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Moody's 2023 ESG and Sustainable Finance Outlook

January 20, 2023



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Moody's published its 2023 Outlook – Macroeconomic challenges to exacerbate ESG credit risks on January 9, 2023, laying out various macroeconomic challenges it expects as a result of climate-related and other issues. Among other things, Moody's expects four trends from 2022 to continue having an impact on credit risk: (1) macroeconomic, financial, and geopolitical consequences from the pandemic and Russia-Ukraine conflict; (2) persistent challenges associated with access to and the affordability of basic services; (3) continued scrutiny of corporate decarbonization pledges; and (4) difficulties arising from a complex regulatory landscape for companies and issuers' governance capabilities across the credit cycle. It also expects that companies with high exposure to climate transition risk will set and endeavor to meet ambitious emissions reductions goals with more transparency and credibility. However, Moody's also concludes that the transition plans of non-financial companies most exposed to carbon transition risks are least likely to disclose ambitious and detailed plans, increasing the challenges these companies confront in light of anticipated regulatory and market scrutiny. In addition, the constantly shifting ESG regulatory framework and varying perspectives on disclosures and investing practices may further complicate compliance, especially for financial institutions. Lastly, as the exposure to and understanding of physical climate risks improves, so will investor focus on companies that face greater exposure—which may be intensified by increasing regulation of high-risk companies.

Taking the Temperature: Moody's predictions underscore the longevity of ESG-focused investing and also emphasize the credit risks that high-exposure companies and sectors will face in the future as they transition to a low-carbon economy. The inconsistent regulatory landscape and, in the U.S., politicized nature of climate change, complicate how companies approach governance and disclosure regarding sustainability and other ESG issues. Moody's Outlook succinctly summarizes what we have been observing and expect to continue in 2023.