisation or alternative energy sources
Law and order	Continue with a tough approach	The violent "war on drugs" will go on, and the government's rhetoric on crime-related issues will focus on crackdown rather than rehabilitation
Civil liberties	Continue to treat human-rights concerns as secondary in policymaking	Independent media and journalists will face further regulatory restrictions or legal challenges from the state or the pro-Marcos camp
Foreign policy	Continue to balance ties between the US and China; however, there will be a noticeable drift towards a pro-US position, while ties with China are kept cordial	Larger military drills with the US; increased co-operation on intelligence and arms sales; no aggressive rhetoric against China over long-running maritime dispute

Source: EIU.

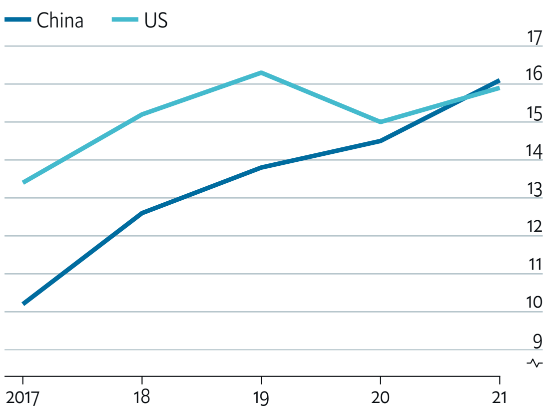
Balance but not equidistance vis-à-vis China and the US

The Philippines and China are embroiled in a long-standing territorial dispute over the South China Sea. Against the background of deteriorating US-China relations and increasing geopolitical competition between the two powers in the region, Mr Marcos's handling of these two sets of bilateral relationships will remain at centre stage as the foremost foreign policy issue.

Under Mr Marcos, the Philippine position will, on balance, continue to trend towards the US, although the incoming administration will also strive to keep ties with China cordial. In essence, this represents continuity with policy under Mr Duterte in the latter stages of his presidency, when he began to oversee a pivot back to the US following years of harsh verbal attacks and flirtation with not renewing vital military agreements.

Mr Marcos's calmer decorum will help to relieve a significant recurring irritation in US-Philippines relations. More fundamentally, amid ongoing incursion by Chinese vessels into the disputed South China Sea and activity aimed at asserting China's expansive territorial claims, the US government's status as the Philippines' primary military ally will remain a powerful anchor for closer US-Philippines ties. That said, Mr Marcos has indicated—unlike his more liberal opponents—that he will maintain his predecessor's relatively restrained approach in handling the territorial dispute with China, with the goal of not allowing it to dominate overall bilateral relations.

The increasingly antagonistic US and China are the Philippines' two most important markets
(goods exports; % of total market share)



Source: Philippines Statistics Authority.

Although political ties between the two Asian countries will remain shallow, owing to the South China Sea issue and the Philippines' traditional status as the US's foremost ally in South-east Asia, building on the strong commercial ties achieved with China in recent years will remain a key priority in the Philippine's management of the bilateral relationship. This also means that EIU maintains its view that major military hostilities between China and the Philippines remain unlikely in 2022-26, despite the simmering tensions.

It is the quality of governance, not platform

The biggest risk to a Marcos presidency (and the country's political stability) lies not in the policy agenda but in the competence of the incoming administration to execute it. While parts of this conservative-leaning policy programme—particularly the violent war on drugs—will remain controversial, Mr Duterte's enduring popularity and Mr Marcos's strong polling ratings suggest that his agenda will face few domestic headwinds.

However, Mr Marcos's lack of executive experience and ties with political families associated with cronyism could prevent him from replicating Mr Duterte's political recipe. For all his bombastic rhetoric and inability to overhaul the country's anti-graft regime, Mr Duterte and his close allies have managed to steer clear of corruption scandals, and he became president following a long and generally successful tenure as mayor of the country's third-largest city.

Mr Marcos, in contrast, can boast only a relatively unproductive stint as a senator, and remains closely associated with the record of his namesake father, who was overthrown as president amid allegations of endemic corruption in 1986. Failure to navigate the oft-fractious parliament and adequately deliver progress on major business-friendly reform and infrastructure upgrade amid an ongoing pandemic, which will require consummate political and communication skills, could jeopardise the country's hitherto impressive recent growth trajectory and trigger an sudden reversal of fortune and ensuing political volatility in 2023.

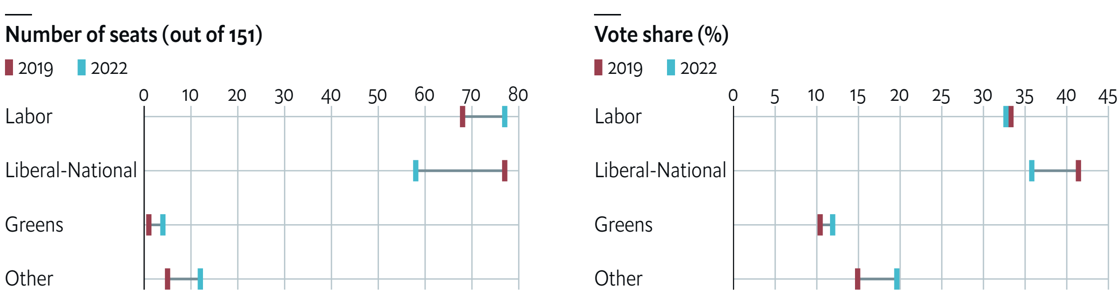
What will the Labor government do in Australia?

Key takeaway: Australia's Labor Party has announced three priorities for the government following victory in the country's May national election. Of these, the creation of an independent anti-corruption commission and constitutional recognition for indigenous Australians have the potential to boost Australia's already high ranking of fifth in the Governance pillar of our ESG rankings.
Australia| Politics| Forecast| Election watch
May 25th 2022

- **Following Labor's election win, EIU expects incremental changes to Australia's policy mix, rather than a series of "big bang" reforms.**
- **Climate change policy will be an area of change and although we expect targets to be stiffened, the green transition in Australia will still lag behind its international peers.**
- **Relations with China will not be "reset", as security ties with the US will be prioritised, but the risk of further deterioration has reduced.**

The centre-left Labor Party won the Australian general election on May 21st and has returned to government for the first time since 2013. Although some seats are still too close to call, it seems likely that the party will have a minimal majority in the House of Representatives (the lower house), following a collapse in the number of seats held by the former Liberal-National centre-right coalition. However, even if Labor has to rely on the support of the Greens and/or several independent members, it is clear that it has a mandate from the Australian people for many of its election pledges. In his first press conference as prime minister on May 23rd, Anthony Albanese outlined three priorities for his government: the creation of an independent anti-corruption commission; constitutional recognition for indigenous Australians; and a summit on jobs.

Drop in support for Liberal-National coalition handed Labor victory
(House of Representatives elections)



Source: Australian Election Commission.

Anti-corruption efforts could have an impact on business

On the first of these, the Liberal-National coalition had proposed, under pressure, a Commonwealth Integrity Commission (CIC), but plans to legislate for it were scrapped after it was widely criticised as being insufficiently powerful. Labor made the launch of a new entity a centrepiece of its campaign and, given that the Greens and a number of the newly elected "teal" independents also support the policy, it should be legislated in time for Labor's self-imposed deadline of end-2022, bolstering Mr Albanese's pledge to clean up politics and the public sector.

We expect the new government's body to allow public hearings into allegations of corruption in the state sector; to act on anonymous tips from members of the public; and to offer protections to whistle-blowers. These are three areas where the CIC was deemed to be insufficiently powerful. One likely consequence will be greater scrutiny of political donations and the role of lobbyists, especially where these are former politicians.

A voice for Indigenous Australians?

Labor will also look to hold a referendum on the establishment of an Indigenous Voice to Parliament. This would involve the creation of a permanent indigenous advisory body to the federal parliament and an amendment to the constitution to make its presence permanent. Negotiations on the issue are likely to take several years. Mr Albanese has already said that he would prefer to receive the support of the coalition before putting the issue to a referendum, but even moderate senior Liberals, such as Malcolm Turnbull, have been lukewarm on it in recent years. The Greens, who are strongly in favour of greater recognition of the abuses endured and disadvantaged faced by indigenous groups, would prefer a sort of truth and reconciliation commission to be established first to hear evidence of wrongdoing against indigenous peoples, and then a Voice legislated afterwards.

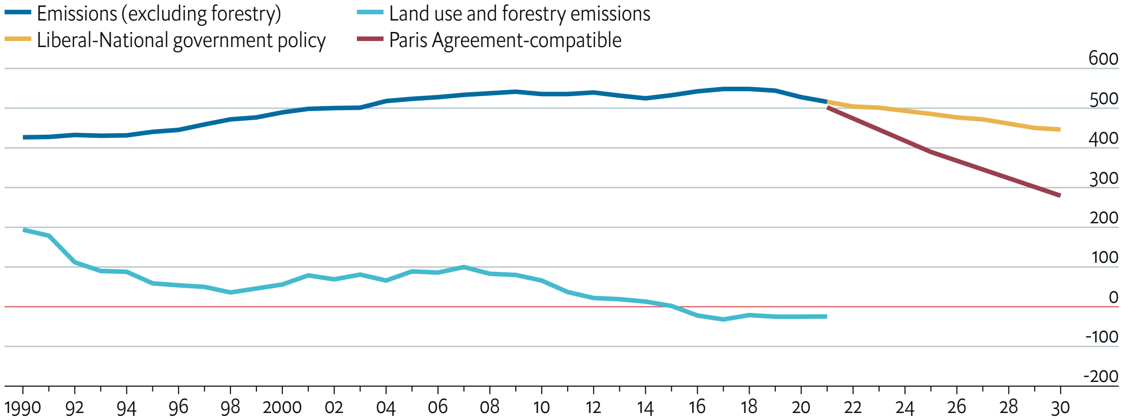
It is possible that a referendum will be held in 2023 or 2024, but there is still a lot of work to be done on the sequence of events. Labor will only proceed with a referendum if there is clear public support for proposals as they are developed, given the hurdles for achieving constitutional change. In the immediate term, we expect more formalised consultations with indigenous groups on policy, and heightened expectations of corporate action and engagement with indigenous communities.

New legislation on tackling climate change, but Australia will still lag international peers

We also expect to see new legislation to combat climate change, one of the dominating themes of the election. Labor has pledged to target a steeper cut in carbon dioxide emissions than that of the coalition, of 43% from 2005 levels by 2030, from 26% at present, while the Greens and teal independents are backing a 75% reduction (that required for compatibility with the 1.5°C goal of the Paris Agreement). Of all 19 seats so far confirmed to have changed hands at the election, nine were to the Greens and teals.

However, the mechanism is more important than the target and here Labor has been deliberately unambitious, perhaps worried about the negative reaction it received when focusing on climate change at the 2019 and 2013 elections. It has proposed a A$20bn (US$14.2bn) fund to expand the electricity network, lower taxes on electric vehicles, and will look to use a baseline-and-credit system, giving most of the incentive power of an emissions trading scheme, but at a lower cost to business. Although Labor needs to take action if it wants to avoid a backlash at the next election, the language coming from the new administration suggests that the green transition in Australia will still be gradual compared with some other advanced economies.

Australia will adopt more ambitious climate goals under Labor, but still fall short of Paris Agreement goal on global warming
(m tonnes; carbon dioxide emissions)



Source: Climate Action Tracker.

No reset with China, while doubling down on existing alliances

In the international sphere, the change of government has opened up a small window of opportunity to reduce political tensions with China. However, although the coalition's election strategy of painting Mr Albanese as soft on China largely failed, it would be a brave move for his government to be seen as making a first move here. Similarly, concessions from China, either on trade tariffs or its treatment of Australian nationals held in China on espionage charges, are unlikely. The scope for further deterioration in relations has been reduced by Labor's election, but we still view the new government as backing trade diversification away from China as a long-term goal.

More broadly, Labor administration will seek to maintain and develop Australia's traditional and new alliances. Labor has expressed its full backing for the AUKUS security deal with the US and UK, and one of Mr Albanese's first tasks since becoming prime minister has been to attend the Quad leaders' summit in Japan. One area of probable adjustment will be in Australia's relations with its Pacific island neighbours, with China's recent security agreement with the Solomon Islands having featured in the election campaign. We expect a step-up in the development budget for Pacific nations and the change in language on climate change to help with diplomacy, but there is realistically no path to stopping China from further developing its influence in the region.

No major economic policy shifts, barring some fiscal realignment

There is unlikely to be a major shift in economic policy in the coming years. The two parties offered very similar visions for the economy on the campaign trail, a fact emphasised by Labor's pledge to honour the income tax cuts scheduled for 2024 that had already been legislated by the coalition. Although the new treasurer, Jim Chalmers, has spoken of a careful review of spending priorities, there is little appetite among the electorate for the sort of higher taxes required to narrow the fiscal deficit (especially at a time of high inflation), nor will Labor want to risk being seen as fiscally irresponsible by pushing the deficit out further.

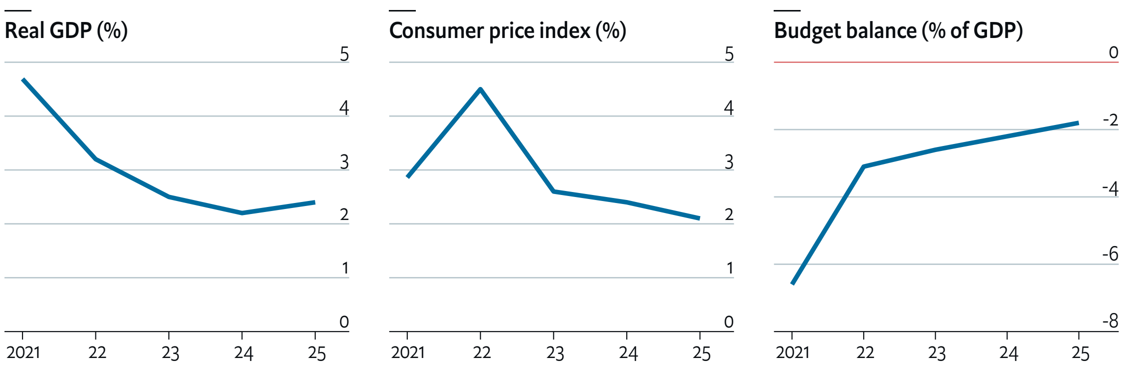
There will be an ideological shift towards pushing government spending towards low-income families, childcare and aged care and away from large corporations, but this will be largely symbolic. Labor is supportive of the OECD's attempt to ensure that multinational corporations pay a minimum tax rate of 15% and impose stricter limits on debt-related deductions.

Liberal move to the right could usher in long period of Labor rule

At present, it is uncertain what sort of political opposition the Labor government will face. The former prime minister, Scott Morrison, resigned immediately after his election defeat was confirmed. The teal independents have also removed several high-profile moderate Liberals, including the former treasurer, Josh Frydenberg. This means that the front-runner to lead the Liberal party is a former defence minister, Peter Dutton, a conservative.

The dissonance between Mr Dutton's own politics and where the electorate appears to have moved means that Labor could be set for an extended period of governance, especially following the emergence of a centrist, independent vote. It would probably take a sharp economic downturn—not EIU's core forecast—or the re-emergence of the internal divisions that helped to undo the last Labor administration in 2010-13 and revive support for the Liberals.

Inflation is a challenge, but Labor inherits a fairly benign economic outlook



Source: EIU.

China's new audit rules will not stop US delistings

Key takeaway: Corporate Governance is one of the three categories that comprise the Governance pillar of our ESG ratings. Reforms in China that will allow foreign auditors to inspect records of companies based on the mainland could improve the country's ranking of 22nd in the Corporate Governance category, which is already the strongest aspect of the country's Governance profile. Ultimately, low scores for Electoral Process and Functioning of Government will still anchor China in the bottom third of our overall Governance ranking.

World| Industry| Highlights| Financial services| Asset management

April 8th 2022

- **US-listed Chinese stocks gained after Chinese authorities announced they were amending a rule that would allow foreign auditors to inspect records of companies based on the mainland.**
- **Only complete compliance with US regulatory requirements, however, would be needed to prevent the delisting of these stocks from American exchanges by 2024, a deadline that the Securities and Exchange Commission (SEC) set earlier this year.**
- **The nebulous definition of what constitutes sensitive data means that Chinese firms delisting from US exchanges would include not just state-owned companies but also tech firms.**

On April 2nd, China's financial markets regulator, the China Securities Regulatory Commission (CSRC) announced that it was changing privacy laws that hindered Chinese companies listed overseas from allowing foreign regulators access to financial information. New draft regulations omit a clause mandating that on-site inspections should either be conducted primarily by Chinese regulators or be based on the results of their inspections. At first glance this amendment substantially clears the path for US regulators to gain complete access to the audit reports of the majority of the nearly 270 Chinese companies listed on the NYSE and Nasdaq.

Long-running tussle

The ongoing tussle between US and China's capital market regulators started last year when the SEC started implementing legislation that the US Congress passed in 2020: the Holding Foreign Companies Accountable Act (HFCAA). According to the HFCAA, companies that fail to comply with US audit rules would have to delist from the country's stock exchanges. This is particularly applicable to companies from countries that prevent the US Public Company Accounting Oversight Board (PCAOB) from inspecting local auditors.

Although the US law is applicable to all foreign companies, in practice its primary focus will be on Chinese companies that have, until now, prevented foreign regulators from reviewing local auditors. On March 10th 2022 the SEC released a list of Chinese companies that would have to delist from US exchanges by 2024 since they had failed to comply with HFCAA norms. According to the

US government, this would amount to more than 200 Chinese companies with a combined market capitalisation of US$2.1trn as at May 2021, including eight state-owned enterprises.

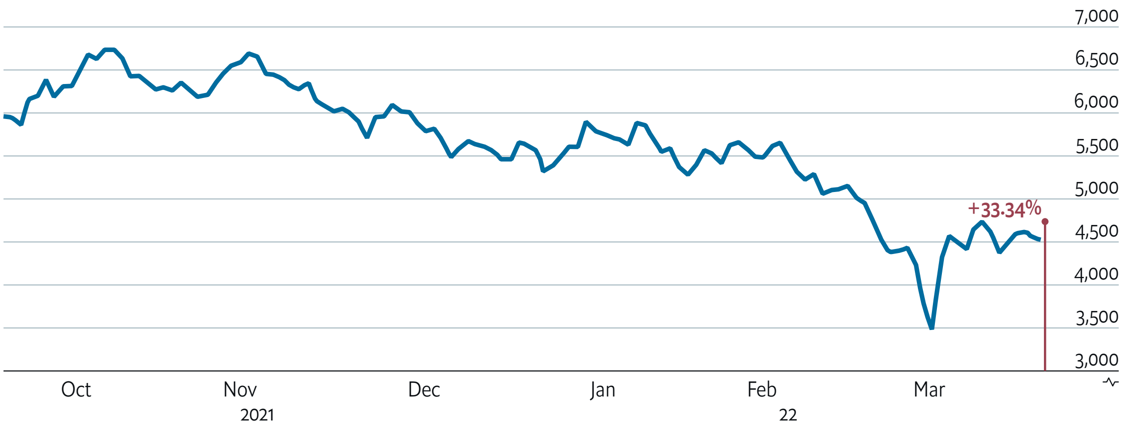
Major hurdles ahead, with delistings inevitable

Even though the latest relaxation in rules was welcomed enthusiastically by market participants, particularly those invested in Chinese stocks listed on US exchanges, many regulatory hurdles lie ahead. Other revisions to rules were also made by the CSRC that actually muddy the waters when it comes to foreign auditors accessing records of Chinese companies. The CSRC now stipulates that Chinese companies must provide a statement of the sensitive information that they provide to auditors, and apply for approval before providing foreign regulators with access to such information. Further, audit reviews would have to adhere to a "co-operation mechanism" between the CRSC and an overseas regulator.

What exactly constitutes state secrets or sensitive information remains unclear at this point, and will continue to be defined by China's new, and evolving, data governance regime. Similarly, the nature of the cross-border regulatory mechanism that the new CSRC rules talks about remains undefined.

It comes as no surprise, therefore, that the SEC believes that a near-term solution to these issues is unlikely, indicating that only total adherence to audit inspections would allow stocks of foreign companies to continue trading on US exchanges. The SEC seems to have taken the position that non-compliant Chinese companies could simply move to an exchange outside the US if they do not want to provide financial documents for inspection.

Despite a recent rebound, the Hang Seng remains 60% below its most recent peak
(Hang Seng TECH Index, last price)



Sources: Bloomberg; EIU.

Chinese tech stocks recover, but for how long?

In terms of firmness, the SEC's regulatory stance is in line with what China exhibited last year when its tightening of rules around variable interest entities (VIEs) forced Didi to announce plans to delist in the US, and we do not expect it to soften going forward. The SEC chair, Gary Gensler, did acknowledge on March 29th that there have been "thoughtful, respectful, productive" exchanges with his counterparts in China, but also acknowledged that it was up to Chinese authorities to fall in line with US regulatory requirements.

Investors in US-listed China stocks chose to focus on the optimism generated by the CSRC statement and soared after the announcement on April 1st with Alibaba, JD.com, Baidu and even Didi moving higher. The Hang Seng gained more than 5%, its highest increase in more than two weeks and has rebounded more than 30% from the low it hit in March after Beijing announced it would make regulatory changes to boost market stability. However, it remains 60% below its February 2021 peak.

However, we do not share this optimism, especially over the longer term and believe that most Chinese state-owned companies will have to delist from US exchanges by 2024. This will be true for several tech companies as well since the definition of sensitive information will remain nebulous for Chinese companies. In line with Didi, most of these firms will pursue listings in Hong Kong or Shanghai, leaving very few listed on US exchanges.

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