

# Methodology

Methodology developed by Covalence for calculating the EthicalQuote reputation score

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Covalence EthicalQuote, 1 avenue Industrielle, CH-1227 Carouge Geneva Switzerland  
Tel: +41 (0)22 800 08 55 ; Fax: +41 (0)22 800 08 56

[info@ethicalquote.com](mailto:info@ethicalquote.com) | [www.EthicalQuote.com](http://www.EthicalQuote.com)

## Overview

The EthicalQuote reputation index integrates thousands of news pieces gathered online and classified according to 50 Environment, Social, Governance (ESG) [criteria](#) inspired by the Global Reporting Initiative, and to their positive or negative sentiment, regarding 2800 companies worldwide.

Covalence has developed a unique combination of automated content processing of texts in original language with qualitative assessment by an international team of analysts. The combined use of Natural Language Processing and human analysis allow us to interpret large amounts of data within a short time. More than 500 intern analysts have contributed to this work since 2001, in partnerships with many [universities](#).

While relying on universally shared values, this methodology faces the characteristics of modern society such as cultural diversity, democratic debate and scientific uncertainty, and the challenges of defining objective ethical criteria and credible information sources.

The EthicalQuote reputation scoring system developed by Covalence, reflecting public opinion in a pragmatic and dynamic way, allows to explore and use potential correlations between extra-financial and financial measures of performance.

Our conviction is that ESG reputation is translating trust and consensus of the different stakeholders in a company, and its ability to adequately factorize social and environmental concerns. It is an indicator of the quality of risk management, brand positioning, innovation capacities, and strategic vision. It is also a vector of the return on investment of Corporate Social Responsibility programs.

## International norms and standards

The EthicalQuote reputation index integrates thousands of news pieces gathered online and classified according to 50 Environment, Social, Governance (ESG) [criteria](#) inspired by the [Global Reporting Initiative's](#) G3.1 sustainability reporting guidelines, as well as by the following international norms and conventions:



- Universal Declaration of Human Rights
- OECD Guidelines for Multinational Enterprises
- ILO Declaration of Principles concerning MNEs and Social Policy
- Rio Declaration on Environment and Development
- Agreements of the World Summit for Social Development
- UN Global Compact
- UN Millenium Goals
- Guiding Principles on Business and Human Rights: Implementing the United Nations “Protect, Respect and Remedy” Framework (2011)

These treaties and conventions represent the values of the international community, the principles and goals that are shared across the world.

## Defining ethical criteria: the problem of subjectivity

While the general goals and principles are objects of wide consensus, there are different opinions on the means to reach these goals and to respect these principles.

The action of defining ethical criteria is highly subjective, it is influenced by the position, beliefs and experience of the subject, of the person or organization that is doing so. The **problem of subjectivity**, the difficulty of defining ethics, comes in a modern, *open society* (Karl Popper), where there exists political pluralism, democratic debate, cultural diversity, social complexity, scientific uncertainty, and philosophical doubt (“I know that I don’t know”, Socrates).



One can think of many ethical dilemmas relating to business ethics, such as:

- GMOs: threat to nature of chance for humanity?
- Nuclear power: potential killer or clean energy source?
- Drug patents: obstacle to treating the poorest or incentive for R&D?
- Boycotting Burma: fostering or slowing democracy?
- Biofuels: green mobility vs right to food?

Beyond the general goals and principles, information is therefore needed for defining ethical criteria, for setting what an ethical behavior means in practice.

## Gathering information for assessing practices: the problem of credibility

Information is also needed for assessing the policies and practices of companies against the set criteria. Such information can be sourced from the companies themselves. Originally social rating agencies tended to use companies as their main source of information.

Such quest for transparency is challenged by confidentiality and by the voluntary nature of sustainability reporting. Companies naturally tend to focus their communications on the positive aspects of their performance.



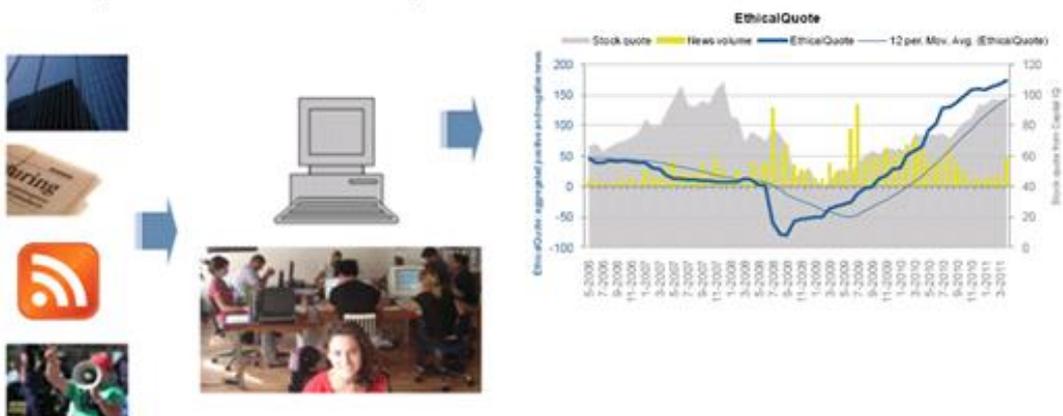
Information for assessing corporate sustainability can also be sourced from third parties such as NGOs, media, or blogs; such information can be positive or negative regarding the role of companies.



So, whom should we believe? Companies or third parties? What kind of information should we use? Positive or negative? Whether considering to use internal or external information, we have to deal with the **problem of credibility** of such information.

## Tracking the ESG reputation of companies

While relying on universally shared values, the methodology developed by Covalence faces the characteristics of modern society such as cultural diversity, democratic debate and scientific uncertainty, and the challenges of defining objective criteria and credible information sources.



Covalence measures the ESG reputation of companies by confronting quantities of positive and negative news pieces gathered on the web from various sources. Covalence has developed a unique combination of automated content processing of texts in original language with qualitative assessment by an international team of analysts. The combined use of Natural Language Processing and human analysis allow us to interpret large amounts of data within a short time. More than 500 intern analysts have contributed to this work since 2001, in partnerships with many [universities](#).

Covalence's approach addresses the problems of subjectivity and of credibility by integrating multiple opinions and information sources in a dynamic and democratic way. Measuring the ESG reputation of companies helps to approach an invisible reality – their real ESG performance.



Due to the complexity of the object of study we rely on systemic theories as applied in political science (See: David Easton, A Systems Analysis of Political Life, 1965). Following such systemic theories, our object of study, the company, is considered as a black box in which one cannot see as it is too complex. The observer rather focuses on information inflows and outflows.

We assume that the raw data mainly consists of text, as opposed to numbers. A parallel can be made with another complex field of research: medicine. Health records are largely composed of text ; text analysis is therefore needed for researching into, and classifying these records.

Other methodologies rely on Key Performance Indicators (KPIs) used to assess companies with quantitative ESG metrics. Such KPIs rely on agreed definitions of criteria and on consensus around the credibility of information sources.

The methodology used by Covalence can be considered as complementary rather than opposed to KPIs. It is interesting to compare numerical performance on KPIs and reputation scores such as Covalence's: it allows to confront different points of views, different perceptions, and to generate broader ethical profiles of companies.

### **Basic metrics: quantities of positive and negative news items**

The basic metrics used by Covalence are quantities of news items gathered on the web (texts, web pages), that can be coded as having a positive or a negative orientation towards named companies (polarity, sentiment). More precisely, a distinction is made between “ethical offers” (“information on what the company does for society”, positive news, compliment), and “ethical demands” (“information on what the company should do for society”, negative news, criticism).

Explicit positive or negative words have to be found in the text for demonstrating an orientation and allowing the document to be coded and accounted in the system. Examples of negative words: “predator”, “undermining”. Examples of positive words: “contributing”, “helping”.

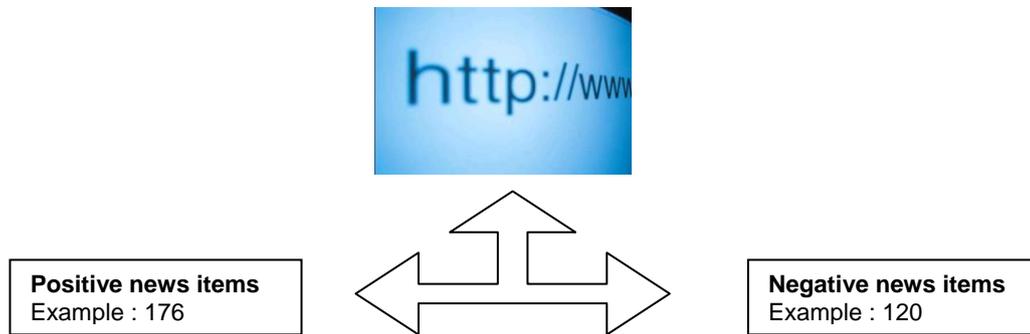
To be coded into Covalence database a text must also be related to at least of the 50 Covalence EthicalQuote Criteria. One criteria only is used if there is little information (usually a short document), and two or more criteria are used if the document provides detailed information (longer document). For the purpose of coherence and stability, 5 criteria is the maximum allowed per news item.

#### **Here is how relevant texts are accounted and weighed:**

- A text receives 1, 2, 3, ... points, whether it is coded with 1, 2, 3, ... criteria.
- The point(s) received by a text gets a positive or a negative sign according to its orientation. Texts can therefore weigh -1, -2, -3, ..., +1, +2, +3,...
- A text may be entered twice if both orientations are found: for example, the same press article can be coded once as a positive news with criteria 3 and 24 (weigh: +2), and once as a negative news with criteria 34 (weigh:-1). The cumulated weigh of the text will therefore be (+2) + (-1) = +1.

## Calculating the EthicalQuote score and ranking

Positive and negative news items are searched everyday on the web and accounted. Quantities of news items are calculated for each company, for each period of time as well as in a cumulative way.



In Covalence research quantities of positive and negative news items are represented in green and red bars and are analyzed in terms of criteria and criteria groups, issues & keywords, companies and sectors, source categories, regions and countries of source.

### Score: an absolute measure biased by media exposure

A reputation score is obtained by subtracting negative news from positive news. When a majority of negative news is observed the score is a negative number.

A = Positive news (ethical offers)

B = Negative news (ethical demands)

S = Score

$S = A - B$

**Score**  
Example:  $176 - 120 = 56$

The score offers an absolute, quantitative view of a company's sustainability communications and perception. It encourages companies to demonstrate their responsibility and be more transparent.

However, the score induces a bias due to media exposure and size, be it in positive or negative territory: a large company, with a large PR budget, will tend to reach a high score; as a large company may also be a favorite target of campaign organisations, it can also get a very low score. The score makes it difficult to compare companies of different size and media exposure as the largest companies tend to be over- or under- rated.

### Rate: a relative measure for controlling the effect of media exposure

To overcome the bias due to media exposure and size, a rate is being introduced in the calculation formula. The rate is an expression of the net ethical performance of the company. It is the score confronted to the overall volume of news affecting the company:

**Volume**  
Example:  $176 + 120 = 296$

$V = \text{Volume} = A + B.$

$R = \text{Rate}$

$S = \text{Score} = A - B$

$R = S / V$

**Rate**

Example:  $56 / 296 = 0.19$

The rate provides a relative, qualitative measure of the ethical reputation of a company, while the score offers an absolute, quantitative view. How do you compare two companies with close scores but broad differences in rates? To solve this problem and allow for the most tangible benchmarking, a rate-adjusted score has been created. To fully validate a score of + 100, a rate of 100% is needed. As a consequence, a rate of 50% would halve the score to + 50.

The rate-adjusted score calculates as following:

$R = \text{Rate}$

$raS = \text{rate adjusted Score}$

$raS = S * |R|$

**Rate-adjusted score**

Example:  $56 * 0.19 = 10.6$

S is multiplied by the absolute value of R. S has always the same sign (-/+ ) as R. There cannot be a positive score with a negative rate, and vice versa, on a given unit of time (week, month, year).

**Erosion factor: controlling the effect of time**

The erosion factor (or value discount on past news) is a means to give less importance to old news than to more recent news – positive news (company PR, initiatives & reporting) and negative news (criticisms, crisis). The objective is to offer a more dynamic measure of ethical reputation allowing companies to progress while dissuading them to “sleep on their laurels”.

As a convention the factor of erosion has been set at 2% per month. A sixty months period (or 5 years) basis has led to 1.66% rate of erosion; this has been rounded to 2%. For instance, 100 points would be valued 80 after 12 months, 49 after 36 months, 30 after 60 months and 10 after 120 months or 10 years.

Here is how the EthicalQuote forms:

$EQ(t) = [S * |R|] + [EQ(t-1) * \{1-E\}]$

$EQ = EQ(t) = \text{EthicalQuote}$

$S = \text{Score}$

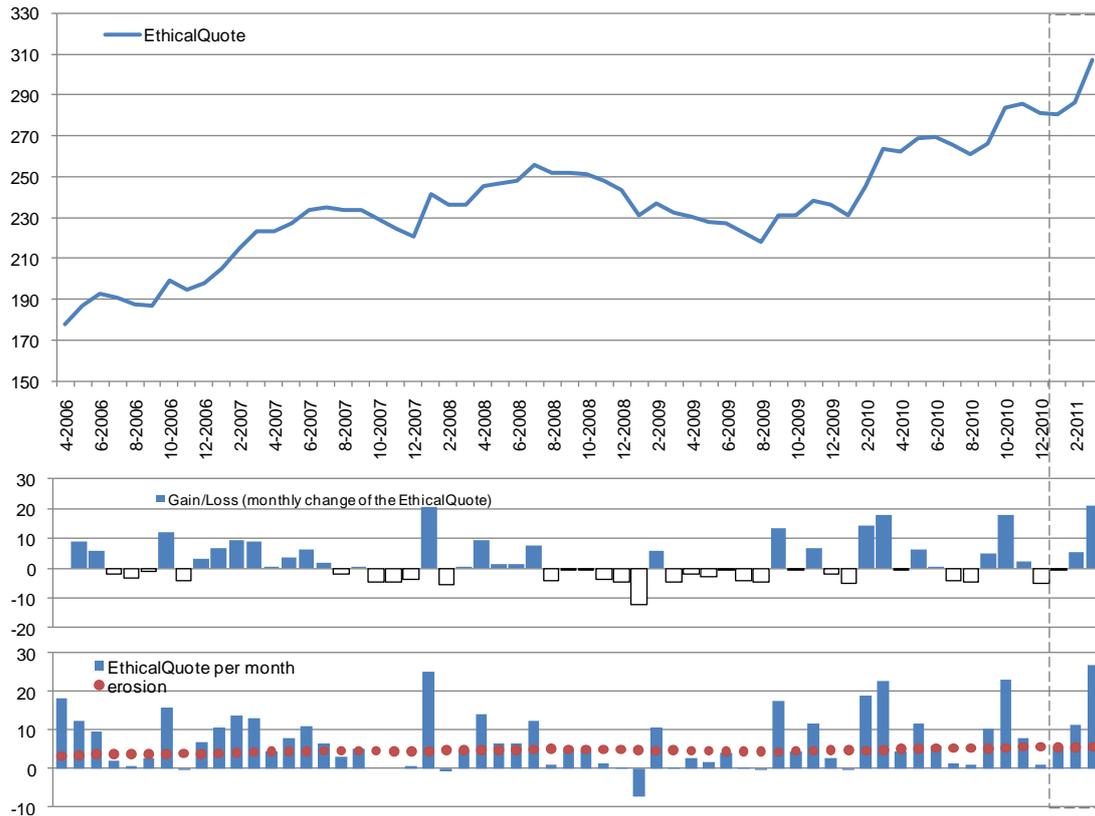
$R = \text{Rate}$

$E = \text{Erosion factor}$

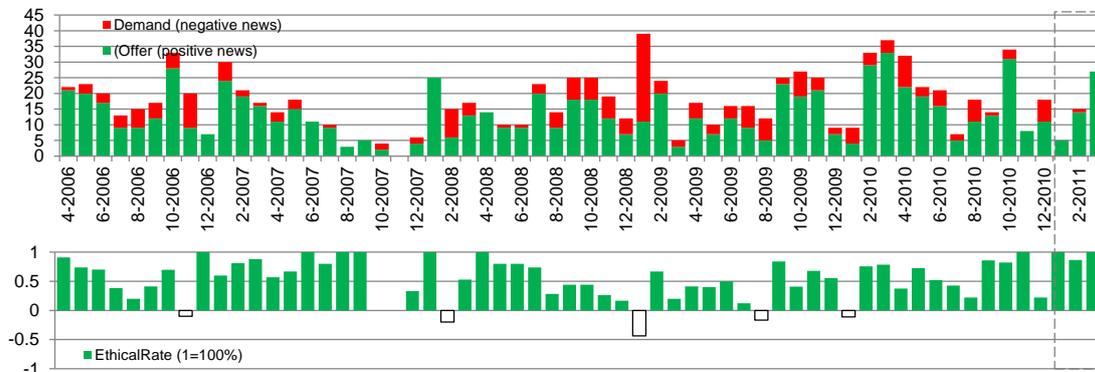
## Summary

The EthicalQuote score combines the difference and the ratio between quantities of positive and negative news items, and it is affected by a historical erosion factor.

The charts above display the EthicalQuote – the actual dynamic ethical reputation tracker, and the Gain/Loss representing the monthly change of the EthicalQuote. The third chart shows the EthicalQuote per month versus the erosion (red dots). The erosion is set at 2% of the EthicalQuote at t-1. It can be considered as the objective to reach in order to keep the EthicalQuote – hence ethical reputation - of the company unchanged.



The two charts below give a view of the gross material at the core of the metrics: Offer (positive news), Demand (negative news), volume (= Offer + Demand); the Rate (Offer – Demand)/ volume).



## Covalence EthicalQuote Ranking: controlling the effect of trends

News items are classified according to 50 criteria embedded in 7 groups: Governance, Commitments, and Engagement; Economic; Environmental; Labor Practices and Decent Work; Human Rights; Society; and Product Responsibility.

An ESG ranking should favor companies that show good performance in various domains, not only regarding a few hot topics. The effect of trends should be controlled, and a balanced approach of sustainability should be encouraged.

**Covalence EthicalQuote Ranking combines the score calculated across criteria (measure of popularity) and the scores calculated in each criteria group (measure of diversified performance).**

The formula used for calculating Covalence EthicalQuote Ranking is the following:

Ethical Ranking = R

RankGroup = Rg

Rank EthicalQuote = Req

A = Group A Governance, Commitments, and Engagement

B = Group B Economic

C = Group C Environmental

D = Group D Labor Practices and Decent Work

E = Group E Human Rights

F = Group F Society

G = Group G Product Responsibility

Rg (A,B,C,D,E,F,G); highest EthicalQuote ranks #1, lowest EthicalQuote #n;

$Rg = [Rg(A) + Rg(B) + Rg(C) + Rg(D) + Rg(E) + Rg(F) + Rg(G)] / 7$ ; lowest Rg ranks #1, highest Rg ranks #n;

Req; highest ranks #1, lowest #n;

$R = (Rg + Req) / 2$ ; lowest ranks #1, highest ranks #n.

### Grade

#### A to E

The capital letter reflects the position in Covalence EthicalQuote Ranking. It is a measure of **reputation**.

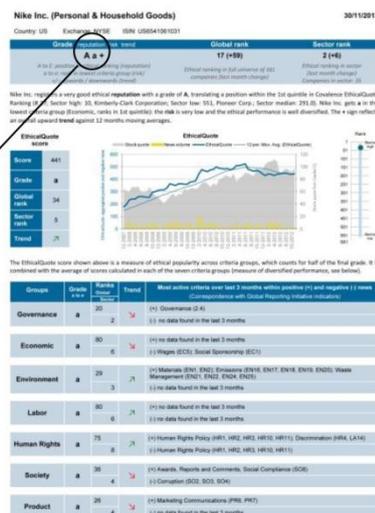
#### a to e

The small letter expresses the rank in the lowest criteria group. It is an indication of **risk**.

The gap between B and e can be interpreted as a lack of consistency of the company's ethical performance; a grade of Aa shows good reputation and consistency.

#### +/-

Upwards / downwards. Indication of **trend** based on 12 months moving averages. The +/- sign is given by aggregating trends calculated for EthicalQuote and the 7 criteria groups.



### Ranking

Covalence EthicalQuote Ranking combines the EthicalQuote score (measure of popularity) and the scores calculated in each criteria group (measure of diversified performance)

### EthicalQuote

Score calculated across criteria groups, measure of popularity

### Criteria groups

Scores calculated in each criteria group, measure of diversified performance

## Universe

Covalence EthicalQuote scoring system covers a universe of 2800 global companies within 18 sectors, as well as the 100 largest companies included in the [Swiss Performance Index](#).

## Criteria

The EthicalQuote reputation index aggregates thousands of documents gathered online from various sources and classified according to 50 sustainability criteria inspired by the Global Reporting Initiative's G3.1 sustainability reporting guidelines, as well as by the experience accumulated by Covalence since 2001.

These criteria follow the dimensions of the Global Reporting Initiative's sustainability reporting guidelines and are distributed in 7 groups:

- Governance, Commitments, and Engagement
- Economic
- Environmental
- Labor Practices and Decent Work
- Human Rights
- Society
- Product Responsibility

The 50 criteria cover the economic, social, environmental and governance impacts of companies. For example: Stakeholder Engagement, Local Sourcing, Emissions, Water Management, Health and Safety, Human Rights Policy, Local Communities, Lobbying Practices, or Product Compliance. They have the following characteristics:

- Rely on the Global Reporting Initiative's sustainability reporting guidelines
- Based on widely accepted principles, not on specific ethical choices, to cope with diversity and pluralism
- Capacity to cover changing aspects of companies' operations
- Capacity to cover diverse actions led by stakeholders and media coverage

Rather than definitive moral judgments, the criteria should be seen as open boxes allowing to store and organize information on a barometer, case-by-case basis. Covalence criteria are not sector-specific. They are designed to cover any multinational company and to allow cross-sector comparisons.

### Download:

- [Covalence EthicalQuote Criteria \(.pdf\)](#)

Additional legal references of Covalence EthicalQuote criteria are: the [Universal Declaration of Human Rights](#), the [OECD Guidelines for Multinational Enterprises](#), the [ILO Declaration of Principles concerning MNEs and Social Policy](#), the [Rio Declaration on Environment and Development](#), the [agreements of the World Summit for Social Development](#), the [UN Global Compact](#), and the [UN Millenium Goals](#), and the [UN Guiding Principles on Business and Human Rights](#).

In the process of setting its initial list of criteria, Covalence has undertaken discussions with, and used feedback from the following NGOs: [ADAP](#) (Association pour le Développement des Aires Protégées), [AGSI](#) (Association Geste Solidaire Immédiat), [GRAD](#) (Groupe de Réalisation et d'Animation pour le développement). The creation of Covalence in 2001 benefited from the support of the [Graduate Institute of International and Development Studies](#) (Geneva, Switzerland).

## Sources

Covalence gathers online information using search engines, individual websites and correspondents:

### Search engines

Search engines are the main providers of news aggregated by Covalence. They are used to gather information from millions of potential sources among Companies, Media, Blogs, NGOs, Consultants, Trade Unions, International Organisations, Governments and Academia.

### Individual websites

Covalence follows individual websites that regularly publish relevant content.

### Correspondents

Covalence allows interested parties to submit information, thus feeding the database and influencing the EthicalQuote of companies, in the spirit of a journal's readers section. Information can be submitted using the contact form or by email to [info@ethicalquote.com](mailto:info@ethicalquote.com).

The objective is to integrate publicly available material with documents and opinions received from a variety of observers.

A study by SustainAbility (UK) and Mistra Foundation, "[Values for Money: Reviewing the Quality of SRI Research](#)" (2004), places Covalence on their short-list and mentions Covalence's approach as among the best & most innovative practices for its "inclusive source model that allows stakeholders to include themselves in information gathering processes."

Covalence's network of local informers in developing countries is supported by the Swiss Agency for Development and Cooperation.

## Languages

Information is searched for in four languages: English, French, German, Spanish.

## Neutrality

Covalence does not see some sources as more reliable than others. Any source is considered equally. Covalence does not validate information sources, neither the content of information. What we do is collect, confront and synthesize the maximum of relevant documents from different sources. Our policy is to put ourselves in the position of an independent newspaper in front of statements, opinions, readers letters: publish any information provided it has relevance and an identified author, without endorsing its content.

<http://www.ethicalquote.com/index.php/services/methodology/sources/>

## **Equal weighing of individual sources**

Covalence follows a principle of equal weighing of individual sources. The “size” of source (audience, quantity of readers / viewers) is not taken as a weighing criteria, neither is placement in print press. Following are our arguments for applying such an equal weighing approach:

a) The modern world is characterized by social complexity, cultural diversity, ethical pluralism and scientific uncertainty: considering “small” sources at the same level as “large” ones is a way to cope with such complexity and diversity.

b) It is technically difficult to measure the size, or popularity of sources and find a weighing factor for such an heterogeneous ensemble of sources as large medias, specialized NGOs, individual correspondents and multinational companies’ headquarters.

c) Western and Anglo Saxon sources are overrepresented in Covalence database, because such sources are more numerous online and are more easily accessible than others. Applying a weighing factor could amplify the already existing overrepresentation of Western and Anglo Saxon sources.

d) Some search engines email alerts used by Covalence only cover pages with the highest popularity (page rank): for a part the most popular pages are already naturally selected.

e) Echoes, repetition make weigh. Often one particular issue is covered by different sources. This produces several points in Covalence database, and this is how a weighing process is naturally working: the system measures the noise made by news, the echoes generated by a story among numerous sources. Rather than one particular document, it is the aggregation of a large number of documents that gives a significant picture of reality.