

Berenberg ESG - ESG 2023: assessing the key themes

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- **ESG is rapidly evolving and will continue to do so in 2023:** We outline the top 10 themes that we expect to affect the ESG and wider investment universe this year and our top 10 ESG stock picks for 2023, as the focus of ESG diversifies beyond carbon and greenwashing concerns are addressed.
 - **The year that ESG diversifies:** We expect the focus to shift from just core carbon problems to other ESG issues in 2023. From a revenue perspective, we expect the share of companies that will reap ESG benefits to diversify beyond typical renewable-energy, electric-vehicle and battery plays to many other sectors, as investors and corporates confront a wider range of environmental and social issues.
- 1) **Industrial decarbonisation – attention pivots to hard-to-abate sector:** Governments are focusing on the largely ignored industrial sector, which represents 20% of emissions. Drivers include the EU Carbon Border Adjustment Mechanism (CBAM), gas prices **and China**. **Top picks: Eaton, Dassault Systèmes.**
 - 2) **Circular economy – circling in on decarbonisation:** A wave of regulation, particularly in the EU, and imminent, mid-2020s sustainable corporate targets should drive the transition to circularity **in 2023**. **Top picks: Autodesk, Croda.**
 - 3) **Biodiversity – finally disclosing:** Nearly every meeting we had with investors in H2 2022 discussed how to invest in biodiversity. The Taskforce on Nature-Related Financial Disclosures (TNFD) should clear that up in 2023, as the count of biodiversity funds continues **to grow**. **Top pick: ENCE.**
 - 4) **Water – an underappreciated risk versus carbon:** Further extreme weather will exacerbate water risk for businesses as we enter an El Niño weather cycle. The EU taxonomy will start to focus **on water**. **Top picks: Belimo, NX Filtration.**
 - 5) **Workers’ rights:** The recessionary environment will not end the trend of growing workers’ rights. Workers are poised for more power as aging demographics reduce the supply of working-age individuals. **Top pick: Marlowe.**
 - 6) **Health:** Despite the “end” of the pandemic in many developed countries, healthcare systems will continue to struggle. We expect easier preventative solutions, such as digitisation, and environmental-related health solutions **to benefit**. **Top pick: Volution.**
- **The year ESG fights back:** After a challenging period, from greenwashing raids to politicisation and backlash, 2023 is when ESG could make a comeback. The work to implement ESG standards is increasingly slotting into place and should start paying dividends by enabling identification of truly decarbonising businesses.
- 7) **Net-zero – move to performance analysis:** Introduction of shorter-term carbon emission cuts and disclosure of post-lockdown emissions data will facilitate the analysis of who is actually serious about cutting greenhouse gases (GHG) **in 2023**. **Food and HPC underperformers: Mondelez, Lindt & Spruengli.**
 - 8) **Carbon removal – first stab at standards:** The EU has proposed the first carbon removal standards while planning to ban offsets from carbon-neutral claims. Meanwhile in the US, the Inflation Reduction Act (IRA) funds **carbon removals**. **Stratification of the carbon removal market is likely.**
 - 9) **ESG standards – increased scrutiny:** Several ESG standards for finance and corporates will be updated in 2023, which should curb greenwashing.
- Our final standout theme relates to one of the major bottlenecks in ESG.
- 10) **Environmental permitting – supercharging renewable development:** The EU eased permitting in December, while the US plans to do the same, but the next bottleneck is looming: limited grid connections could **slow development**. **Top sectors and pick: smart grid equipment providers, wind installers, DEME.**