

# ENVIRONMENTAL, SOCIAL, AND GOVERNANCE

## SUMMARY REPORT 2023



European Stability Mechanism

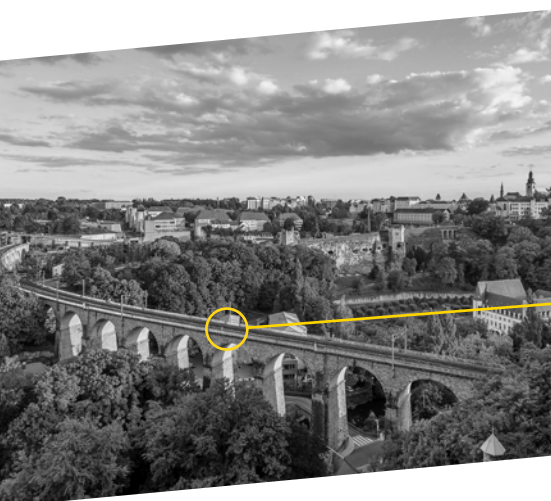




ENVIRONMENTAL, SOCIAL,  
AND GOVERNANCE

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SUMMARY REPORT  
2023



At a time when Luxembourg was rapidly developing its railway infrastructure, a viaduct that spans the Alzette valley in Luxembourg-city, the Pulvermuhl Viaduct (Biisser Bréck), was built. Constructed between 1859 and 1861, it opened along with the railway track one year later. In 2009, the construction of a second viaduct started to the west of the old one. It was inaugurated in 2019. The increased capacity of the lines facilitates railway traffic and contributes to reducing CO2 emissions.

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# Message from the Managing Director

24 June 2024



It is with great pleasure that I introduce our second edition of the European Stability Mechanism (ESM) summary report on environmental, social, and governance (ESG) activities.

Climate change has been ranked one of the top 10 key risks for the next two years by the World Economic Forum<sup>1</sup>. Therefore, the merits and urgency of ESG topics are key. Despite the challenging credit market conditions in 2023, worldwide issuance of green, social, sustainable, and sustainability-linked bonds totalled USD939 billion for the year, an increase of 3% compared to 2022.

The euro remains the dominant currency for ESG bond issues and represents close to 50% of the total ESG debt issued in 2023.

Even without the Covid-19 pandemic of 2020 or the current challenges to traditional sources of energy, ESG initiatives are a positive driving force that should lead to significant improvements in our societies. Without a sustainable economy, citizens' prosperity and financial stability are at risk.

The ESM continued to innovate and develop its ESG credentials in 2023.

For the last 12 years, the ESM's mission has been to help guarantee financial stability in the euro area. In 2023, climate change and social and governance conditions

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<sup>1</sup> [The global risks report 2024, World Economic Forum](#)

remained important challenges we at the ESM both face and on which we focus our attention.

The ESM published the ESG scores for its assets, including investments and loans, for the first time in last year's summary report. This year's report includes the ESG scores for both the ESM and European Financial Stability Facility (EFSF) balance sheets, as well as a historical perspective for our loans' ESG scores.

The release of the ESM's first transparency report by the United Nations (UN)-backed Principles for Responsible Investment marked another milestone in 2023. This report underscores our commitment to transparency, accountability, and responsible investment practices regarding the management of the ESM's entire paid-in capital. It is an important step in our efforts to enhance our responsible investment approach.

Furthermore, the ESM has begun integrating climate risk considerations into its risk management framework, ensuring that sustainability becomes increasingly relevant to the institution's analytical work.

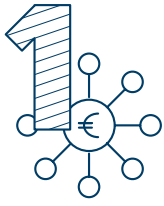
As a part of efforts to integrate ESG considerations into our investment framework, the ESM has been monitoring the ESG score of its paid-in capital since 2022. I am delighted to report that the ESM maintained the highest rating possible for our investment portfolio, as assessed by Moody's Vigeo Eiris. The ESM has also remained an active investor in ESG-labelled bonds with a total of €5.2 billion invested across green, social, and sustainable bonds at the end of 2023.

Witnessing the ESM's journey toward the integration of ESG considerations across the entire institution has been profoundly meaningful to me. As someone deeply devoted to fostering a more sustainable planet, I find great significance in the remarkable progress the ESM has made over the years. ESG principles have become an intrinsic part of the ESM's ethos, woven into its operational fabric.

Considering the growing interest from investors, policymakers, and the public in ESG matters, the objective of this report, in digital format of course, is to provide more insight into what the ESM is doing for Europe and the sustainability of our planet.



**Pierre Gramegna**  
Managing Director, ESM  
Chief Executive Officer, EFSF



## About the ESM



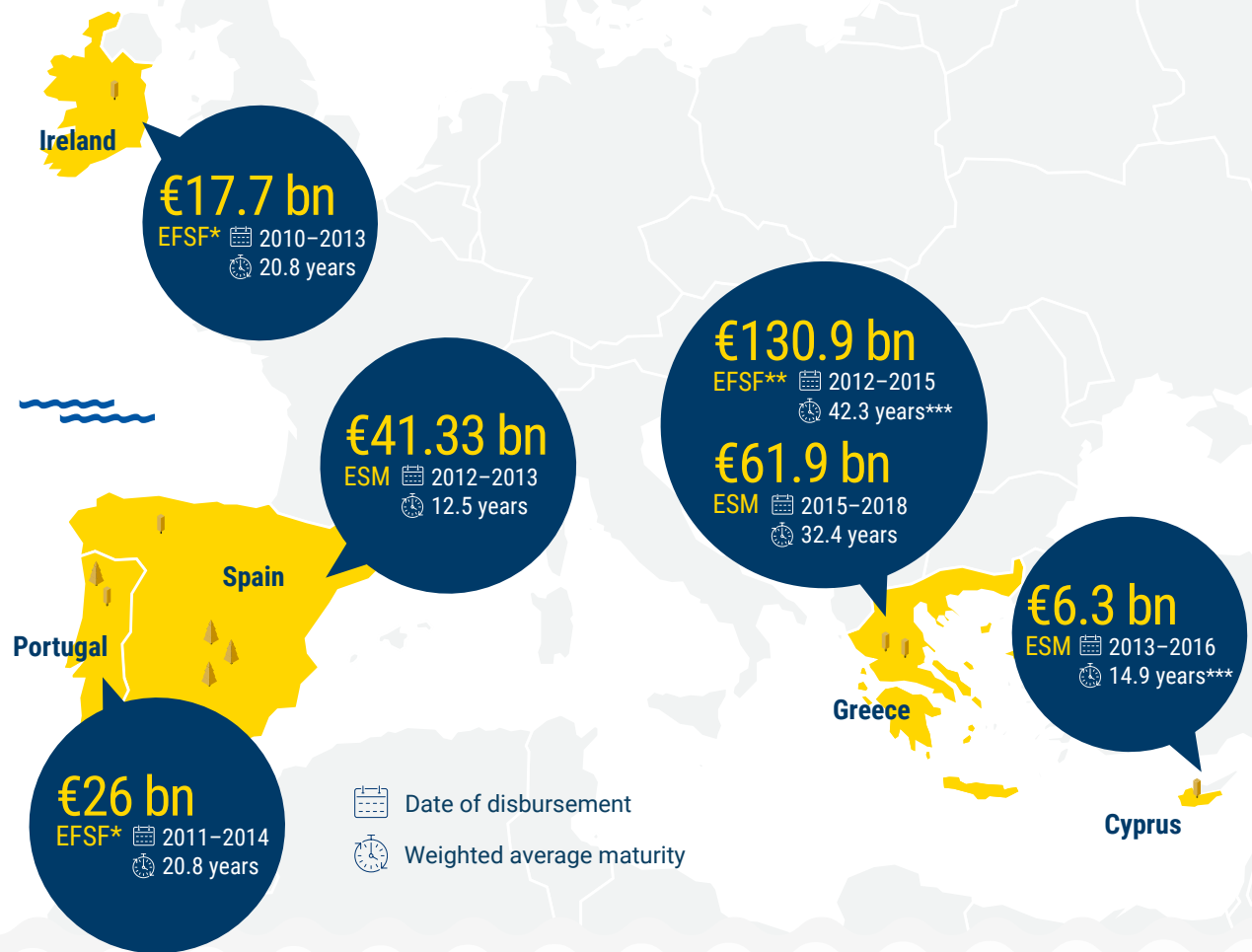
The ESM is an international financial institution established by the euro area member states as a permanent crisis prevention and resolution mechanism to safeguard financial stability within the euro area. The ESM provides various types of financial assistance with conditions that are in line with the instruments chosen by member states experiencing or threatened by severe financing problems. To finance this assistance, the ESM raises funds through the issuance of bonds, bills,

and commercial papers in the debt capital markets at competitive rates due to its solid capital structure and credit quality. As of 31 December 2023, the total ESM subscribed capital was €708.5 billion, out of which €81.0 billion was paid-in.

The funds raised in the markets are lent to ESM Member States who have lost market access and/or face financial difficulties. The EFSF, the ESM's temporary predecessor institution, provided support to euro area member states during the early stages



## ESM and EFSF loans



\* The nominal amount shown in EFSF financial statements and the programme database is the face value of the loans to be repaid by Portugal and Ireland. Certain amounts (e.g. margin and fees) were retained up front as cash reserve from the actual disbursements of the early EFSF loans. Those retained amounts, therefore, represent the difference from the disbursed amount, as presented on our [website](#).

\*\* The initial programme amount for Greece was €144.6 billion. This final amount is derived by excluding the undisbursed amount

of €0.95 billion of the private sector involvement facility as well as €10.93 billion and €1.81 billion instalments of the Master Financial Assistance Facility Agreement that have either been prepaid or not used respectively.

\*\*\* Following the implementation of the weighted average maturity extension as part of the medium-term measures in April 2019.

of the euro sovereign debt crisis. As of July 2013, the EFSF is not allowed to enter into new financial assistance agreements, and the ESM took over these tasks. The funding activity of both the EFSF and the ESM is centralised under the ESM Funding and Investor Relations team.

The ESM and EFSF have provided €295 billion in financial assistance to five countries: Ireland, Greece, Spain, Cyprus, and Portugal. The long-term loans and favourable interest rates have enabled

these countries to carry out necessary reforms that helped them return to market financing and economic growth. Such loans have also contributed to European integration and prosperity in the euro area and, together with the savings generated, have allowed member states' governments to restore economies, create employment, and become more resilient to external shocks.



# The ESM's ESG commitment

In response to increasing interest in ESG topics, the ESM began reporting on its ESG-related activities in 2018 and has since significantly broadened its approach to each of the three ESG pillars. The ESM remains committed to ESG-related practices and has therefore maintained ESG and climate change considerations as strategic priorities.

This ESG Summary Report, the ESM's second edition, offers further transparency on the institution's ESG efforts. The report covers the ESM's internal environmental efforts and ESG efforts within its investment and funding activities, along with climate risk management work.

## Contributions to EU initiatives on sustainable finance

Having become a signatory of the UN-backed Principles for Responsible Investment in February 2020, the ESM has achieved a milestone in its commitment to responsible and sustainable practices by completing its first [Principle for Responsible Investment transparency report](#). This first publicly available report offers stakeholders and the wider community insights into the ESM's

responsible and sustainable investment practices, as well as the institution's commitment to transparency and accountability.

To better inform, shape, and enhance ESG-related thought leadership and objectives in 2023, the ESM continued to communicate with credit- and ESG-rating agencies, as well as with investors, peer institutions, and policymakers.

The ESM also participates in policy discussions on the transition towards a low-carbon economy in Europe beyond its corporate efforts. An observer of the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) since 2022, the ESM contributes to the development and promotion of best practices aimed at strengthening environmental and climate risk management. A member of the International Capital Market Association's Social Bond Working Group since 2019, the ESM participates in various sub-working groups such as the Impact Reporting of Green and Social Projects and the Sustainability-Linked Bonds working groups. Moreover, the ESM is part of the European Commission's Platform on Sustainable Finance as an observer, participating in the work of the data usability subgroup.





## ESG ratings

### ESG considerations in credit ratings

Credit rating agencies increasingly include qualitative considerations on the ESG factors that could impact the creditworthiness of supranational issuers, like the ESM. These agencies, to a greater or lesser extent, have developed additional scoring criteria to better reflect the impact of ESG factors on their ratings.<sup>2</sup>

### ESG rating agencies

Investors and market participants predominantly rely on ESG rating agency assessments, given the complexity, wide range of data, and expert knowledge required to provide ESG scorings. These assessments provide useful information while following different methodologies, depending on

their focus; while some agencies focus on exposure to ESG risks (e.g. level of impact by and contribution to climate change, hence the lower score the better), others emphasise ESG own performance (e.g. impact on ESG activities, hence the higher score the better). Agencies can also prioritise ESG components differently. Given all these factors, the ESM maintains close contact with two major agencies: Morningstar Sustainalytics and Morgan Stanley Capital International (MSCI). Both the ESM and the EFSF receive unsolicited ESG scoring from MSCI and Morningstar Sustainalytics.

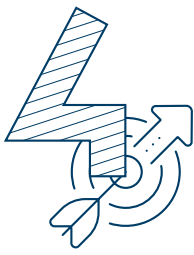
In 2023, Morningstar Sustainalytics assessed both the ESM and the EFSF at low risk of experiencing material financial impacts from ESG factors.<sup>3</sup> In 2022, both the ESM and the EFSF received an ESG rating of A (on a scale of AAA-CCC) from MSCI.<sup>4</sup>



<sup>2</sup> See Annex 1 for further information on the ESM's ESG credit rating impact.

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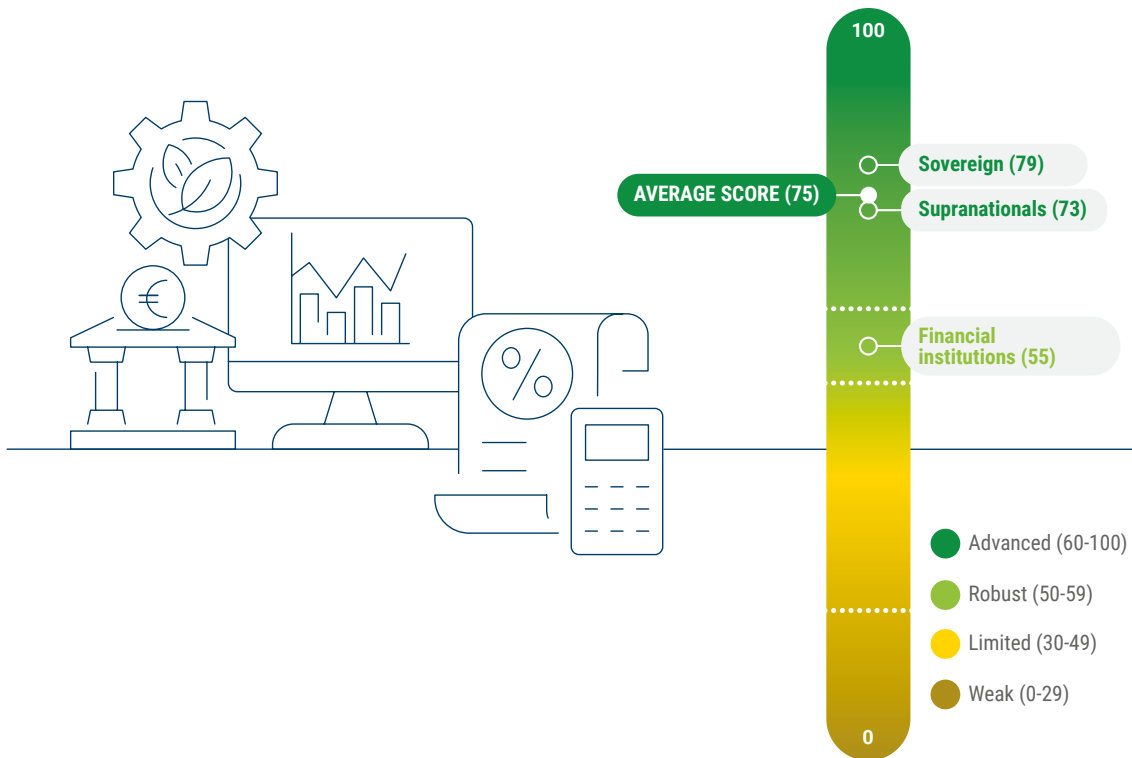
# Responsible investment

The ESM's first [Principle for Responsible Investment transparency report](#) in 2023 provides insights into how ESG considerations are built into the ESM's investment activities, as well as its policy and governance framework.

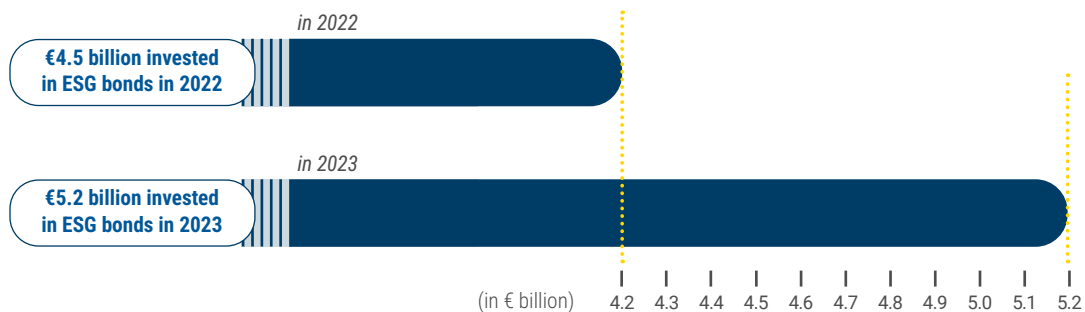
The ESM monitors the ESG score of its paid-in capital using Moody's Vigeo Eiris as the data provider. The

ESM's weighted average ESG score remained high at 75 out of 100 at the end of 2023, corresponding to Moody's advanced category, defined for scores between 60 and 100. The favourable score reflects the large allocation of the paid-in capital to bonds by sovereign and supranational issuers, associated with weighted average scores of 79 and 73 respectively. The financials category, representing covered bond

## Paid-in capital ESG score per issuer type



The ESM's ESG bond holdings



issuers, on average scores 55 (Moody's robust category, for scores from 50 and 60) and represents a smaller share of ESM's assets.

To compute these scores, the ESM applies the sovereign score on the aggregate exposure to all sovereign, sub-sovereign, and agency issuers from a given country. This approach ensures consistent methodology for all public sector issuers, despite significant differences in the domestic public financing systems across countries. It also overcomes some data limitations, because not all eligible issuers are

scored by the data provider. More information on the ESM's ESG scoring can be found in the [2022 ESM Annual Report](#).<sup>5</sup>

The ESM also increased its allocation into ESG-labelled bonds. At the end of 2023, the ESM held €5.2 billion of such bonds in marked-to-market terms, up from €4.5 billion in 2022. Of these, €5.1 billion were compliant with the International Capital Market Association principles and guidelines, with a predominant share dedicated to green bonds and the remaining amount evenly distributed between social and sustainability bonds.

<sup>5</sup> ESM enhances responsible investment by monitoring the ESG score of its paid-in capital, page 38.

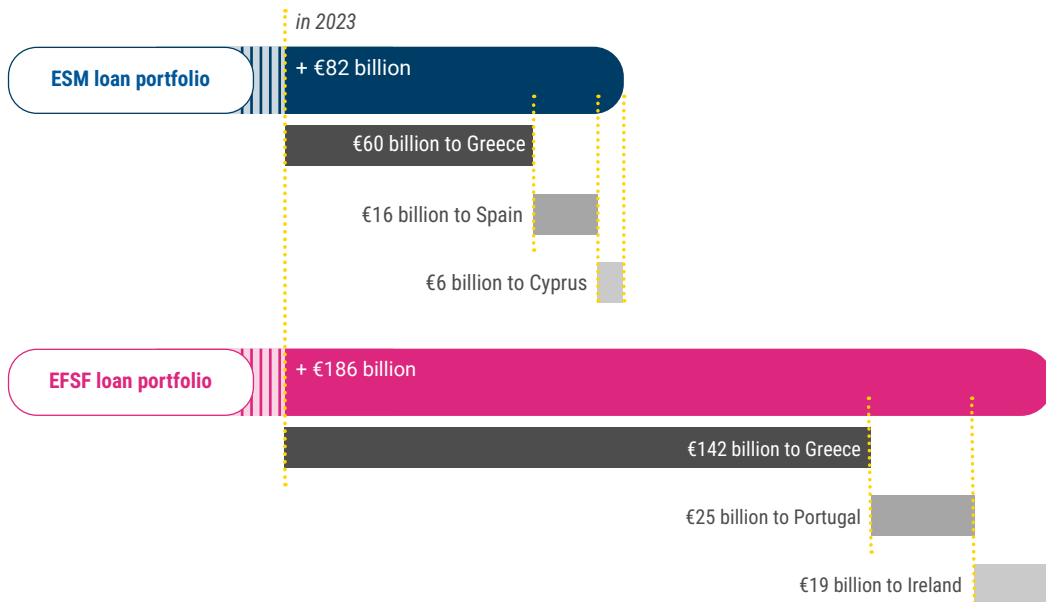


## ESG scoring of ESM assets and EFSF loans

Moody's scoring approach for the paid-in capital has been extended to the ESM and EFSF balance sheets' total assets, including outstanding loans to euro area member states. As of end-2023 the ESM's loan portfolio amounted to €82 billion, comprising €60 billion to Greece, €16 billion to Spain, and €6 billion to Cyprus. For the same period, the EFSF loan portfolio stood at €186 billion, with €142 billion provided to Ireland, €142 billion to Greece, and €25 billion to Portugal.

Applying Moody's ESG sovereign scores to the loan portfolios for these countries, the ESM and EFSF obtained a weighted average score of 72 and 71, respectively. These scores place them in Moody's advanced category, a strong starting point for measuring the ESG performance of ESM and EFSF loans. The weighted average score for the ESM assets, combining the loans and paid-in capital investments (excluding cash), remains in the advanced category with a score at 73. The ESG scores for the assets held by the ESM and EFSF generally demonstrate strong ESG performance.

### The ESM's loan portfolio

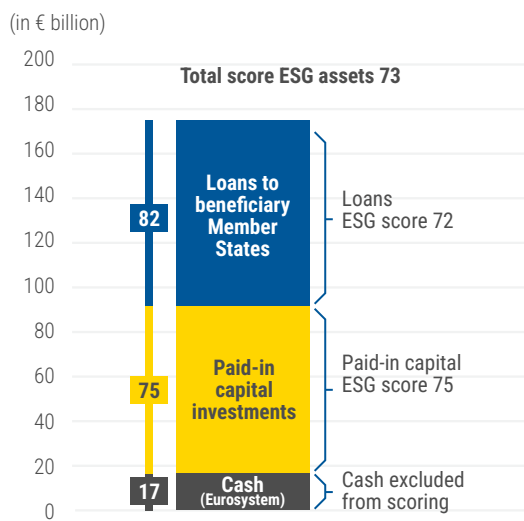


Moody's scoring is based on a balanced weighting of the three ESG dimensions to measure the degree to which entities consider and manage material ESG factors. For sovereigns, the scores capture a wide range of factors. The environmental category

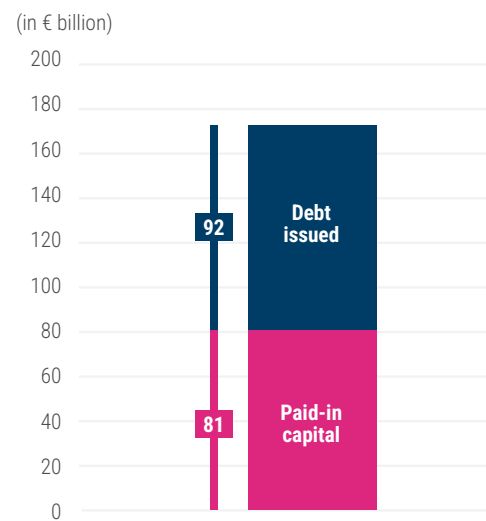
considers the transition to green growth, climate change mitigation, the reduction of carbon emissions, the protection of water resources, and biodiversity. The social category considers the promotion of education, health, social protection, gender equality,

**ESM** ESG scoring of ESM assets

**Assets**

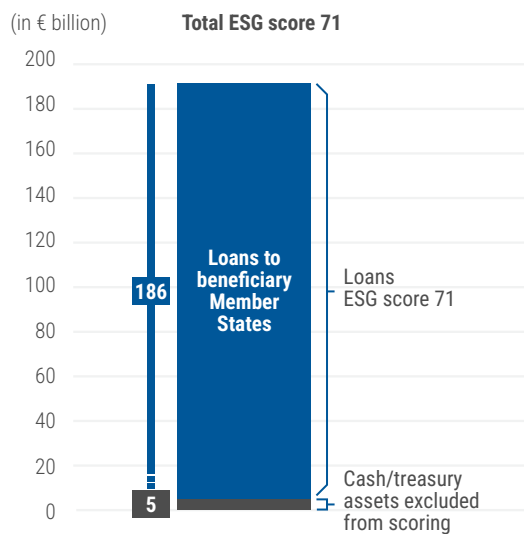


**Liabilities/Equity**

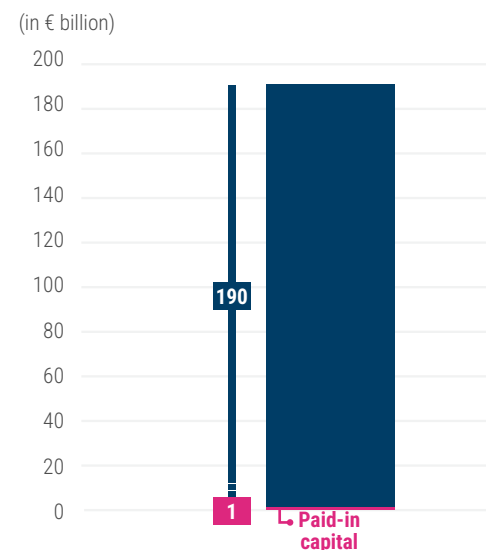


**EFSF** ESG scoring of EFSF assets

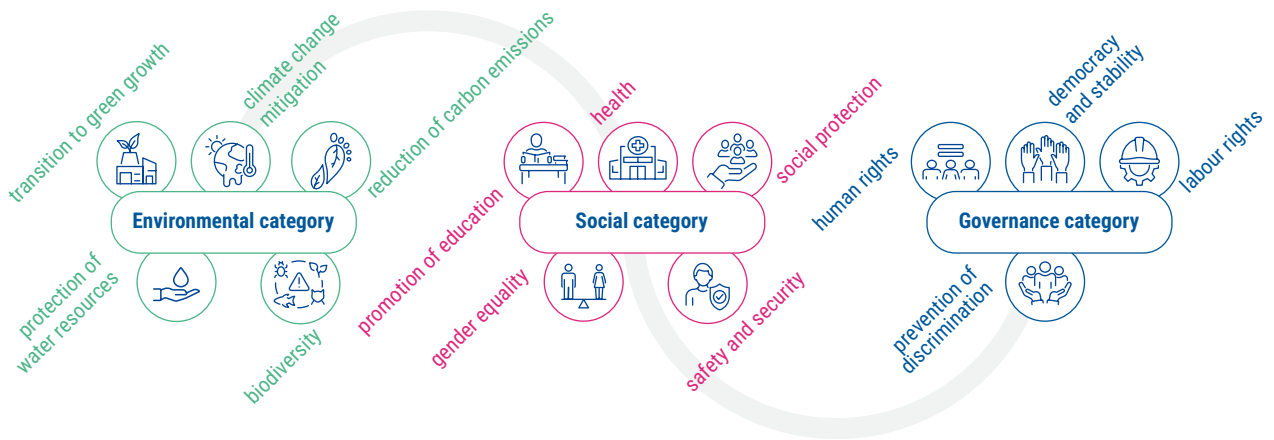
**Assets**



**Liabilities/Equity**



Moody's ESG dimensions



and safety and security. The governance category considers the respect of human rights, democracy and stability, labour rights, and the prevention of discrimination. Similar elements are assessed for supranational issuers and financial institutions, with some differences in how the different inputs are weighted and a stronger focus on business practices.

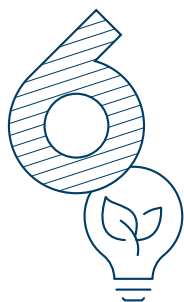
A historical review was performed to recreate the ESG profile of ESM and EFSF loans for 2018–2022. Using Moody's methodology, ESM loans garner an average ESG score of 72, well into the advanced

category. Analysing further each of the three ESG dimensions of the total score, ESM loans obtained the highest scores in the governance category, with an average score of 81, followed by the environmental category with an average of 67 and the social category with an average score of 65. The EFSF historically presents slightly lower ESG loan performance, averaging a score of 70. For the EFSF, governance averaged a score of 80, social a 62, and environmental a 66. Overall, all scores, including the three components, rank in Moody's advanced category.

ESG profile of ESM and EFSF loans for 2018–2022







## Funding at the ESM and EFSF

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The integration of ESG considerations across the institution reflects the ESM and EFSF approach to the market and its investors. Since the expansion of ESG topics into debt capital markets, there has been a surge in the development of ESG products to meet the demand for green, social, and sustainable bonds.

The evolution of the ESG market has led to different approaches in how issuers and investors make their funding and investment decisions. While there is still a substantial focus on labelled product assessment (use of proceeds product approach), there is also a growing trend to take a wider perspective and focus on a global sustainable strategy at an institutional level (holistic approach).

### **The ESM's holistic approach**

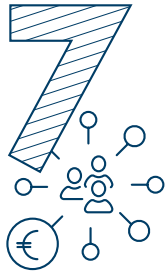
The ESM has a holistic approach in its ESG strategy, sustained by its social mission to contribute to financial stability. Therefore, our loans can be considered for the public good, and hence the ESM as a public institution with a social mandate.

To that end, the ESM funding and investor relations

activities focus on increasing communication on its ESG efforts with investors, as well as other external counterparts like rating agencies.

The ESM has taken various actions to follow a holistic approach by integrating ESG considerations into the full balance sheet, covering all areas and activities.

The ESM remains flexible and ready for the design of specific labelled programmes. Its social bond framework, developed during the Covid-19 pandemic to finance its Pandemic Crisis Support credit line, proved the ESM was well equipped for mandates requiring or allowing dedicated use of proceeds financing. This framework, maintained between June 2020 and December 2022, was compliant with the four components of the International Capital Market Association's social bond principles: (i) use of proceeds, (ii) project evaluation and selection, (iii) management of proceeds, and (iv) reporting. In connection with this expired framework, the ESM received an independent Second Party Opinion from Morningstar Sustainalytics, which positively assessed the alignment of the framework with the four social bond principles.



## Research on the macroeconomic and social impact of ESM financial assistance

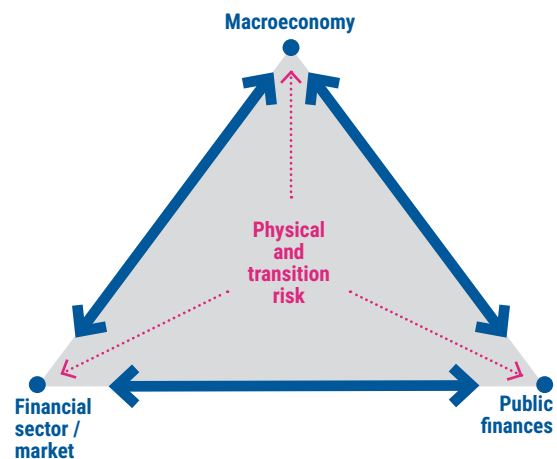
The ESM is continuously improving its understanding of financial support programmes, embarking on research and analysis to better inform its future work.

With concerns about rising inequality and the need to support vulnerable groups during crises, the ESM has begun research on the social and distributional consequences of its past financial assistance programmes. Using advanced statistical methods and restricted microeconomic data, the project assesses income developments across different social groups. A cross-country comparison helps identify best practices and measures that mitigate increases in poverty and inequality. Sharing lessons learned supports the community of international institutions in delivering on the promise to tackle challenging times.

The ESM is also investigating the impact of governments' capacity to implement reforms to set their economies on a better path. In reaction to independent [recommendations on its financial assistance](#), the ESM strives to better understand risks related to countries' institutional capacity constraints. During the past programmes, national administrative capacity constrained reform implementation at the country level. To boost its expertise, the ESM has developed a dedicated tool to analyse institutional vulnerabilities such as weak regulatory environment potentially translating into economic risks. It also started engaging with more specialised international and European peers to boost its analysis in the area.

To better understand how climate-related risks pose challenges to economic activity, public finances,

### A structured approach to analysing climate physical and transition risk



and the financial sector, the ESM has developed a strategy to incorporate climate-related risks in its monitoring framework.

This contributes to its mission to help countries avoid and overcome financial crises and maintain financial stability and prosperity.<sup>6</sup> In 2023, with a view to strengthen the risk assessment capacity of its regular Early Warning System exercise, created to detect loan repayment risks and allow for corrective action, the ESM completed a pilot climate-risk analysis for one of the beneficiary Member States. The ESM is considering gradually extending such analysis to all other beneficiary Member States, conditional on data availability. Indeed, when countries face both climate change

<sup>6</sup> See also Matthieu Bellon, Martin Iseringhausen, and Bernhard Mayr, "[Assessing climate risks at the ESM](#)", ESM blog, March 2024.

and economic vulnerabilities, such as high debt-to-GDP ratios, integrating climate risk assessments is particularly relevant for the ESM. The ESM's analysis of climate-related risks leverages existing work, including the work of other international organisations and networks. For example, the ESM regularly participates in the NGFS meetings and closely collaborates with external experts to support its climate risk assessment work and contribute to building institutional expertise.

The ESM is also actively contributing to good governance in Greece. In partnership with the Greek authorities, the ESM supports the Hellenic Corporation of Assets and Participations (HCAP) (cf. dedicated box below) that aims to unlock untapped value in state-owned companies to modernise the Greek economy. The partnership started during the financial assistance programme for the country and continues today.

## A partnership for good governance and value creation

The ESM has played an important role in the creation and monitoring of HCAP, whose mission is to support good governance in the Greek economy. The idea for HCAP developed during the sovereign debt crisis, shedding light on the poor performance of many of the country's state-owned enterprises. These companies play a large role in the Greek economy in important sectors such as public transportation, utilities, real estate, and infrastructure. A lack of transparency, vested interests, and mismanagement generated significant financial losses in many of these companies, burdening the public purse and stymying potential economic growth and the creation of new jobs in Greece.

### The inception

As part of its ESM financial assistance programme, the Greek government created a new holding company, HCAP, to manage state-owned enterprises and real estate to increase their value and performance. HCAP's governance structure<sup>7</sup> was set up to depoliticise the management of these assets and increase transparency and accountability.

It operates at arm's length from the state, with the state as the sole shareholder that can give periodic high-level guidance. The supervisory board appoints the members of the board of directors and approves the company's annual financial results. The ESM and the European Commission jointly appoint two out of the five members to this board.

HCAP also guarantees the ESM loans to Greece. The

ESM participates in regularly monitoring HCAP's activities and performance, under the Financial Assistance Facility Agreement with Greece and the ESM's Early Warning System.

### The portfolio

HCAP has three direct subsidiaries: a privatisation fund, a real estate management company (called ETAD), and a bank recapitalisation fund (HCAP does not exercise practical supervision over the bank recapitalisation fund). It also has a portfolio of stakes in companies active throughout the Greek economy, including the Public Power Corporation, Athens International Airport, Hellenic Post, and the Athens metro.

### The first successes

To shift from stagnation to performance, the portfolio companies began paying dividends and preparing business plans, in some cases for the first time ever. HCAP began publishing audited financial statements and has now paid dividends to the Greek state, helping reduce public debt and boost domestic investment. HCAP has increased the impetus for its portfolio companies to invest more, improve their products and services, and generate more value overall.

HCAP's role in appointing and monitoring board members of portfolio companies has helped improve performance. Notable achievements include reaching breakeven at Athens' public transport company, overcoming

<sup>7</sup> HCAP was set up to reflect the Organisation for Economic Co-operation and Development's Principles of Corporate Governance of State-Owned Enterprises, widely recognised as the international benchmark for good governance practices.

longstanding infrastructure problems at the Corinth Canal, and improving financial performance and production capacity at Greece's salt works. HCAP also highlighted areas in need of strengthening, such as internal audit functions and sustainability reporting.

HCAP approves the annual budgets of portfolio companies and business plans, a task previously done by line ministries, to increase the flexibility in procurement and executive hirings compared to other state-owned companies.

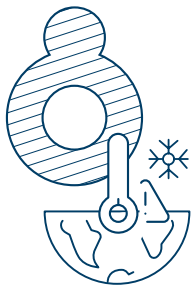
### **Into the future**

HCAP is strengthening its own accountability and transparency by better measuring the commercial impact of its work. For example, HCAP has given the impetus to start a large-scale valuation exercise in its portfolio

company ETAD, a major real estate owner in Greece. This exercise will ultimately help identify new commercial opportunities for the company.

HCAP is also overhauling its procedures to monitor and systematically assess the performance of board members of portfolio companies. Enhancing its own risk management and investment functions are also near-term priorities.

Cooperation between the ESM, the European Commission, the European Central Bank and HCAP demonstrates how institutions can join forces with a country to improve the governance of state-owned enterprises to the ultimate benefit of citizens and businesses. HCAP has made significant progress since its inception, and the ESM is committed to supporting HCAP's mission and to contributing to the sustainable growth and stability of the Greek economy.

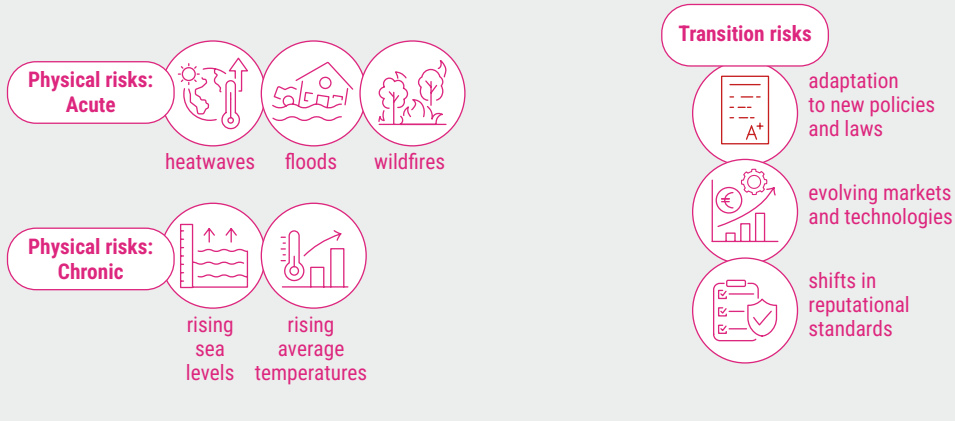


# Integrating climate risk into the ESM's risk management framework



**Physical risks** arise from changes in weather and climate that impact economies and are distinguished into two categories, acute and chronic. Acute risks are related to extreme weather events such as heatwaves, floods, wildfires, etc., while chronic risks are more long-term and associated with the gradual shifts in climate such as rising sea levels or average temperatures.

**Transition risks** stem from changes implemented to move towards a more sustainable low-carbon economy. Transition risks may include adaptation to new policies and laws, or evolving markets and technologies, or shifts in reputational standards.



To better understand its exposure to climate-related risks, in 2023 the ESM began incorporating climate considerations into its risk management framework as part of the institution's longer-term sustainability goals. As part of these efforts, the ESM conducted a pilot materiality assessment on the potential effects of both physical and transition risks on the ESM's investment portfolios and counterparties. This exercise produced a list of issuers and instruments most likely exposed to climate risk for further analysis. As a next step, the institution is working on better capturing the ESM's long-term exposure to climate risks through scenario analysis. Under this materiality assessment, Risk Management follows an 'outside-in' perspective by considering the impact

of climate change risks on the ESM's investments. The ESM will perform this material exposure assessment regularly as part of its annual review process and the UN-backed Principles of Responsible Investment reporting. The in-house approach is based on in-depth research that builds upon the latest literature, data sources, and methodologies. The materiality assessment methodology will be updated as relevant guidelines, counterparty-level data, and other best practices become increasingly available. This methodology is formalised in an internal operating procedure that documents the approach, roles, and responsibilities of ESM's Risk Management for this process.

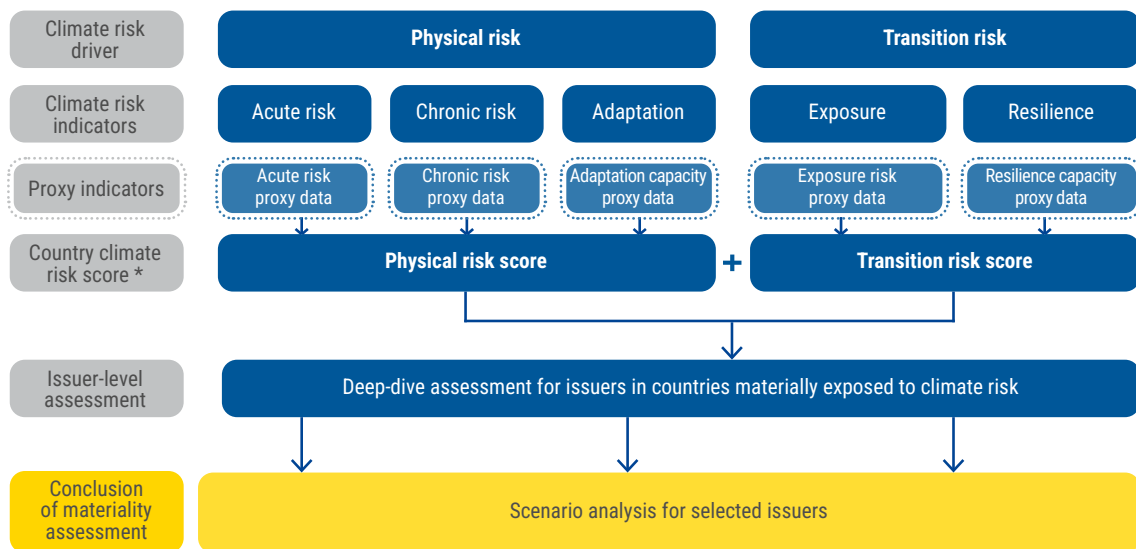
### Materiality assessment methodology

The ESM reviewed the current literature on climate risks to identify the types of financial risks most relevant to the institution’s activities, setting the scope to assess how climate change effects may impact its investment activities across five categories of risk (credit, market, operational, reputational, and liquidity). It is important to note that financial assistance risks associated with lending to beneficiary Member States are out of scope. Based on these criteria, the scope was refined to the ESM’s investment portfolios and counterparty credit exposures, with the hope to expand the climate risk assessment to other forms of traditional financial risk in the future.

Due to existing limitations in climate risk data at issuer level, the ESM developed an in-house methodology to compute country climate risk scores. These scores capture a country’s physical

and carbon transition exposure and resilience. Scores are derived through a relative ranking of different climate risk indicators (see chart below).<sup>8</sup> A materiality threshold defines those countries that are relatively more impacted by physical and transition risks. Issuers from the identified countries are further assessed via climate risk scenario analysis. The materiality assessment aims to build institutional knowledge and capacity to monitor the impact of climate risks on the ESM’s investment portfolio. The ESM’s investment portfolio includes only highly rated countries and issuers, that have strong mitigation and adaptation capacity to climate change. A regular review of the country climate risk scores and methodology for the materiality assessment will be performed to take into account evolving guidelines and market best practices.

#### Overview of 2023 pilot ESM materiality assessment methodology



\* Country climate risk scores are calculated for countries in the ESM’s investment portfolios.

<sup>8</sup> For physical risk, indicators are provided by the Inter-Agency Standing Committee Reference Group and European Commission. For transition risk, indicators are produced by the University of Notre Dame, the World Economic Forum, and the World Bank in collaboration with University College London.



# ESG aspects of the ESM's operations

## Environmental considerations

In the spirit of ESM's increased environmental commitment, a high-level internal ESG-focused strategic steering committee coordinates and implements cross-divisional ESG activities. The group includes members of the Management Board and provides guidance to a working-level ESG liaison group.

The ESM monitors, measures, and reports on the environmental impact of its internal operations to enhance environmentally friendly practices and the use of natural resources. The ESM published its fifth carbon footprint report in September 2023, which registered a decline in emissions compared to its 2018 base year – albeit the emissions were higher than in 2022 – largely the result of phasing out Covid-19 related restrictions on office presence and staff travel. Another factor was the widened reporting scope that added new emission categories to generate more transparent reporting in carbon methodology.

The ESM has also introduced sustainability considerations into its procurement and travel

policies to formalise such criteria in the underlying activities addressed by these policies.

For a detailed overview of the environmental measures implemented so far, please refer to the latest published [2022 carbon footprint report](#).

## Social responsibility

The ESM is tasked with safeguarding financial stability in the euro area, demonstrating the social responsibility of its mandate.

With view to its internal activities, the ESM ensures that its conduct is in accordance with the highest standards of professional ethics and integrity. The ESM's [Code of Conduct](#) requires staff to perform their duties in a manner that safeguards and enhances the public confidence in their integrity and that of the ESM.

The ESM ethical standards as reflected in the Code of Conduct are reviewed and amended periodically to ensure that they are in line with best practice. The ESM compliance function monitors compliance with the Code of Conduct as well as other policies,

### The ESM behavioural framework



**CARE**  
Foster an inclusive, safe, and respectful environment



**DEVELOP**  
Seek to adapt, grow, and develop self and others



**SHARE**  
Effectively communicate and collaborate



**THINK BROADER**  
Develop big picture thinking and explore new ways



**THRIVE**  
Proactively take ownership and drive towards our success

including the [Whistleblower and Witness Protection Policy](#), the [Policy on the Prevention of Money Laundering, Terrorism Financing and Sanctions Violations](#), and the Information Barriers Policy. The ESM launched its revised behavioural framework in 2023 to reinforce its culture of integrity, respect, accountability, and non-discrimination. To ensure equitable employment conditions, the ESM appointed an independent external party in 2023 to identify any internal equity or gender pay gap issues. The analysis confirmed that no corrective action had to be put in place. Nonetheless, the ESM will continue monitoring and strengthening its processes to ensure internal equity and compliance with the requirements for non-discrimination contained in the ESM [By-Laws](#) (article 18.5).

In 2023, ESM also reinforced its commitment to diversity and inclusion by signing the Luxembourg Diversity Charter and organising dedicated events that promote these values. These institutional initiatives were complemented by activities organised by staff-led groups. The ESM also actively supports the health and wellbeing of its staff by offering flexible working arrangements, including parental leave and unpaid leave to care for family members. Lastly, the ESM maintains regular and constructive social dialogues with the staff-elected representatives. Independent bodies are in place to hear, assess, and judge staff employment matters,

as needed. Learn more on our dedicated webpages about [how we work](#).

## Importance of governance

The ESM boasts a robust governance framework that ensures accountability and transparency towards its shareholders and other stakeholders. The governing bodies consist of the Board of Governors and Board of Directors, with the Managing Director being appointed by the former. To ensure accountability, the ESM has three further layers of audit oversight. This includes the independent Board of Auditors appointed by the Board of Governors, along with an internal and external audit function. The ESM actively maintains strong ties with its shareholders by engaging with them in various political forums, and conducting an annual Shareholder's Day where representatives from the finance ministries of all ESM Members are invited.

Regarding internal ESG activities, an ESG liaison group discusses, coordinates, and reports on internal ESG initiatives, with periodic reports to the management board for oversight. In addition, a high-level strategic Steering Group coordinates and guides the working groups in charge of cross-divisional ESG projects. They act as an internal forum for discussion and collaboration on current and upcoming ESG efforts.



# Annex 1

## ESG considerations in credit rating

### ESG credit rating impact on ESM

Moody's	<b>Credit impact score</b>	<b>Positive (Material impact on Rating)</b>	Very strong governance framework coupled with neutral-to-low exposure to environmental and social risks.	
	<b>ESG profile scores</b>	<b>Environmental</b>	<b>E-2: Neutral-to-Low</b>	Limited exposure to environmental risks, concentrated on its three sovereign borrowers (Greece, Spain, Cyprus). The risk management framework helps to mitigate these risks.
		<b>Social</b>	<b>S-2: Neutral-to-Low</b>	As the euro area's crisis-resolution mechanism, social considerations such as customer relations, responsible production or demographic and societal trends are not relevant to the ESM's credit profile.
		<b>Governance</b>	<b>G-1: Positive</b>	Robust risk management and good quality of management. A key feature is the ESM's Early Warning System which enables the ESM to rapidly call on additional capital from shareholders.
FitchRatings	<b>Overall ESG scale (relevance to credit rating)</b>	<i>Not a rating driver</i> 8 <i>Potential rating driver</i> 3 <i>Rating driver</i> 3 <i>Key rating driver</i> 1		
	<b>ESG scales</b>	<b>Environmental</b>	<b>Up to 2</b>	<b>Exposure to environmental impacts (score 2).</b> References to Asset quality, and Risk Management
		<b>Social</b>	<b>Up to 4</b>	<b>Human Rights, Community Relations, Access &amp; Affordability (Score 4)</b> References to Public Mandate, Credit Risk, Propensity to support <b>Exposure to Social Impacts (Score 4)</b> References to Credit Risk, non-performing loans, capitalisation, and Strategy <b>Labour Relations &amp; Practices (Score 2)</b> References to strong governance
		<b>Governance</b>	<b>Up to 5</b>	<b>Policy Status and mandate effectiveness (Score 5)</b> References to concentration credit risk, access to central bank refinancing <b>Rule of law and institutional &amp; regulatory quality (Score 4)</b> References to risk management policies and governance <b>Management Strategy and governance structure (Score 3)</b> References to business profile, strategy, and governance
S&P Global	<b>Qualitative assesment</b>	ESM facing increased scrutiny on its environmental and social impact, while structurally benefitting from shareholder support for its countercyclical role in supporting economies and livelihoods. The ESM strives to implement environmental, social, and governance best practices both for its corporate activity and footprint. This includes various policies and initiatives like consistent tracking of its carbon footprint and external certifications such as becoming a signatory of the UN principles for responsible investments.		

# Annex 2

## ESM assessment of principal adverse impacts

While the ESM is not subject to the requirements of the EU's Sustainable Finance Disclosure Regulation, it has included a list of principal adverse impact (PAI), indicators that have negative, material or likely material effects, addressed by the various ESM activities for information purposes.

Thematic Scope	PAI #	Principal Adverse Impact Indicator	ESM
Greenhouse gas (GHG) emissions	PAI 1	GHG emissions (Scope 1,2,3 and total)	<p>The ESM prepares its carbon footprint report in accordance with the International GHG Protocol. Additionally, teleworking-related emissions are estimated based on the EcoAct 2020 Emissions Whitepaper.</p> <p>Scope 1,2, and 3 have been calculated since 2018 and are publicly reported on the ESM website. Results are internally used to put action plans in place.</p>
GHG emissions	PAI 2	Carbon footprint	<p>The ESM is in the process of developing its sixth carbon footprint report.</p> <p>The ESM registered that total emissions have more than halved, declining by 53.8% in net terms and 51% in gross terms compared to the base year (2018). This, in part, is driven by reduced office presence due to the pandemic and in part by emissions-cutting measures in day-to-day operations.</p> <p>The ESM's total GHG emissions for 2022 amounted to 573.5 metric tonnes (t) of CO<sub>2</sub>e (tCO<sub>2</sub>e) on a gross basis and to 501.3 tCO<sub>2</sub>e on a net basis. Compared to 2021, both net and gross emissions have nearly doubled. This is driven by the increase in mobility-related activities due to relaxed Covid-19 restrictions and the inclusion of new categories that were not in scope in previous years. Read more in the ESM <a href="#">Carbon Footprint Report 2022</a>.</p>

Thematic Scope	PAI #	Principal Adverse Impact Indicator	ESM
GHG emissions	PAI 4	Exposure of companies active in the fossil fuel sector	<p>"Companies active in the fossil fuel sector" refers to companies that derive any revenues from exploration, mining, extraction, production, processing, storage, refining, or distribution, including transportation, storage, or trade, of fossil fuels as defined in Article 2(62), of Regulation (EU) 2018/1999 of the European Parliament and of the Council.</p> <p>The ESM does not have any economic activity in the fossil fuel sector.</p>
GHG emissions	PAI 5	Share of non-renewable energy consumption and production	<p>72.2 tCO<sub>2</sub>e, which accounts for 83.8% of electricity emissions, were derived from renewables evidenced through Guarantees of Origin. In 2022 the ESM has added 'shared building consumption' to the reporting scope, which resulted in 14 tCO<sub>2</sub>e net emissions from non-renewable electricity. The ESM is committed to decreasing its net emissions, aiming to cover its shared-building electricity emissions evidenced via Guarantees of Origin. However, minor net emissions are possible in the event of unexpected power outages as current building is backed by diesel powered generator (ESM report, 2022).</p>
Biodiversity	PAI 7	Activities negative affecting biodiversity sensitive areas	<p>The ESM does not have sites and or operations located in or near to biodiversity-sensitive areas. The ESM does not yet have a strategy towards conservation of biological diversity, including our upstream and downstream activities.</p>
Water	PAI 8	Emissions to water	<p>The ESM reduced its water consumption by 34.5% between 2021 and 2022 through various water conservation measures. This reduction was also an effect of reduced staff office presence in light of the pandemic, compared to the 2018 base year, water-related emissions have decreased by 86.6%, both on a gross and net basis.</p> <p>Additionally, after the ESM's annual carbon footprint methodology review, the ESM changed its water emissions methodology for 2022, moving away from relying on invoices for consumption figures to using water meter readings instead (ESM Carbon Footprint Report, 2022).</p>



Thematic Scope	PAI #	Principal Adverse Impact Indicator	ESM
Waste	PAI 9	Hazardous waste and radioactive waste ratio	<p>The ESM has shown the evolution of the breakdown of emissions and weight of waste generated by ESM activities within its carbon footprint reports. Hazardous waste in ESM's carbon footprint report is defined as polystyrene, plastic waste, high-density polyethylene bottles, and various bulky waste objects. The ESM has reduced it from 60% in 2020 to 23% in 2022.</p> <p>The waste generated by the ESM activities continue to represent a minor source of ESM building-related emissions, accounting for 0.5 tCO<sub>2</sub>e on both gross and a net basis. For the calculation of emissions resulting from polystyrene and plastic waste (i.e. hazardous waste), Bilan GES (Ademe) was used as a conversion factor.</p> <p>The ESM does not have any radioactive waste.</p>
Social and employee matters	PAI 10	Violations of UN Global Compact principles and Organisation for Economic Co-operation and Development (OECD) Guidelines for Multinational Enterprises	<p>The ESM is not currently a signatory of UN Global Compact principles and OECD Guidelines for Multinational Enterprises. The ESM does not invest in companies.</p> <p>The ESM has not been involved in violations of the UN Global Compact principles or OECD Guidelines for Multinational Enterprises.</p> <p>Nevertheless, with view to its suppliers the ESM may exclude candidates from participation in procurement procedures at any time if they are in breach of applicable environmental, social, or labour law obligations established by European Union law, national law, collective agreements, or the international social and environmental conventions listed in Annex X to <a href="#">Directive 2014/24/EU</a> of the European Parliament and of the Council, or any other applicable legal obligations as emphasised under Article 9.13 in the <a href="#">ESM Public Procurement Policy</a>.</p>

Thematic Scope	PAI #	Principal Adverse Impact Indicator	ESM
Social and employee matters	PAI 12	Unadjusted gender pay gap	<p>Gender equality and equal pay for work of equal value are fundamental principles at the ESM. The ESM By-Laws explicitly require that the recruitment, employment, classification, training, promotion, and career development of ESM staff shall be made without discrimination. The ESM is committed to building a culture that is genuinely inclusive, which empowers all its members of staff to thrive and feel they belong to the organisation, and which rewards them based on merit.</p>
Social and employee matters	PAI 13	Board gender diversity	<p>See our website for information on the <a href="#">ESM's Management Board</a> composition. ESM is committed to maintaining a work environment free from violence and harassment. Around 50 nationalities are represented within the ESM staff, of which 60% are men and 40% are women. The ESM institutional initiatives promoting diversity and inclusion are complemented by activities organised by an employee-led resource group.</p>
Social and employee matters	PAI 14	Insufficient whistleblower protection	<p>The ESM is committed to a culture of professionalism, integrity, respect, accountability, and non-discrimination, and to fostering and maintaining a work environment characterised by these values. It is committed to, and actively supports, the right of members of staff to work in an environment free from misconduct, including integrity violations and behavioural misconduct, such as discrimination, harassment, bullying, and retaliation. The ESM's whistleblower and witness protection procedures are intended to safeguard this culture, and the ESM pursues all reasonable steps to protect whistleblowers and witnesses and ensure that they are not subject to retaliation. The ESM also raises awareness and understanding of misconduct.</p> <p>More information can be found under the ESM's <a href="#">Whistleblower and Witness protection policy</a>.</p>
Social and employee matters	PAI 15	Exposure to controversial weapons (antipersonnel mines, cluster munitions, chemical weapons, and biological weapons)	<p>The ESM is not involved in the manufacture, sale, or financing of controversial weapons (e.g. anti-personnel mines, cluster munitions, chemical weapons, and biological weapons).</p>

# Annex 3

## Sustainable development goals

While the ESM does not pursue a strategy focused on the alignment of Sustainable Development Goals (SDGs) through specific measurable objectives, the ESM finds it contributes to four SDGs due to its institutional values and the nature of its activities. The following table summarises the progress made on various initiatives and their contribution to each SDG listed.

SDG	ESG Area / Scope	Achievements / Progress
<b>SOCIAL</b>		
 <p><b>8</b> DECENT WORK AND ECONOMIC GROWTH</p>	Concerns about rising inequality and the need to support vulnerable groups during crises	Research on the social and distribution consequences of ESM's past assistance programmes. Additional Information: <a href="#">How programme evaluations can benefit from quality of life considerations</a>
	Impact of governments' capacity to implement reforms	Development of a tool to analyse sovereign vulnerabilities associated with institutional capacity and engaging with other peers to boost such analysis.
 <p><b>10</b> REDUCED INEQUALITIES</p>	Understanding impact of climate risk on financial stability	Development of a strategy to incorporate climate-related risks in the ESM's monitoring framework, contributing to its mission to enable countries avoid and overcome financial crises and maintain financial stability and prosperity. Additional Information: <a href="#">Assessing climate risks at the ESM</a>
	<b>GOVERNANCE</b>	
 <p><b>16</b> PEACE, JUSTICE AND STRONG INSTITUTIONS</p>	Fostering a culture of integrity, respect, accountability, and non-discrimination	Review of the ESM's behavioural framework to reinforce values that are in line with the ESM's culture. Additional Information: Social responsibility
	Ensuring equitable employment conditions	Appointment of an independent external party to identify any internal equity or gender gap. Additional Information: Cf. <a href="#">PAI #12</a>
	Diversity and Inclusion	Signature of the Luxembourg Diversity Charter and organisation of dedicated events to promote these values.
 <p><b>17</b> PARTNERSHIPS</p>	Contributing to good governance in Greece	Progress shown on the partnership with Greek authorities to support HCAP. Additional Information: Dedicated Box on <a href="#">page 14</a>
	Strengthening the Regional Financing Arrangements' (RFAs) cooperation	The ESM continues its efforts in RFA cooperation, participating in the 8th high-level RFA Dialogue. Additional Information: <a href="#">Press Release 10/10/2023</a>
	Inter-institutional cooperation on climate change	Collaboration with various institutions in the publication of a discussion paper: "Global efforts to fight the consequences of climate change: the role of RFAs". Additional Information: <a href="#">Publication of joint paper</a>
	Inter-institutional cooperation on climate risk	Strengthening our partnership with the NGFS to support the ESM's climate risk assessment work and contribute to building institutional expertise.

European Stability Mechanism



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