

## Global Economic Policy Lab

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# Environmental, Social, and Governance Ratings Across the TSX Top 50

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- Investments guided by Environmental, Social, and Governance considerations grew from CAD\$2.1T in 2017 to CAD\$3.2T in 2019.
- The proportion of S&P 500 firms reporting ESG data rose to 90% in the last decade, along with over 600 ESG ranking and ratings systems globally.
- Across the top 50 largest firms on the Toronto Stock Exchange, there is significant heterogeneity in the ESG evaluations of four industry-leading ratings providers.
- An international ESG ratings standard which provides a growing investor base with comparable data is essential to channel capital to the highest performing sustainable companies.

## Background

### The Growth in Sustainable Investing

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Sustainable investing, often used as a synonym for responsible investing, impact investing, or social investing, is a newer investment thesis that is quickly gaining traction across both the public and private sectors. It [refers to investment strategies](#) that consider environmental, social, and governance [“ESG”] issues as part of the comprehensive investment decision-making process. Specifically, investors utilising these strategies target companies and projects with sustainable and transparent ESG performance.

The growth of this investment type in the private sector has been meteoric, especially in Canada. A [2020 report by the Responsible Investment Association of Canada](#) found that sustainable investing grew in Canada from CAD\$2.1T in 2017 to CAD\$3.2T in 2019. The same organization also released a more [recent report](#) detailing how the COVID-19 pandemic has poised this investment sector for accelerated future growth. Similarly, the Global Impact Investing Network presented a [report in 2020](#) detailing how impact investing will flourish in the wake of the pandemic as investors focus on establishing more sustainable, resilient portfolios.

Several institutional investors drive rapid growth in this space. Blackrock [committed to net-zero investing by 2050](#), and recently completed its [goal of ESG integrating 100% of its active portfolios](#). The OTPP similarly [committed to net-zero investing by 2050](#), and the New York State Pension Fund set an even more ambitious [target of achieving net-zero investing by 2040](#). Finally, a coalition of 30 leading global asset managers recently announced the [Net Zero Asset Managers Initiative](#) - pledging to align USD\$9T of managed assets with net-zero targets by 2050 or sooner.

Canada’s public sector is also an active participant in this growth, seeking to use it to its advantage as much as possible. The [Government of Canada’s 2019 Expert Panel on Sustainable Finance](#) outlined the growth opportunities for sustainable investing in Canada, how the government could support this growth, and, in turn, how this investment sector can support Canada’s economy. Additionally, Canada’s pandemic recovery focused [Build Back Better](#) plan places a heavy emphasis on ensuring all government investments contribute to establishing a more socially inclusive and environmentally friendly economy.

These commitments and initiatives, spanning both the public and private sectors indicate that sustainable investing is the new long-term focus for many investment managers. This has resulted in the rapid development and expansion of metrics to help investors evaluate ESG performance when making investment decisions.

## The Explosion in ESG Rating Systems

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As sustainable investing has grown, and with it the need for better data to facilitate these investments, there has been an explosion in the number of available ESG rating systems. The proportion of S&P 500 firms releasing ESG performance data rose from 20% in 2011 to 90% in 2019. The scope and contents of these reports also dramatically increased according to the [Governance and Accountability Institute](#). As of 2018, [there were more than 600 ESG rating and ranking systems globally](#). This rapid growth in ESG data and reporting, combined with investor appetite for sustainability, influence corporate reporting and disclosure and led to the creation of ESG-focused investment products. Ultimately, these ESG reporting metrics have had a large impact on the public perception surrounding corporate objectives and performance.

### ***Are all ESG Rating Systems Made Equal?***

ESG ratings and rankings [guide and inform sustainable investment decisions](#). However, the methodologies, data points, and scopes used to inform these ratings [vary greatly by provider](#). As a result, the ESG ratings landscape is highly heterogeneous. Though the frequency with which they are being used to evaluate companies is increasing, inconsistent methodologies [result in dramatically different investment portfolios](#) depending on which ESG provider investors use to guide their decisions.

We explore how ESG providers evaluate publicly traded Canadian companies. Specifically, we detail the variance between corporate ESG ratings in Canada. This is critical to understand whether objective performance measures or contrasting methodologies guide sustainable investments.

## Comparing ESG Ratings in Canada

### The Companies

We analyse the ESG ratings of the [50 largest companies, by market capitalization, listed on the Toronto Stock Exchange \["TSX"\]](#).

### ESG Ratings Providers

Our analysis examines ESG ratings published by broadly applicable and available providers. A [report by Research Affiliates](#) classified ESG providers as either being fundamental, specialist, or comprehensive. We focus on four prominent providers of comprehensive ESG ratings: [Sustainalytics](#), [MSCI](#), [Refinitiv](#), and [S&P Global](#).

Table 1. ESG Providers   Summary Information				
Provider	Coverage	Scale	Methodology	Data Sources
Sustainalytics	6,500 companies	Risk Score ranging from 0 to > 40+	Key ESG issues split into 3 themes (environmental, social & governance) Set of analyzed issues varies by industry At least 70 indicators in each industry <b>Split into 3 categories: preparedness, disclosure and performance</b>	CO2 emissions Company Reporting Third Party Research Government databases Company disclosures
		0 to 10: Negligible risk 10 to 20: Low risk 20 to 30: Medium risk 30 to 40: High risk >40: Severe risk		
MSCI	6,000 companies & 400,000 equity & fixed income securities	AAA-CCC Scale: CCC,B: Laggard BBB, BBB, A: Average AA, AAA: Leader	<b>37 ESG key issues, divided into 3 pillars (environmental, social, governance) and 10 themes:</b> Climate change, natural resources, pollution & waste, environmental opportunities, human capital, product liability, stakeholder opposition, social opportunities, corporate governance, corporate behavior	Macro data at segment or geographical level from academic, government and NGO databases
Refinitiv	9,000 companies	Point Score out of 100 across 4 quartiles: 0-25 Poor 25-50 Satisfactory 50-75 Good 75-100 Excellent	<b>More than 500 ESG metrics across 10 main themes:</b> emissions, environmental production innovation, resource use, workforce, human rights, community, product responsibility, management, stakeholders, CSR strategy	Annual Reports, Company Websites, NGO Websites, Stock Exchange filings, CSR reports, News Sources
S&P Global	7,300 companies	Point Score out of 100 across 4 quartiles: 0-25 Poor 25-50 Satisfactory 50-75 Good 75-100 Excellent	<b>Weighted Criteria Score for each of 3 criteria (social, environmental &amp; governance)</b> resulting from 1,000 data points from assessed values, text, checkboxes, documents	Survey Questions: 100-question exploration guided by 61 industry-specific approaches for each criteria score  Publicly Available Data

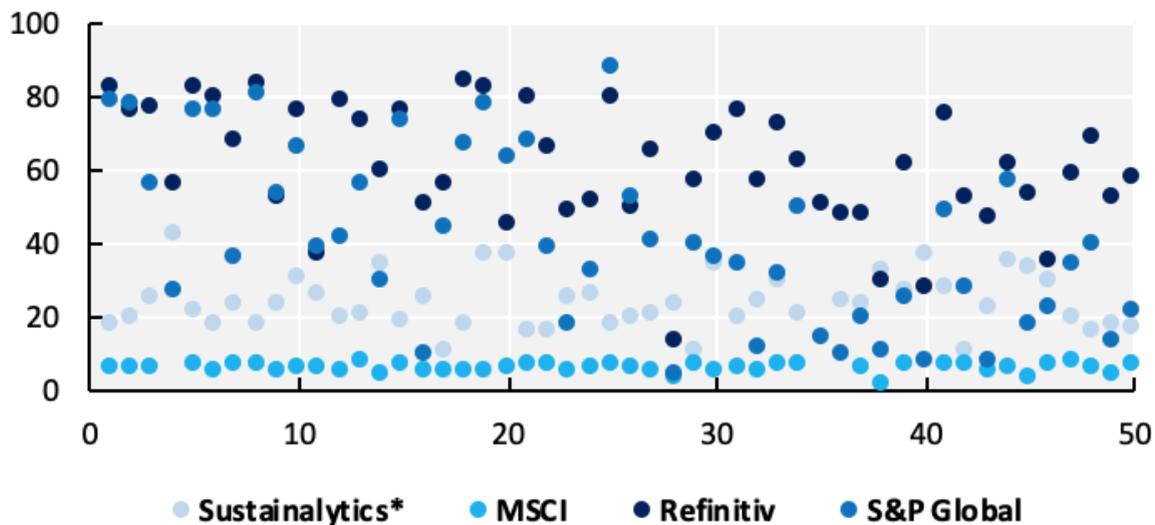
These ratings differ across 4 key dimensions: Coverage, Rating Scale, Methodology and Data Sources. Table 1 summarizes the key differences between the providers analysed in this report.

## Analysis

### Distribution of ESG Scores

Figure 1 illustrates the distribution of raw ESG scores across our sample.

**Figure 1. Raw ESG Score Across Providers**



Source: providers listed, GEPL calculations

Unsurprisingly, the spread in raw score ratings is sizable but is not indicative of the true variance between each company's ratings. Inconsistent ratings methodologies make any attempt to compare the ratings imprecise.

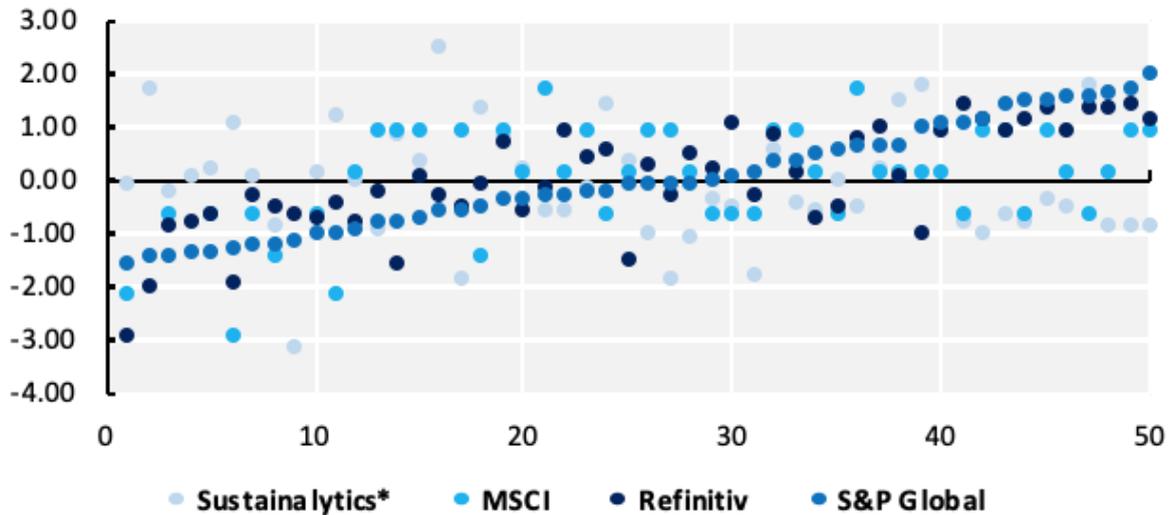
As a result, we calculated z-scores to normalize and compare our findings. This facilitated more detailed analysis. Readers should note that we converted MSCI's alphabetical scale to a 7-point range to perform these calculations. We summarise this normalization in Table 2 and illustrated the ratings spread in Figure 2 for all fifty companies.

Table 2. Summary Statistics ESG Providers   TSX50					
Raw	Sustainalytics*	MSCI	Reuters Refinitiv	S&P Global	
Mean	23.1	4.8	60.3	40.2	
Standard Dev	7.4	1.3	16.4	23.6	
Min	9.4	1	12	3	
Max	41.7	7	84	87	
Spread	<b>32.3</b>	<b>6</b>	<b>72</b>	<b>84</b>	
Normalized					
Min	-3.11	-2.94	-2.95	-1.58	
Max	2.51	1.68	1.45	1.99	
Spread	<b>5.63</b>	<b>4.62</b>	<b>4.40</b>	<b>3.56</b>	

\* Sustainalytics ratings reversed high/low ESG level

Source: providers listed, GEPL calculations

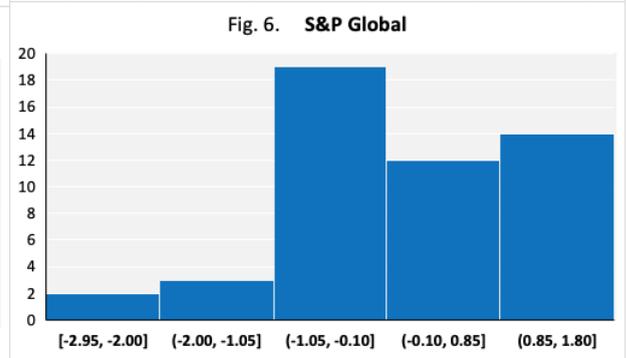
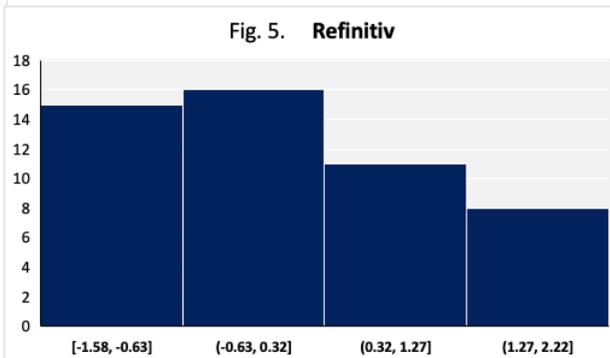
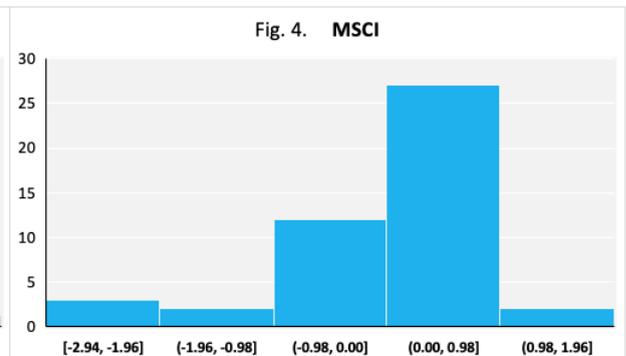
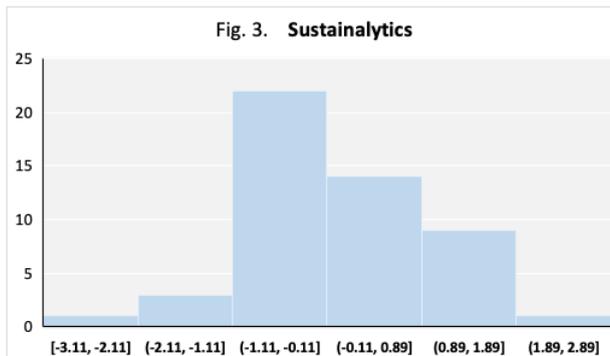
Figure 2. Normalized ESG Score Across Providers



Source: providers listed, GEPL calculations

This normalization showed that each provider’s rating system has a spread of several standard deviations - with Sustainalytics having the largest range while S&P Global presents the most compact distribution. Further, the normalization revealed that MSCI and Refinitiv have the most comparable rating systems.

**ESG Normalized Score Histograms**



Source: providers listed, GEPL calculations

Figures 3-6 display histograms for each provider's normalised ratings, demonstrating that the distributions are not similar and that each has a significant, unique skew. For example, the S&P Global rating system has a significant right-tail while Sustainalytics has a heavy rightward skew. The lack of uniformity in these distributions indicates the reality that there is little consensus among ESG ratings. A company ranked highly by one provider may not necessarily be viewed favourably by another, and vice versa. Assuming that firms truthfully provide performance data and metrics to each provider, this becomes problematic for investors. Though each provider's unique methodology could explain variability, this drives investor uncertainty around objective ESG performance for each company.

**Comparing High and Low Performers**

Table 3. ESG Score Across Providers Top 10/Bottom 10   TSX50 Company				
ESG Rank	Sustainalytics	MSCI	Refinitiv	S&P Global
1	Wheaton Precious Metals	Manulife Financial Corporation	Canadian Pacific Railway	Telus Corporation
2	Franco-Nevada Corporation	Molson Coors Canada	Bank of Montreal	Bank of Montreal
3	Thomson Reuters Corporation	George Weston	Barrick Gold Corporation	Royal Bank of Canada
4	Open Text Corporation	Fortis	Royal Bank of Canada	Toronto - Dominion Bank
5	Sun Life Financial	Agnico Eagle Mines	Bank of Nova Scotia	Barrick Gold Corporation
6	Rogers Communications	Intact Financial Corporation	Canadian National Railway Company	Canadian National Railway Company
7	Hydro One	Brookfield Asset Management	Telus Corporation	Bank of Nova Scotia
8	Bank of Montreal	Bank of Nova Scotia	Sun Life Financial	Canadian Imperial Bank of Commerce
9	Royal Bank of Canada	National Bank of Canada	BCE (Bell Canada Enterprises)	Sun Life Financial
10	Telus Corporation	Canadian Imperial Bank of Commerce	Enbridge	Canadian Pacific Railway
50	CNOOC Limited	Fairfax Financial Holdings	Constellation Software	Constellation Software
49	Nutrien	Saputo	Brookfield Infrastructure Partners	Brookfield Infrastructure Partners
48	Barrick Gold Corporation	Constellation Software	Fairfax Financial Holdings	Brookfield Renewable Partners
47	Brookfield Infrastructure Partners	Canadian Natural Resources	George Weston	Brookfield Property Partners
46	Cenovus Energy	Shaw Communications	Shopify	Alimentation Couche-Tard
45	Imperial Oil	Barrick Gold Corporation	Nutrien	Fairfax Financial Holdings
44	Canadian Natural Resources	Imperial Oil	Brookfield Renewable Partners	Restaurant Brands International
43	Saputo	Alimentation Couche-Tard	Magna International	Shaw Communications
42	Fairfax Financial Holdings	Waste Connections	Brookfield Property Partners	Power Financial Corporation
41	Suncor Energy	Restaurant Brands International	Waste Connections	Waste Connections

Table 4. ESG Score Across Providers Top 10/Bottom 10   TSX50 Industry				
ESG Rank	Sustainalytics	MSCI	Refinitiv	S&P Global
1	Precious Metals	Insurance	Transportation	Telecommunications
2	Precious Metals	Beverages	Bank	Bank
3	Professional Services	Food Products	Precious Metals	Bank
4	IT Services	Utilities	Bank	Bank
5	Insurance	Precious Metals	Bank	Precious Metals
6	Telecommunications	Insurance	Transportation	Transportation
7	Utilities	Financial Services	Telecommunications	Bank
8	Bank	Bank	Insurance	Bank
9	Bank	Bank	Telecommunications	Insurance
10	Telecommunications	Bank	Oil & Gas	Transportation
50	Oil & Gas	Insurance	IT Services	IT Services
49	Chemicals	Food Products	Utilities	Utilities
48	Precious Metals	IT Services	Insurance	Utilities
47	Utilities	Oil & Gas	Food Products	Real Estate
46	Oil & Gas	Entertainment	IT Services	Retail
45	Oil & Gas	Precious Metals	Chemicals	Insurance
44	Oil & Gas	Oil & Gas	Utilities	Restaurants & Leisure
43	Food Products	Retail	Automobiles	Entertainment
42	Insurance	Commercial Services	Real Estate	Financial Services
41	Oil & Gas	Restaurants & Leisure	Commercial Services	Commercial Services

\* Sustainalytics ratings reversed high/low ESG level  
Source: providers listed, GEPL calculations

Looking deeper at how each provider ranks the highest and lowest performing TSX companies, Tables 3 and 4 show further discontinuity. There is no single observation that appears in either category for all four providers at the company level. Some companies make it into three of the lists, but it is impossible to create a definitive list of high or low performers across ESG providers. Table 4 compares industry level performance in our sample to show some trends. Banks perform very well, frequently landing in the top 10 ESG rated

companies regardless of the provider. As expected, oil and gas companies dominate the bottom quintile of ESG rated companies in our sample across providers. While examining ESG scores by industry group does demonstrate some high-level consensus between ESG providers, it remains clear that these providers do not arriving at uniform ratings.

### Correlation Coefficients

**Table 5. Cross-Correlation Matrices**

<b>Raw Scores</b>				
	Sustainalytics	MSCI	Refinitiv	S&P Global
Sustainalytics	1.00	-0.34	-0.26	-0.20
MSCI		1.00	0.42	0.40
Refinitiv			1.00	0.75
S&P Global				1.00

<b>Standardized Scores</b>				
	Sustainalytics	MSCI	Refinitiv	S&P Global
Sustainalytics	1.00	0.02	-0.26	-0.20
MSCI		1.00	0.42	0.40
Refinitiv			1.00	0.75
S&P Global				1.00

Source: providers listed, GEPL calculations

To further our comparison between ESG raters, we built cross-correlation matrices between both raw and standardised scores across the four studied rating systems. A score of 1 signals perfect positive correlation, -1 signals perfect negative correlation, and 0 signals no correlation. We conclude that the difference between raw and standardised scores do not change the observed relationship between the four raters given that the coefficient remains static.

Furthermore, in line with our earlier analysis, S&P Global and Refinitiv are closely positively correlated with a score of 0.75. Similarly, A negative relationship exists between Sustainalytics, Refinitiv, and S&P global. More interestingly, these scores are not highly correlated, with values between -0.26 and -0.20. The score of 0.02 between Sustainalytics and MSCI demonstrate virtually no correlation, indicative of incoherence between ratings systems. MSCI's relationship with Refinitiv and S&P Global shares a modest positive correlation.

## Conclusion

### Improving the ESG Landscape

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Ultimately, our analysis shows no agreement or convergence between the ESG ratings of the TSX top 50. Both a lack of uniformity and correlation indicates an immaturity and incoherence in information available to a growing sustainable investment base. We conclude that investors who base their decisions on ESG information guide their portfolios by differential scoring methodologies rather than objective and comparable company ESG performance.

It is crucial to note that a lack of consensus surrounding sustainability, rather than technical inability or misconduct, drives investor uncertainty in this domain. Given these findings and the eminence of sustainable investing, we forward the imperative to create internationally accepted sustainability reporting standards inspired by the [Sustainability Accounting Standards Board](#). Such standards should become entrenched to the same degree as financial reporting conventions over several years. A more coherent ratings system will pioneer greater comparability, transparency, and precise decision-making. Doing so will ensure that capital flows to the most sustainable companies and encourage more ESG consciousness.

Overall, ESG rating systems are an essential source of information for millions of sustainable investors. However, there is still regulation necessary to ensure that investors can access high quality and comparable ESG data. Currently, it is clear that sustainable portfolios and investments are dictated not by consistent information and objective analysis, but instead by the rating systems an analyst or investor chooses to rely on. As sustainable investing continues to grow in popularity, work needs to be done to ensure that these investments are flowing to the right places.

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