

Climate and sustainability benchmarks and their contribution to compliance with Sustainable Development Goals

María José Gómez Yubero
Bárbara Gullón Ojesto (*)

(*) María José Gómez Yubero and Bárbara Gullón Ojesto work in the General Directorate of Policy and International Affairs of the CNMV. The opinions contained in this article are the sole responsibility of its authors and do not necessarily reflect those of the CNMV. The authors wish to thank Jorge Medina Sánchez-Seco, Paloma Cachón Domínguez and Jesús Cuéllar Escudero for their valuable collaboration.

Table of contents

Acronyms used	5
Summary	7
1 Introduction	9
2 Sustainable development: evolution and context	10
3 The role of benchmarks	11
4 Regulation of climate and sustainability benchmarks	14
4.1 New types of climate benchmarks	16
4.2 New disclosure obligations	19
4.2.1 ESG factors and how they should be published	19
4.2.2 Transparency of the methodology	22
4.3 Issues that require clarification or improvement	23
5 ESG ratings: a necessary base for consolidating sustainable benchmarks	24
5.1 Vulnerabilities and risks of the ESG ratings market	24
5.2 Proposed measures to build confidence in ESG ratings	25
6 Relationship between investment products and climate and sustainability benchmarks	26
6.1 The Sustainable Finance Disclosure Regulation	27
6.2 Indices used by sustainable investment funds registered with the CNMV	31
6.3 Comparative analysis of the performance of traditional indices and climate and sustainability benchmarks	32
7 Conclusions	35
References and bibliography	36

Tables

Table 1	Key dates for the implementation of the Climate and Sustainability Benchmark Regulation	16
Table 2	Similarities and differences between PA and CT benchmarks	17
Table 3	Number of mandatory disclosure ESG factors for each type of underlying asset	20
Table 4	Mandatory disclosure of ESG factors according to the type of benchmark asset	21
Table 5	ESMA recommendations on the regulation of ESG ratings	26

Table 6	Product classification under the SFDR	27
Table 7	Transparency obligations for financial products with a designated benchmark	30
Table 8	Accumulated returns at 1, 2 and 3 years of the Ibex 35, FTSE 4Good Ibex, HDAX, Dax 50 ESG, Eurostoxx 50 and Eurostoxx-ESG Leaders 50 indices	34

Figures

Figure 1	Number of sustainable investment funds registered with the CNMV based on the type of index used as a benchmark	31
Figure 2	Comparative performance of the Ibex 35 and the FTSE 4Good Ibex in the period from January 2018 to July 2021	33
Figure 3	Comparative performance of the HDAX index and the Dax 50 ESG in the period from January 2018 to July 2021	33
Figure 4	Comparative performance of the Eurostoxx 50 index and the Eurostoxx-ESG Leaders 50 in the period from January 2018 to July 2021	34

Exhibits

Exhibit 1	Statement and methodology	19
-----------	---------------------------	----

Illustrations

Illustration 1	Role of climate and sustainability benchmarks	13
----------------	---	----

Acronyms used

Acronyms	Meaning
ESG	Environmental, social and governance
BMR	Benchmark Regulation – Regulation (EU) 2016/1011 of the European Parliament and of the Council, of 8 June 2016, on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds.
CNMV	Comisión Nacional del Mercado de Valores (Spanish National Securities Market Commission)
CSRD	Corporate Sustainability Reporting Directive
OTC derivatives	Over-the-counter derivatives
ESMA	European Securities and Markets Authority
ETF	Exchange Traded Fund
EUR	Euro
GHG	Greenhouse gases
IIA	Index Industry Association
CIS	Collective investment scheme
PA benchmarks	EU benchmarks aligned with the Paris Agreement
CT benchmarks	EU climate transition benchmarks
IR and FX benchmarks	Interest rate and foreign exchange benchmarks
IOSCO	International Organization of Securities Commissions
IPCC	Intergovernmental Panel on Climate Change
ISDA	International Swaps and Derivatives Association
Libor	London InterBank Offered Rate
SMEs	Small- and medium-sized enterprises
EGD	European Green Deal
SFDR	Sustainable Finance Disclosure Regulation – Regulation (EU) 2019/2088 of the European Parliament and of the Council, of 27 November 2019, on sustainability-related disclosures in the financial services sector
TEG	EU Technical Expert Group on Sustainable Finance
EU	European Union

We will all know that there is only one path and that is the path of change. Change in human behaviour, as we are the last link in the evolution of living beings on our planet, in other words, change in the awareness of human beings.

Félix Rodríguez de la Fuente¹

Summary

Benchmarks are tools that are increasingly used to build investment strategies and measure and monitor their performance. This means that they have a clear role to play in the transition to a low-carbon economy that is aligned with the Sustainable Development Goals.

The recent regulation of climate and sustainability benchmarks recognises this role and is a first step in the European Union (EU) effort to increase their number and use to achieve these objectives.

Improvements in the information provided by companies that make up, or may in the future make up, the benchmarks and the availability of reliable, easily accessible and comparable data sources are measures that will improve their effectiveness as a catalyst for the mobilisation of financial resources towards a more sustainable economy.

1 Inaugural speech at Montejo de la Vera camp in 1975. This quote is taken from the book Rodríguez de la Fuente (2020). Félix Rodríguez de la Fuente is a key figure in our understanding of the changes in environmental awareness that have taken place in Spain since the last third of the 20th century. His written and audiovisual work has contributed decisively to raising awareness among several generations of Spaniards of the need to care for the environment and the land we live on. The 40th anniversary of his death took place during the lockdown caused by the COVID-19 pandemic.

1 Introduction

Sustainability and sustainable financing are setting the agenda for regulators and supervisors, and also for corporations, financial institutions, advisers, managers, investors and people in general.

Sustainable global investment has gained a great deal of traction in recent years, with estimates placing the total value of assets pursuing sustainable investment strategies at €45 trillion in 2020,² double the figure seen in 2016.

The desire for sustainability, a concept that permeates all aspects of life today, responds to an institutional drive and social demand and to investors themselves, who are increasingly seeking sustainable investment products. Climate and sustainability benchmarks,³ which have recently been regulated in the EU, have been called upon to play a pivotal role in promoting what has come to be known as “sustainable finance”, whose objective is to redirect capital flows into investments that allow more sustainable growth to be achieved. Ultimately, it is about the financial system supporting the EU’s climate and sustainable development agenda.

The benchmarks with objectives that include reducing the carbon footprint or even those that simply consider sustainability factors, be they environmental, social or governance (ESG factors), which offer sustainable investments by creating (individual and group) portfolios, are an incentive for companies to commit to decarbonisation and include sustainability factors in their strategy and business models, and also to improve their transparency. Ultimately, these indices help redirect funds towards a sustainable economy and avoid the risk of greenwashing⁴ or the misleading use of a “green” or “sustainable” label in the marketing of products.

This article analyses the evolution and context of raising awareness and subsequent regulation of sustainability objectives and the role played by benchmarks to achieve these goals.

2 ESMA (2021a).

3 This article broadly refers to sustainability benchmarks as those indices that consider ESG factors or pursue ESG objectives.

4 A term generally known as “ecobleaching” or “greenwashing”.

2 Sustainable development: evolution and context

There has been an awareness of the need to take care of the planet since Roman times.⁵ However, experts consider the 1972 Stockholm Conference and, more particularly, the Brundtland Report⁶ of 1987 to be the main developments⁷ that culminated in the definitive Paris Agreement⁸ of December 2015, when the Member States of the United Nations approved the 17 goals and 169 targets for sustainable development, committing to achieving them by 2030.

The European Union has taken decisive steps in its strategy to finance the transition to a sustainable economy. In 2018, it launched a first action plan⁹ with three priority objectives: i) redirect capital flows into investments that permit more sustainable and inclusive growth,¹⁰ ii) manage the financial risks deriving from climate change, and iii) promote transparency and long-term vision in financial and economic activities.

The implementation measures include the creation of a common taxonomy to identify economic activities that help mitigate climate change, guidelines for companies when they report on the impact of their businesses on the climate and the impact of climate change on their businesses, and a new category of low-carbon benchmarks.

The European Union strategy has been stepped up recently with new initiatives to increase investment and include small- and medium-sized enterprises in the EU transition to a sustainable economy.¹¹ The new measures aim to extend the EU Ecolabel to financial products and create new labels for ESG benchmarks, as well as to improve the transparency of credit ratings and regulate ESG-related ratings (see Section 5).

5 The work of Bravo-Bosh (2014) offers extensive references to the norms of ancient Rome, demonstrating that sensitivity to environment issues already existed at that time.

6 This report pinpoints environmental protection as a global task and defines sustainable development as development that meets the needs of the present without compromising the ability of future generations to meet their own needs. It revolves around three main lines: environmental, social and economic sustainability, and links reducing poverty with the protection and preservation of the environment. World Commission on Environment and Development. United Nations (1987).

7 At the 1992 Earth Summit in Rio de Janeiro and the 2002 Johannesburg Summit.

8 The Paris Agreement of 2015 is a legally binding international treaty on climate change. It was implemented by 196 countries on 12 December 2015 and entered into force on 4 November 2016. Its purpose is to strengthen the global response to the threat of climate change in the context of sustainable development and efforts to eradicate poverty. To do this, the aim is to reduce global warming to 1.5 C (setting the limit at 2°C) above pre-industrial levels and the secure the commitment of the countries signing the agreement to decarbonise their economies and reduce their greenhouse gas emissions with the goal of obtaining climate neutrality by 2050. At the same time, it seeks to bring financial flows to a level that is compatible with a path that leads to climate-resilient development with low greenhouse gas emissions. United Nations (2015).

Spain signed the Paris Agreement on 22 April 2016 and it was published in the Official State Gazette (BOE) of 2 February 2017.

9 European Commission (2018).

10 The Plan contemplates the movement of more than €1 billion into sustainable investments in the next decade and to cease financing certain projects linked to fossil fuels.

11 The new EU strategy was published in July 2021 to step up and accelerate the completion of the 2019 European Green Deal objectives and recover from the COVID-19 pandemic. European Commission (2021).

In response to the commitments undertaken with the EU and under the Paris Agreement, in November 2020, the long-term strategy on climate neutrality was adopted in Spain,¹² and the Climate Change and Energy Transition Law was approved.¹³ In line with the decarbonisation and prevention of global warming objectives, this regulation establishes a series of measures and goals to achieve climate neutrality in 2050, driving the transition of energy towards a more efficient model based on renewable sources. The law also addresses the consideration of climate risks by companies and financial institutions and their monitoring by financial supervisors.

In this context, considering that the securities markets have an important role to play in the transition to more sustainable and inclusive growth, the CNMV has also taken on a commitment to sustainable finance both as an organisation and in the exercise of its powers. Sustainability is one of the strategic lines that will guide the CNMV's activity in the coming years.¹⁴ Among its goals, the authority will work towards the creation of climate benchmarks based on the carbon footprint, in line with recent regulation on this topic.¹⁵

3 The role of benchmarks

Market indices, better known as benchmarks, are a numerical indicator that is calculated based on the value of one or more underlying assets or prices to measure and monitor the evolution of an economy or a financial market.

Benchmarks are calculated using economic data, such as share prices, and non-economic figures or values, such as atmospheric or consumption parameters. They have multiple uses, most notably the pricing of cross-border transactions, as well as a wide range of financial instruments and services. They are also used to establish the value of financial instruments or contracts and to measure the performance of funds or investment portfolios.

Benchmarks belong to an area of the financial sector that has been the subject of regulatory attention recently, moving from a sector with relatively little financial regulation or supervision to a regulated area due to its systemic nature and its importance for consumer and investor protection, given that there are a great many index-referenced financial instruments, services and contracts available. These include mortgages, consumer loans, investment funds and other instruments marketed to retail investors. Therefore, it is necessary for any potential conflicts that may arise to be duly addressed and that the governance and calculation methodology of the index must respond to the principles of independence, control and transparency.

12 Government of Spain (2020).

13 Law 7/2021 of 20 May on climate change and energy transition.

14 This is included in the CNMV's Activity Plan for 2021-2022. CNMV (2021c).

15 The new Article 19 quinquies of Regulation (EU) 2016/1011 (introduced by Regulation (EU) 2019/2089, of 27 November) calls on the administrators of the main benchmarks to work to provide EU climate transition benchmarks by 1 January 2022.

Benchmarks have also developed a systemic dimension, mainly in the case of the most well-known and widely used interest rate benchmarks, such as Libor and Euribor,¹⁶ due to the crucial role they play in the economy and the financial system. Thus, regulation and supervision activities are also aimed at preserving financial stability.

For all these reasons, benchmark rates are currently being broadly reformed, largely due to the implementation of EU Benchmark Regulation published in 2016, which entered into force in January 2018.¹⁷

Benchmarks allow investment strategies to be aligned with preset targets and can also be used as a reference to measure the performance of these strategies in terms of risk and return. This gives them a clear role to play in the alignment of the asset management industry with long-term sustainability considerations and the transition to a low-carbon economy.

In recognition of this role, more recently, in December 2019, an amendment to the Benchmark Regulation was published through Regulation 2019/2089,¹⁸ which creates two new index labels that factor in the carbon footprint of the constituent assets and at the same time improve and harmonise the transparency of ESG goals and factors in the methodology of the indices they use or that pursue objectives related to these factors.

Climate and sustainability indices are used for sustainable investment both through passive management – including index funds and ETFs – and in active investment strategies.

These indices are usually built on a parent index or an investable universe of securities,¹⁹ while maintaining risk-return characteristics similar to those of the parent index. In this way, the performance of the global portfolio can be compared with that of the index that includes extra-financial aspects.²⁰

In its construction, an exclusion methodology can be applied that allows investors to eliminate certain types of exposures. Exclusions may include companies that are deemed not to meet certain ESG standards or companies engaged in activities that involve controversial weapons, tobacco, or fossil fuels. These indices can also be constructed to gain exposure to high ESG ratings, either jointly or separately, in relation to a specific ESG factor or theme, or to generate positive environmental or social impact. They can also combine elements of these approaches.

16 These indices are currently undergoing a historical reform, the status, origin and implications of which are analysed by Gómez-Yubero and Palomero (2021).

17 Regulation (EU) 2016/1011 of the European Parliament and of the Council, of 8 June 2016, on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds and amending Directives 2008/48/EC and 2014/17/EU and Regulation (EU) No. 596/2014.

18 Regulation (EU) 2019/2089 of the European Parliament and of the Council, of 27 November 2019, amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks.

19 The investable universe refers to all investable instruments of an asset class or a group of asset classes.

20 Section 6.3 shows a comparison between general indices and sustainability indices.

The new regulation for climate and sustainability benchmarks responds to the pivotal role these indices are called on to play in the transition to a decarbonised economy that is consistent with achieving the Sustainable Development Goals.

Role of climate and sustainability benchmarks

ILLUSTRATION 1



Source: Compiled by the authors.

As the activity carried out by the capital markets is decisive for channelling funds into projects and companies that contribute to reducing greenhouse gas emissions, in accordance with the objectives set in the Paris Agreement, the benchmarks can and should encourage these investments by facilitating the creation of individual and group portfolios to compare returns and even hedge the risks of exposure to carbon emissions through the derivatives markets.²¹

A growing number of investors are trusting in these benchmarks and more and more private investors and institutions are demanding robust and reliable global indices with which to create investment products, to measure and compare the performance of products and investment portfolios, and establish asset allocation strategies.

This is corroborated by the Index Industry Association, which has disclosed that the number of ESG benchmarks worldwide increased by more than 40% in 2020, compared to almost 15% in 2019.²²

21 The ISDA document (2021) analyses the potential role of derivatives in sustainable finance and describes the range of product structures and types of transactions that make up the universe of ESG-related derivatives.

22 IIA (2021).

According to recent data published by ESMA,²³ EU investor appetite for ESG funds has risen during the COVID-19 crisis. Since March 2020, ESG equity funds have seen net inflows of €72 billion (representing asset growth of 19%), compared to €86 billion for non-ESG equity funds (asset growth of 0.3%). This brings the total assets of EU ESG equity, bond and mixed funds to €835 billion, an increase of 55% from March, representing 11% of total ESG and non-ESG equity, bond and mixed fund assets.²⁴

In addition, creating these benchmark labels reduces the risk of greenwashing, i.e. the misleading use of the green or sustainable labels in the marketing of products.

The widespread use of these benchmarks is also expected to encourage companies to adopt and publish credible targets for reducing carbon emissions, as when the administrator of an EU climate transition benchmark selects or weights underlying assets, they must consider companies that have these goals and ensure that they are public and credible, in the sense that they represent a genuine commitment to decarbonisation, and that they are sufficiently detailed and technically feasible.

To allow benchmarks to perform this function effectively, the data sources and background information available for the construction of the indices must be reliable, comparable and easily accessible. Section 5 addresses the role of ESG ratings and ongoing proposals to improve their availability, integrity, and transparency.

4 Regulation of climate and sustainability benchmarks

The regulation of climate and sustainability benchmarks was approved recently (in December 2019), with the publication of the amendment to the Benchmark Regulation, through Regulation 2019/2089.

The new European regulation creates two new categories or benchmark labels that consider the carbon footprint of the constituent assets (see Section 4.1) and at the same time reinforces and harmonises the level of transparency for ESG targets and factors in the index methodology in general (see Section 4.2).

It is important to highlight that this new regulation affects all benchmarks and administrators, not just the new low-carbon impact indices, as:

- i) All main EU benchmark administrators are called on to market one or more climate transition benchmark.
- ii) It establishes disclosure obligations for all administrators, who must publicly disclose whether or not they manage low-carbon impact benchmarks and must also declare, for each of their indices, whether or not they apply ESG criteria

²³ ESMA (2021a).

²⁴ Section 6.2 contains information on investment funds with ESG strategies registered with the CNMV.

and, where appropriate, how they apply them. From December 2021, they must also disclose how their methodology is aligned with the goal of reducing carbon emissions or achieving the objectives of the Paris Agreement. In terms of data and breakdowns, these reporting obligations will be more demanding for equity and bond indices that are considered significant benchmarks.

In the EU, three delegated regulations have been approved that complement Regulation 2016/1011 and develop the new types of benchmarks and the corresponding advertising requirements:²⁵

- i) Delegated Regulation (EU) 2020/1818,²⁶ as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks.
- ii) Delegated Regulation (EU) 2020/1817,²⁷ as regards the minimum content of the explanation on how environmental, social and governance factors are reflected in the benchmark methodology.
- iii) Delegated Regulation (EU) 2020/1816,²⁸ on the minimum content of the explanation of ESG factors in the benchmark statement.

Its content is based on the recommendations of the report published by the Technical Expert Group on Sustainable Finance (TEG).²⁹ However, as recognised by the European Commission, it deviates in some areas to achieve greater proportionality and to give the benchmark providers greater flexibility to design their methodologies.

25 These delegated acts were published at the end of 2020, when they were expected to have entered into force by April 2020, at the same time as the amendments made to Regulation (EU) 2016/1011. This delay caused some uncertainty for benchmark administrators as to how they were expected to comply with the new disclosure requirements, which led ESMA to take the unprecedented step of issuing a no action letter (ESMA, 2020) addressed to the competent authorities, which indicated that supervisory actions should not be prioritised with respect to these new requirements until the delegated acts had been applied.

26 Commission Delegated Regulation (EU) 2020/1818, of 17 July 2020, supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards minimum standards for EU Climate Transition Benchmarks and EU Paris-aligned Benchmarks.

27 Commission Delegated Regulation (EU) 2020/1817, of 17 July 2020, supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards the minimum content of the explanation on how environmental, social and governance factors are reflected in the benchmark methodology.

28 Commission Delegated Regulation (EU) 2020/1816, of 17 July 2020, supplementing Regulation (EU) 2016/1011 of the European Parliament and of the Council as regards the explanation in the benchmark statement of how environmental, social and governance factors are reflected in each benchmark provided and published.

29 This working group was created by the European Commission to assist in the development of its 2018 legislative proposal. It is made up of experts from different backgrounds and professional profiles and its mandate is to identify a classification system, known as the EU taxonomy, to establish whether an economic activity is environmentally sustainable, draw up a draft EU green bond standard, the methodologies for EU climate benchmarks and disclosures for these benchmarks, and to provide guidance on how to improve the corporate disclosure of climate-related information. The TEG report on climate benchmarks and disclosure requirements was published in September 2019 (EU TEG, 2019a) and complemented with a manual released in December 2019 (EU TEG, 2019b).

The new regulation was published on 9 December 2019 and its content, in terms of the requirements for constructing new climate benchmarks and transparency obligations, is applicable from different dates, as shown in Table 1, which also summarises the main measures contained in this regulation.

Key dates for the implementation of the Climate and Sustainability Benchmark Regulation

TABLE 1

Adaptation of methodology	From 30 April 2020	→ Use of labels: Administrators of PA benchmarks and CT benchmarks must comply with the new methodology requirements.	Applicable only to PA and CT benchmarks.
	From 31 December 2022	→ CT benchmark administrators must select companies that publish specific reduction target deadlines, based on a breakdown at subsidiary level that is updated annually, provided that their activities do not significantly impair other ESG targets.	Applicable only to CT benchmarks.
	From 1 January 2022	→ Administrators of significant benchmarks must work to provide at least one CT benchmark.	Applicable only to significant benchmarks.
Reporting obligations	From 30 April 2020	→ The publication of the benchmark's methodology (BMR art. 13) and statement (BMR art. 27) must contain an explanation of how ESG factors are (or are not) reflected.	Applicable to all types of benchmarks (except IR and FX benchmarks).
		→ The administrator must declare that it has no climate transition or Paris-aligned benchmarks, or that it has no benchmarks that pursue or consider ESG factors.	Applicable to all types of benchmarks (except IR and FX benchmarks).
		→ Significant equity and bond indices and labelled benchmarks must include data and a breakdown of whether, and to what extent, emission reduction targets or Paris Agreement targets are guaranteed under Regulation 2019/2088.	Applicable to significant equity and bond benchmarks, and CT and PA indices.
	From 31 December 2021	→ Administrators must disclose in the benchmark statement an explanation of how their methodology is aligned with the goal of reducing carbon emissions or achieving the objectives of the Paris Agreement.	Applicable to all types of benchmarks (except IR and FX benchmarks).

Source: Own compilation based on Regulation (EU) 2016/1011.

4.1 New types of climate benchmarks

Two new categories or benchmark labels have therefore been created that consider the carbon footprint of the underlying assets to help investors who seek sustainable investment products:

- i) EU climate transition benchmarks (CT benchmarks), which take into account a company's decarbonisation trajectory in their selection criteria.
- ii) EU benchmarks aligned with the Paris Agreement (PA benchmarks), which only select constituents that contribute to achieving the target to reduce global warming to 1.5°C compared to pre-industrial levels established in the Paris Agreement.

In both cases, these are voluntary labels, which can only be used by benchmark administrators when they provide climate benchmarks that comply with the methodology and transparency requirements established in the regulation.

These benchmarks, which we refer to generically as climate benchmarks, are designed to guide investors who wish to pursue a climate-aware investment strategy, with varying levels: CT benchmarks may be a low-carbon alternative to commonly used benchmarks, while PA benchmarks offer a portfolio that is aligned and committed to the goal of reducing global warming.

Both types of benchmark select companies with a trajectory of decarbonisation – the objective is to reduce the intensity (or absolute emissions) of GHGs by at least 7% per year on average. GHG intensity is the main parameter used to calculate a decarbonisation strategy as it guarantees comparability and is not biased in favour or against any particular sector.

The main differences in construction lie in the exclusions from the indices and the greater percentage reduction required by PA benchmarks to exposures to GHG-intensive assets compared to their parent benchmark or investable universes. Table 2 presents the main similarities and differences in the design of PA and CT benchmarks.

Similarities and differences between PA and CT benchmarks

TABLE 2

		PA benchmarks	CT benchmarks
Common features	Base scenario for temperature	To design their methodology, the 1.5°C scenario with no or limited overshoot as referred to in the IPCC special report on the impacts of global warming of 1.5°C, is taken as the base scenario.	
	Restrictions on the allocation of shares	In equity benchmarks, exposure to sectors that contribute most to climate change (such as oil, gas, mining and transportation) should not be less than the exposure of their investable universe. ¹	
	Parameter to calculate the decarbonisation strategy	<ul style="list-style-type: none"> – GHG intensity: absolute GHG emissions (equivalent tons of CO₂) divided by the million euro value of the company, including cash, which is the sum of the market capitalisation of its ordinary and preferred shares, and the book value of total debt and non-controlling interests with no cash deducted. – In bond indices made up of unlisted companies, GHG emissions can be used as an absolute figure. – The calculation must be made annually and the same currency used for all underlying assets. – The annual variation is calculated as a percentage difference between the data at the end of year <i>n</i> and the data at the end of year <i>n</i>-1. A new base year should be used whenever significant changes are made to the calculation methodology. 	
	Gradual inclusion in Scope 3	Scope 3 GHG emissions data ² are included in phases according to the sector: ³ <ul style="list-style-type: none"> – December 2020: energy and mining. – December 2022: transport, construction, buildings, materials and industry. – December 2024: all other sectors. 	
Common features	Weightings	The weighting of companies that set and publish GHG emission reduction targets can be increased if the following two requirements are met: <ul style="list-style-type: none"> – Companies consistently and accurately publish their Scope 1, 2 and 3 GHG emissions. – Companies have reduced their GHG intensity or, where appropriate, their absolute emissions by at least 7% per year on average for at least three consecutive years. 	
	Decarbonisation strategy	The following objectives are pursued depending on the type of underlying assets: <ul style="list-style-type: none"> – Listed equities: an average reduction of at least 7% in GHG intensity per year. – Fixed income of listed companies: an average reduction of at least 7% in GHG intensity or absolute emissions per year. – Fixed income of unlisted companies: an average reduction of at least 7% in absolute GHG emissions per year. 	
	Loss and recovery of label	The label will be lost if the goals are not reached in one year and are not offset in the following year, or if they are not reached three times in a period of ten years. It may be recovered if the goals are reached in two consecutive years, unless the label has been lost on two occasions, in which case it will be permanently removed.	

		PA benchmarks	CT benchmarks
Differences	GHG exposure reduction requirements	50% lower than the investable universe.	30% lower than the investable universe.
	Exclusions ⁴	<ul style="list-style-type: none"> – Activities related to controversial weapons. – Cultivation and production of tobacco. – Companies that do not comply with the United Nations Global Compact or the OECD Guidelines for multinationals. – Companies that obtain: <ul style="list-style-type: none"> • 1% or more of their income from the prospecting, mining, extraction, distribution or refining of anthracite, coal and lignite. • 10% or more of their income from exploration, extraction, distribution or refining of liquid fuels. • 50% or more of their income from exploration, extraction, production or distribution of gaseous fuels. • 50% or more of their income from electricity generation with a GHG intensity greater than 100g CO₂/ kWh. – Companies that do significant harm to one or more of the environmental goals.⁵ 	<p>From 31 December 2022:</p> <ul style="list-style-type: none"> – Activities related to controversial weapons. – Cultivation and production of tobacco. – Companies that do not comply with the United Nations Global Compact or the OECD Guidelines for multinationals. <p>Exclusion applicable from 31 December 2022.</p>

Source: Own compilation based on Regulation (EU) 2016/1011 and Delegated Regulation (EU) 2020/1818.

- 1 This requirement is intended to provide a true picture of the real economy, including the sectors that must significantly reduce their emissions so that investors committed to decarbonisation can exert their influence in the transition of companies to more sustainable activities.
- 2 In accordance with the Annex to EU Regulation 2019/2089, Scope 1 refers to carbon emissions generated from sources that are controlled by the company that issues the underlying assets. Scope 2 relates to emissions from the consumption of purchased electricity, steam, or other sources of energy generated upstream from the company that issues the underlying assets. Scope 3 refers to indirect emissions, not covered in Scope 1 and 2, that occur in the value chain of the reporting company, including both upstream and downstream emissions, in particular for sectors with a high impact on climate change and its mitigation.
- 3 Due to the insufficient quality of Scope 3 GHG emissions, they will be included in the calculation gradually, according to the sector.
- 4 Any additional exemption criteria based on climate or other ESG factors must be disclosed in the benchmark methodology.
- 5 Established in Article 9 of Regulation (EU) 2020/852: mitigation of climate change, adaptation to climate change, sustainable use and protection of water and marine resources, transition towards a circular economy, prevention and control of pollution, and protection and recovery of biodiversity and ecosystems.

In terms of the transparency, quality and accuracy of data sources, both PA and CT benchmarks must formalise, document and disclose:

- i) The methodology on which the estimates of GHG emissions and significant harm in regard to the environmental goals is based, including the research approach and methodology used, the main assumptions and the precautionary principles of the estimates.
- ii) When using external datasets, the name and contact details of the data providers, the methodology used and the main assumptions and precautionary principles, where available, as well as a hyperlink to the website of the data provider and the relevant methodology used, where available.

The decarbonisation strategy should be formalised, documented and disclosed, including the base year and instances of non-compliance with targets, reasons for failure to comply and corrective actions to be taken to achieve the adjusted target for the following year.

Data on GHG emissions for Scopes 1, 2 and 3 must be accurate and consistent with global or European standards,³⁰ and must disclose the standard used in the methodology.

4.2 New disclosure obligations

One of the objectives of the regulation is to establish new transparency obligations to show how the benchmark methodology contributes to achieving ESG goals. These requirements will affect all types of benchmarks, not just those labelled climate benchmarks, with the exception of interest rate and foreign exchange benchmarks, as it is considered that these are not directly linked to the Sustainable Development Goals.

All administrators must specify in the statement for each index whether or not their benchmarks or families of benchmarks pursue ESG objectives and, where applicable, how they are reflected and whether the benchmark administrator offers these indices.

Harmonising and standardising the information to be published on these benchmarks makes them comparable and users will be able to select those that best meet their investment needs, thus including and encouraging the consideration of sustainability factors in their investment decisions.

Statement and methodology

EXHIBIT 1

The benchmark statement and publication of the methodology used

The BMR contains two transparency requirements. Article 13 establishes that the administrator must disclose the key elements of the calculation methodology used, details of the internal review and approvals, and the procedures for consultation and user complaints.

The statement is regulated in Article 27. The administrator must publish and keep an updated statement that defines the market or economic reality measured by the benchmark, its reliability, data sources, any exercise of discretion, corrections of errors, cases in which publication may be stopped, the methodology approved and its corresponding reviews, etc.

4.2.1 ESG factors and how they should be published

Benchmark statements other than for interest rate and foreign exchange indices must explain, using the model contained in Annex I of Delegated Regulation (EU)

30 Such as:

- The product environmental footprint or the organisation environmental footprint methods contained in Commission Recommendation 2013/179/EU, of 9 April 2013, on the use of common methods to measure and communicate the life cycle environmental performance of products and organisations.
- The corporate value chain accounting and reporting standard (Scope 3) (September 2011), supplementing the greenhouse gas protocol corporate accounting and reporting standard.
- UNE-EN ISO 14064 or UNE-EN ISO 14069.

2020/1816, how the ESG factors listed in Annex II of the same regulation are considered, including:

- How ESG factors are reflected for each of the underlying assets.
- The ESG factor score for the corresponding benchmark and benchmark family as an aggregated weighted average value.
- Scores for any additional ESG factors considered by the benchmark administrator.
- References to the data sources and standards used for the ESG factors disclosed.
- The additional disclosures applicable to PA and CT benchmarks, as required in Sections 2 and 3 of Annex I.

The administrator of each benchmark can replace the above information with a hyperlink to a website that contains all the required information. The information must be updated at least annually and whenever there are significant changes.

The regulation identifies 28 factors that must be published by the benchmark administrator according to the types of underlying assets, as described in Tables 3 and 4. All benchmarks must report using the template included for this purpose in Annex I of the regulation. When the underlying assets of the benchmark are equities, 16 factors must be disclosed, 13 for fixed income, 11 for sovereign debt, 4 for commodities and 6 for other categories of assets.

Number of mandatory disclosure ESG factors for each type of underlying asset

TABLE 3

	Combined	Environmental	Social	Governance
Shares (EQ)	–	5	9	2
Fixed income (FI)	–	5	9	–
Sovereign debt (SD)	1	3	4	3
Commodities (C)	–	1	1	2
Other (O)	–	2	3	1

Source: Own compilation based on Regulation (EU) 2020/1816.

In addition to the above, PA and CT benchmarks must also disclose other factors in their statement and comply with additional disclosure requirements, in accordance with their objectives:

- Forward-looking year-on-year decarbonisation trajectory.
- Degree to which the IPCC decarbonisation trajectory (15°C with no or limited overshoot) has been achieved on average per year since creation.
- Overlap between those benchmarks and their investable universe using the active share at asset level.

Lastly, all benchmarks must provide, from different dates depending on the type of index (see Table 1) the following information on their alignment with the objectives of the Paris Agreement:

- Whether the benchmark aligns with the target of reducing carbon emissions or the attainment of the objectives of the Paris Agreement.
- The temperature scenario, in accordance with international standards, used for alignment with the target of reducing GHG emissions or attaining of the objectives of the Paris Agreement.
- The name of the provider of the temperature scenario used for alignment with the target of reducing GHG emissions or the attainment of the objectives of the Paris Agreement.
- The methodology used for the measurement of alignment with the temperature scenario.
- A hyperlink to the website of the temperature scenario used.
- The date the information was last updated and the reason for the update.

Mandatory disclosure of ESG factors according to the type of benchmark asset

TABLE 4

Mandatory ESG factors		EQ	FI	SD	C	O
Combined factors						
1	The percentage of underlying fund management companies signed up to international standards.			✓		
Environmental						
2	Degree of exposure of the portfolio to the sectors listed in Sections A to H and Section L of Annex I to Regulation (EC) No. 1893/2006 as a percentage of the total weight in the portfolio.	✓	✓			✓
3	GHG intensity of the benchmark.	✓	✓	✓		✓
4	Percentage of reported versus estimated emissions.	✓	✓	✓		
5	Exposure of the benchmark portfolio to companies the activities of which fall under Divisions 05 to 09, 19 and 20 of Annex I to Regulation (EC) No. 1893/2006.	✓	✓			
6	Exposure of the benchmark portfolio to activities included in the environmental goods and services sector, as defined in Article 2(5) of Regulation (EU) No. 691/2011 of the European Parliament and of the Council.	✓				
7	Percentage of green bonds in the benchmark portfolio.		✓	✓		
8	Degree of exposure of the underlying commodities to climate-transition risks, measuring the financial impacts resulting from the effects of the implementation of low-carbon strategies (low, moderate or high).				✓	
Social						
9	International treaties and conventions, United Nations principles or, where applicable, national law used in order to determine what constitutes a “controversial weapon”.	✓	✓			✓
10	Weighted average percentage of benchmark constituents in the controversial weapons sector.	✓	✓			✓
11	Weighted average percentage of benchmark constituents in the tobacco sector.	✓	✓			✓

Mandatory disclosure of ESG factors according to the type of benchmark asset (continuation)

TABLE 4

Mandatory ESG factors	EQ	FI	SD	C	O
12 Number of benchmark constituents subject to social violations (absolute number and relative number divided by all benchmark constituents), as referred to in international treaties and conventions, United Nations principles and, where applicable, national law.	✓	✓	✓		
13 Exposure of the benchmark portfolio to companies without due diligence policies on issues addressed by Conventions 1 to 8 of the International Labour Organization.	✓	✓			
14 Weighted average gender pay gap.	✓	✓			
15 Weighted average ratio of female to male board members.	✓	✓			
16 Weighted average ratio of accidents, injuries and fatalities.	✓	✓			
17 Numbers of convictions and amount of fines for violations of anti-corruption and anti-bribery laws.	✓	✓			
18 Average human rights performance of the issuers (including a quantitative indicator and the methodology used to calculate it).			✓		
19 Average income inequality score, measuring the distribution of income and economic inequality among the participants in a particular economy (including a quantitative indicator and the methodology used to calculate it).			✓		
20 Average freedom of expression score measuring the extent to which political and civil society organisations can operate freely (including a quantitative indicator and the methodology used to calculate it).			✓		
21 Degree of exposure of the underlying commodities to social risks (low, moderate or high).				✓	
Governance					
22 Weighted average percentage of board members who are independent.	✓				
23 Weighted average percentage of female board members.	✓				
24 Average corruption score measuring the perceived level of public sector corruption (including a quantitative indicator and the methodology used to calculate it).			✓		
25 Average score for political stability that measures the probability that the current regime will be forcibly overthrown (including a quantitative indicator and the methodology used in the calculation).			✓		
26 Average political stability score, measuring the likelihood that the current regime will be overthrown by the use of force (including a quantitative indicator and the methodology used to calculate it).			✓	✓	
27 Degree of exposure of the underlying commodities to governance risks (low, moderate or high).				✓	
28 Percentage of underlying funds with stewardship policies in place, including measures for the planning and management of resources.					✓

Source: Own compilation based on Regulation (EU) 2020/1816.

4.2.2 Transparency of the methodology

Regulation (EU) 2020/1817 defines the minimum content of the explanation on how environmental, social and governance factors are reflected in the benchmark methodology. In this case, the philosophy is the same as that followed for the benchmark statement.

With the exception of commodity benchmarks, administrators must explain, using the standard template for each benchmark or family of benchmarks, which of the ESG factors have been considered in the design of their methodology. They must

explain how these factors are reflected in the key elements of this methodology, and also with regard to the selection of underlying assets, weighting factors, parameters or metrics and proxy variables.

When a benchmark combines different types of underlying assets, the administrator must explain how the ESG factors are reflected for each of the relevant assets.

Administrators must clearly indicate whether or not the benchmarks pursue ESG objectives. The information on the methodology provided must be updated at least once a year or each time it is changed, and the reasons for the update must be indicated.

In regard to data and sources, it must be specified whether the data are reported, modelled or obtained internally or externally, and the name of the external data provider must be indicated when applicable, in addition to the processes used to assess the quality of the data. The international standards used in the methodology must also be described.

4.3 Issues that require clarification or improvement

The new regulation on climate and sustainability indices is broad and technically complex. Therefore, its practical application has generated uncertainties for the sponsors of these benchmarks and some issues have been identified that could be improved in the future.

In order to ensure a harmonised and consistent application of the new regulation, ESMA has included a section on climate and sustainability benchmarks in its question and answer document on benchmarks,³¹ which is regularly updated with the responses to questions submitted by the public, financial market participants, competent authorities and other interested parties.

Some of the issues that have been clarified to date include the level of information that must be provided by benchmarks that consider sustainability factors compared to those that pursue ESG objectives, or the possibility of considering additional or different factors to those envisaged in the corresponding delegated regulations.

Several aspects have also been identified that could be taken into account in future amendments of this regulation. These include the lack of a central register for climate and sustainability benchmarks, and the lack of specific rules of use in the benchmark name, which makes them hard to identify, use and compare by potential users.

Due to the limited scope of application of BMR, ESG benchmarks could be created that fall outside regulation, i.e. that do not meet any of the three requirements set out in the definition of a “benchmark” in Article 3.3 of the BMR. If this situation were to arise, it could put the entities that offer these benchmarks in a much more

³¹ ESMA (2021d).

favourable competitive position than the administrators that offer benchmarks subject to the BMR. Providing these benchmarks could also give rise to greenwashing practices. Therefore, in the future, adapting the definition of these indices could be considered to give them a broader subjective scope.

Another aspect that has been drawn to the attention of regulators is the difficulties experienced by users in accessing ESG information, as well as the lack of quantitative selection criteria. Furthermore, some small- and medium-sized enterprises have mentioned the high cost of generating this information, which can make it harder for them to be included in the benchmarks.

5 ESG ratings: a necessary base for consolidating sustainable benchmarks

As sustainable finance gains a foothold and sustainable investment rises, ESG ratings have become increasingly important for investors and issuers alike and there is growing demand for these services. However, the lack of a proper regulatory framework accentuates certain problems and risks which reduce the usefulness of these ratings.

The lack of a standard definition and comparability, the lack of transparency in methodologies, the risk of conflicts of interest and the absence of supervision are some problems that have a significant impact on the construction of green portfolios and the production of benchmarks linked to ESG factors. Therefore, assessments must be available that: i) provide information about the ESG profile of an entity, ii) have proper safeguards to ensure that the information referred to is robust, and iii) are reliable, to prevent the risk of greenwashing.

5.1 Vulnerabilities and risks of the ESG ratings market

Recent studies show that, compared to credit ratings, ESG ratings show very low levels of correlation between providers, causing problems throughout the investment value chain, as well as for the construction of ESG benchmarks, as the choice of rating provider significantly affects the constituents of the indices.

In a work recently published by ESMA³² it is estimated that while for traditional credit quality ratings the correlation in the ratings awarded by different agencies to the same issuer is very high (close to 99%), this figure drops to 60% for environmental or ESG ratings.

The fact that companies that operate in highly polluting industries can obtain high environmental scores from some ESG rating providers may lead to confusion among investors, and underscores the need for greater transparency and standard definitions.

32 Mazzacurati (2021).

This particularly affects the construction of ESG benchmarks, bearing in mind the significant volumes of assets that pursue these objectives. In the work carried out by ESMA, the Eurostoxx ESG Leaders 50 index has been analysed. This index selects the 50 leading companies based on ESG criteria, according to Sustainalytics ratings, from a universe of 1,800 companies that make up the STOXX Global 1800 index. However, only 62% to 72% of the companies identified by Sustainalytics as leaders are also considered as such by MSCI and Refinitiv. All three providers agree on only 40% of the index constituents

The impact on index performance has also been analysed by replicating it using the same methodology but applying the ratings assigned by Refinitiv to select the 50 top companies in terms of ESG factors. The synthetic index was found to outperform the original index by 12 basis points (cumulative) between March and December 2020 as a result of the different composition.

Given the current growth trend in sustainable investing and passive investment products such as ETFs, measures aimed at reducing the risk of erroneous allocation of capital will be crucial in the transition to a more sustainable financial system.

5.2 Proposed measures to build confidence in ESG ratings

The ESG ratings and assessments market is complex and still in development. There is a wide variety of vendors of varying size and scope. This means that any regulatory action must be properly weighed up to include the broad spectrum of existing products while ensuring that future innovations are not left out.

Likewise, any regulatory action must be proportionate in order to include large multinational providers, which may be subject to existing regulatory frameworks, and smaller entities that do not have the same regulatory compliance experience but will have a valuable role to play in the future.

ESMA and other authorities have proposed, in response to the public consultation on the EC's new strategy for sustainable financing,³³ a European regulation that includes a standard definition of ESG ratings that covers the wide range of evaluations currently offered. Table 5 shows ESMA's proposals.³⁴

33 The results of the recently-published public consultation show that 80% of responses are in favour of the European Commission acting on this issue.

34 ESMA (2021c).

Legally binding definition	→	An ESG rating is an opinion on the impact of an entity, issuer or debt security on exposure to ESG factors, alignment with international climate agreements or on sustainability characteristics issued using a defined classification system of rating categories.
Registration and supervision	→	It should be overseen by an authority to ensure that all entities are subject to the same organisational, conflict of interest and transparency requirements. ESMA could take responsibility.
Product requirements	→	There should be specific product requirements applicable to ESG ratings and assessments: up-to-date, reliable and transparent data sources, and robust methodologies that are transparent and verifiable.
Proportionality	→	The regulatory framework should ensure that larger and more systemic entities are subject to organisational and conflict of interest requirements that reflect their growing importance in the area of sustainable finance. At the same time, it should ensure that smaller entities benefit from appropriate exemptions.

Source: Own compilation based on ESMA's response to the EC consultation.

Among the proposed measures, the advantage of ESMA assuming the role of direct supervisor of these agents is highlighted due to the high concentration of providers in the ESG ratings market and the experience of that authority in supervising credit ratings providers, which would ensure economies of scale for supervisory resources and benefit the industry in general by sidestepping different regulatory or supervisory mandates.

6 Relationship between investment products and climate and sustainability benchmarks

The EU has taken appropriate steps to build a sustainable financial ecosystem. As explained in Section 2, the Taxonomy Regulation, the Regulation on the disclosure of information related to sustainability in the financial services sector (SFDR)³⁵ and the Benchmark Regulation (BMR) are key pieces of the European Commission's Sustainable Finance Action Plan that aim to bring about changes in the behaviour patterns of the financial sector, discouraging greenwashing, increasing transparency, promoting responsible and sustainable investment and providing investors with the tools to identify investment opportunities that meet their sustainable investment objectives.

In this context, the relationship between investment products and benchmarks in the area of sustainability disclosures in the financial services sector is analysed below, the obligations of which are set out in the SFDR and in the amended BMR,³⁶

35 Regulation (EU) 2019/2088 of the European Parliament and of the Council, of 27 November 2019, on sustainability-related disclosures in the financial services sector.

36 Regulation (EU) 2019/2089 of the European Parliament and of the Council, of 27 November 2019, amending Regulation (EU) 2016/1011 as regards EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks.

alongside the corresponding technical development standards.³⁷ Subsequently, information is presented on the types of benchmarks used by sustainable investment funds registered with the CNMV, showing the relationship between the benchmarks and the asset management industry in the alignment of sustainability considerations and the transition to a low-carbon economy. This section also contains a comparison of the performance of general market indices with sustainability benchmarks linked to the growing preference for sustainable investment.

6.1 The Sustainable Finance Disclosure Regulation

The objective of the SFDR, which entered into force on 1 March 2021, as indicated in Article 1, is to lay down harmonised rules for financial market participants and financial advisers on transparency with regard to the integration of sustainability risks and the consideration of adverse sustainability impacts in their processes and the provision of sustainability-related information with respect to financial products.

To meet this objective, the SFDR establishes new reporting obligations that are aligned with the level of transparency and commitment to the ESG criteria of the financial product, which are more stringent and detailed for products that pursue sustainable investment objectives, known as “dark green products” or products included in Article 9 of the SFDR, than for those applied to “light green products” or products included in Article 8 of the SFDR that offer ESG features. The new obligations also apply to conventional products or products that are not related to ESG factors (see Table 6) and affect the information contained on the website, pre-contractual information (the prospectus in the case of collective investment products) and annual periodic reports.

Product classification under the SFDR

TABLE 6

Level of demand for ESG transparency ↓		Conventional products (Article 6 SFDR) These products cannot be presented as sustainable even when entities disclose how they integrate sustainability risks and principal adverse impacts (PAIs) into their investment management decisions.
		Products promoting ESG factors (Article 8 SFDR) The management of these products explicitly integrates environmental or social considerations, beyond the simple inclusion of sustainability risks.
		Products with an ESG objective (Article 9 SFDR) These products aim to have a positive effect on the environment and society, and define an explicit objective applicable to their investment strategy.

Source: Own compilation based on the SFDR.

37 In the case of the SFDR, on the date of publication of the article, the delegated technical standards had not been approved (https://www.esma.europa.eu/sites/default/files/library/jc_2021_03_joint_esas_final_report_on_rts_under_sfdr.pdf; [jc_2021_22_-_joint_consultation_paper_on_taxonomy-related_sustainability_disclosures.pdf](https://www.esma.europa.eu/sites/default/files/library/jc_2021_22_-_joint_consultation_paper_on_taxonomy-related_sustainability_disclosures.pdf) (europa.eu)).

This ensures that products can be easily compared and improves the final investor's knowledge of the sustainability credentials of financial products. In order to comply with the new disclosure obligations, the product management or distribution entities must classify them according to one of the three categories shown in Table 6.

In accordance with the criteria established by the CNMV³⁸ on the inclusion of ESG factors in the names and commercial communications of these products, those included under Article 8 of the SFDR may contain ESG elements in their name only if the minimum amount of investments indicated in their prospectus to achieve the environmental or social characteristics that they promote is greater than 50%.

Beyond their name, in regard to the use of ESG elements in commercial communications in general, only the financial products referred to in Article 8 or 9 of the SFDR may include these terms, provided that the content of the advertising message is aligned with the information contained in the prospectus.

The transparency obligations can be summarised as follows:

- Information about policies on the integration of sustainability risks in the investment decision-making process: to be published on websites (Article 3) and in pre-contractual information at product level (Article 6).
- A statement about the policy on adverse impacts of investment decisions or advice on sustainability factors, which must be included on the entity's website (Article 4) and in the pre-contractual information at the product level (Article 7).
- Transparency on websites about the entity's remuneration policies in relation to the integration of sustainability risk (Article 5).
- When a product promotes environmental or social characteristics of a product (provided that the companies in which it is invested observe good governance practices) this must be shown on the entity's website (Article 10), in pre-contractual information (Article 8) and in the corresponding periodic information, annual reports in the case of CISs (Article 11).
- Information on products aimed at sustainable investments: to be included on websites (Article 10), in pre-contractual information (Article 9) and in the corresponding periodic information, annual report in the case of CISs (Article 11).

It is usual practice for financial products that consider or pursue ESG objectives to designate specific benchmarks to facilitate their investment strategy and allow their performance to be compared. For these products, there are specific requirements for compliance with the disclosure obligations, the most relevant aspects of which are listed below:

38 CNMV (2021a).

- Financial products with ESG characteristics must disclose whether, and in what way, the designated benchmark is consistent with these characteristics and if a benchmark is not used information must be given on how the product meets sustainability requirements.
- Financial products that claim to have a positive effect on the environment and society must disclose the sustainability benchmark they use to measure sustainable performance and if a benchmark is not used explain how the sustainability target has been met.
- Managers of products that designate specific benchmarks will need to publish information on their websites about the benchmark calculation, such as the methodology used to select the data or how the index is calculated (alternatively, a hyperlink to the website of the benchmark administrator can be used).
- From 1 January 2022, managers must include in their periodic reports information on the overall impact of their financial products on sustainability through indicators that measure the selected sustainable investment objective. Where a benchmark has been designated, they should provide information on that benchmark, as well as a general market index for purposes of comparison.
- Managers that indicate that a financial product has the goal of reducing carbon emissions, must provide a detailed explanation of how the low-carbon objective will be guaranteed in order to meet the long-term global warming objectives of the Paris Agreement. If a climate benchmark is designated, these obligations are more easily fulfilled by making a reference to the index and indicating where its methodology can be found.

Table 7 sets out the specific disclosure obligations applicable to financial products that have designated a benchmark.

	SFDR Articles	Products that promote ESG criteria (Art. 8 SFDR)	Products with sustainable investment goals (Art. 9 SFDR)
Pre-contractual information	Articles 8 and 9 SFDR Articles 18, 25 and 26 of the draft RTS	<ul style="list-style-type: none"> – An indication of whether a specific index has been designated as a benchmark to determine whether the financial product is aligned with the ESG characteristics it promotes. – How the benchmark takes into account ESG characteristics so that it is continually aligned with the characteristics it promotes and the investment strategy. – How the designated benchmark differs from a broad market index. – Information on where to find the index calculation methodology. 	<ul style="list-style-type: none"> – An indication of whether a specific index has been designated as a benchmark to meet the sustainable investment objective. – How the benchmark takes into account sustainability factors so that it continually aligns with the sustainable investment objective. – Why and how the designated benchmark differs from a broad market index. – Information on where to find the index calculation methodology. – How the alignment of the investment strategy with the index methodology is ensured at all times. – For financial products that aim to reduce carbon emissions, if a CT/AP benchmark is used, information must be included on where to find the index calculation methodology. Otherwise, an explanation must be included of the extent to which the financial product meets the methodology requirements established in Delegated Regulation (EU) 2020/1818.
Website	Article 10 SFDR Articles 32, 44 and 45 of the draft RTS	<ul style="list-style-type: none"> – Description of how the index used as a benchmark aligns with the characteristics or objectives of the product, including the data sources, the methodologies used to select that data, the rebalancing methodologies and how the index is calculated. – A link to the administrator's website can be included if it contains this information. 	<ul style="list-style-type: none"> – A description of how the index used as a benchmark aligns with the objectives of the product, including the data sources, the methodologies used to select that data, the rebalancing methodologies and how the index is calculated. – A link to the administrator's website can be included if it contains this information. – For financial products that aim to reduce carbon emissions, if a CT/AP benchmark is used, a hyperlink must be included showing the index calculation methodology. Otherwise, an explanation must be included of the extent to which the financial product meets the methodology requirements established in Delegated Regulation (EU) 2020/1818.
Periodic reports	Article 11 SFDR Articles 63, 69 and 70 of the draft RTS	<ul style="list-style-type: none"> – An explanation of the difference between the ESG index and a general market index. – An explanation of the performance of the sustainability indicators that determine the alignment of the index with the characteristics or objectives of the product. A specific section must be included for CT and PA benchmarks. – A comparison of financial product performance with the ESG index and the general market index. 	

Source: Own compilation based on the SFDR, draft regulatory technical standards on the content, methodologies and presentation of information (draft RTS)¹ and the implementation criteria published by the CNMV.²

1 Joint Committee of the European Supervisory Authorities (2021).

2 CNMV (2021a) and CNMV (2021b).

6.2 Indices used by sustainable investment funds registered with the CNMV

Up until July 2021, 135 investment funds had been registered with the CNMV in the categories described in Articles 8 and 9 of the SFDR, belonging to 56 management companies: Most of these funds are classified as products that promote ESG criteria, i.e. light green funds under Article 8 of the SFDR.

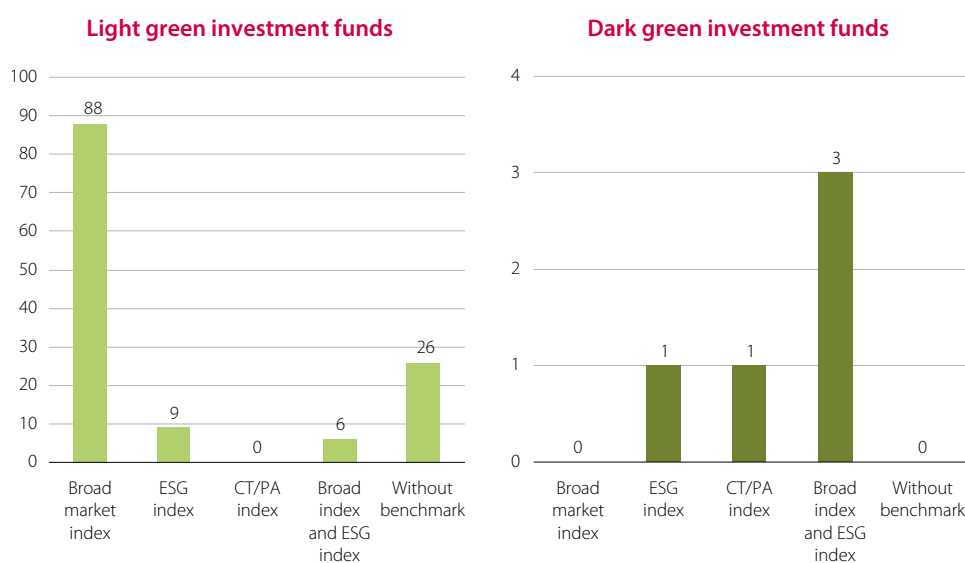
Only six dark green funds (Article 9 SFDR) that pursue ESG objectives have been registered to date.

As shown in Figure 1, sustainable investment funds make wide use of indices as a benchmark to measure their performance.

In a more detailed analysis of index types, it can be observed that light green investment funds mostly use general market indices, while the number of funds that use specific climate or sustainability benchmarks is significantly lower. However, most dark green investment funds use specific climate or sustainability benchmarks.

Number of sustainable investment funds registered with the CNMV based on the type of index used as a benchmark

FIGURE 1



Source: Own compilation based on data from the CNMV investment fund registry.

Only one dark green fund, with an objective of reducing carbon emissions, has designated an EU climate transition benchmark. The management objective of this fund is to replicate the Solactive 360 Euro IG Corporate CTB index, classified as a CT index, to thus meet the sustainable investment objective of a minimum 7% decarbonisation per year, with a maximum deviation of 5% per year.

According to the fund prospectus,³⁹ the index is replicated mainly synthetically through an OTC derivative and, to a lesser extent, through the direct acquisition of the securities that make up the index.

In order to comply with its transparency obligations, the fund manager compiles the information published by the benchmark administrator. Thus, aspects such as the definition of the sustainability objective, the sustainability indicators used to measure its achievement (in this case, GHG) or the criteria followed to select the investments that allow the sustainable investment objective to be achieved come from information published by the benchmark administrator,⁴⁰ in accordance with the provisions of the regulation on climate and sustainability benchmarks.

6.3 Comparative analysis of the performance of traditional indices and climate and sustainability benchmarks

The growth in assets that pursue sustainable investment strategies in recent years responds to rising demand from both individual investors and investment managers. A recent study by Zeb and Morningstar⁴¹ shows that the net assets of sustainable funds have more than doubled since 2018 and that more than half (52%) of new net inflows in 2020 went to sustainable funds registered in Europe.

However, the incentives to invest in these sustainable products do not always correspond to a better expected return on investment, and in many cases investors are willing to receive lower returns in exchange for investing in more sustainable companies.

A recent work published in the *Journal of Financial Stability*⁴² concludes that companies' alignment with sustainability factors and the quality of their transparency levels are highly valued by the market, but only in combination. The same work shows that investors will accept lower returns in order to hold greener and more transparent stocks. Another study by Bolton and Kacperczyk⁴³ points out that there is a "carbon premium" in the stock markets, in other words, companies with higher emissions compensate investors by offering higher returns.

If the performance of the Ibex 35 index is compared⁴⁴ with the FTSE 4Good Ibex⁴⁵ over the three and a half years between January 2018 and July 2021 – when the two

39 Abanca Renta Fija Transición Climática 360, Fondo de Inversión. Prospectus. 23 July.

40 This information is included in a document attached to the prospectus that contains information on sustainability in accordance with Article 9 of the SFDR.

41 Zeb and Morningstar (2021).

42 Alessi, Ossola and Panzica (2021).

43 Bolton and Kacperczyk (2021).

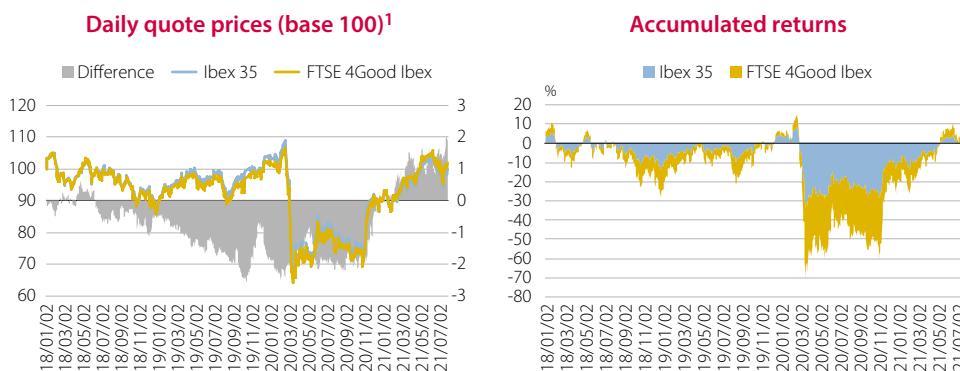
44 The Ibex 35 index, calculated and published by Sociedad de Bolsas, S.A. (BME Group), is made up of the 35 most liquid securities traded on the Spanish stock market. Its components are weighted by market capitalisation adjusted for free float.

45 The FTSE 4Good Ibex index, managed by FTSE Russell and published daily by Bolsas y Mercados Españoles (BME), contains companies from the Ibex 35 and the FTSE España All Cap index that demonstrate good sustainability practices, with some specific ESG ratings awarded by FTSE Russell. Currently the index is made up of 46 stocks, of which 30 are also part of the Ibex 35.

indices were almost perfectly correlated (0.99) –, it can be observed that the Ibex 35 systematically outperforms the FTSE 4Good Ibex index throughout the period (see Figure 2).

Comparative performance of the Ibex 35 and the FTSE 4Good Ibex in the period from January 2018 to July 2021

FIGURE 2



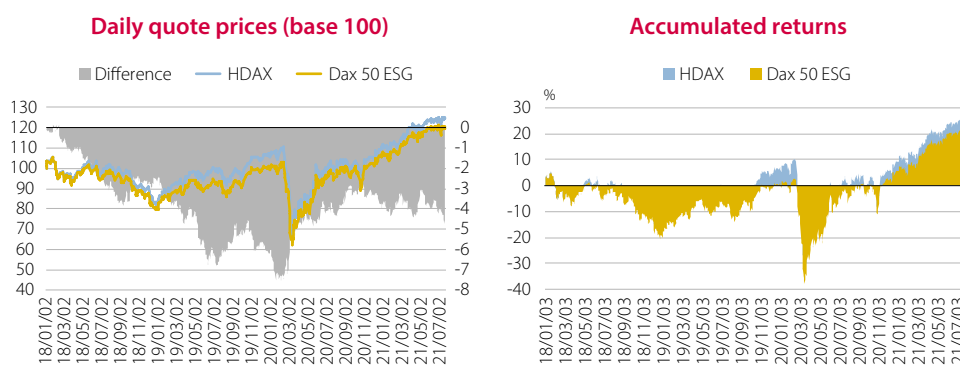
Source: Own compilation based on data from Bloomberg.

- 1 The secondary axis shows the difference between the daily prices (base 100) of the ESG index and those of the general market index.

The same conclusion is obtained when the HDAX⁴⁶ and Dax 50 ESG⁴⁷ indices are compared for the same period. With an almost perfect correlation (also 0.99), the German stock market general index, which comprises shares of the 110 largest and most liquid companies, is always more profitable than the index that selects ESG criteria.

Comparative performance of the HDAX index and the Dax 50 ESG in the period from January 2018 to July 2021

FIGURE 3



Source: Own compilation based on data from Bloomberg.

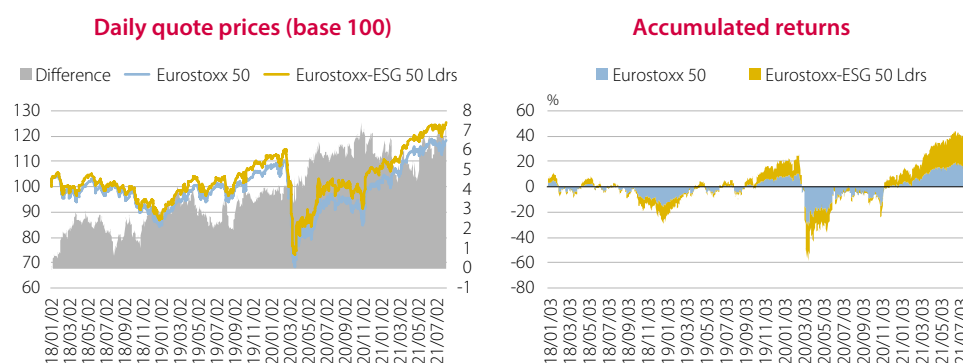
46 The HDAX index, managed by Deutsche Börse AG, contains all the companies that make up the Dax indices (containing the 30 largest and most liquid companies on the German market), MDAX (includes the 50 companies with international transparency standards that are located immediately below those included in the Dax index, excluding the technology sector) and TecDAX (comprising 30 shares of the main technology sector companies in Germany also trailing those that make up the Dax in terms of earnings and market capitalisation).

47 The universe for the Dax® 50 ESG index is the HDAX index. This includes the 50 largest and most liquid stocks on the German market that meet certain ESG criteria.

However, this outperformance by the general indices does not occur in all cases. If the daily quote prices and accumulated returns from the beginning of 2018 to August 2021 are compared, the Eurostoxx-ESG Leaders 50 index⁴⁸ outpaces the general Eurostoxx 50 index⁴⁹ in almost the entire period analysed.

Comparative performance of the Eurostoxx 50 index and the Eurostoxx-ESG Leaders 50 in the period from January 2018 to July 2021

FIGURE 4



Source: Own compilation based on data from Bloomberg.

Table 8 presents the accumulated returns of the indices analysed at 1, 2 and 3 years.

Accumulated returns at 1, 2 and 3 years of the Ibex 35, FTSE 4Good Ibex, HDAX, Dax 50 ESG, Eurostoxx 50 and Eurostoxx-ESG Leaders 50 indices¹

TABLE 8

%	FTSE 4Good				Eurostoxx-ESG	
	Ibex 35	Ibex	HDAX	Dax 50 ESG	Eurostoxx 50	Leaders 50
1 year	-11.709	-12.264	-16.498	-19.150	-14.240	-11.564
2 year	4.325	2.533	7.226	1.038	8.683	12.392
3 year	-9.970	-9.859	9.333	5.544	2.126	8.152

Source: Own compilation based on data from Bloomberg.

¹ Initial reference date: 2 January 2018.

A recent study published by ESMA⁵⁰ also identifies some dispersion in the performance of the ESG indices to some extent as a result of the different composition of these indices and also of the different providers of ESG ratings, which, as noted in Section 5, tend to show a low level of correlation.

48 The Eurostoxx-ESG Leaders 50 index, managed by Stoxx Ltd, according to information published by its administrator, covers the world's 50 leading companies based on ESG criteria from 11 euro area countries (Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain).

49 The Eurostoxx 50 index, also managed by Stoxx Ltd, according to information published by its administrator, covers the 50 largest companies from 19 sectors based on capitalisation in 11 euro area countries (Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain).

50 The sustainable finance section of the ESMA report (2021a) contains an analysis of the performance of ESG indices.

However, demand for sustainable investment products is expected to remain strong so long as less polluting companies remain consistently more profitable for investors than polluting companies. Otherwise, investments based on sustainability principles could be particularly volatile during severe economic crises.

A study by Döttling and Kim⁵¹ looks at how retail investors' preferences for socially responsible investing respond to market distress and corroborates that funds with the highest sustainability ratings experience steeper drops in their inflows during times of stress, such as the COVID-19 pandemic. This suggests that there tends to be a shift away from sustainability among retail investor preferences in the event of economic shock, highlighting a source of weakness in the increasingly popular socially responsible investment market.

7 Conclusions

Climate and sustainability benchmarks have been called on to play a pivotal role in meeting the Sustainable Development Goals as drivers of the mobilisation of financial resources into an economy that is more resilient to climate change and consistent with the principles of sustainability.

Notable progress has been made in the area of regulation in recent years, especially in the EU, which is the leading jurisdiction in this subject. This regulation has boosted the growing demand for sustainable investment products. However, there is still a long way to go before the tools that are available to access financing for the transition become truly effective.

There is a need to include, with the appropriate incentives, small and medium-sized enterprises, to make progress on the standardisation and transparency of sustainability disclosures, to achieve the broadest and fullest implementation of the taxonomy for sustainable activities, to have reliable, comparable and easily accessible sustainability ratings in place, and to broadly improve our knowledge, monitoring and control of sustainability risks – both direct climate and transition risks and risks related to a transition that is too costly or not directed towards sustainability.

This will help benchmark indices to more effectively exercise the role they are called upon to play, helping to encourage markets to make an efficient allocation of capital to facilitate the transition to a more sustainable financial system.

51 Döttling and Kim (2020).

References and bibliography

Abanca Renta Fija Transición Climática 360, Fondo de Inversión. Prospectus. 23 July.

Alessi, L., Ossola, E. and Panzica, R. (2021). “What greenium matters in the stock market? The role of greenhouse gas emissions and environmental disclosures”. *Journal of Financial Stability*. Vol. 54. 31 March.

Bravo-Bosh, M.J. (2014). “La protección del medio ambiente en la antigua Roma”. *Notebooks of Roman studies. International Survey of Roman Law*, No. 42.

Bolton, P. and Kacperczyk, M.T. (2021). *Global pricing of carbon-transition risk*. 20 July.

CNMV (2021a). *Questions and answers on sustainability regulations applicable to financial products: Regulation 2019/2088 (SFDR) and Regulation 2020/852 (taxonomy)*. 1 June.

CNMV (2021b). *Public statement on the forthcoming application of Regulation 2019/2088 on sustainability-related disclosures in the financial services sector (cnmv.es)*. 18 February.

CNMV (2021c). *Strategic lines of the CNMV 2021-2022. 2021 Activity Plan*. 17 March.

Döttling, R. and Kim, S. (2020). “Sustainability preferences under stress: Mutual fund flows during COVID-19”. VoxEU & CEPR. 19 August.

European Commission (2018). *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions. Action plan: Financing sustainable development*. 8 March.

European Commission (2021). *Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions. Strategy for financing the transition to a sustainable economy*. 6 July.

ESMA (2020). *No action letter on sustainability-related disclosures for benchmarks*. 29 April.

ESMA (2021a). *Report on Trends, Risks and Vulnerabilities*. No. 1, 2021.

ESMA (2021b). “Fund portfolio networks: a climate risk perspective”. *ESMA Report on Trends, Risks and Vulnerabilities*. No. 1, p. 73.

ESMA (2021c). “ESMA calls for legislative action on ESG ratings and assessment tools”. 29 January.

ESMA (2021d). *Questions and Answers on the Benchmarks Regulation (BMR)*. Last update 29 July.

EU TEG (2019a). *Report on Benchmarks. Interim Report on Climate Benchmarks and Benchmarks' ESG Disclosures*. June.

EU TEG (2019b). *Handbook of Climate Transition Benchmarks, Paris-Aligned Benchmark and Benchmarks' ESG Disclosures*. 20 December.

Gómez-Yubero, M.J. and Palomero, M. (2021). "Status of the interest rate benchmark reform". CNMV. *Quarterly Bulletin 1/2021*, pp. 103 et seq.

Government of Spain (2020). "Long-term strategy for a modern, competitive and climate-neutral Spanish economy in 2050". 3 November.

IIA (2021). *Fourth Annual IIA Benchmark Survey*. 28 October.

ISDA (2021). "Overview of ESG-related Derivatives Products and Transactions". 11 January.

Joint Committee of the European Supervisory Authorities (2021). *Final Report on draft Regulatory Technical Standards with regard to the content, methodologies and presentation of disclosures pursuant to Article 2a(3), Article 4(6) and (7), Article 8(3), Article 9(5), Article 10(2) and Article 11(4) of Regulation (EU) 2019/2088*. 2 February.

Mazzacurati, J. (2021). "ESG ratings: Status and key issues ahead". *ESMA Report on Trends, Risks and Vulnerabilities*. No. 1, p. 105.

Red Eléctrica de España (2021). *The Spanish electricity system. Advance 2020*. 12 March.

Rodríguez de la Fuente, O. (2020). *Félix. Un hombre en la tierra*. Editorial GeoPlaneta.

United Nations (2015). Paris Agreement.

World Commission on Environment and Development. United Nations (1987). *Our Common Future: Brundtland Report*. 20 March.

Zeb and Morningstar (2021). *European sustainable investment funds study 2021: Catalysts for a greener Europe*.

