

ESG Now Podcast

“Unwrapping the Green Claims of Plastic Packaging”

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Margarita Grabert:

Hello and welcome to the weekly edition of ESG Now, the show that explores how the environment, our society and corporate governance affects and are affected by our economy. I'm Margarita Grabert, your host for this episode. Plastic. Plastic has just become a basic reality in everyday life, which isn't surprising. It's cheap, durable, and incredibly versatile. And with the way that plastic use is growing, some estimates reckon we'll double our use of plastic by 2050. There's increasing pressure from governments, regulators, consumers, and NGOs to do something about the negative side effects of plastic. The companies that make this plastic or rely on it for their packaging have taken notice as well. A lot of them are releasing a colorful array of pledges, targets and promises about how they are tackling the challenge of plastic waste. And that colorful array is what we're going to tackle on this episode. The types of claims that companies are making about the recyclability of their products, just how feasible these pledges are and what risks might manifest in the coming years. So thanks for joining me today, and let's see where this story takes us.

So in preparing for this episode, I tried to imagine my average day without plastic, and I didn't get very far. Not much past brushing my teeth or even have an alarm clock wake me up in the morning. I did also browse for some more edgy concepts like fully compostable shoes, but I couldn't get quite past the aesthetics. And the peace of mind that comes from how durable plastic is, is precisely because it doesn't compost. For the most part it can't biodegrade and can last for hundreds of years in the environment. Which is great when you're looking for something durable but not so great when you actually want it to biodegrade. And aside from being this long-lasting material, making plastic in the first place is itself an environmentally impactful process with most manufacturing relying on inputs like gas, coal, and oil. So given this combination – how much plastic we use, its persistence and the impact of its manufacturing, there are a lot of stakeholders that have been thinking about how to recycle it and how to build a circular economy around plastic.

A big part of this is around trying to figure out a way in which we can use existing plastics and turn them into new products and reuse these materials rather than sending them to a landfill or extracting new resources for their production. And the idea of a circular economy for plastic is not just arising in environmentally conscious NGOs. It's becoming a much more embedded concept for the average consumer and for governments and regulators too. For investors, it might be useful to understand just how exposed their portfolio is to different kinds of plastics, how individual companies are addressing risks like recyclability, and how these risks might ultimately manifest and even potentially affect their bottom line. To help me figure out all of that, I called up Sam Block out of MSCI's Chicago office, and to start off, I asked Sam about what types of plastics there are, and the first thing he did was give me a rundown of the seven types of resins that make up plastics and how they all relate to specific recycling symbols. But more importantly, he tells us how recyclable these plastics might actually be.

Sam Block:

Most plastic packaging is usually categorized as either rigid or flexible, but most people are probably familiar with the seven categories of resins that makes up plastics. Recycling symbols one through seven, they tell everyone what's what. Number one, polyethylene terephthalate, most commonly

referred to as PET or P-E-T, the most common type of plastic drinking bottles. But while we're able to identify all these different plastics by the recycling symbol that they have on them, the actual ability to recycle them definitely differs a lot. I would say there's three main factors that determine the recyclability of a package. The first one is just where the product is sold or consumed and the capabilities of the recycling in that area. The second factor I'd say is the resin used. And the third is just the design of the package if it's designed to be recycled or not. And many places, the type of plastics that are accepted by the MRFs, the Material Recovery Facilities, they restrict a lot of different types of plastics.

Several of the seven resin categories, despite the recycling symbols, are just not commonly suitable for recycling. Flexible plastics like plastic bags, films, in many cases, the MRFs just won't accept flexibles because these flexibles, they can get into these mechanical recycling machines, they can clog them up. It can reduce the yield of the recycling streams. It leaves us with just a few resin categories that are actually really suitable for recycling, which are the PETs and the HDPEs, the number one and number two. But the success rate still varies a lot depending on location. Some parts of Europe have recycling rates of like 80 to 90% of PET while in the US it's still less than 30%.

Margarita Grabert:

So as Sam just told us, not all plastics are created equally, at least when it comes to recyclability. There seem to be a few main issues at play here. The first is that there's no universally defined list of materials and designs that might be recyclable. There are various recycling standards and guidelines that companies can refer to, but they all seem to have many different approaches on what they consider designed for recycling. Like Sam told us, even when packaging does include steps on how to separate materials and divide them into recyclable and non-recyclable, a lot of people don't see this or won't go the extra step to do this, which in turn limits how much can be recycled. And when it comes to the materials that are used, there's just as many challenges. Depending on which plastic resins are used this can affect the recyclability, the cost of recycling, and whether it can be used in another generation of plastic.

This is what Sam was telling us when he explained the difference between various types of plastic. He mentioned that even certain types of plastic like the flexibles can actually create more problems for material recovery facilities or MRFs, as Sam put it, as they can create blockages, have low yields at the end and might even be producing lower quality plastic once it's recycled. So it might not even be profitable for many of them to process such materials. And the second barrier to recycling is that even if the material could be recycled, in theory, it might not be possible in practice. This is because in many parts of the world, the infrastructure needed to recycle the plastics is just not there yet, where things like large-scale waste collection and management systems would be needed. This means that even if many plastic products might be recyclable, in theory, they might not actually end up recycled or reused. And this leads to my next question for Sam. Given these challenges around recycling, I wanted to know a bit more about the claims and commitments the companies are making about the recyclability of their products.

Sam Block:

Well, we saw that around a thousand different organizations, including NGOs and governments, but also corporates that represented about 20% of the global plastic packaging use, as well as about 27 financial institutions with over \$4 trillion in assets under management rallied behind this Ellen McArthur Foundation's global commitment. And that was focused on the circular economy. And one of the goals was for companies to commit to making 100% of their packaging recyclable, reusable, or compostable by 2025. And companies have been making a lot of strides in improving on these metrics. But what we saw was even though they want a hundred percent in these three categories, almost all of them and almost all of the activities we saw was focused on making their packaging more recyclable. We saw very little uptick in reusability over certainly, as I spoke to earlier, making something recyclable does not necessarily mean that it will be recycled in practice.

Mondelez reported that 84% of its packaging was technically recyclable, but it was only able to say that 5% was recyclable at scale. And that's based on kind of a technical definition by the Ellen McArthur Foundation that states that to claim something is recyclable, that needs to be recyclable in practice and at scale. And that is defined as having over a 30% recycling rate in a region that contains over 400 million people. They're not the only company like that. Unilever, Starbucks, Target, Kellogg and others have targeted 100% of their packaging to be recyclable, reusable, or compostable by 2025, but still had over 50% of their packaging made from plastics that we identified as being less suitable for recycling.

Margarita Grabert:

All right, so it's clear, companies are making commitments on plastic recycling. As Sam just explained, around 20% of global businesses involved in plastic production rallied behind the Ellen McArthur Foundation's global commitment on the circular economy. And as Sam just put it, there have been positive strides in making packaging more recyclable, but it seems like these plastic manufacturers are focusing more on the recyclability aspect and not so much on the reusability, which arguably would be the better outcome. And when Sam crunched the numbers, he found that from 89 companies that were in the global progress report, 77 of them had less than 10% reusable plastic packaging by weight. In comparison, 18 companies had 80% or more that was recyclable in theory. And this is the crux of the problem, just because something in theory is recyclable doesn't actually mean it will be recycled. I asked Sam to tell us a bit more about the actual recycling achievements he's seen and what might be hindering companies from reaching their circular economy goals.

Sam Block:

Many companies really have a hard time moving into the circular economy in a real impactful way for a variety of reasons, number one being that it can be hard to use post-consumer recycled materials, especially for food applications. I would also add, in many cases, virgin plastic resins are cheaper than recycled plastic resins. To be fair, a lot of companies have made a lot of progress. One of the major steps that we have been seeing a lot of companies take is eliminating unnecessary plastics moving away from some of these plastic resins that are most difficult to recycle. H&M for instance, stated that in 2022, around 50% of their plastic packaging was actually from polystyrene. And the reason they used so much of that was actually because for the clothes hangers that they were using. But it's stated that it since shifted away and made now most of its hangers are going to be using recycled polypropylene. It may be better, but still hard to recycle polypropylene. I would say overall the beverages' industry is probably leading in recycling. Most of the other industries, apparel, household, personal care, food, cosmetics, retail, they only had about 50% or less of the resins that they use were actually of the type that were most suitable for recycling. We'll say many companies have made a lot of progress in terms of eliminating unnecessary types of plastics and eliminating designs that just make recycling harder, but they're still out there.

Margarita Grabert:

So it seems like there is some light at the end of the tunnel. As Sam just told us across various industries we are seeing more companies focus their plastic use on plastics that are easier to recycle, or companies that are even eliminating unnecessary types of plastic like H&M, for example. But even with more companies focusing on making, recycling and reusing a possible reality, it is challenging to verify their claims and commitments, especially with the still limited disclosures we are seeing. As Sam told us, while major players like Mondelez, Kellogg and Starbucks are disclosing more, our data shows that only around 20% of the companies from the MSCI-ACWI Index that are dependent on packaging materials provided a full material mix disclosure. Even with these gaps in the disclosures, it seems like there are positive strides towards incorporating plastics into a circular economy. Sam tells us more about why companies are diving into this recycling topic now and how regulators are becoming more savvy and seeing past some of the soft commitments companies have been making.

Sam Block:

The plastic issue, I think has been ramping up for several years. I mean, it certainly took a backseat during COVID. It's grabbing headlines since 2018 when China started to restrict the import of plastic waste and a bunch of other countries followed. And there was a bit of a scramble, especially in Europe, that we started to see a lot of new anti-plastic rules getting passed. Regulators have begun to act. Number one, I think maybe most importantly potentially is a new UN treaty that basically stated that there needs to be an enforceable way to reduce plastic pollution. I think one of the main developments have been around crackdown on greenwashing, the environmental claims that companies make that may actually be misleading if the company claims environmental benefit and that benefit's not really there.

Or maybe even worse, that can be a problem in regulators eyes and there may be a problem for companies in the future. For instance, Australia, this past December, published new rules that stated that making sustainability claims that they basically consider as misleading could come with a 50 million Australian dollar fine. And the EU has also proposed a rule that said misleading environmental claims could actually cost a company 4% of the annual turnover in the region. And I certainly think that companies that make circular economy claims could be vulnerable to some of these crackdowns by the regulators.

Margarita Grabert:

It looks like the debate on what is greenwashing and what is actually contributing to the circular economy might be here for a while, but companies claims about environmental benefits that are misleading are more under scrutiny as Sam just told us. So it seems like in the coming years, companies involved in plastic packaging will need to provide more details on how they're going to recycle and reuse plastic and not just if their products are recyclable in theory. Even with this tightening regulatory landscape, where we are today isn't good enough, as there's still a lot of claims from companies that are just too vague or unclear or just outright don't disclose anything. For example, a 2020 study by the EU Commission found that around 54% of environmental claims made in the EU were vague, misleading, or even unfounded.

Companies might need to start providing clearer commitments and strategies on how they want to manage their plastics, or these claims might become real financial risks in the coming years, especially as more regions around the world have passed or are likely to pass rules that are going to try to limit misleading and vague claims around plastic recycling, which in turn could cause companies to pay hefty financial fines and penalties and really affect their bottom line. So with these increasing levels of scrutiny on the circular economy claims, I wanted to know what could investors go out and do, especially as they begin to think about the potential financial impacts companies could be facing in the coming years. Sam tells me a bit more about his investor engagement suggestions to try and fill this gap.

Sam Block:

So I think investors can start by identifying those industries that most contribute to plastic pollution and the ones that are most vulnerable to future market restrictions due to dependency on single-use plastics and understanding that this is a long-term sustainability challenge and businesses will probably have to change to address it. The reality is many companies over the past few years have really increased their rhetoric around circular economy trying to at least brand themselves as being on board with solutions for circular economy. But I do think the real solutions in many cases are really lacking. So knowing which companies are making claims about recyclability, but understanding also where those gaps are in recyclability and those claims are certainly important.

But once the investor identifies companies or industries that are most vulnerable here and they want to make sure that the company is doing what it can, certainly we want to make sure that the company itself is managing the issue and is even aware of the risks and is transparent about it and making sure

that the company is working with its suppliers, working with its customers, understanding the customer's perspectives, and also working in collaboration with waste management companies, making sure that what it designs and what it produces is something that waste management companies are able to recycle and the capacity is there and that they're selling it in locations... The product that they're selling aligns with the capabilities in the location that they're selling it. So maybe asking companies how they're adapting to different challenges in different locations around the world, asking them to increase transparency on the issue, asking them just to gain a better understanding about the challenges are for the companies from moving forward and offering more circular economy solutions.

Margarita Grabert:

Right. We've come a long way since I was contemplating compostable shoes. We've seen that not all plastics are created or recycled equally, and the type of plastic that a company makes or relies on can have a big impact on its ambitions in a circular economy. It's also fair to point out that there has been a lot said about the ills of plastic, but in some cases, the risk to companies of not rising to the challenge have been pretty small. But as Sam sees it, that's starting to change, more quickly in some places than in others. And sure, consumers may be appreciative of companies that advertise water bottles that are made with recycled plastic, or would even be willing to meet companies halfway by risking a delicious smoothie on a paper straw.

But investors might be less forgiving, especially if companies aren't forthright about their product risks, about how recyclable their packaging really is, or about how they plan to reformulate their materials. So that's it for this week. I want to say a big thank you to Sam for joining me today and giving us his take on the news with an ESG twist and a big thanks to you for listening. If you enjoyed our content, feel free to give us a like or some stars or even subscribe on whichever platform you are listening from so that you can hear me or one of our other regulars again next week. Thanks again and talk to you soon.

Bentley Kaplan:

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