Stronger Together

Exploring the EU Taxonomy as
a Tool for Transition Planning

December 2023

Contents

Foreword

As the first year that companies are legally bound to report under the EU Taxonomy, 2023 has seen an unprecedented goldmine of granular sustainability data released into the public domain. However, it's one thing to have access to this data, it's quite another to understand how to interpret and use it. In these pages we take on the challenge of unlocking this data for decision making – made possible by the addition of CDP's unique questions on sustainable finance taxonomies in its 2023 questionnaire and Clarity AI's advanced technology capabilities. The goal of this is to help unleash the potential of the EU Taxonomy to truly fulfil its mission to scale up sustainable investment in Europe and make the European Green Deal a reality.

In this report CDP and Clarity AI go beyond the surface to analyze the disclosures from around 1,700 companies, finding that there is more than meets the eye when it comes to Taxonomy eligibility and alignment. Our report makes a unique contribution, revealing how the EU Taxonomy can be used to support companies' transition planning and how investors should analyze that data to make truly informed sustainable finance decisions.

Of course, the EU Taxonomy is only one of dozens of sustainable finance taxonomies around the world against which global companies may need to report. Our hope is that the insights in this report can help inform the practical implementation of, as well as interoperability between other high-quality taxonomies. That is crucial to reduce fragmentation and increase global momentum towards a net-zero and nature-positive future.

Maxfield Weiss
Managing Director,
CDP Europe

Lorenzo Saa
Chief Sustainability
Officer, Clarity AI

Executive summary

EU Taxonomy: A powerful tool when used hand in hand with transition planning

This report explores the alignment of European companies' to the EU Taxonomy objectives of climate change adaptation and mitigation, in the first year the market has access to this granular data. It explores how Taxonomy eligibility and alignment are related to companies' greenhouse gas emissions and emission reduction targets. The conclusions point to a need to take a nuanced approach when interpreting Taxonomy data, and to put it in the context of a transition plan.

In 2023, EU Taxonomy alignment disclosures made unprecedented granularity in reported sustainability data accesible to financial markets. This report is the first to compare EU Taxonomy KPIs to existing indicators linked to corporate transition such as GHG emissions and science-based targets.

Taxonomy data reveal a company's current and potential future alignment with the net-zero transition - at the level of their economic activities that generate revenues or the activities towards which they direct their spending. To demonstrate how the Taxonomy can be used to support and mobilize investments towards the objectives of the European Green Deal, it is essential to understand how this activity-level information can inform entity-level transition.

Data from over 1,700 companies analyzed in this report shows that average numbers of eligibility and alignment hide large differences across and within sectors, both for revenues and capital expenditures. Additionally, the level of details provided by companies and their compliance with the official reporting templates varies, suggesting the need for further guidance and improvements in the quality of reported Taxonomy data. These points underscore the importance of taking a careful and nuanced approach when drawing general or sector-based conclusions from the first year of disclosures.

Our analysis finds no strong correlation between emission performance and Taxonomy revenue alignment, which means that EU Taxonomy alignment doesn't always equate to a company's position in the transition journey. Since companies with similar emission intensities can have varying levels of Taxonomy revenue eligibility and alignment, there is a need to contextualize this data within a company's transition plan. This report presents early-stage evidence from approximately 600 companies that already disclose on the EU Taxonomy in the context of transition planning when reporting to CDP, in the identification of revenues and spending aligned with their climate transition.

Indeed, considering forward-looking indications of corporate transition, we find that the approximately 300 companies in our analysis that have set science-based emission reduction targets (SBTs) demonstrate greater alignment of their capital expenditures, highlighting the value of the Taxonomy to evaluate companies' commitment to these targets.

To effectively leverage the EU Taxonomy going forward, companies, investors, and policymakers should use this tool in conjunction with transition plans

Recommendations for companies using the EU Taxonomy
1. Develop complete transition plans and adopt the EU Taxonomy as a tool to demonstrate and support the alignment of expenditure with decarbonisation targets.
2. Use the EU Taxonomy criteria to define the highest level of ambition for decarbonization actions, and the Taxonomy KPIs to support the financial planning associated with the overall transition strategy, which can lead to setting Taxonomy KPI targets when relevant.
3. Make an explicit link between actions taken to transition and their associated spending, thus helping to put Taxonomy KPIs into context[2].

Recommendations for financial institutions
1. For a more comprehensive view of climate performance, interpret Taxonomy alignment data in tandem with corporate emissions, targets, and other elements of corporate transition plans
2. Avoid using general or sectoral thresholds to benchmark Taxonomy KPIs unless activity-level clustering is applied.
3. Consider year-on-year observations to assess how decarbonization trends relate to alignment trends, when relevant to the company's transition.

Recommendations for EU policymakers
1. Develop and publish guidance to improve the market's understanding and interpretation of the Taxonomy at KPI and activity level.
2. Consider an extended version of the EU Taxonomy to improve the interpretation of what eligibility and alignment mean for real economy GHG emissions.
3. Monitor EU companies' decarbonization trends alongside Taxonomy KPIs over time to evaluate the success of the Taxonomy framework.

Introduction

This report is the first to compare EU Taxonomy KPIs to existing indicators linked to corporate transition

In 2023, the full disclosure of EU Taxonomy metrics in annual reports became mandatory for companies subject to the EU's Non-Financial Reporting Directive (NFRD). **Europe was the first region to make taxonomy disclosures mandatory for over 2,000 large public companies,** representing around €10 trillion of market capitalization, and close to 2 gigatons of direct greenhouse gas (GHG) emissions.[3] **This has resulted in a substantial amount of new sustainability-related data being made available to the market.** However, it is not yet clear how to interpret and utilize this data for decision-making, including within sustainable finance. Guidance published in the June 2023 sustainable finance package put forward by the European Commission[4] is a helpful source of ideas for practical applications, which should be further explored. Analyzing and understanding this new data will be vital to help companies, investors and policymakers leverage the Taxonomy going forward.

This report aims to contribute to the existing literature on the EU Taxonomy in multiple ways. **First,** at the time of this writing, **most publications analyzing EU Taxonomy disclosures were published before the finalization of companies' annual reports**, resulting in smaller sample sizes (ranging from 100 to 700 companies). Such existing papers generally found that alignment is low across all three key performance indicators (KPIs) - revenue, capital expenditures (CapEx), and operational expenses (OpEx), (OpEx); however, CapEx alignment tends to be higher than revenue, with highest numbers observed for the Utilities and Real Estate sectors[5]. **Those findings support the view that the EU Taxonomy can be used as a forward-looking transition tool**.

Starting with a much larger sample of approximately 1,700 companies, this report aims to confirm or challenge findings of previous reports analyzing EU Taxonomy disclosure

Meanwhile, some publications stress the low numbers for alignment without consideration for eligibility, which we believe leads to incomplete insights. **Starting with a much larger sample of approximately 1,700 companies,** this report aims to confirm or challenge some of these previous findings.

Second, most of the existing literature uses sector averages to depict eligibility and alignment behaviors. **This report challenges the use of averages and delves deeper into the differences within sectors.** Companies within similar sectors have multiple revenue streams and are involved in very different economic activities, which can explain this dispersion and suggests more granular clustering is required to enhance comparability. Varying interpretations of the regulation[6] can also be a driver of differences, which cast doubts on the comparability of information provided by companies in this first year of reporting.

Finally, **we aim to showcase how data providers can partner to expand their coverage and deepen insights.** This collaboration combines Clarity AI's expertise, which has collected one of the largest samples of NFRD reports to date, with the data and insights of CDP's global disclosure system. This approach places the EU Taxonomy within the broader context of corporate climate transition.

---
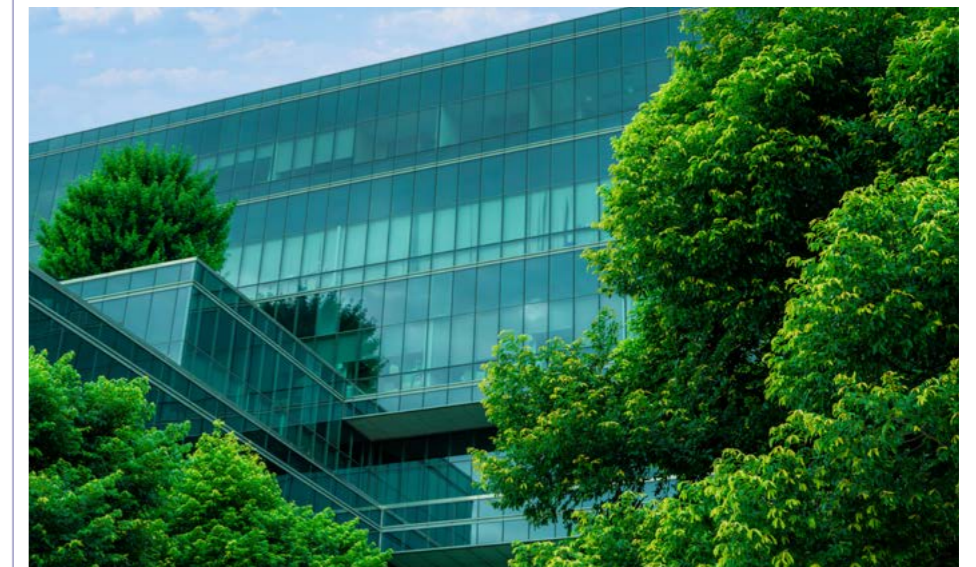
3 Market capitalization and Scope 1 GHG emissions figures refer to totals for companies in our sample.
4 https://finance.ec.europa.eu/publications/sustainable-finance-package-2023_en
5 Sources: PwC (2023 EU Taxonomy report), EY (EU Taxonomy barometer 2023), ESG Book (Challenging road ahead, 2023)

6 Source: We Mean Business Coalition 2023 white paper "EU Green taxonomy in practice"

Trends from the first year of EU Taxonomy reporting

CDP's role in the landscape of sustainable finance taxonomies

Sustainable finance taxonomies stand at the heart of efforts to propel the transition to a net-zero, nature-positive future, and serve as a fundamental pillar in policy packages seeking to drive capital allocation towards this objective.

While the EU Taxonomy remains one of most widely recognized public sustainable finance taxonomies, there are now over 50 different taxonomies in development globally, spanning public and private spheres. This proliferation introduces a notable risk, as highlighted in CDP's 2025 strategy, wherein fragmented taxonomies lacking compatibility may compromise their fundamental objectives.

Amongst the challenges impeding the successful global adoption and implementation of taxonomies, CDP's primary focus centers on the reporting requirements of taxonomy key performance indicators (KPIs). For taxonomies to effectively combat greenwashing, science-based technical screening criteria (TSC) must be coupled with reporting obligations against KPIs. These indicators not only empower stakeholders to monitor alignment over time but also demonstrate progress towards targets within credible transition plans.

Disclosures play a pivotal role in the practical implementation of taxonomies and their KPIs, necessitating legal and regulatory measures for seamless integration into the reporting landscape. Furthermore, taxonomies, coupled with their corresponding reporting systems, contribute to shaping credible transition plans by furnishing robust indicators of a company's sustainability and monitoring alignment over time.

CDP is actively exploring several critical areas regarding disclosures and taxonomy reporting requirements, including mandatory disclosures, international interoperability, transition plans, tracking credible disclosures, and capacity-building. Collaboration lies at the core of our approach to addressing these challenges. CDP acknowledges ongoing initiatives aimed at ensuring the international interoperability and success of taxonomies. Leveraging our disclosure platform, we are uniquely positioned to engage with jurisdictional and multilateral stakeholders, steering towards a globally harmonized approach to taxonomy-related reporting requirements, and embedding these in assessments of entity- and sector-wide alignment of progress towards the transition.

1

1. Trends from the first year of EU Taxonomy reporting

What is the EU Taxonomy?

The EU Taxonomy is a classification tool. It defines the set of criteria for how an economic activity can be aligned with an environmental objective.

The EU Taxonomy classifies economic activities along six environmental objectives[7]:
- ◣ Climate change mitigation
- ◣ Climate change adaptation
- ◣ The sustainable use and protection of water and marine resources
- ◣ The transition to a circular economy
- ◣ Pollution prevention and control
- ◣ The protection and restoration of biodiversity and ecosystems

Since January 2022, the regulation has been in force in the European Union for the first two objectives (climate change mitigation and climate change adaptation). The four additional new objectives have already been adopted by the European Commission and will be applicable from January 2024.

For the first two years of application, companies based in the European Economic Area[8] and in scope of the EU's Non-Financial Reporting Directive (NFRD)[9] have had to report on:
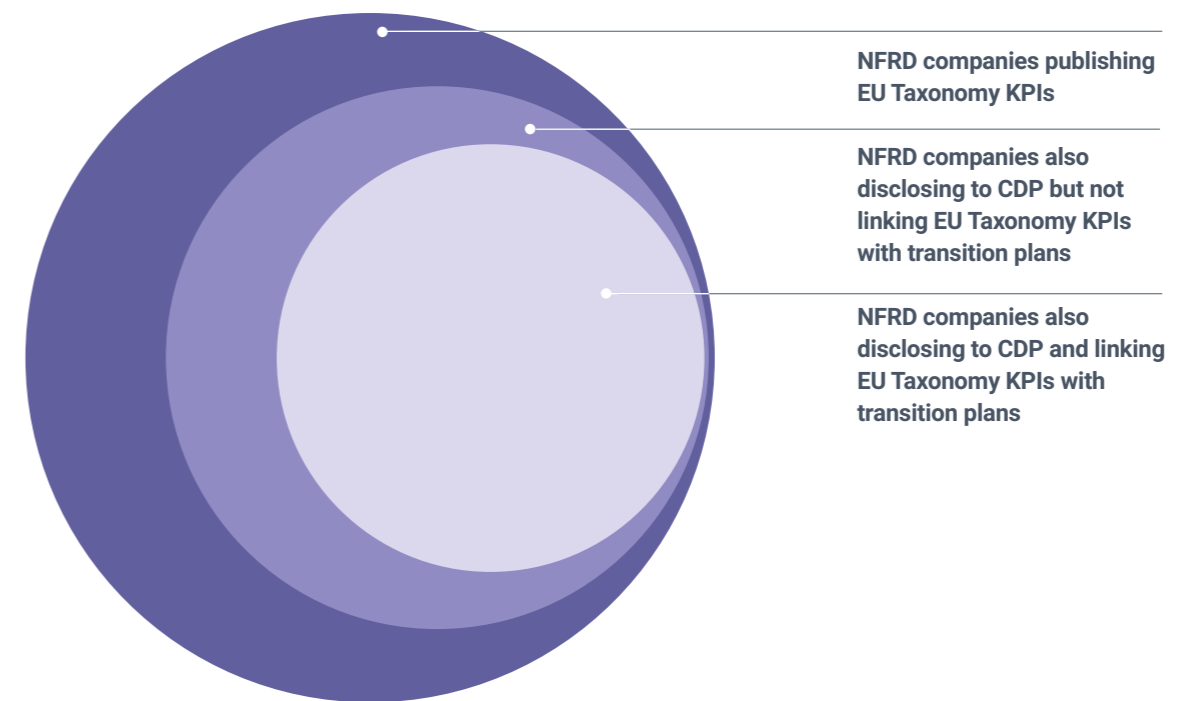- ◣ **Their Taxonomy eligibility:** The proportion of a company's activities that falls within the scope of the EU Taxonomy, by fitting the description of one of the 107 activities currently included in the regulation.[10]
- ◣ **Their Taxonomy alignment[11]:** The proportion of a company's activities that are eligible for the EU Taxonomy while also:
- Meeting the technical screening criteria for substantial contribution;
- Doing no significant harm (DNSH) to any of the other environmental objectives;
- Complying with minimum safeguards (MS) - this point is measured at entity, not activity, level.
- ◣ **These across three main types of KPIs:** revenue*, CapEx and OpEx for non-financial companies in percentage of total and monetary amounts, both for eligibility and alignment.
- ◣ **Per economic activity:** The specific activity through which a company is claiming eligibility or alignment.

Companies are required to use official templates[12] to disclose the information above.

A major milestone: over 1,800 companies reported EU Taxonomy data in their official reports

Throughout 2023, companies have mostly disclosed EU Taxonomy information in publicly available annual or sustainability reports[13]. In addition, starting in 2022 CDP began collecting data on corporates' use of sustainable finance taxonomies. In 2023 this was expanded to collect data on their EU Taxonomy KPIs, with an explicit link to financial planning associated with their transition. **For this report we therefore use both data reported to CDP as well as data gathered from official reports by Clarity AI**, drawing insights by comparing companies that link Taxonomy KPIs to transition planning to those that don't.

Figure 1
Sample structure, for illustrative purposes only

NFRD companies publishing EU Taxonomy KPIs

NFRD companies also disclosing to CDP but not linking EU Taxonomy KPIs with transition plans

NFRD companies also disclosing to CDP and linking EU Taxonomy KPIs with transition plans

We screened official reports of close to 3,000 companies with a high likelihood of having reported EU Taxonomy data, identifying 1,814 companies that actually did report it. This report uses a smaller sample of 1,704 companies for which supplementary data (e.g., country, sector, emissions data) was available. This sample includes the approximately 700 companies that also disclosed EU Taxonomy data to CDP in this first reporting year, as illustrated by Figure 1.

This large number of reporting companies marks a major milestone towards the integration of sustainable data disclosure in corporate mainstream reporting.

---

7 The activity details for climate change mitigation and climate change adaptation are described here.
8 The 27 countries that make up the European Union plus Norway, Iceland, and Liechtenstein
9 A company is subject to NFRD disclosure requirements if it meets all three conditions: 1) it is a public-interest entity, meaning it is either publicly listed in the EU, a credit institution, an insurer, or from a sector deemed as public-interest by an EU member-state; 2) it has more than 500 employees; and 3) it has either more than €40M in revenue or more than €20M in total assets. Source
10 Source: EU Taxonomy navigator, list of sectors included in the EU Taxonomy. Source
11 Report on eligibility from 2022 for non-financial companies and 2023 for financials, and on alignment from 2023 for non-financial companies and 2024 for financials.
12 Source: June amendments of the EU's sustainable finance package
* In this report, we use "revenue" and "turnover" interchangeably

13 From here on referenced as "official reports"

1. Trends from the first year of EU Taxonomy reporting

Until now, companies have only been asked to disclose EU Taxonomy KPIs related to the two environmental objectives currently in force: climate change mitigation and climate change adaptation. In this report, we will focus on total KPIs across both objectives, although we note that companies report more on climate change mitigation than climate change adaptation. The great majority (94%) of companies in our sample have reported on their EU Taxonomy KPIs because they were mandated to do so by the regulation. That said, we estimate that 6% of them (110 companies) have voluntarily reported this information using the screening methodology highlighted above.

Companies need more time to fully comply and adopt consistent reporting methods

Alongside this initial uptake of the EU Taxonomy, we also see challenges, including the existence of **a large cohort of companies that have not yet reported their EU Taxonomy figures despite being required to do so under the NFRD**. When collecting data for identified publicly listed NFRD companies (which represent close to 2,200 companies), we could find no EU Taxonomy disclosures for close to 500 of them.

Though companies typically report this information in their official reports, not all companies use the official template provided by the European Commission[14]. Meanwhile, in our sample, we observe that not all companies report on all three KPIs; nor do they report both eligibility and alignment figures. The latter is true even for companies outside of the financial sector (which, for this year, only need to report eligibility figures).

This finding is in line with the recently published review[15] of the European regulator ESMA and suggests room for improvement in terms of adoption of the regulatory templates and consistency of disclosures across companies. **While the general uptake is high, companies still need more time to fully comply and adopt the disclosure rules of the Taxonomy.** In the meantime, those differences in adoption and interpretation can impact the usability and comparability of the EU Taxonomy data.

At the time of writing (November 2023), companies still have a few weeks to publish their Taxonomy disclosures for the 2022 fiscal year, so additional data may become available before the end of the year.

As expected, most companies reporting EU Taxonomy data are based in the European Economic Area (Figure 2).

14 PwC found only around 66% of companies use the official template (Source in Spanish)
15 Source: ESMA

Reporting companies reflect European market capitalization and country representation in the European economy

The country breakdown of NFRD reporting companies below **shows a higher representation of the largest European countries** — expected given the size of these markets.

Figure 2
Companies reporting on EU Taxonomy by country

Legend:
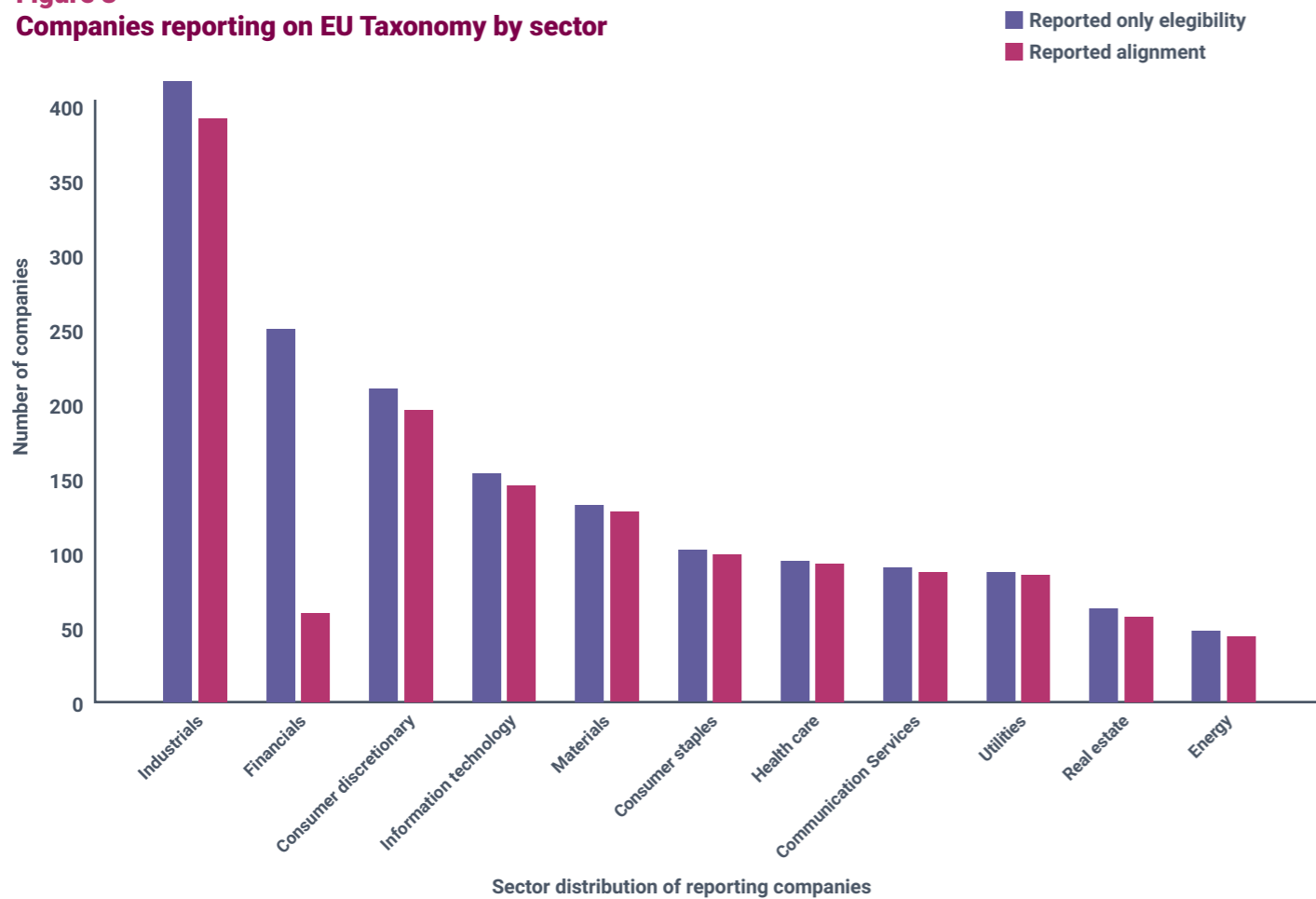- EEA company
- non-EEA company
- Mix

Number of companies
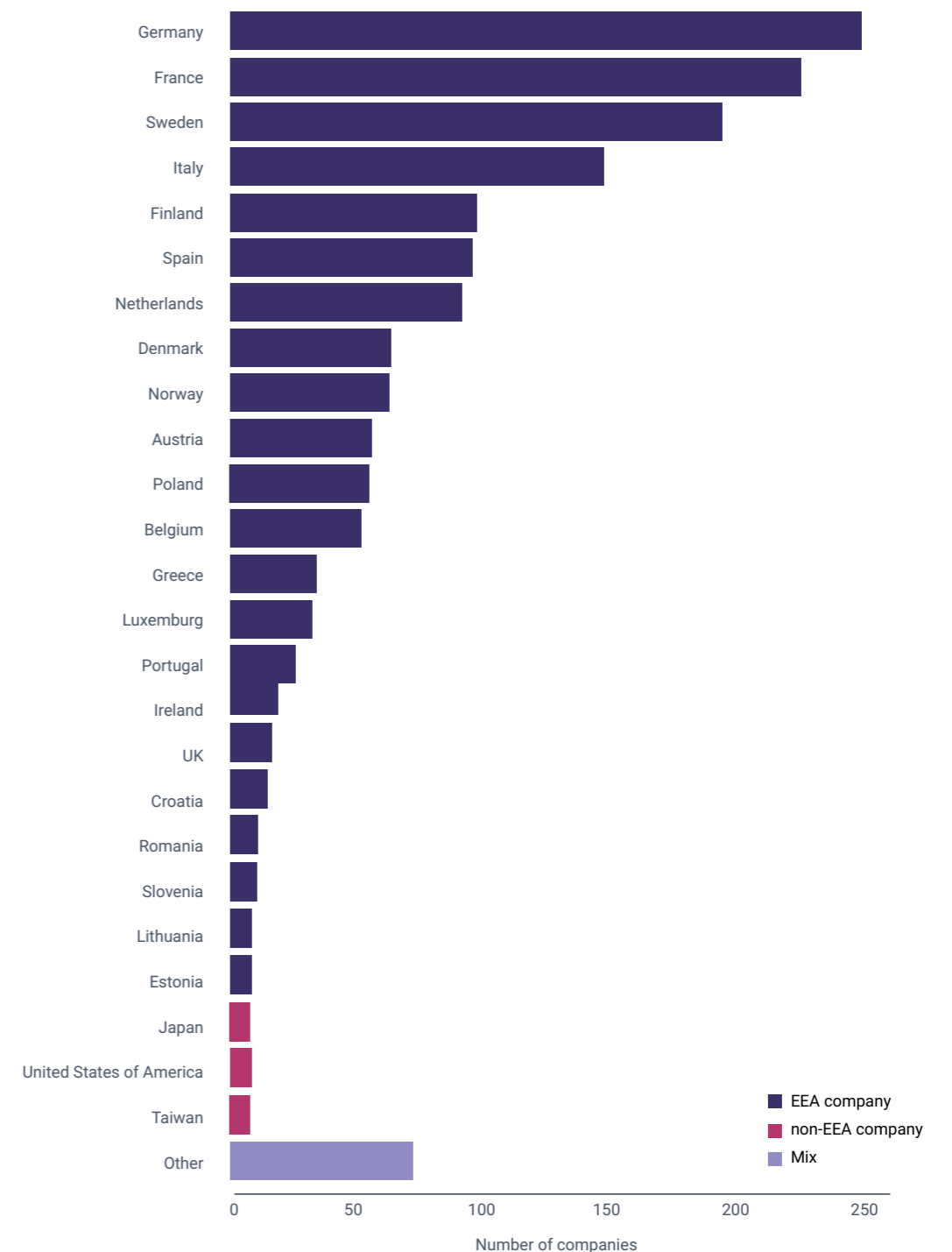
1. Trends from the first year of EU Taxonomy reporting

In this report, we use the Global Industry Classification Standard (GICS) for sectoral breakdowns due to its wide use by financial market participants, including for financial products reporting.

As can be seen in Figure 3, the **industrial, financial and consumer discretionary sectors represent a large proportion of reporting companies**, a trend which is broadly in line with European market capitalization. As mentioned previously, financial companies - such as credit institutions, asset managers, and insurers - need to report only their eligibility figures this year.

Figure 3
Companies reporting on EU Taxonomy by sector

- Reported only elegibility
- Reported alignment

Number of companies (y-axis: 0, 50, 100, 150, 200, 250, 300, 350, 400)

Sectors: Industrials, Financials, Consumer discretionary, Information technology, Materials, Consumer staples, Health care, Communication Services, Utilities, Real estate, Energy

Sector distribution of reporting companies

Over 600 companies link their EU Taxonomy KPIs with spending and revenue in line with their transition plan

Figure 4
Responses to CDP on whether spending and revenue are aligned with climate transition
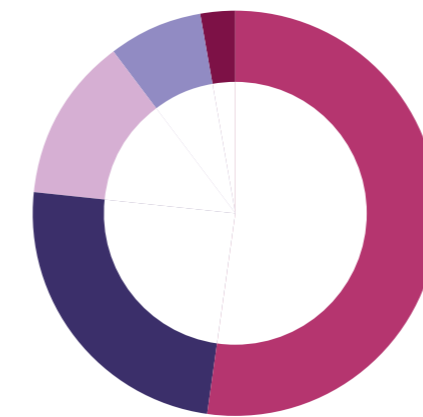
- ◤ No, but we plan to in the next two years **52%**

- ◤ No, and we do not plan to in the next two years **24%**

- ◤ Yes, we indentify alignment with our climate transition plan **13%**

- ◤ Yes, we indentify alignment with a sustainable finance taxonomy **8%**

- ◤ Yes, we indentify alignment with both our climate transition plan and a sustainable finance taxonomy **3%**

As part of CDP's recommended best practice for a credible transition plan, companies should identify their revenues and spending associated with their plan. In the business strategy section of CDP's climate change questionnaire, a series of questions requires companies to disclose elements of their climate transition plan aligned towards 1.5 degrees. It is in this section that CDP began collecting data on corporates' use of sustainable finance taxonomies in 2022[16]. By asking companies to disclose their taxonomy KPIs and related verification methodology within the context of transition planning, **CDP piloted the use of the EU Taxonomy as a tool for transition planning in the real economy.**

Of the close to 2,500 companies that report already identifying spending and revenue in line with their transition plans, **over 1,000 (44%) replied that they identify alignment with a sustainable finance taxonomy.**

Despite many companies taking action to align revenues and spending with their transition plans, there is currently a fragmentation in approaches to defining alignment. Among those 1,093 companies, close to **700 have identified alignment with the EU Taxonomy specifically.** Almost all those companies overlap with the sample of NFRD companies described in the previous section, which means they also disclosed EU Taxonomy data in their official reports.

Of those that disclose through CDP who do not identify spending/revenues in line with their transition plan[17], some are NFRD companies, implying that not all companies reporting on the EU Taxonomy are yet able to make this link with their transition plan. Around 130 NFRD companies explicitly disclosed to CDP that they do not identify spending and revenues in line with their transition plan.

To ensure quality, CDP data was checked against companies' official reports. The reported KPIs were found to be identical, with the exception of a few observations (seven companies) that were removed from our analysis[18].

16 See the report's annex for CDP's questions on sustainable finance taxonomies.
17 We count as "no" the companies that answer: "No, but we plan to in the next two years", or "No and we don't plan to in the next two years".
18 See appendix I

About climate transition plans

CDP defines a climate transition plan[19] as a time-bound action plan that clearly outlines an organization's strategy to pivot its existing assets, operations, and entire business model in order to align with the latest and most ambitious climate science recommendations (i.e. halving greenhouse gas emissions by 2030 and reaching net-zero by 2050 at the latest, thereby limiting global warming to 1.5) and ensuring that its business model remains relevant (i.e. profitable).

A fundamental element of any credible transition plan is robust forward-looking financial planning. As part of the recommended best practice for a credible transition plan, companies should identify their revenues and spending associated with their plan. Financial planning supports a company in classifying how and for which technologies current and future operating and capital expenditures (including research, development and innovation expenditures) are and will be deployed to achieve objectives and targets.

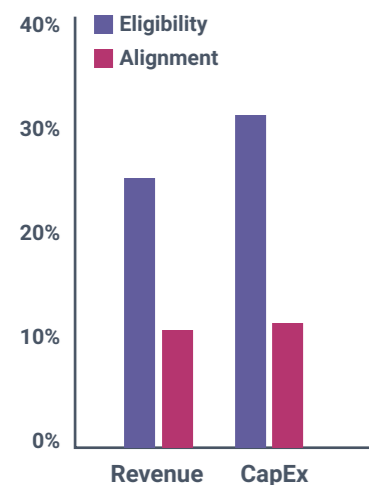# Insights from EU Taxonomy data analysis

2

19 Please refer to the CDP Climate Transition Plan technical note for more details

As noted above, companies can report their alignment with the EU Taxonomy via three KPIs: revenues, capital expenditures (CapEx), and/or operational expenses (OpEx). Our analysis focuses on revenues and CapEx, although given lower number of disclosures on OpEx we recommend that future research explores the role of OpEx and how it complements the other two KPIs.

Companies report relatively low EU Taxonomy eligibility and alignment on average

Figure 5
Average eligibility and alignment of reported revenue and CapEx

In line with other findings highlighted previously, Figure 5 shows that companies report, on average, 25% and 30% eligible revenues and CapEx respectively, and 11% and 12% aligned revenues and CapEx respectively.

The relatively low eligibility figures can be explained by the scope of the EU Taxonomy, which has an initial focus on economic activities that can make a substantial contribution to the climate objectives, including activities that are either:
1. The sustainable alternative to another high-impact activity (own performance activities such as renewable energy)
2. Enabling those sustainable activities to develop (such as manufacturing of technologies for renewable energy), or
3. High-impact activities without existing alternatives, but where best-available techniques enable a greener production (transitional activities such as manufacturing of cement).

Large sectors, such as healthcare, consumer staples, telecommunications, and much of the technology sector are not represented in the EU Taxonomy and are therefore non-eligible. Some of the high-impact activities, such as mining or agriculture, are also not represented in the EU Taxonomy and therefore non-eligible at the time of writing this report.

Hiding behind averages are large dispersions: still utilities and real estate lead on eligibility and alignment, while country analysis yields more mixed results

Given the wide range of eligibility and alignment identified within sectors, **averages do not necessarily capture the core of the information contained in EU Taxonomy data.** For this reason, we have analyzed eligibility and alignment figures using distributions within the different sectors. Figure 6 highlights the extent of that dispersion: **the data on Taxonomy eligible revenues suggests that companies within the same sectors are involved in very different economic activities.**

Some sectors, such as materials, are quite relevant to the objectives of the EU Taxonomy as they are responsible for a large share of emissions in value chains. While materials include activities such as the manufacture

of cement, the manufacture of aluminium, and the manufacture of iron and steel, this sector is not fully represented in the EU Taxonomy. Most mining and chemicals activities have not been included, which can explain the lower median eligibility for the materials sector compared to other high-impact sectors.

Aside from the utility sector, **percentages of alignment both for revenue and CapEx tend to display lower dispersion within sectors, compared to eligibility.** The real estate sector also stands out, with high and concentrated eligibility across the companies in this sector – suggesting they all are involved in similar economic activities covered by the Taxonomy.

Lower and less dispersed alignment across sectors could be explained by some of the technical screening criteria being hard to reach. For instance, cement manufacturers identified in our sample display only around 6% of their revenues aligned with the full technical requirements.

In terms of **revenue, utilities and real estate are the sectors with the highest median Taxonomy eligibility and alignment.** As Figure 6 shows, the high revenue alignment for utilities hides a wide dispersion: a quarter of companies in this sector have 76% or above revenue aligned and another quarter has 3% or below revenue aligned.

Figure 6
Eligible and aligned revenue by sector (interquartile range and median values)
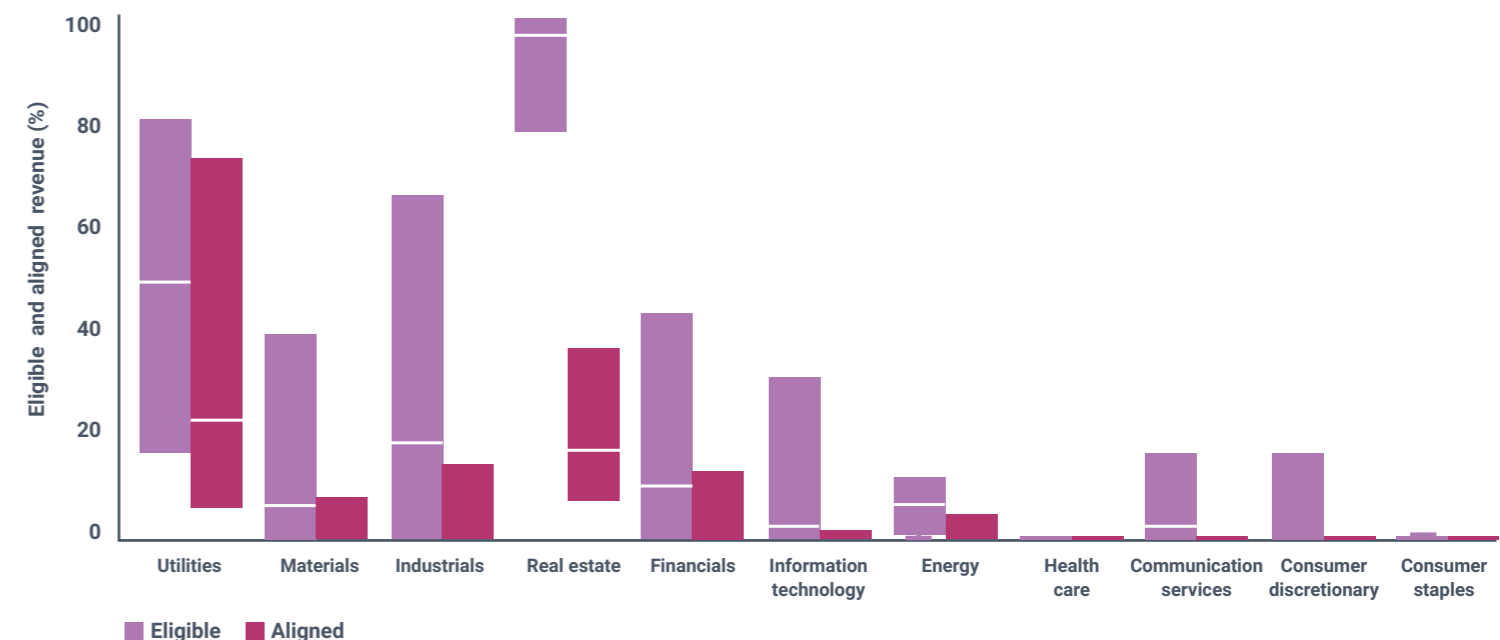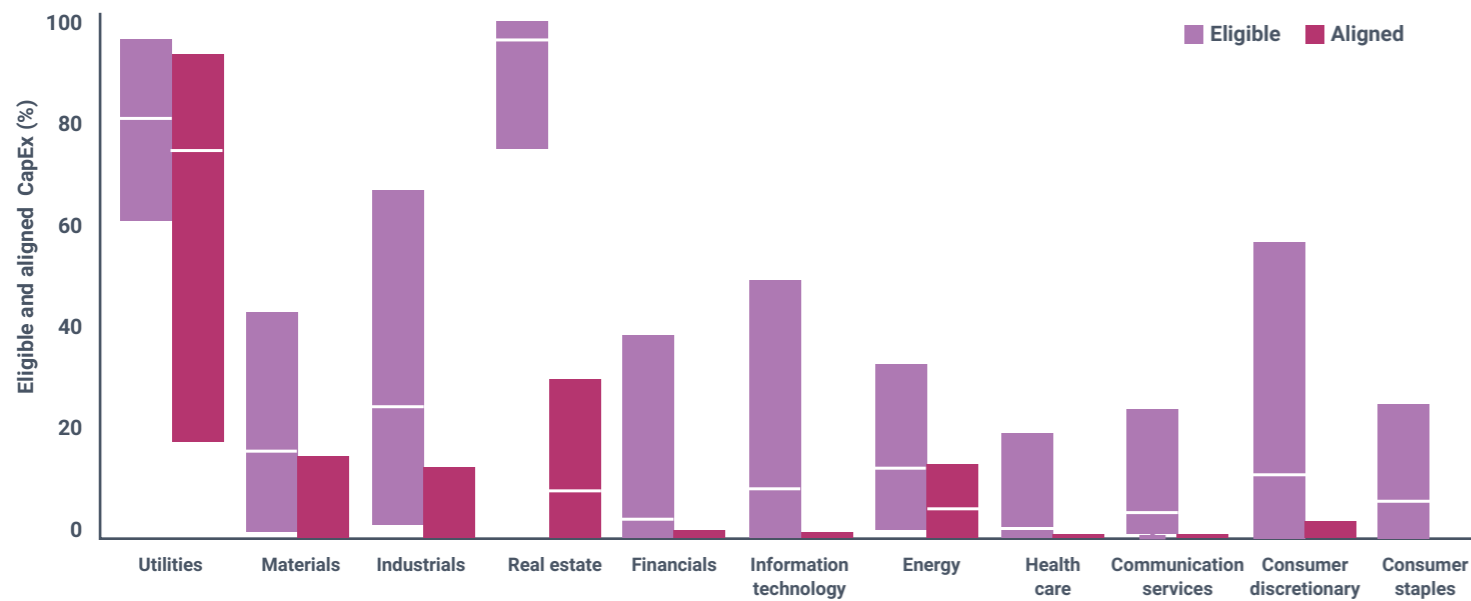
2. Insights from EU Taxonomy data analysis

Figure 7 shows that **CapEx across sectors displays a similar pattern**. It is worth noting, however, that for the utilities sector, the entire distribution is shifted upwards compared to revenue, with much lower dispersion in CapEx eligibility and much higher median alignment —supporting evidence that this sector is on a path towards transitioning its activities to be more aligned with the EU Taxonomy.

Among the research papers published so far, very few provide an analysis of differences across European countries regarding EU Taxonomy eligibility and alignment. The economies of European countries differ greatly in their exposure to certain sectors, which should lead to divergences in countries' exposures to taxonomy eligible activities[20] - an indication of where sustainable capital should be flowing.

Figure 8 highlights those differences, with **highest median revenue eligibility observed for companies headquartered in Norway, Austria, and Greece.** As most of the companies reporting under NFRD are from Germany, France, and Sweden, those numbers suggest that many companies under the Taxonomy scope have very low percentages of eligible revenues. In terms of revenue alignment, Norway and Spain lead the way while Portuguese companies show higher CapEx alignment.

Outside the EEA, the UK and the US display eligibility and alignment numbers that are very similar, hinting at the fact that companies in those countries report on their EU Taxonomy KPIs in a voluntary way to showcase their alignment rather than to give a comprehensive overview of their activities.

Figure 8
Eligible and aligned revenues by country (interquartile range and median values)

Figure 7
Eligible and aligned CapEx by sector (interquartile range and median values)
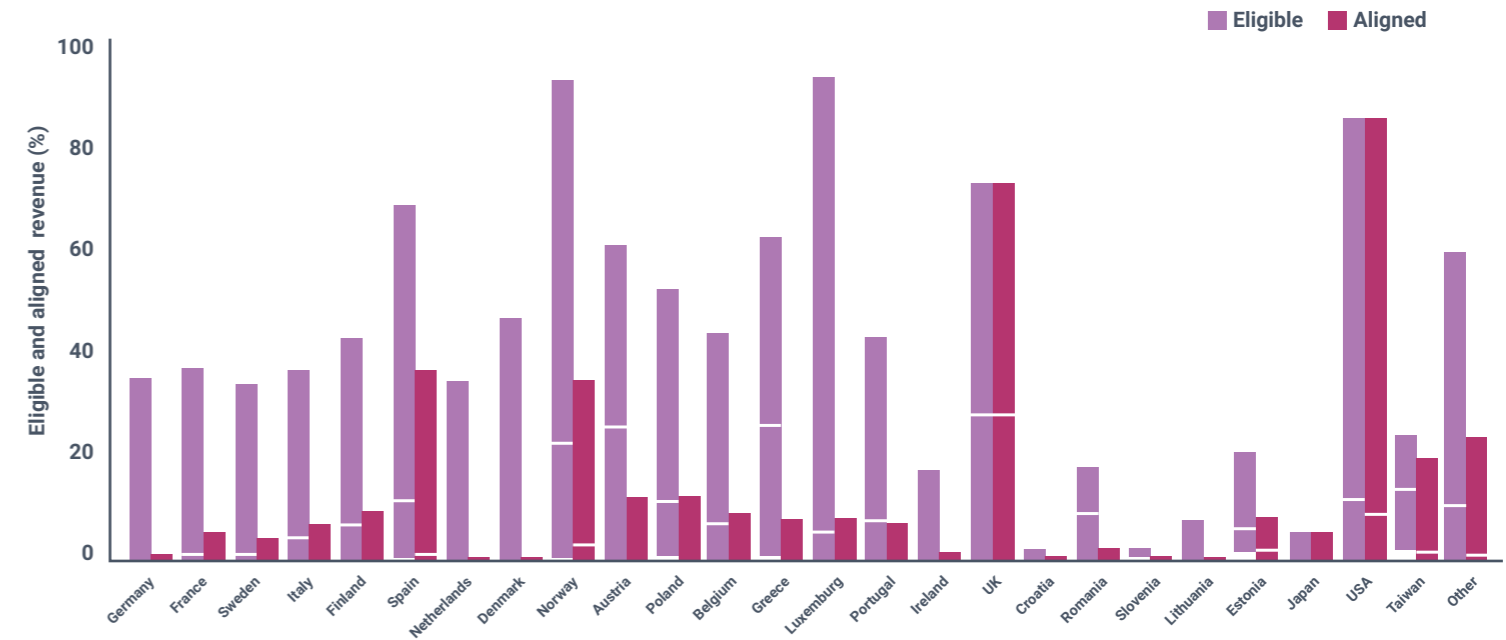
Figure 9
Eligible and aligned CapEx by country (interquartile range and median values)
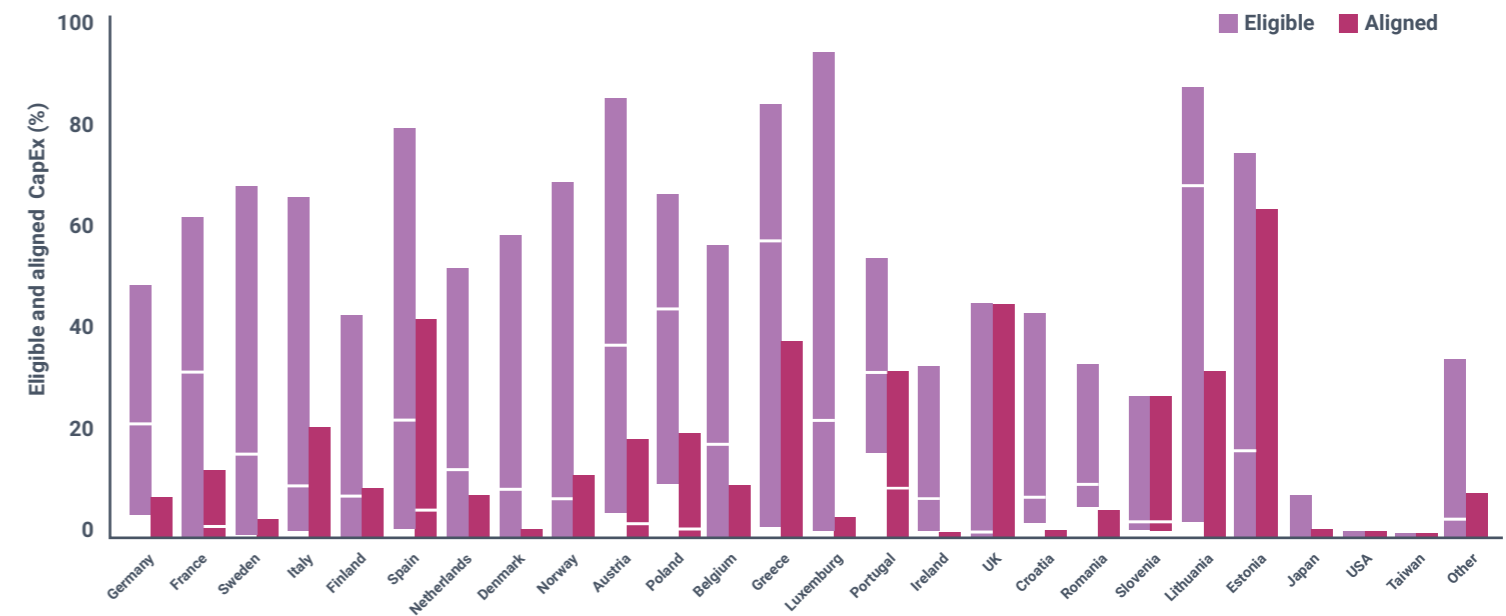
2. Insights from EU Taxonomy data analysis

Data users should explore distributions instead of averages

Overall, these results are in line with existing findings[21]. First, utilities and real estate lead on revenue alignment. Second, CapEx alignment tends to be higher than revenue alignment across sectors. **Our findings complement those insights by showing that companies within similar sectors can be involved in very different economic activities and have multiple revenue streams** as highlighted by the wide distribution of values for revenue eligibility across most sectors. This also has implications for the interpretation of a company's alignment to the EU Taxonomy.

We recommend that data users explore distributions instead of averages and look at eligibility to interpret alignment. We also recommend that financial institutions avoid using general or sectoral thresholds to benchmark Taxonomy KPIs unless activity-level clustering is applied.
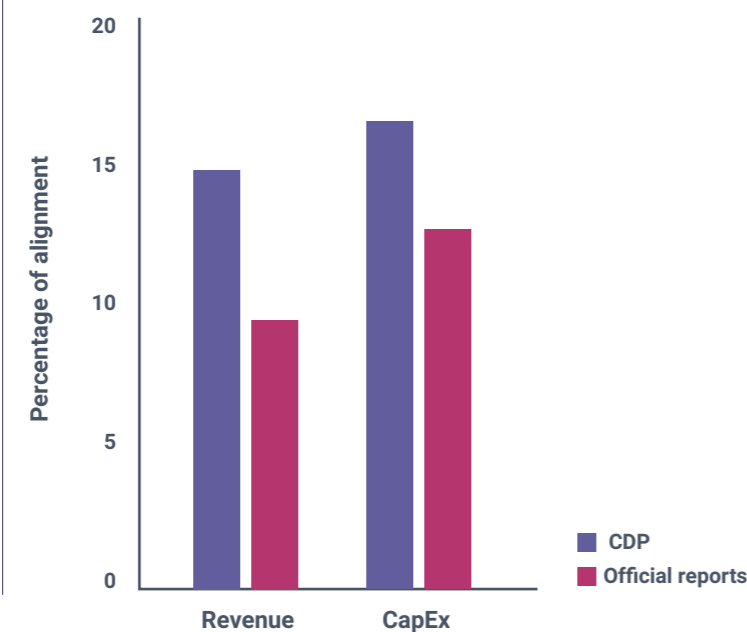
Companies that report on their EU Taxonomy in the context of transition plans tend to come from higher impact sectors and show higher degrees of alignment

On average, **companies linking the Taxonomy with their transition plans disclosed a revenue alignment of 14%, significantly higher than the 9% reported by the rest of the companies in our sample.** This observation also applies to CapEx.
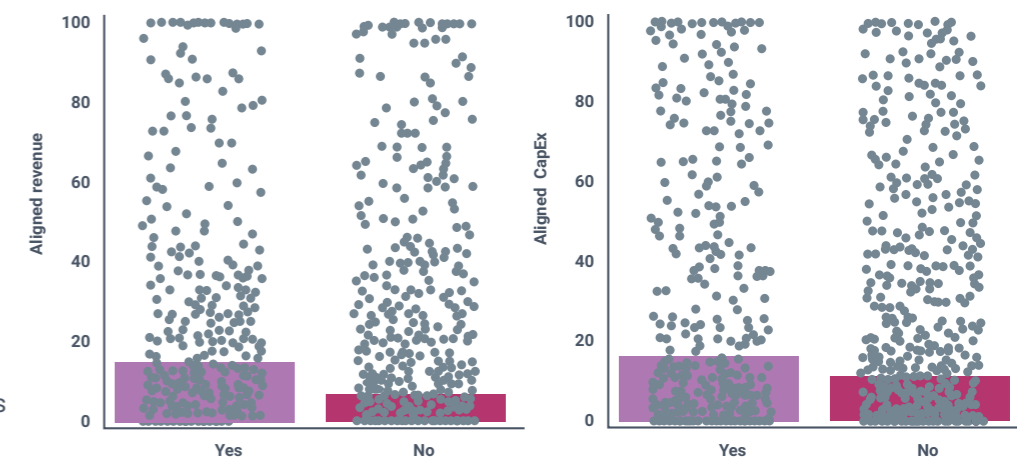
Figure 10
Average alignment of companies reporting EU Taxonomy to CDP compared to those only disclosing these values in their official reports

These differences are large enough to be meaningful with high level of confidence when looking at the distribution of our observations as highlighted in Figure 11.

Figures 10 and 11 suggest that **companies that already started identifying associated revenues and spending in line with their transition using the EU Taxonomy tend to have higher Taxonomy-aligned KPIs.**

These results should however be interpreted carefully, as it is difficult to identify the driver of the relationship. The difference could be driven by a sectoral bias. While overall the cohort of companies linking the Taxonomy with their transition plans is broadly proportional to the wider NFRD sample, we can see differences between sectors (Figure 12). For example, materials, utilities and energy companies represent a higher share of companies that identify the EU Taxonomy KPIs in their financial planning. We observe the opposite for lower impact sectors such as healthcare and IT.

As the Taxonomy covers few activities in low impact sectors, it seems intuitive that companies within those sectors will have fewer links to make between their KPIs and transition planning. Those sectors also display much lower eligibility and alignment figures, which could contribute to the difference observed in Figure 10 and 11.

When companies are asked about their expected alignment for 2025 and 2030 in the CDP questionnaire, two-thirds of companies in the CDP sample, regardless of sector[22], stated that their alignment would be higher in the future. We also see higher planned CapEx alignment over revenue alignment, although the growth rate is similar as highlighted in Figure 13 on page 24.

Figure 11
Percentage of aligned revenue (left) and CapEx (right) from companies that disclosed on EU Taxonomy to CDP ('Yes') vs. those that did not ('No')

Sample includes 705 companies that have responded with alignment figures in the 2023 CDP questionnaire and 1,270 companies that did not - having only reported alignment figures in their official disclosures collected by Clarity AI.

21 Referenced in the introduction of this report

22 See Appendix II

Figure 12
Comparison between the proportion of companies in each sector reporting EU Taxonomy data to CDP and NFRD companies reporting EU Taxonomy data collected from their official reports
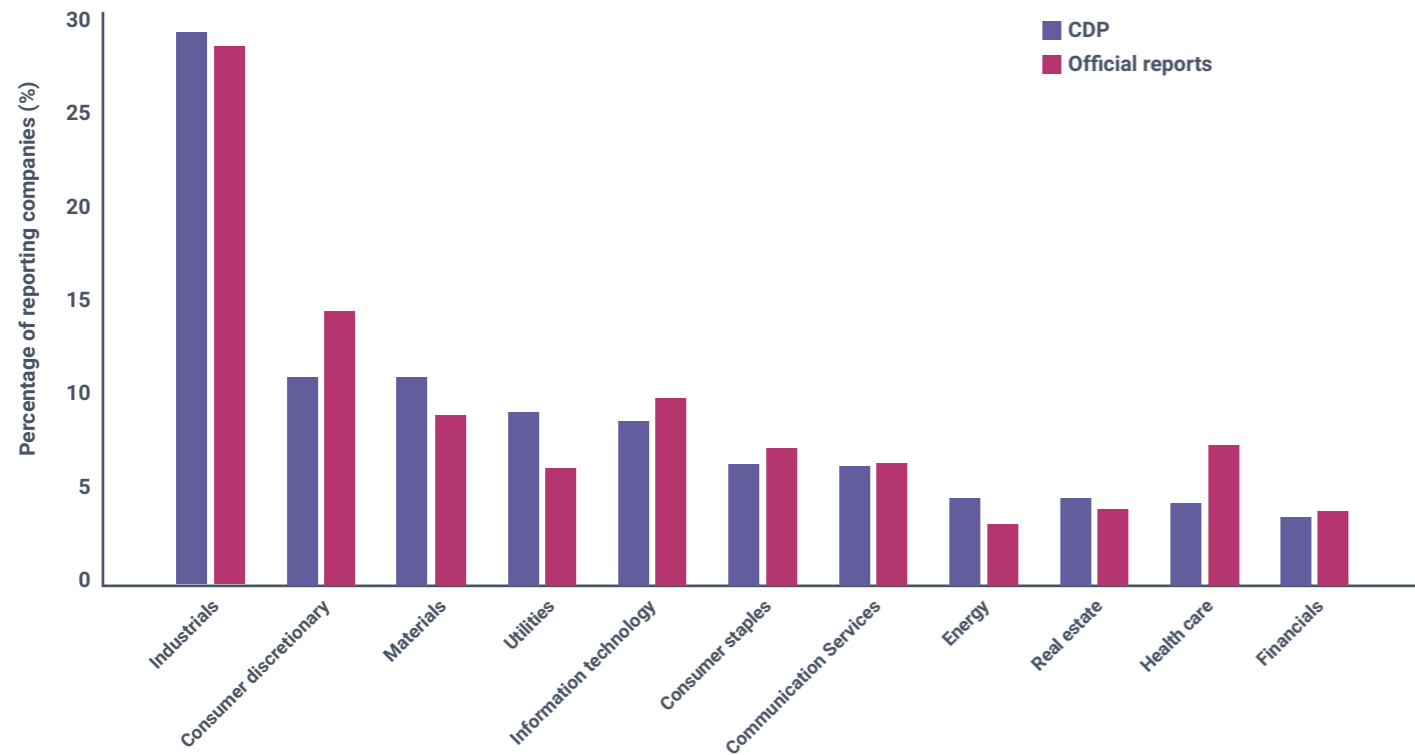
Figure 13
Mean alignment (%) of expected revenue and CapEx over time
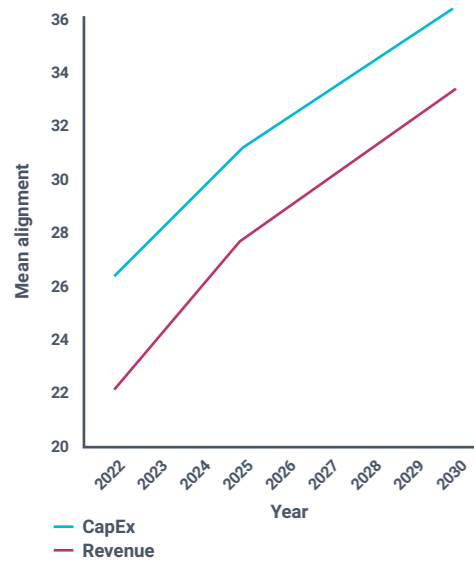
When putting this in the context of transition plans, it is encouraging to see this tool being adopted as part of financial planning, but **the degree of usability and strategic integration should vary per company.**

We encourage companies to develop all elements of their transition plans and use the Taxonomy in support of its delivery and credibility. This interlinkage will be key to the success of companies' transition and to the scaling up of financial flows in support of the climate objectives.

The EU Taxonomy and decarbonization

3

3. The EU Taxonomy and decarbonization

The European Commission transition finance recommendations published in June[23] highlight opportunities available to link economic activity-level actions to entity-level transition, which should be further explored with data now available. It re-emphasized the aim of the EU Taxonomy (for the climate change mitigation objective) **to be used as a tool for real economy decarbonization, leading to a clear outcome: GHG emissions reduction.**

In the following section we compare economic-activity-level EU Taxonomy KPIs with current corporate-level GHG emissions and commitments. **This aims to help bring the EU Taxonomy back into the context of real economy decarbonization and corporate level transition.** As highlighted in the beginning of this report, the companies in our sample account for almost 2 gigatons of GHG direct emissions (Scope 1).

High emitting companies will have varying uses for the EU Taxonomy in their decarbonization journey
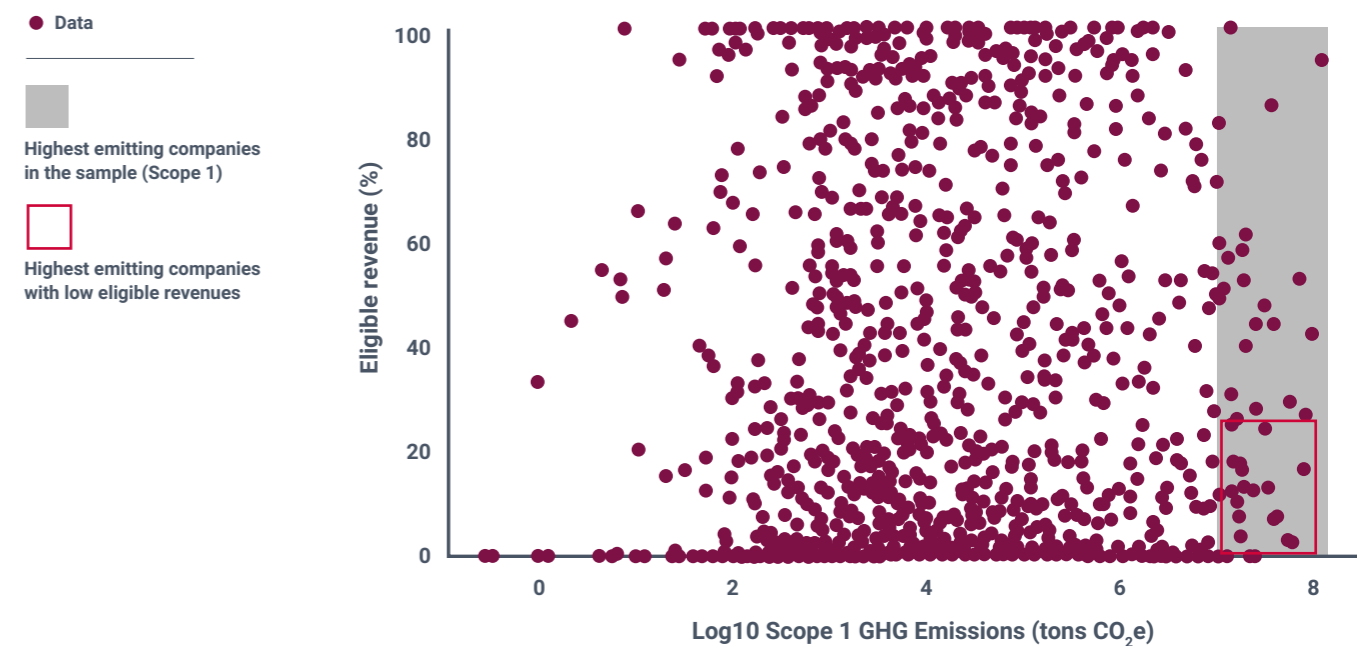
Eligible activities are a priority area given their potential to substantially contribute to climate change mitigation - and high emitting sectors and companies urgently need to decarbonize their production.

The purpose of this analysis is to **illustrate the extent to which eligible activities are currently present in the revenues of the highest emitters,** measured in absolute direct GHG emissions (Scope 1)[24], and to explore the relationship between current emissions and revenue alignment.

As shown in Figure 14, there seems to be **no strong correlation between a company's direct emissions and how much of its economic activity is captured by the EU Taxonomy.**

This is unsurprising as the Taxonomy's non-eligible activities capture both low and high environmental impact activities, and that eligible activities capture both climate solutions (such as renewables) and transitional activities (such as manufacturing of cement). We note that our initial focus on Scope 1 emissions has limitations for some sectors that generate most of their emissions from Scope 3 (i.e. car manufacturers and sectors for which the bulk of emissions result from consumer use).

Figure 14
Percentage of eligible revenue vs. absolute Scope 1 GHG emissions (tons CO2e)

● Data

▢ Highest emitting companies in the sample (Scope 1)

▢ Highest emitting companies with low eligible revenues

X-axis: Log10 Scope 1 GHG Emissions (tons CO_2e)
Y-axis: Eligible revenue (%)

24 It is worth noting that we rely on the quality of disclosed emissions data to evaluate the highest emitters, and not all high emitting companies are part of our sample – notable exclusions being private and or state-owned companies.

3. The EU Taxonomy and decarbonization

The following examples provide concrete industry cases of high-emitting companies that report low revenue eligibility (Figure 15).

▼ **Electricity generation:** Seven companies are included in this group, which contains large conventional utilities such as Uniper SE and PGE Polska Grupa Energetyczna SA. They still generate much of their revenue from coal-based electricity generation, which is not listed among EU Taxonomy eligible economic activities.

▼ **Oil & gas exploration, production, and associated activities:** Such oil associated activities are not on the Taxonomy list of eligible economic activities.

▼ **Passenger airlines:** This industry is newly included in the latest version of the Taxonomy regulation, under the activity of "passenger and freight air transport"[25], and will be in force starting January 2024. This highlights that eligibility will change over time, since the scope of the EU Taxonomy allows for the progressive inclusion of economic activities.

▼ **Fertilizers & agricultural chemicals:** Companies producing fertilizers such as Yara International ASA and OCI NV are some of the largest emitters of GHG emissions in the European Union. Despite this, only a small subset of their activities are eligible under the EU Taxonomy (those that relate to anhydrous ammonia and nitric acid). GHG emissions reduction initiatives for those companies will not necessarily lead to an increase in Taxonomy eligible revenues.

There is no strong relationship between direct emissions and percentage of aligned revenue

On the other hand, **the highest emitting companies**, represented on the right-hand side of Figure 16, **can display high Taxonomy alignment figures**. Figure 16 shows there is **no strong** relationship between direct emissions and percentage of aligned revenue, which can be observed across companies in our sample.

As Scope 1 emissions in metric tonnes are obviously influenced by the size of the company, we complement this analysis by looking at a measure of efficiency instead of absolute direct GHG emissions. GHG intensity is often used by market participants, as it enables a comparison of emissions between companies of different sizes. We focus on Scope 1 emissions in metric tons adjusted by revenue.

Figure 15
Highlight of the industry (GICS level 4) of a subset of high-emitting companies that have less than average eligibility

▼ Electricity generation **30.4%**
▼ Integrated oil & gas **26.1%**
▼ Passenger airlines **13.0%**
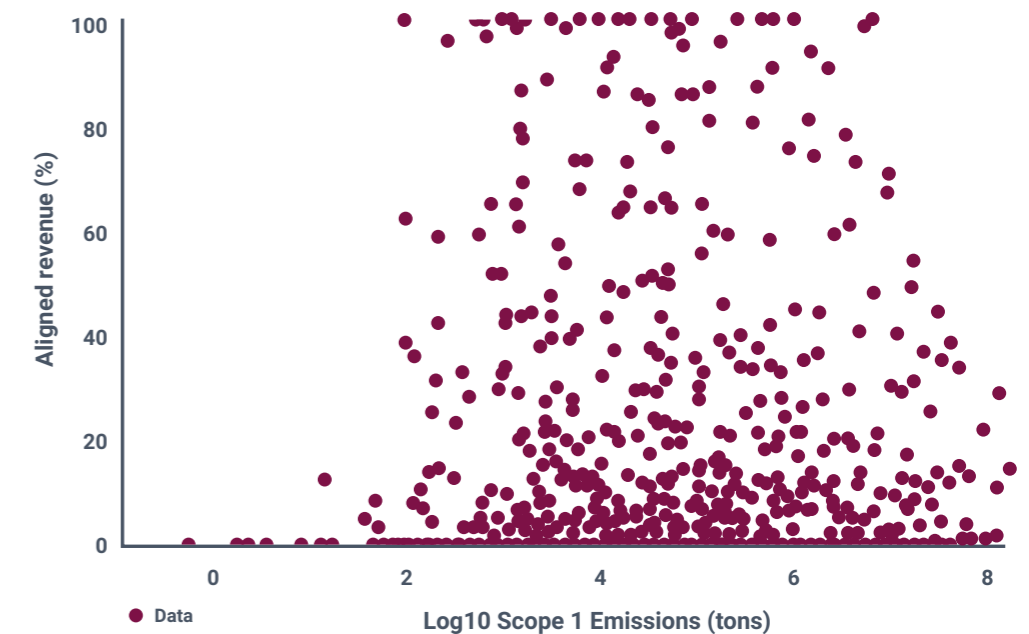▼ Fertilizers & agriculture **8.7%**
▼ Other **21.7%**

Figure 16
Percentage of aligned revenue vs. absolute Scope 1 GHG emissions (tons CO$_2$e)

- **Data**

X-axis: Log10 Scope 1 Emissions (tons)
Y-axis: Aligned revenue (%)

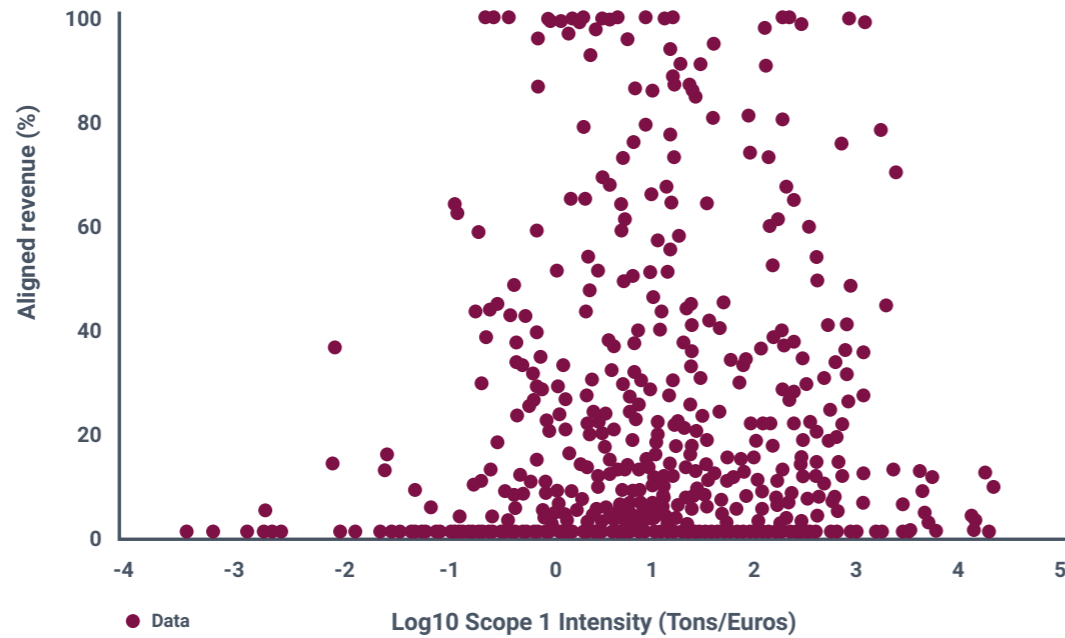25 Source: Commission Delegated Regulation - EU Taxonomy - 2023

3. The EU Taxonomy and decarbonization

We find no correlation between GHG intensity per revenue and Taxonomy alignment

We test the following hypothesis: companies having a higher percentage of Taxonomy aligned revenues should have a lower carbon intensity, on average, compared to companies with lower alignment in similar sectors. This relies on the assumption that the intensities of companies within the same sector are comparable as they are involved in similar economic activities[26].

Overall, **we find no strong correlation between GHG intensity per revenue and Taxonomy alignment**, with the exception of the utilities sector, where we detect a small relationship.

Figure 17
Reported percentage of aligned revenue vs.Scope 1 intensity (tons CO2e/EUR)

Figure 18
Sector breakdown of aligned revenue (%) vs. Scope 1 intensity (tons CO2e/EUR)

Across sectors, companies with high intensities can have high revenue alignment and vice versa.

Commonly used sectoral breakdowns do not capture the diversity of economic activities undertaken by companies that may or may not be eligible under the Taxonomy

A few reasons can explain these observations on revenue alignment and emission intensity:

◥ Commonly used sectoral breakdowns do not capture the diversity of economic activities undertaken by companies that may or may not be eligible under the Taxonomy. For example, the Industrials GICS includes transportation, commercial services, electrical equipment, construction and other diverse activities. Companies with higher eligibility might show higher alignment without necessarily being less carbon intensive.

◥ The share of revenues can't always proxy the highest source of GHG emissions at the corporate level. For instance, a company may show alignment of 40% while being among the highest GHG intensive companies in the sample. Non-eligible activities can generate most of the GHG emissions of a company even if the share of revenue is below 50% (e.g. thermal coal).

◥ Alignment to the Taxonomy is often determined by physical intensities rather than revenues. Additionally, alignment is also determined by criteria unrelated to direct GHG emissions (e.g. DNSH).

◥ Total revenue can comprise many different activities if the company is well diversified, which dilutes the information on efficiency.

Future research could run similar analysis for a more granular subset of transitional and own performance activities to cluster the companies in the sample.

In summary, this analysis suggests that **high emitting companies will have varying use for the EU Taxonomy in their decarbonization journey.** For financial institutions pursuing decarbonization strategies, it is worth noting that revenue-based Taxonomy KPIs and corporate level emissions complement each other as insights rather than correlate to one another.

A highly emitting company will tell one story if its revenues are 100% aligned and another if they are 100% eligible and not aligned. Likewise, a company with 60% aligned revenue can still be involved in harmful and carbon intensive activities such as coal, which emissions data should help interpret.

Companies with science-based emission reduction targets tend to have higher CapEx alignment

Discussions on the EU Taxonomy's role in corporate transition tend to focus on forward-looking information captured by the CapEx KPIs, which should help assess if the money spent by a company is financing its alignment to a 1.5 degree future. **One of the key elements of a corporate transition plan and assessment of its credibility is the presence of an ambitious and science-based target (SBT)[27] set by the company.**

We analyze the relationship between EU Taxonomy-aligned CapEx percentages and the presence of near-term science-based targets validated by the SBTi. Among the sample of companies analyzed for this report, around 300 have SBTi validated near-term targets (with a timeframe that spans between 5 and 10 years).

Figure 19 suggests that companies with science-based emission reduction targets have higher CapEx median Taxonomy alignment than companies without an SBTi validated emission reduction targets.

Figure 19
Aligned CapEx (%) of companies that have validated science-based emission reduction targets (Yes) vs. those that do not (No)

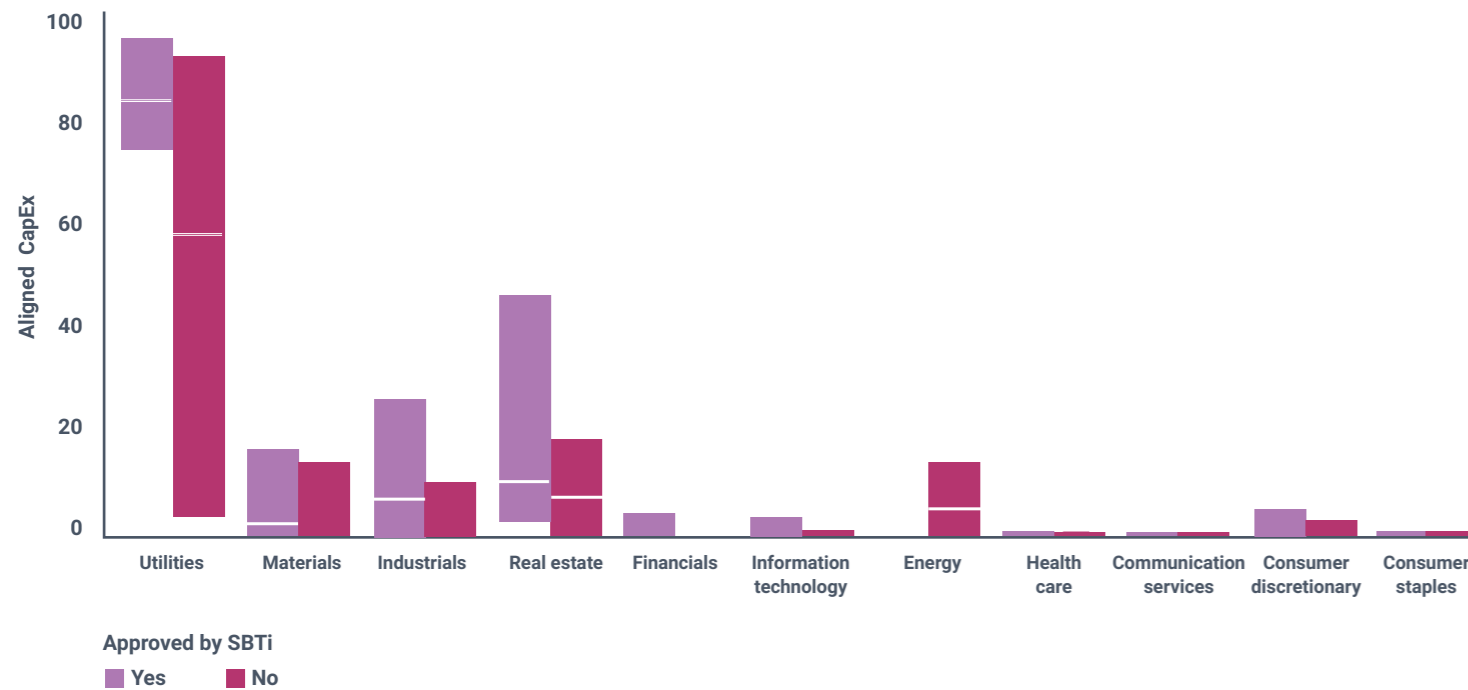Company has a emission-reduction targets approved by SBTi
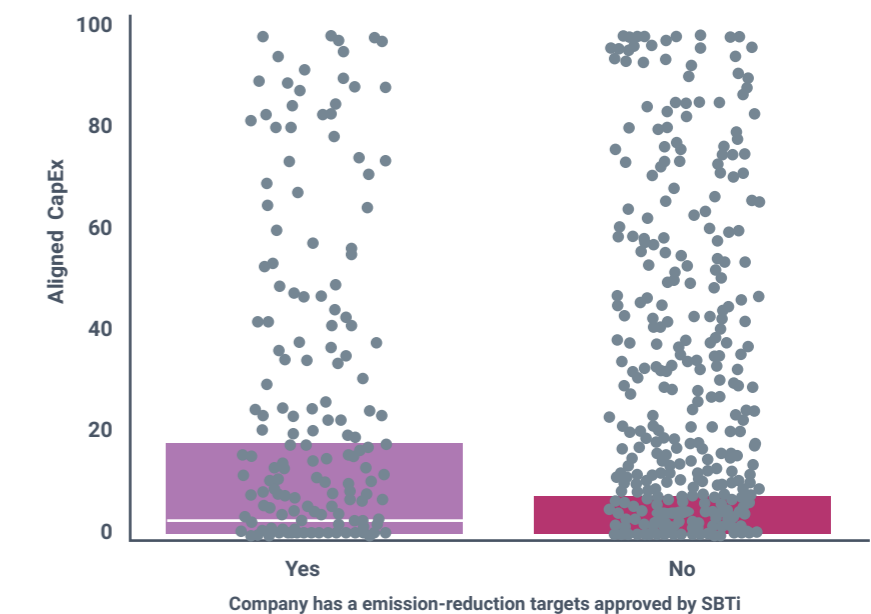
27 The Science Based Targets initiative drives corporate climate action by enabling businesses and financial institutions globally to set science-based greenhouse gas (GHG) emissions reduction targets. It was formed as a collaboration between CDP, the United Nations Global Compact, World Resources Institute (WRI), the World Wildlife Fund (WWF), and the We Mean Business Coalition

Figure 20 shows this by sector: this relationship between SBTi-validated targets and aligned CapEx holds for most sectors. The notable exception is energy for which there is no science-based target-setting methodology available at the time of writing of this report. This despite companies in the energy sector showing signs of investing in other economic activities aligned with the EU Taxonomy.

When evaluating SBT alignment with average revenue alignment, we find the relationship to be weaker. This finding is consistent with the view that to achieve decarbonization targets, investments toward future activities may be more important than current operations. This is particularly evident in the utilities sector. Figure 21 shows how utilities companies with a validated science-based target are indeed showing much higher CapEx alignment numbers.

Electricity generation accounts for over 26% of greenhouse gas emissions in the EU[28] and is one of the most strategic sectors targeted by the EU Taxonomy. As such, it is encouraging to see utilities reporting high EU Taxonomy CapEx alignment paired with science-based targets.

These preliminary findings provide initial evidence of the value of incorporating Taxonomy KPIs as a means to display commitment to a target and is an example of how activity-level and entity-level information that is science-based can be used in tandem to support the transition. **However, we note that, to date, the number of NFRD companies in our sample that have SBTi-approved targets remains low.**

Figure 20
Breakdown by sector: aligned CapEx (%) of companies that have validated science-based emission reduction targets (SBT) vs. those that do not (interquartile ranges and median values)

Approved by SBTi
■ Yes ■ No

Figure 21
Percentage of aligned CapEx (left) and revenue (right) of companies in the Utilities sector that have approved science-based emission reduction targets (SBT) vs. those that do not

28 EEA greenhouse gases
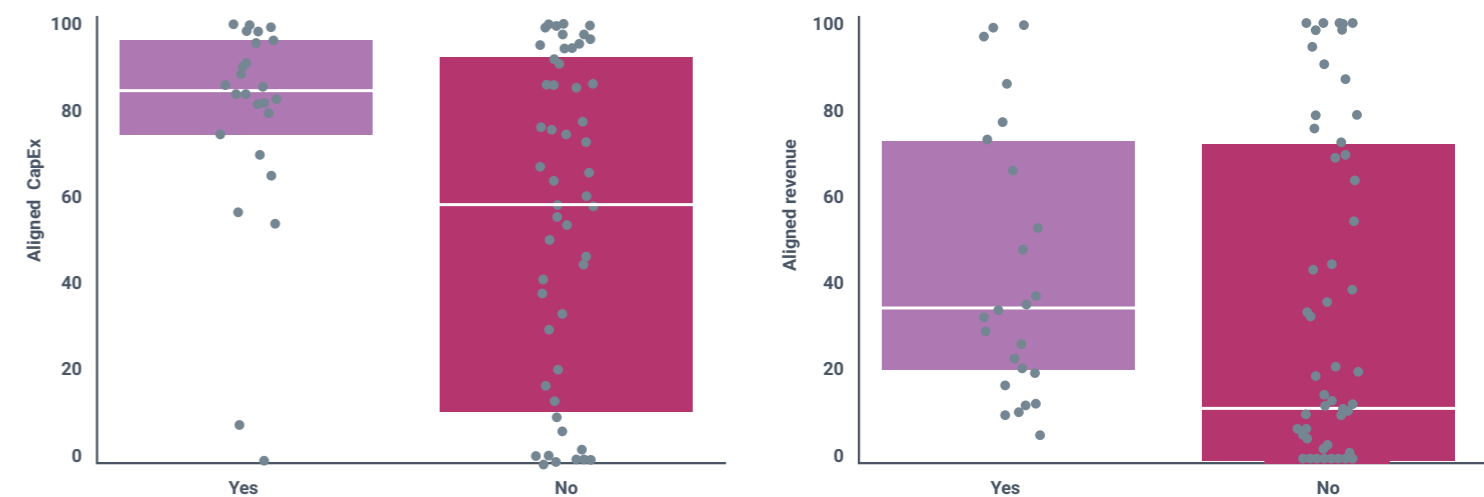
Conclusions

We close this third section by providing recommendations for the use of the EU Taxonomy as a tool to help the real economy decarbonize, both for companies who may use it in transition planning and for financial institutions that need to interpret the information it provides.

First, credible transition plans should focus on reducing key sources of GHG emissions; therefore, we can expect actions and decarbonization levers that will vary in types. The result of those actions can lead to an increase in revenues generated from low carbon products and services (using Taxonomy revenue alignment as a common definition), but this relationship is not systematic.

Second, the Taxonomy does not cover all activities, and therefore while increasing taxonomy-aligned revenues where relevant, companies should actively work towards all decarbonisation levers. Activity-based criteria can also be used to support specific actions across companies. For example, actions such as improving energy efficiency in industrial processes or consuming low-carbon energy can be benchmarked to technical screening criteria.

In other words, **we see multiple use cases for the Taxonomy**, as a classification system that can be used to define the highest level of ambition for some of the actions taken to decarbonize, **while the Taxonomy KPIs can be used as a tool to support the financial planning associated with a company's overall transition strategy**. More specifically, current and future CapEx alignment can signal the amount of financing in place or needed to support those actions.

To finalize, we recommend that data users interpret EU Taxonomy revenue alignment in the context of companies' emissions, their key drivers and decarbonization levers, as percentages on their own do not inform the climate performance of companies. Year-on-year observations will be key to assess how decarbonization trends relate to trends in revenue alignment, when relevant for a company's transition. Looking ahead, CapEx alignment can be analyzed in tandem with corporate science-based targets.

The EU Taxonomy moving forward

4

Key findings

Of the 1,700 NFRD companies that published EU Taxonomy reports this year, around 600 identified their revenues and spending as part of their transition plans, and approximately 300 have validated science based targets, both of which correlate to higher taxonomy alignment overall

We find that out of the 1,700 NFRD companies that published EU Taxonomy reports this year, around **600 identified their revenues and spending as part of their transition plans**, and approximately **300 have validated science-based targets**, both of which correlate to higher taxonomy alignment overall.

There is a large dispersion of eligibility across companies within similar sectors which suggests that individual companies are involved in a variety of economic activities.

This influences the low correlation between corporate GHG emissions and Taxonomy eligibility and alignment, as non-eligibility can be the result of exposure to either very high-impact or very low-impact economic activities. **We observe that higher taxonomy alignment does not necessarily lead to lower carbon intensity when comparing companies within sectors.** It is important to highlight that the largest source of corporate emissions might not always be well reflected in revenue shares.

As one of the first widely reported sustainable finance taxonomies globally, the EU Taxonomy gives us a very important set of data to analyze and shed light on the idiosyncrasies of corporate activities within and across sectors. This ultimately points to the potential weaknesses of assessing the ambition of corporate transition plans on the basis of the sector they belong to. **There is a clear case and need for science-based economic activity level criteria to define the highest ambitions for corporate actions.**

What's next

The EU Taxonomy is constantly evolving and growing in breadth and applicability. Just next year, there are several developments taking place:

- The regulation's four new environmental objectives will soon start applying. As a result, most companies will have to publish the eligibility of their activities for these four new objectives during 2024, and their alignment during 2025.
- New mitigation and adaptation activities will be added, including airline transportation and aircraft manufacturing.
- Credit institutions, asset managers, and insurers will be required to report the percentage of their activities that are aligned with the EU Taxonomy, according to their industry-specific KPIs

CDP and Clarity AI will continue to support the successful uptake of the EU Taxonomy

Meanwhile, there is **a movement to expand and improve on climate transition plans by integrating nature**[29], meaning companies will increasingly be asked how they plan to protect and restore nature as part of their transition strategy. The use of the EU Taxonomy within climate-focused transition plans already introduces the notion of "Do No Significant Harm" to other environmental objectives, which has not been part of many transition plan frameworks so far. The upcoming reporting on the 'Taxo 4' - meaning the remaining environmental objectives of sustainable water use, biodiversity preservation, pollution prevention and circular economy - could also play a role in shaping holistic transition strategies.

As reporting requirements and disclosures continue to proliferate and evolve, **CDP and Clarity AI will continue to support the successful uptake and use of the EU Taxonomy**. Leveraging our unique strengths as data and insight providers, we will continue to help stakeholders to leverage the Taxonomy's potential as a tool for green investment and guide data users to maximise the use of its data to drive the flow of capital towards sustainable activities.

CDP will continue to guide companies on a journey towards more comprehensive disclosure, as we drive the creation of further reporting capacity across indicators of credible climate transition plans, which includes taxonomy-related reporting. We will also continue to work with stakeholders to explore how to streamline reporting requirements across multiple jurisdictions to maximise the usability of this data and drive cross-border sustainable financial flows.

FUTURE ANALYSIS OF THE EU TAXONOMY

EU Taxonomy reporting has resulted in a substantial amount of new sustainability-related data made available to the market. Analyzing and understanding this new data will be vital to help companies, investors, and policymakers leverage the Taxonomy going forward.

This report focused exclusively on climate change mitigation but there is much more Taxonomy data to explore to inform insights on climate change adaptation. Additionally, using the nuances provided by the classification of economic activities into 'transitional', 'enabling' and 'own performance' could take the analysis further, especially when comparing Taxonomy KPIs to GHG emissions for various scopes.

Further research exploring the relationship between the Taxonomy and transition plans is encouraged, to foster the use of this data for transition finance. To this end, year-on-year observations will be instrumental.

29 WWF Nature in Transition Plans: Why and How?

For media requests, please contact us at:
clarityAI@edelmansmithfield.com

For media requests, please contact us at:
media.europe@cdp.net

About Clarity AI
Clarity AI is a sustainability technology platform that uses machine learning and big data to deliver environmental and social insights to investors, corporates, governments, and consumers. Clarity AI's capabilities are an essential tool for end-to-end sustainability analysis related to investing, corporate research, benchmarking, consumer e-commerce, and regulatory reporting. Clarity AI's platform analyzes more than 70,000 companies, 430,000 funds, and 400 national and subnational governments, which represents more breadth than any other player in the market.

CDP
CDP is a global non-profit that runs the world's environmental disclosure system for companies, cities, states and regions. Founded in 2000 and working with more than 740 financial institutions with over $136 trillion in assets, CDP pioneered using capital markets and corporate procurement to motivate companies to disclose their environmental impacts, and to reduce greenhouse gas emissions, safeguard water resources and protect forests. Over 24,000 organizations around the world disclosed data through CDP in 2023, with more than 23,000 companies – including listed companies worth two thirds global market capitalization - and over 1,100 cities, states and regions. Fully TCFD aligned, CDP holds the largest environmental database in the world, and CDP scores are widely used to drive investment and procurement decisions towards a zero carbon, sustainable and resilient economy. CDP is a founding member of the Science Based Targets initiative, We Mean Business Coalition, The Investor Agenda and the Net Zero Asset Managers initiative.