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「Assessing the MSCI ESG Ratings Model」

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Abstract

This report outlines the results of mapping the MSCI (Morgan Stanley Capital International) ESG Ratings against the Value Model, a model that has aggregated and synthesized more than 45 of the world's top ESG and sustainability reporting frameworks into a 7-stakeholder, 27-theme, 81-goal model for value creation and measurement. To do so, our research team investigated a set of MSCI's ESG Ratings methodology documents, especially its 33 ESG Key Issues methodologies designed by MSCI ESG Research LLC from February to March 2024, and subsequently analyzed all the sub-metrics to be assessed for scoring the 33 Key Issues from the documents against our Value Model based on the same 5 step process that were followed for the integration of all other similar frameworks in our previous research. Overall, MSCI ESG Ratings covers all 7 stakeholders (100%), 24 of 27 themes (89%), and 58 out of 81 goals (58%) within the Value Model.

Keywords: value, value measurement, ESG, sustainability, MSCI, sustainability report

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Executive Summary

This report outlines the results of mapping the MSCI (Morgan Stanley Capital International) ESG Ratings against the Value Model, a model that has aggregated and synthesized more than 45 of the world's top ESG and sustainability reporting frameworks into a 7-stakeholder, 27-theme, 81-goal model for value creation and measurement. To do so, our research team investigated a set of MSCI's ESG Ratings methodology documents, especially its 33 ESG Key Issues methodologies designed by MSCI ESG Research LLC from February to March 2024, and subsequently analyzed all the sub-metrics to be assessed for scoring the 33 Key Issues from the documents against our Value Model based on the same 5 step process that were followed for the integration of all other similar frameworks in our previous research. Overall, MSCI ESG Ratings covers all 7 stakeholders (100%), 24 of 27 themes (89%), and 58 out of 81 goals (58%) within the Value Model.

This result shows overall coverage of all 7 stakeholders and a wide coverage of themes, nearly 90% of the Value Model. Nevertheless, our research team found 5 notable concerns for MSCI ESG Ratings as follows:

1) Takeaway 1: Complex and Convoluted ESG Ratings Process

We found the MSCI ESG ratings to be complex and convoluted by design, a clear indicator of value washing. Because such complexity exists, the MSCI ESG Ratings can be abused as a tool for subjective ESG scoring due to the barriers it for outsiders to independently check and access results. For example, in order to score the key issue, "Biodiversity and Land Use", more than 5 sub-indicators should be considered such as 1) Management score, 2) Exposure score, 3) Business exposure score, 4) Business segment exposure score, and 5) Geographic Exposure score, and each sub-indicator also needs to be calculated by applying different formulas. This complicated approach almost guarantees that results will be calculated differently depending on the analyst, and bars assurance by outside independent auditors. This in turn creates a new market for consultants who are paid to help companies score better. However, a high score is not necessarily correlated with greater value creation nor improved sustainability outcomes for the company itself or its stakeholders.

2) Takeaway 2: The High Potential for Value Washing

Although MSCI was found to address a wide range of topics related to all stakeholders and many themes within the Value Model, we were surprised to find that 82% of the MSCI impact measurements (72 out of 88) received only 2 points and another 18% (16 out of 88) only achieved 3 points on our 5-point impact measurement quality ratings scale. Even more concerning was that we found none of these 88 scored 4 or 5 points. In our impact measurement quality ratings, higher points represent that sustainability indicators are devoid of value washing potential, where lower scores open more opportunities for businesses to value wash their sustainability efforts. Therefore, their below-average scores warn that their impact measurements may result in an incomplete understanding of corporate sustainability efforts while claiming to effectively do the opposite.

3) Takeaways 3: The Mishmash of Requirements and Missing Goals Required in Existing Frameworks.

In addition to the risk of the value washing, we found MSCI's sub-indicators below each of MSCI's 33 Key Issues failed to effectively measure corporate sustainability topics. On one hand, MSCI often and repeatedly focused on one sustainability topic from multiple viewpoints, but on the other, fail to mention 42% (34 out of 81) of Value Model goals. For example, MSCI did not include topics such as living wages and human rights reporting in the Employee stakeholder category nor the topic of local employment in the Society stakeholder category, both of which are prominent in the GRI framework.

Combining these two limitations, MSCI's ratings do not appear to offer a holistic view of a company's overall sustainability activities or impacts.

4) Takeaways 4: Single Materiality, Firm and Financial Performance Focused View.

MSCI's impact measurements heavily emphasize the views of the Firm and its Shareholders, at the expense of other important stakeholders. This can be seen in Figure 1 below where topics related to firm (n=7, 88%) and shareholder value (n=1, 100%) were highly represented in the MSCI ratings while goals related to other stakeholders such as Employees (n=6, 26%), Society (n=6, 50%), and Partners (n=6, 67%) were represented in far lower levels. These results suggest that the single materiality view, when amplified through a ratings system such as this, has overlooked a number of key topics and goals related to stakeholder impacts and their outcomes.

5) Takeaways 5: Absence of the Standardized Metrics and End-goals.

Finally, MSCI does not provide common standard metrics that can be applied to each impact measurements irrespective of industry or country, except for its governance topics. Thus, it is difficult if not impossible to compare the sustainability performance of individual companies or industries based on their MSCI ratings. Additionally, at no point in time does MSCI present a set of clear end-goals and then benchmark corporate performance against these. For example, while Biodiversity is clearly highlighted throughout the MSCI scoring, at no point is a Biodiversity end goal given and then used to benchmark corporate performance against.

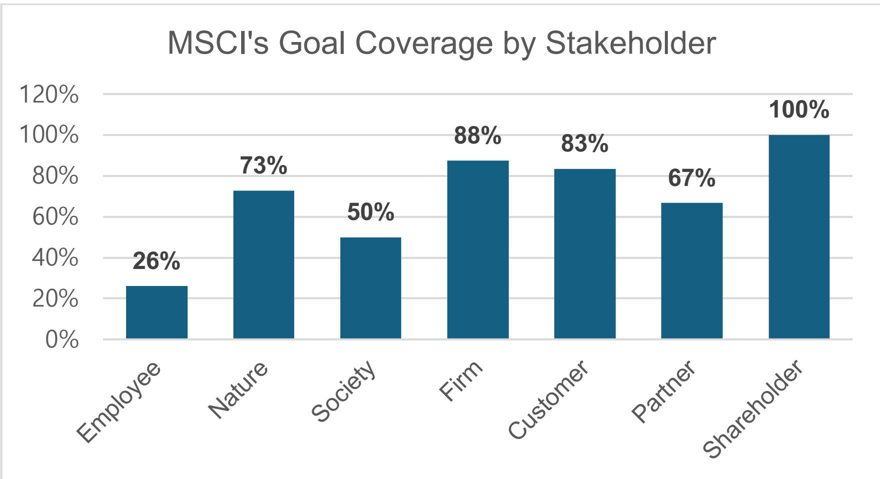

Figure 1. MSCI's Goal Coverage by stakeholder against VM

Since MSCI's ESG Ratings service has been in existence since 1999, this model has great influence on assessing the sustainability performance of companies in the ESG Rating market. However, for all of the ratings given, carbon emissions and negative biodiversity impacts have increased significantly over this same time period. Because of this, we fear that MSCI ESG Ratings have become a platform for widespread value washing by corporations, rather than a system to reduce impacts, increase sustainability performance outcomes and overall value creation across a company and its stakeholders.

To understand what the MSCI ESG ratings actually measure across their 33 key issues and the overall value of this system to understand sustainability impacts and the value created from them, we have mapped these against the 7 stakeholders, 27 themes, and 81 goals of the Value Model.

It should be noted that this assessment has been conducted independently of any government, corporation or outside third party, and funding for this research was generously provided by a Doshisha University SDGs support fund from April 2023 – March 2024.

Introduction

MSCI Inc. is an American finance company that globally provides equity, fixed income, real estate indices, multi-asset portfolio analysis tools, ESG and climate products. In line with their mission, "to power better investment decisions", MSCI has over 50 years of expertise in research, data, and technology to analyze corporate risk and return for its global investment clients. In this context, MSCI ESG Ratings provide expert insights on corporate management capabilities on critical ESG-related financial risks and opportunities from an investor's perspective.

This ESG rating system is built as a hierarchy, consisting of 3 pillars (Environmental, Social, Governance), 10 themes, and 33 ESG Key Issues. According to its own ESG Ratings Methodology documents, key features of the MSCI ESG ratings service include:

- MSCI ESG Ratings are industry-relative measures, providing company ratings using a seven-band scale from AAA (the highest rating) to CCC (the lowest rating) which are based on the relative assessment results to a company's industry peers.
- Companies are assessed by their relevant key issues (ranging from 2 – 7) in Environmental and Social areas, which are selected according to the company's exposure to material risks determined by industry and market specific factors.
- Unlike the Environmental and Social areas, all companies are evaluated on the Governance Key Issues through an absolute assessment and deduction-based scoring. If a deduction factor is found, a company can use up to 10 points from their total score.
- To assess company ESG performance, MSCI collects raw data from various secondary sources such as a company's financial and sustainability disclosures, third-party data sets published by governments, academic journals, the media, and its own or outside analysts. MSCI rankings are therefore not solely based on data provided by companies themselves.

The Value Model as a "Health Check" for Companies' Sustainable Performance

The Value Model consists of 7 stakeholders, 27 themes, 81 goals with clear KPIs for value measurement, and benchmarks sustainability performance across and between different companies. Because it offers a goal-based approach to multistakeholder value measurement derived from more than 45 of the world's top ESG and sustainability reporting frameworks, it provides transparent, objective guidance for businesses and their leadership team to (1) understand their overall stakeholder impacts in context, and (2) create forward looking strategies for future value creation activities based on these.

To conduct this analysis, we accessed MSCI ESG Ratings Methodologies documents from February to March 2024 and mapped all the 33 MSCI's Key issues presented in the ESG Ratings model and scored them in two ways. First, we assessed their coverage of Value Model stakeholders, themes and goals, and second we then scored the quality of each of the MSCI Key Issues in terms of their ability to remove value washing when used to score another company's ESG and sustainability performance.

Section 1. MSCI's Overall Coverage against Value Model

MSCI ESG Ratings Coverage by Stakeholders

Beginning with the positive elements of our assessment, MSCI should be commended for its broad stakeholder coverage, as its 33 Key Issues in aggregate spanned across all Value Model stakeholders, and a commendable 89% of Value Model themes. As outlined in Table 1 below, the detailed contents of the MSCI Key Issues cover all seven stakeholders and 24 themes out of the Value Model's 27 (89%). In particular, themes within the Nature, Society, Firm, Customer, and Shareholder stakeholder categories were found to be 100% covered, and the other two areas, Employee (n=4) and Partner (n=3) presented also highly respectable coverage results with 67% and 75% against the Value Model. Such a broad coverage of stakeholders and themes by MSCI may be interpreted as a sign of its holistic view of companies' sustainable performances related to all 7 stakeholders' value, and conversely helps once again confirm the alignment with the Value Model with global sustainability frameworks, standards and ratings systems.

While MSCI should be applauded for these high-level results, when looking more closely within these themes at the overall coverage of the 81 Value Model goals, unfortunately, they are still missing 34 goals (42%) out of the total 81 goals from the Value Model. As outlined in Table 1 below, MSCI meets 58% or 47 goals in total against the Value Model and in particular, two stakeholders including the Firm (n=7, 88%) and Shareholders (n=1, 100%) were found to cover approximately 90% or more of the Value Model goals included within them. However, the goal coverage rates in other stakeholder categories were found to have significant room for improvement, with coverage of Employee-related goals only at 26% (n=6), Society at only 50% (n=6), and Partner at 67%. Details of MSCI's overall Value Model goal coverage is outlined in Appendix 1.

	Theme Coverage			Goal Coverage		
	MSCI	VM	%	MSCI	VM	%
All Stakeholder	24	27	**89%**	47	81	**58%**
Employee	4	6	**67%**	6	23	**26%**
Nature	6	6	**100%**	16	22	**73%**
Society	4	4	**100%**	6	12	**50%**
Firm	3	3	**100%**	7	8	**88%**
Customer	3	3	**100%**	5	6	**83%**
Partner	3	4	**75%**	6	9	**67%**
Shareholder	1	1	**100%**	1	1	**100%**

Table 1. MSCI Overall Coverage against the Value Model

Missing Goals Required Reporting in Existing Frameworks

These results show that MSCI emphasizes two stakeholders, the Firm and its Shareholders above all others, and despite its significant coverage achievement in these two areas, its overall coverage of Value Model goals remains at only 58% (n=47). This unbalanced emphasis on the Firm and

Shareholder should be noted because MSCI's ratings do not currently measure a company's comprehensive sustainability efforts across all stakeholders emphasized by many of the world's top ESG and sustainability reporting frameworks and standards. The examples in Table 2 below demonstrate that MSCI neglects a number of important topics related to various Value Model goals. We find these omissions surprising because Value Model goals are derived directly from existing disclosure standards and frameworks suggesting that regulators and investors are not aligned in their interests within important sustainability topics. Using just the Global Reporting Initiative (GRI) disclosure framework as an example, Table 2 below shows examples of this misalignment across a few important topics:

Missing goal	GRI Indicator
E1-C: Gender Diversity and Equity-based policy	Disclosure 202-1 Ratios of standard entry level wage by gender compared to local minimum wage.
E2-A: Transparent Reporting on Employees	Disclosure 2-7 Employee Disclosure 401-1 New employee hires and employee turnover.
E3-C: Family/Medical Leave	Disclosure 401-3 Parental leave: Employees entitled to parental leave means those employees that are covered by organizational policies, agreements or contracts that contain parental leave entitlements. To determine who returned to work after parental leave ended and were still employed 12 months later, an organization can consult records from the prior reporting periods.
E5-C: Freedom of Association	Disclosure 2-30: Collective bargaining agreements
E6-A: Human Rights Reporting	Disclosure 2-25: Process to remediate negative impacts
E6-B: Human Rights Corrective Action	Disclosure 410-1 Security personnel trained in human rights policies or procedures: can refer either to training dedicated to the subject of human rights or to a human rights module within a general training program. Training can cover issues such as the use of force, inhuman or degrading treatment or discrimination, or identification and registering.
S3-A: Local Employment	Disclosure: 202-2 Proportion of senior management hired from the local community
P1-A: Report on Stakeholder Structure in the Supply Chain	Disclosure 2-29: Approach to stakeholder engagement Disclosure 102-40: List of stakeholder groups Disclosure 102-42: Identifying and selecting stakeholders. Disclosure 102-43: Approach to stakeholder engagement Disclosure 102-44: Key topics and concerns raised

Table 2. MSCI's Missing goals required by GRI framework related to social domain stakeholders.

If MSCI Ratings are truly a proxy for a company's sustainability practices, highlighting both risks and opportunities for investors beyond financial measures, it is clear that a number of key topics remain hidden and out of view of investors, and such coverage gaps should be addressed in future iterations of the MSCI Ratings.

Single Materiality Perspective: Firm and Shareholder Focused Indicators

MSCI's ESG Ratings model has been created based on the Single Materiality view of sustainability disclosure which dictate that ESG risks and opportunities should only be assessed in terms of how these impact the company and its financial performance without integrating the additional view of how businesses in turn impact their stakeholders, or the Double Materiality view.

This Single Materiality perspective underlying the MSCI's key issues' impact measurements can be seen across all Environmental, Social, or Governance issues in their ESG scoring approach. Table 3 shows how this difference of perspective affects data collected and disclosed. For example while MSCI calls "Climate Change Vulnerability" an environmental topic, carefully reading the details of the data that they collect and use to score this topic shows in fact that this is firm-specific data according to the Value Model. This is because it only includes management's views and actions related to mitigating climate risks to the company (a Firm-specific view) rather than climate specific actions taken to reduce negative impacts on Nature (a Nature-specific view). Three other examples are similarly shown for comparison and illustrative purposes.

MSCI Key Issue	MSCI Pillar	Related Text in the documents	Related Stakeholder
The Climate Change Vulnerability	Environmental	Companies are assessed on the physical risk that climate change may pose to insured assets or individuals.	Firm
Financing Environmental Impact	Environmental	Financial institutions are evaluated on the environmental risks of their lending and underwriting activities and their ability to capitalize on opportunities related to green finance.	Firm, Nature
Opportunities in Nutrition & Health	Social	Companies are evaluated on their positioning to meet market demand for products with improved nutritional or health profiles.	Firm, Customer
Responsible Investment	Social	Companies are evaluated on their integration of environmental, social and governance considerations in the management of their own assets or the assets they manage on behalf of others.	Firm, Shareholder

Table 3. The examples of Mistaken Labels

ESG Ratings based on Single Materiality can in fact help investors understand an organizations' sustainability efforts. But because this perspective prioritizes the interests and viewpoints of the company management or shareholders over its other key stakeholders, it creates the risk of value washing the actual impacts that companies have. "Value washing" is defined as "actions taken by organizations to misrepresent value outcomes for themselves or their stakeholders", and manifested through (1) the absence of clear goals, (2) the absence of objective measures of these goals, (3) the absence of transparent reporting, (4) the absence of impartial, third party feedback loops, and (5) a complexity of terms, systems or words used in sustainability reports (Sugai, 2021)[1].

Based on these five elements of value washing, we next measured the quality of all 33 Key Issues within MSCI's rating system according to our impact data quality scoring approach, which ranges

[1] Sugai, P. (2021). The Definition, Identification and Eradication of Value Washing. *Journal of Creating Value*, *7*(2), 165-169.

from 0 points for highest value washing potential to 5 points for lowest value washing potential. Scores are given as follows:

(1) Does the impact measurement have clear goals (No = 0 points, Yes = 1 point)
(2) Does the impact measurement show evidence that it can be objectively measured? (No = 0 points, Yes = 1 point)
(3) Does the impact measurement show evidence that it can be transparently confirmed by an independent outside 3rd party? (No= 0 points, Yes, but no clear evidence it is currently being done = 1 point, Yes, with clear evidence it is currently being done = 2 points). For example, an impact measurement for plastic pollution would typically score 1 point, as it "could" be independently verified by an outside 3rd party but there is currently no trusted 3rd party that does this. While metric tons of carbon emissions would receive 2 points as there are verified independent auditors who do this (for example, those certified by the UNFCCC).
(4) Does the impact measurement use a scale variable rather than a binary, yes/no answer? (No = 0 points, Yes = 1 point)

Section 2. Quality and Coverage of Impact Measurements in MSCI

In order to analyze the possibility of value washing potential embedded within MSCI's impact measurement system, we first collected the complete documentation for all of their 33 Key Issues from the MSCI website. In our initial review, we found that within these 33 Key Issues, there were multiple sub-issues mixed together, and for clarity in our own scoring of the MSCI ratings, we further separated their 33 Key issues into 88 sub-issues. We then mapped these 88 sub-issues against the 7 stakeholders, 27 themes and 81 goals from the Value Model. Details of these 88 sub-issues identified on the basis of our Value Model within the 33 key issues designed by MSCI presents in Appendix 2.

After mapping the 88 sub-issues within the 33 key issues against Value Model's goals, we scored each of these according to the scoring approach outlined above. Within each Key Issue, we found on average that these included 3 representative Value Model goals, making our scoring difficult and cumbersome. To illustrate the complexity of scoring the MSCI ratings using a standardized approach, we have listed some Key Issues that included more than 3 value model goals in Section 3.

After scoring each of the impact measurements categorized by stakeholders against the Value Model, we calculated a "total points" score by adding the points earned across all of them. We then determined a "total possible" score by multiplying each impact measurement by the maximum score of 5 points. By dividing the total points score by the total possible score, we arrived at the overall score, which we presented as the percentage of total possible points that MSCI achieved.

Impact Measurement Quality Coverage by Stakeholder

Table 4 presents the quality coverage data across the 7 stakeholders against Value Model. Most of the stakeholders' quality coverage achievement lie between 40 and 50 % and even the two highest stakeholders' areas such as Firm and Shareholder achieved 50% (n=57) and 53% (n=8) of the full impact measurement quality potential. This poor result is obviously due to the fact that 72 impact measurements (82%) from the MSCI's documents received 2 points and the other 16 impact measurements (18%) scored 3 points out of the total possible score, 5 points. This remarkably low quality of impact measurements shows the high potential for value washing with the MSCI Ratings system, which is in stark contrast to the wide coverage that they showed for Value Model stakeholders and themes.

MSCI Quality Coverage by Stakeholder					
Stakeholder	2 points	3 points	Total	VM	%
Employee	7	0	14	35	40%
Nature	25	0	50	125	40%
Society	8	2	22	50	44%
Firm	12	11	57	115	50%
Customer	9	0	18	45	40%
Partner	10	1	23	55	42%
Shareholder	1	2	8	15	53%
Total	72	16	192	440	44%

Table 4. MSCI's impact measurement quality coverage by stakeholders

Value Washing Possibility under the Guise of Assessment

As discussed earlier, while MSCI generally achieved wide coverage of topics related to the stakeholders, themes, and goals within the Value Model, we found it quite disappointing that 72 impact measurements (82%) received only 2 points and another 16 impact measurements (18%) merely scored 3 points out of the total 5 points as shown in Table 5. Even more discouraging, none of their impact measurements achieved 4 or 5 points (Figure 2), which shows high potential of value washing in MSCI's ESG ratings model. Here, higher points represent sustainability indicators that are devoid of value washing potential, where lower scores open more opportunities for businesses to value wash their sustainability efforts.

Value Washing Score	%	No. of impact measurement
0	0%	0
1	0%	0
2	**82%**	**72**
3	**18%**	**16**
4	0%	0
5	0%	0
Total	100%	88

Table 5. Distribution of MSCI value washing score

To understand the severity of this finding, MSCI is of the most widely adopted and trusted sustainability rating agencies in the world. Businesses globally hire teams of consultants to help them improve their MSCI ratings and collections of high-scoring companies are bundled into portfolios and indices. However, with such high potential for value washing, the underlying risks of ratings being out of line with actual impacts is similarly high. Towards this end, and based on our assessment above, it is difficult to conclude that a high MSCI ESG rating actually correlate with true value creation across a company's stakeholders. This result aligns with other academic articles (c.f. Pucker & King, 2022) that have been dubious about the connection between ESG ratings and financial performance.[2]

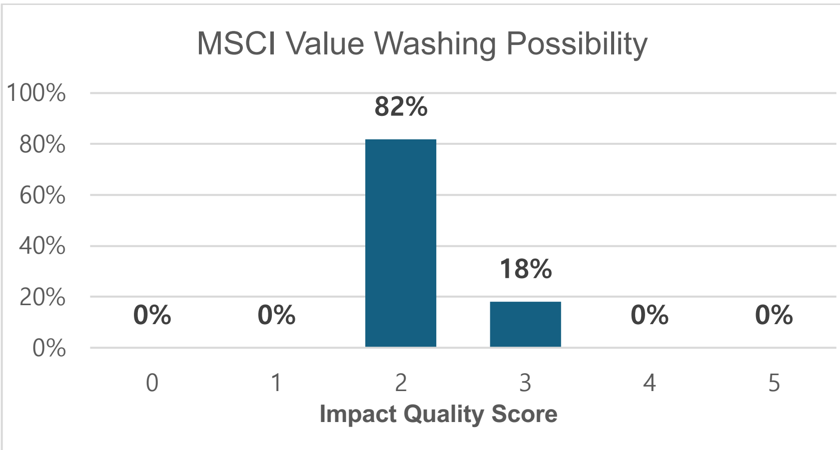

Figure 2. MSCI value washing possibility.

[2] Pucker, K., & King, A. (2022). ESG investing isn't designed to save the planet.

Through this mapping of MSCI's Key Issues and related impact measurements against the Value Model, we have reached the conclusion that the MSCI ESG Ratings could be improved to remove all possibilities for value washing, specifically by enhancing their ratings methodology to be 1) independently checkable, 2) objectively measured, and to provide 3) clear end-goals. More discussion on each of these suggested improvements are outlined in the next section of this report.

Section 3. Recommendations for Improvement

While MSCI's overall coverage of stakeholders and themes is respectable, they have unfortunately overlooked 34 (42%) Value Model goals especially in the Employee, Society, and Partner stakeholder categories. More importantly, the quality of their impact measurements were found to be severely lacking. To address these points, we suggest the following improvements be made to the overall MSCI ESG Ratings methodology:

Recommendation #1: Reduce Complex and Convoluted ESG Ratings Process

As discussed earlier, MSCI mixes various indicators and metrics into each of their Key Issues, using various formulas and metrics in order to calculate a score for each. For example, one of the MSCI'S key issues in the Environmental area, "Biodiversity and Land Use" requires more than 5 sub-indicators to evaluate it. Additionally, this key issue is calculated with 2 constants: An Exposure score and a Management score (Figure 3), and each of these in turn is calculated with different formulas with their own unique sub-indicators. Continuing further, one of these sub-indicators, the "Exposure score" is calculated by combing another 2 what we'll call "sub-sub-indicators" including a Business Exposure score and Geographic Exposure score (Figure 4). To continue even further, one of these sub-sub indicators, the Business Exposure score is defined using another formula and set of sub-metrics including 1) a Business Segment Exposure Score for the business segment, 2) the weight of that business segment for the company based on its contribution to total company assets, and 3) the number of business segments within the overall company (Figure 5). As expected, theses sub-sub-sub metrics also require different formulas and variables for scoring them, but these are omitted due to the limitations of this paper's space.

$$KI_i = 7 - (\max(EXP_i, 2) - MGMT_i)$$

Where:

- KI_i is the Key Issue Score for company i.
- EXP_i is the Exposure Score for company i.
- $MGMT_i$ is the Management Score for company i.

Figure 3. The formula for Biodiversity & Land Use Key issue score

$$EXP_{BIO,i} = BUS_{BIO,i}(1 + 0.1(GEO_{BIO,i} - 5))$$

Where:

- $EXP_{BIO,i}$ is the Biodiversity & Land Use Exposure Score of company i.
- $BUS_{BIO,i}$ is the Business Exposure Score of company i.
- $GEO_{BIO,i}$ is the Geographic Exposure Score of company i.

Figure 4. The formula for the Exposure score in Biodiversity & Land Use key issue

$$BUS_{BIO,i} = \sum_{j=1}^{n_i} w_{Asset,i,j} BSE_{BIO,j}$$

Where:

- $BSE_{BIO,j}$ is the Business Segment Exposure Score for business segment j.
- $w_{Asset,i,j}$ is the weight of business segment j for company i based on the contribution to total company assets.
- n_i is the number of business segments of company i.

Figure 5. The formula for the Business Exposure score in Biodiversity & Land Use key issue

For an outsider, this complex process may make it look like MSCI is using a highly advanced scientific method which takes into consideration many metrics and sub-indicators to assess each MSCI Key Issue. However, their model does not provide a clear explanation of these calculations nor does it provide a replicable if/then relationship between an impact measurement and a final MSCI ESG Rating score. That is to say, if score X goes up, we have no idea how the final result Y will be calculated. Thus, it is almost impossible for outsiders to check independently, and may requires a team of analysts to figure out what needs to be done in order to score well. This creates a market for ESG Ratings Institutions like MSCI but does not in fact lead to greater value creation for a firm's multiple stakeholders.

Why this matters: If the MSCI Ratings system is so complex, subjective and opaque, performance measurement dashboards with clear, consistent benchmarks that can be used to compare and contrast corporate performance and achievement of the various sustainability goals are impossible to develop and implement.

Complexity by design such that a PhD and a team of academic researchers are required to make sense of how sustainability topics can be measured and scored is not a winning formula for addressing our most important sustainability challenges, nor for creating value across a company's stakeholder ecosystem. While sustainability consultants and sustainability data businesses may flourish under such a complex system, we do not believe that this is the point of corporate sustainability practices today or of successful ones in the future.

Recommendation #2: Transform the Mishmash of Requirements into Clear, Logical and Reasonable Objective Measurements of Sustainability Impacts and Outcomes

In addition to the highly complicated formulas used to assess a company's sustainability performance, MSCI's overlapping requirements in each of their Key Issues also hinders the rigorous measurement of corporate sustainability performance. MSCI frequently mixes too many requirements within one Key Issue, which are then in turn discussed repeatedly throughout many other of their 33 Key Issues. For example, one of the MSCI's social key issues, "Community Relations" covered 6 different goals related to 4 different stakeholders within the Value Model all at the same time, including (1) Healthy, Safe, Resilient Community, (2) Transparent Social Reporting, and (3) Local Value Chains in the Society stakeholder category, (4) Suppliers and Distributor Impact Reporting in the Partner stakeholder category, (5) Human Rights Training in the Employee stakeholder category, and (6) Biodiversity Impact in the Nature stakeholder category. Among these, the "Healthy, Safe, Resilient Community" goal was found to be included multiple times within other parts of the MSCI's ranking system, including its Key Issues of: (A) Consumer Financial Protection, (B) Access to Finance, (C)

Access to Health Care, and (D) Opportunities in Nutrition & Health. Table 6 presents more examples that show how one Key Issue includes various goals from the Value Model.

Why this matters: By definition sustainability is a complex issue and because of this clearly defined metrics are a requirement for proper measurement and management of any sustainability topic. By mixing together so many issues, measures and weights into the MSCI Key Issues, in the end we cannot be sure what is truly being measured, and to what extent results from one company can be compared to others or even that one company's performance in one year can be used to benchmark its own sustainability performance in subsequent years.

What is most disappointing here is that MSCI is so deeply embedded in the finance industry that itself thrives on consistent reporting of financial metrics such as profits, earnings, ROA, ROI, etc. That this same level of rigor has not been applied to their ESG ratings is both surprising and disappointing, especially as MSCI has the market power to immediately address such shortcomings, and that doing so would immediately change how businesses globally measure and report on their sustainability performance.

MSCI Key Issue	Related Value Model Goal	Related Stakeholders	No. of goals included
Community Relations	Healthy, Safe, Resilient Community, Transparent Social Reporting, Local Value Chains, Suppliers and Distributor Impact Reporting, Human Rights Training, Biodiversity Impact	Society, Partner, Employee, Nature	6
Privacy & Data Security	Data Security, Customer Privacy, Governance Reporting, Human Rights Training, Supporting MSMEs, VCSEs, MWOBEs, and/or SDVOBs through education and training	Consumer, Employee, Firm, Partner,	5
Controversial Sourcing	Suppliers and Distributor Impact Reporting, Audited Fair labor practices throughout supply chain and distribution channels, Sustainable Sourcing of Raw Materials, Truth in Labeling	Partner, Environment, Customer,	4

Table 6. MSCI's Key issues included various goals.

Based on what we have learned from our analyses, we therefore cannot with any level of confidence believe that that even two experienced analysts using the exact same MSCI ESG scoring methodology on the exact same company data would arrive at the same scores at the end of their analyses. We would welcome any feedback from MSCI or analysts who regularly work with their ratings methodology to prove our concerns to be wrong. But until that time, we would recommend that anyone basing investment decisions on the MSCI ESG Rankings to carefully review their methodology documentation to reach their own conclusions as to the validity and veracity of results achieved through them.

Recommendation #3: Development of Standard Metrics and End-goals

Lastly, MSCI ESG Ratings lack clear objectives or end-goals that companies can use to benchmark their performance against for greater value creation today or in the future. For example, one of the Environmental key issues "Opportunities in Clean Tech", present its target, "to increase investment in clean tech" in the Management score category, which is unclear and not a specific goal, lacking a standardized measurement method. Moreover, there are no common metrics that can be applied to all

Key Issues regardless of the types of business, industry, or country, except for their governance issues. Such an approach might be effective when comparing the financial risk of companies within the same industry or similar geographical market. However, it will be very difficult to apply this approach to different companies from different industries or markets.

Why this matters: Is the purpose of the MSCI ESG Ratings to (1) improve sustainability related outcomes and the value generated from them or (2) to generate data on ESG topics that can be consumed and sold for profit? If the former, then MSCI should continuously work to develop clear end goals that could then be used to benchmark corporate sustainability performance against. If the latter, then it is important for all industry players to be clear about this and not conflate the first with the second. We of course also hope that the true purpose of this system is aligned with #1 above, and that in turn, our feedback can be considered constructive and supportive of future changes.

Conclusion

The MSCI ESG Ratings model focuses on the scoring of topics related to how effectively individual companies and their competitors manage ESG-related risks and opportunities against larger industry and country performance benchmarks. For this reason, MSCI excels in its coverage of Firm and Shareholder issues, in particular, governance structures and economic value added. Additionally, MSCI covers most all stakeholders and themes covered within the Value Model (100% coverage by stakeholder, 89% coverage by themes on average). However, 34 Value Model goals (42%) are missing from their coverage of sustainability topics

More importantly, all of MSCI's impact measurements scored either 2 or 3 out of 5 possible points when measured against our impact measurement quality scoring system. Such surprisingly low scores suggest that MSCI ESG Rankings can be used as a value washing tool masquerading as an ESG performance assessment. We have also found that MSCI's convoluted approach to ratings, complicated requirements, lack of end-goals, and highly variable processes must be improved if their aim is to truly provide meaningful insights into a company's, industry's or market's commitment to sustainable practices and impacts.

MSCI has been a global leader within the ESG Rating market for decades, and considering their dominance, we are deeply concerned that MSCI ESG Ratings can be used as a platform for widespread value washing. Thus, we strongly recommend that organizations or investors who use such ESG Ratings do so understanding both their strengths and limitations. Moreover, we hope that our findings prompt the broader sustainability assessment and ratings industries to shift their perspective to measuring actual multi-stakeholder impacts in simpler, clearer and more straight-forward ways. Such a change would enable us to celebrate companies that create increasing levels of value for themselves and their stakeholders in aggregate, rather than those that simply report on their performance. By championing more simple, standard, evidence-based assessments, future sustainability discussions and efforts could be refocused on actually achieving the sustainability outcomes that we consistently discuss, but collectively have yet failed to achieve.

Appendix 1. MSCI's Goal Coverage by stakeholders

*Dark color: covered goals, white color: uncovered goals by MSCI

Stakeholder	81 Value Model Goals											
Employee	E1-A Full-time Employment	E1-B Ethnic Diversity	E1-C Gender Diversity and Equity-based policy	E1-D Broad Diversity and Representativeness of employees	E2-A Transparent Reporting on Employees	E2-BTransparent Reporting on Wages	E2-C Living Wage	E2-D Employee Healthcare	E3-A Physical Health	E3-B Retirement Provision	E3-C Family/Medical Leave	E3-D Employee Healthcare
	E3-E Occupational safety and Health Coverage	E3-F Employee Mental health and wellbeing	E4-A Training and Education	E4-B Performance Feedback and Review	E5-A Turnover, Inclusion & Engagement	E5-B Work Flexibility	E5-C Freedom of Association	E5-D Employee Ownership	E6-A Human Rights Reporting	E6-B Human Rights Corrective Action	E6-C Human Rights Training	
Nature	N1-A Carbon Neutral	N1-B Zero non-GHG air emissions	N1-C Zero Plastic Pollution	N1-D 100% Waste reclamation & recycling	N1-E Zero Sound and Light disturbances	N2-A Water infrastructure interaction strategy	N2-B Water use reporting	N2-C Discharge water quality	N3-A Energy Consumption Reporting	N3-B Renewable Energy Use	N3-C Carbon Neutral Products	N4-A Transparently Reported Product Impact
	N4-B Sustainable Sourcing of Raw Materials	N4-C Products with Positive Societal and Environmental Impact	N4-D Efficient Packaging	N4-E Efficient Transportation	N5-A Biodiversity Impact	N5-B Humane, Compassionate Treatment of All Animals	N5-C 100% Sustainably Sourced Palm Oil	N6-A Transparently Reported Building and Land Use	N6-B 100% certified safe & accessible buildings	N6-C 100% of new buildings are carbon neutral		
Society	S1-A Transparent tax reporting	S1-B Appropriate Taxes Paid	S2-A Healthy, Safe, Resilient Community	S2-B Benefit-based capital spending	S2-C Transparent Social Reporting	S3-A Local Employment	S3-B Local Ownership	S3-C Equitable purchasing	S3-D Local Value Chains	S3-E Supporting Local Youth	S4-A Community volunteering	S4-B Charitable giving
Firm	F1-A Transparent reporting on financial performance	F1-B Government relationship	F2-A Mission Driven	F2-B Governance Reporting	F2-C Board Composition	F2-D Outside Director Ratio	F2-E Zero Corruption	F3-A Positive EVA				
Customer	C1-A Truth in Labeling	C1-B Truth in Advertising	C2-A Data Security	C2-B Customer Privacy	C3-A Customer Satisfaction	C3-B Customer Health & Safety						
Partner	P1-A Report on Stakeholder Structure in the Supply Chain and Distribution Channel	P1-B Report on Supply Chain Diversity, Equity and Inclusion	P2-A Supporting MSMEs, VCSEs, MWOBEs, and/or SDVOBs through business partnerships	P2-B Supporting MSMEs, VCSEs, MWOBEs, and/or SDVOBs through education and training	P3-A Suppliers and Distributor Impact Reporting	P3-B Environmental and Social operating requirements	P3-C Supply Chain Carbon Certification	P4-A Audited Fair labor practices throughout supply chain and distribution channels	P4-B Living wage paid by all suppliers and distributors in partner network			
Shareholder	SH1-A Positive EVA											

Appendix 2. Mapping MSCI Key Issues & Sub-Issues against Value Model Goals

Pillar	No.	MSCI Key Issues	No.	Sub-Issues Identified	VM Goals Mapped
E	1	Carbon Emissions	1	**Carbon neutral-specific**	N1-A :Carbon Neutral
			2	**Renewable energy - specific**	N3-B :Renewable Energy Use
	2	Climate Change Vulnerability	3	**Governance reporting- specific**	F2-B :Governance Reporting
	3	Financing Environmental Impact	4	**Mission driven- specific**	F2-A :Mission Driven
			5	**Positive impact product-specific**	N4-C :Products with Positive Societal and Environmental Impact
	4	Product Carbon Footprint	6	**Carbon neutral product-specific**	N3-C : Carbon Neutral Products
			7	**Carbon neutral-specific**	N1-A :Carbon Neutral
			8	**Raw material sourcing-specific**	N4-B :Sustainable Sourcing of Raw Materials
	5	Biodiversity & Land Use	9	**Biodiversity impact- specific**	N5-A :Biodiversity Impact
			10	**Transport reporting-specific**	N6-A :Transparently Reported Building and Land Use
			11	**Water use reporting-specific**	N2-B :Water use reporting
	6	Raw Material Sourcing	12	**Raw material sourcing-specific**	N4-B :Sustainable Sourcing of Raw Materials
			13	**Palm oil- specific**	N5-C 100% Sustainably Sourced Palm Oil
			14	**Labeling- specific**	C1-A Truth in Labeling
	7	Water Stress	15	**Water strategy- specific**	N2-A : Water infrastructure interaction strategy
			16	**Water use reporting- specific**	N2-B :Water use reporting
			17	**Mission driven- specific**	F2-A : Mission Driven
	8	Electronic Waste	18	**Waste recycling- specific**	N1-D :100% Waste reclamation & recycling
			19	**Positive impact product-specific**	N4-C :Products with Positive Societal and Environmental Impact
	9	Packaging Material & Waste	20	**Efficient packing- specific**	N4-D : Efficient Packaging
			21	**Waste recycling- specific**	N1-D :100% Waste reclamation & recycling
			22	**Plastic pollution- specific**	N1-C :Zero Plastic Pollution
	10	Toxic Emissions & Waste	23	**Non-GHG emission- specific**	N1-B : Zero non-GHG air emissions
			24	**Governance reporting- specific**	F2-B: Governance Reporting
			25	**Operating requirement- specific**	P3-B :Environmental and Social operating requirements.
	11	Opportunities in Clean Tech	26	**Financial reporting-specific**	F1-A :Transparent reporting on financial performance
			27	**Positive impact product-specific**	N4-C :Products with Positive Societal and Environmental Impact
	12	Opportunities in Green Building	28	**Safe & accessible building- specific**	N6-B: 100% certified safe & accessible buildings
			29	**Building & land reporting- specific**	N6-A: Transparently Reported Building and Land Use
	13	Opportunities in Renewable Energy	30	**Renewable energy - specific**	N3-B :Renewable Energy Use
			31	**Government relationship- specific**	F1-B : Government relationship

Pillar	No.	MSCI Key Issues	No.	Sub-Issues Identified	VM Goals Mapped
S	14	Health & Safety	32	**Employee safety-specific**	E3-E: Occupational safety and Health Coverage
			33	**Goverance reporting- specific**	F2-B :Governance Reporting
			34	**Fair labor in partner- specific**	P4-A: Audited Fair labor practices throughout supply chain & distribution channels
	15	Human Capital Development	35	**Employee Inclusion- specific**	E5-A Turnover, Inclusion & Engagement
			36	**Employee training- specific**	E4-A Training and Education
			37	**Performance feedback- specific**	E4-B Performance Feedback and Review
	16	Labor Management	38	**Employee living wage-specific**	E2-C Living Wage
			39	**Employee training- specific**	E4-A Training and Education
			40	**Retirement- specific**	E3-B Retirement Provision
	17	Supply Chain Labor Standards	41	**Fair labor in partner- specific**	P4-A Audited Fair labor practices throughout supply chain & distribution channels
			42	**Living wage in partner-specific**	P4-B Living wage paid by all suppliers and distributors in partner network
			43	**Supporting partners- specific**	P2-B Supporting MSMEs, VCSEs, MWOBEs, and/or SDVOBs through education & training
	18	Chemical Safety	44	**Customer health- specific**	C3-B Customer Health & Safety
			45	**Labeling- specific**	C1-A Truth in Labeling
			46	**Product impact reporting- specific**	N4-A Transparently Reported Product Impact
	19	Consumer Financial Protection	47	**Advertising- specific**	C1-B Truth in Advertising
			48	**Healthy community- specific**	S2-A Healthy, Safe, Resilient Community
	20	Privacy & Data Security	49	**Data security- specific**	C2-A Data Security
			50	**Customer privacy- specific**	C2-B Customer Privacy
			51	**Goverance reporting- specific**	F2-B Governance Reporting
	21	Product Safety & Quality	52	**Customer health- specific**	C3-B Customer Health & Safety
			53	**Advertising- specific**	C1-B Truth in Advertising
			54	**Partner impact reporting- specific**	P3-A Suppliers and Distributor Impact Reporting
	22	Responsible Investment	55	**Firm EVA- specific**	F3-A Positive EVA (Firm)/EVA (Industry) ratio
			56	**Shareholder EVA- specific**	SH1-A Positive EVA
			57	**Goverance reporting- specific**	F2-B Governance Reporting
	23	Community Relations	58	**Healthy community-specific**	S2-A Healthy, Safe, Resilient Community
			59	**Social reporting- specific**	S2-C Transparent Social Reporting
			60	**Partner impact reporting- specific**	P3-A Suppliers and Distributor Impact Reporting
	24	Controversial Sourcing	61	**Partner impact reporting- specific**	P3-A Suppliers and Distributor Impact Reporting
			62	**Fair labor in partner- specific**	P4-A Audited Fair labor practices throughout supply chain & distribution channels
			63	**Raw material Sourcing-specific**	N4-B Sustainable Sourcing of Raw Material

Pillar	No.	MSCI Key Issues	No.	Sub-Issues Identified	VM Goals Mapped
S	25	Access to Finance	64	**Healthy community-specific**	S2-A Healthy, Safe, Resilient Community
			65	**Goverance reporting- specific**	F2-B Governance Reporting
			66	**Charitable giving- specific**	S4-B Charitable giving
	26	Access to Health Care	67	**Healthy community- specific**	S2-A Healthy, Safe, Resilient Community
			68	**Local value chain- specific**	S3-D: Local Value Chains
			69	**Supporting partners- specific**	P2-A: Supporting MSMEs, VCSEs, MWOBEs, and/or SDVOBs through business partnerships
	27	Opportunities in Nutrition & Health	70	**Customer health- specific**	C3-B Customer Health & Safety
			71	**Goverance reporting- specific**	F2-B Governance Reporting
			72	**Healthy community-specific**	S2-A Healthy, Safe, Resilient Community
G	28	Board	73	**Goverance reporting- specific**	F2-B Governance Reporting
			74	**Board composition- specific**	F2-C Board Composition
			75	**Zero corruption- specific**	F2-E Zero Corruption
	29	Pay	76	**Goverance reporting- specific**	F2-B Governance Reporting
			77	**Shareholder EVA- specific**	SH1-A Positive EVA
			78	**Firm EVA- specific**	F3-A Positive EVA (Firm)/EVA (Industry) ratio
	30	Ownership & Control	79	**Shareholder EVA- specific**	SH1-A Positive EVA
			80	**Governance reporting- specific**	F2-B Governance Reporting
	31	Accounting	81	**Goverance reporting- specific**	F2-B Governance Reporting
			82	**Financial reporting-specific**	F1-A :Transparent reporting on financial performance
	32	Business Ethics	83	**Zero corruption- specific**	F2-E Zero Corruption
			84	**Government relationship- specific**	F1-B : Government relationship
			85	**Partner impact reporting- specific**	P3-A: Suppliers and Distributor Impact Reporting
	33	Tax Transparency	86	**Government relationship- specific**	F1-B Government relationship
			87	**Tax reporting- specific**	S1-A Transparent tax reporting
			88	**Tax paid- specific**	S1-B Appropriate Taxes Paid

*For more detailed information on Value Model, please visit our Value Research Center Website: https://www.valueresearchcenter.com/value-mode