



Thematic Engagement: 2024 Scope 3 Emissions

A FIXED INCOME & PRIVATE CAPITAL COLLABORATION | January 23, 2025

Stewardship is an important part of MetLife Investment Management's (MIM) sustainable investing efforts and it is an increasing area of focus for many of our clients. As an institutional asset manager, with asset class expertise across Fixed Income, Private Capital and Real Estate, our primary way to conduct stewardship is via engagement.

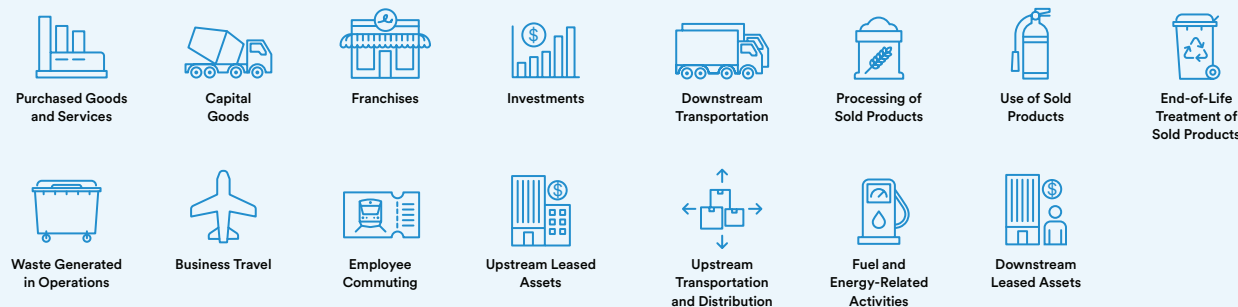
MIM conducts thematic engagements each year as part of our stewardship activity. For these engagements, we select a pertinent sustainability topic and engage with a range of issuers in different sectors and regions. Through our thematic engagements, we gain insights into the approaches being taken by issuers across the market and advocate for best practices.



Our 2024 thematic engagement focused on scope 3 greenhouse gas (GHG) emissions. This topic has risen in prominence in recent years because, in many sectors, scope 3 can account for the largest share of a company’s emissions.¹ Additionally, with new reporting requirements being introduced in places such as the EU, Japan, Australia and California, scope 3 emissions will be an increasingly relevant topic going forward. Issuers face significant obstacles in reporting on their scope 3 emissions as well as reducing them. Through our thematic engagement, we sought to obtain insights into how issuers across both Fixed Income and Private Capital are tackling scope 3 emissions with respect to data availability, reporting, target setting and emissions reductions.

Overview of scope 3 emissions

Scope 3 emissions are the indirect emissions that occur within a company’s upstream and downstream value chain, such as the emissions generated in the supply chain or from the use of the products a company sells. For example, for a car manufacturer, these emissions would include the fuel used to power the car once it has been sold to an operator, and the energy used to produce the materials used to make the car. The GHG Protocol’s Scope 3 Standard² defines 15 categories within scope 3 emissions (depicted below). It is crucial for issuers to understand and quantify these emissions in order to develop robust decarbonization strategies.



The data and reporting for Scope 3 are currently more variable than for scope 1 and 2, as it is more complex to accurately measure emissions across an entire value chain compared to one entity’s own operations. The uncertainty around scope 3 reporting figures means there is currently a general lack of confidence in setting scope 3 emissions reduction targets and adequately tracking progress against these. We were therefore interested in engaging with companies across public and private markets to understand the challenges and opportunities regarding scope 3 emissions.

In this thematic engagement, we engaged with a range of primarily investment-grade public and private debt issuers from different sectors and regions, with a focus on those for whom scope 3 emissions represent the largest share of emissions. These included issuers that have already reported their scope 3 emissions as well as those that are yet to do so, giving us insights from issuers at different stages of data collection and disclosure. Our engagements addressed a common set of scope 3 considerations, along with tailored questions for each issuer. The Sustainability Research teams at MIM engaged with 38 issuers³ during this thematic engagement, and a number of key insights were identified.

Access to GHG emissions data in supply chains varies significantly across sectors and regions

One of the central challenges in reporting scope 3 emissions is the level of data availability. Due to this, issuers tend to use a “hybrid approach,” which prioritizes data collected directly from their suppliers and customers where available, before supplementing this with estimates to fill any gaps. Estimations can rely on i) activity-based data — the more accurate option — which is based on the nature and scale of activities in the issuer’s value chain, such as the tons of steel it procured, or on ii) spend-based data, which is based on the amount being spent on different products and services, such as the total amount spent on steel procurement.

For upstream scope 3 emissions, several issuers we engaged with are able to collect at least some data directly from their suppliers. However, this data is not always used in the scope 3 calculations due to concerns around data quality. As a result, several issuers that we engaged with are setting up processes to validate their collected data, before including it in their scope 3 calculations.

The availability of direct data for scope 3 upstream calculations varies significantly across sectors. It is linked to factors including the complexity of an issuer’s supply chain, its regional distribution and the type of product/service it sells. Some sectors provide a detailed level of emissions-related data. For example, companies in the aviation sector must disclose substantial data on flight time, fuel use and passenger numbers. This makes it easier for issuers to account for flight-related emissions in their value chain. Other sectors have specific challenges for calculating scope 3 emissions. For example, companies in the food and agriculture sector can have highly dispersed supply chains with inputs coming from a large number of small suppliers. This makes it difficult to obtain direct data because smaller companies may not have the resources to prioritize GHG emissions reporting due to the number of entities that need to be accounted for.

Regional differences are another factor driving differences in scope 3 data availability. Issuers whose supply chains are concentrated in regions with stringent sustainability regulations tend to have better access to upstream emissions data. The differences between regions are expected to increase as the Corporate Sustainability Reporting Directive comes into force in the EU, and other reporting regulations are introduced in the U.S., Australia and Japan, but other regions remain at earlier stages. Therefore, while regulation is expected to drive improvements in data availability in some locations, issuers will need to be proactive in order to access data outside of these regions.

Issuers are driving improvements in data quality by engaging with their suppliers and utilizing industry initiatives and technology

Companies aim to source more data directly from suppliers and customers, which is the gold standard in scope 3 data. Expanding the availability of such data requires collaboration between the issuer and entities within its value chain. Some issuers that we engaged with use voluntary supplier surveys to obtain more direct data. Additionally, several now include data requirements in their supplier policies and procurement processes. While these requirements are not always mandatory, they can be a way of starting conversations with suppliers and understanding where to focus engagement efforts.

Knowledge sharing plays an important role in promoting better emissions disclosures from suppliers. This can address the challenges around resource constraints and lack of know-how. Certain issuers we engaged with are supporting their suppliers in measuring and reporting on scope 3 emissions through educational programmes, workshops or other events. These efforts increase issuers' access to robust data. Issuers noted that they see value-chain collaboration as an opportunity to get ahead on regulation, meet customer data requests and identify decarbonization opportunities.

When direct data is available from suppliers, issuers we engaged with highlighted that this needs to be assessed to ensure it has been calculated using an established methodology. However, some also noted that there can be room for flexibility in terms of what they require, with some data points being essential but others nice to have. This can be a way of obtaining sufficient data at a sooner date, rather than waiting for more advanced reporting further down the line if this is not crucial.

Industry initiatives are another factor driving improvements in data quality and availability. They provide guidance on emission reporting for specific value chains, creating synergies and cost efficiencies across issuers. For example, issuers in the financial sector benefit from established frameworks for calculating financed emissions, such as PCAF, as well as sector-specific frameworks like the Poseidon Principles.⁴ Other sectors have joined together to gain better disclosure, such as U.S. electric utilities with the Sustainable Supply Chain Alliance, which jointly surveys suppliers on behalf of the 27 alliance members.

Some issuers highlighted the benefit of newer technologies in improving their access to data, such as smart-metering systems for real estate firms. In addition, issuers with more advanced scope 3 estimation methodologies are exploring the use of new tools to enhance the accuracy of their estimation models in cases where direct data is not available. One example noted was the use of cameras and software to monitor the volume and type of transport being used at an issuer's sites.

Issuers are taking steps to reduce scope 3 emissions, especially in sectors and regions with increasing GHG emissions regulations

Many issuers we engaged with are taking action to reduce scope 3 emissions. Several issuers have set decarbonization targets covering their scope 3 emissions, while others are at earlier stages due to a lack of reporting or data quality issues. Nonetheless, it was encouraging to see that data limitations are not obstructing issuers from addressing their scope 3 emissions.

Leading issuers we engaged with highlighted that internal collaboration across departments is important for achieving scope 3 emissions reductions. Sustainability teams often need to work together with procurement, capital program teams, as well as product design teams and others to access relevant data and prioritize lower carbon inputs. Considering the complexity of scope 3 emissions, a holistic approach needs to be taken to reduce them. This inherently requires contributions from multiple areas across each organization.

To reduce upstream scope 3 emissions, some issuers have introduced responsible sourcing guidelines. Several have also established responsible sourcing teams to focus on greener materials and supplier engagement. Procuring very low-carbon products is not always straightforward, however, as they can entail green premiums, which may be hard to pass on to customers. Issuers highlighted a few ways to address this in the short term. These included working closely with the procurement team to place low-carbon products as a default within product/project specifications wherever possible, collaborating with other buyers to achieve economies of scale and targeting

the client segments with the greatest demand for green products. For the most challenging cases, issuers noted that regulation was likely to drive greater uptake of low-carbon products. One such example is the European Union's Carbon Border Adjustment Mechanism, due to come into effect in 2026, which will impact the price of carbon intensive inputs from affected sectors including iron and steel, cement, aluminium, fertilizers and electricity.⁵

Issuers are also using engagement as a tool to reduce supply chain emissions. Several issuers are asking suppliers to set science-based targets and to set out their decarbonization strategies. These engagements are met with a variety of reactions, largely determined by the maturity of each supplier's sustainability strategy. There is recognition from the issuers that, while progress is materializing, it will take time to see large-scale benefits from these engagements.

It is essential to acknowledge that scope 3 emissions are also impacted by external factors such as sector developments, economic cycles, regulations and customer demand for lower carbon products and services. As such, there must be an understanding that these emissions are unlikely to follow a linear reduction pathway. It is important for companies to take steps to measure and reduce their scope 3 emissions, but these actions must be assessed within the boundaries of what can be reasonably expected.

Conclusion

Scope 3 reporting is currently challenging for many companies for a variety of reasons. However, we found that all the issuers we engaged with are working to increase their access to data and ultimately to reduce their scope 3 emissions. Scope 3 is a topic of growing importance and through this engagement, we have identified a number of themes that will be particularly relevant going forward. Firstly, it is important for issuers to engage throughout the value chain and with industry initiatives in order to access scope 3 data and promote data availability. Further, collaboration within companies and between companies is critical for enhancing scope 3 data, disclosure and decarbonization. Thirdly, technology has significant potential to improve data availability and accuracy across a variety of sectors. Regulation is a key factor that is increasing reporting standards, but this is not the case for all regions, and issuers will need to be proactive to obtain broad scope 3 data coverage. Finally, there is a continued commitment from many issuers to measure, report and reduce their scope 3 emissions, and it will be important to monitor how these efforts materialize.

Future of Reporting



Engagement

Engagement with suppliers, customers and industry initiatives is key to enhancing scope 3 data availability and quality.



Collaboration

Collaboration both within and between companies is critical for measuring and reducing scope 3 emissions.



Technology

Technology is expected to make scope 3 calculations more accurate and efficient in many sectors.



Regulatory

Regulatory developments will drive data improvements in some locations, but others are further behind.



Commitment

Many issuers remain committed to enhancing their scope 3 reporting and reducing these emissions.

Endnotes

¹ https://cdn.cdp.net/cdp-production/cms/guidance_docs/pdfs/000/003/504/original/CDP-technical-note-scope-3-relevance-by-sector.pdf?1649687608

² <https://ghgprotocol.org/corporate-value-chain-scope-3-standard>

³ Of these engagements, 18 took place via virtual meetings and 20 were via email.

⁴ <https://www.poseidonprinciples.org/finance/>

⁵ EU carbon border adjustment mechanism

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² Source: Pensions & Investments Managers Ranked by Total Worldwide Institutional Assets Under Management as of December 31, 2023.

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