NEWS RELEASE

EULER HERMES

Euler Hermes becomes first credit insurer to include ESG risks into its country risk ratings

Euler Hermes country risk rating methodology now includes ESG-related risks of non-payments by companies, especially environmental vulnerabilities and rising societal risks.

PARIS, 28 January 2020 – Environmental, Social and Governance (ESG) issues have reached a tipping point in the global economy: for companies and investors, it is now clear that these issues will impact growth, market share and profitability. For non-payment risk, the correlation between non-payments and severe climate-related events (supply chain interruptions), or between insolvencies and social unrests (looting, profit loss) are increasing over time. New payment risks could come from more difficult access to financing for companies with higher carbon footprint or with assets at risk of stranding because of regulatory decisions.

In this context, Euler Hermes decided to augment its country ratings with a set of indicators related to environmental sustainability on the one hand (E-block); and to add sentiment analysis crawling from social media in its political risk rating on the other (S-block). Governance issues (G-block) such as the regulatory and legal frameworks and control of corruption have already been included in the country ratings since 2003. Hence, Euler Hermes is the first trade insurance company to include ESG indicators for all ESG-related issues into its rating methodology.

What does it change in the methodology?

The Euler Hermes country risk rating methodology measures the risk of non-payment by a company in a given country due to conditions or events outside its control. It is composed of three medium-term components which measure macroeconomic imbalances, political risk and the Structural Business Environment (SBE); and two additional short-term components (Cyclical Risk Indicator, and Financing Flow Indicator) allow analysts to detect recessions and balance of payment crises. The rating includes more than 140 indicators and is available for 194 countries.

The SBE component (which includes Ease of Doing Business and Control of Corruption indicators for instance) will now be complemented by 6 indicators assessing environmental sustainability:

1. Energy use per GDP: kg of oil equivalent per USD1,000 GDP, constant 2011 PPP
2. Renewable electricity output: share of total electricity output
3. CO2 emissions per GDP: kg per 2011 PPP USD of GDP
4. Water stress : annual freshwater withdrawal as a proportion of available freshwater resources
5. Recycling rate: share of total waste
6. Climate change vulnerability: people affected by climate-related disasters, per 100,000 population, 5-year average

The political risk component will include sentiment analysis from social media. It uses proprietary data science algorithms applied to large data sets from crawling social networks. They help capture risks of social unrests as recently field-proofed in the Middle East and Latin America. The methodology already included, since the Arab Springs, a series of indicators aiming at measuring pervasive inequalities, and social immobility.

"*Our new country risk rating methodology aims to capture the vulnerabilities related to climate change and social unrests on companies, which could face higher costs of financing and disrupted supply chains, and business interruption. Small island developing states, countries with a carbonated energy mix, or countries where floods risks are high are on the watch list for* *their impact on B2B trade. These exogenous shocks are often a blind post for providers who do not think of extending their due diligence on their clients to include these risks of non-payment. In the future, as awareness increases, I would not be surprised that some countries exhibit lower nonpayment risks thanks to successful adaptation policies.",* said **Ludovic Subran, Chief Economist of the Allianz Group and Euler Hermes Group.**

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