

CDP Europe's comment on European Commission's Fitness Check of the EU Water Framework Directive, its associated Directives (Groundwater Directive and Environmental Quality Standards Directive) and the Floods Directive

Background

Flowing through every part of our economy, water is a fundamental necessity for lives and livelihoods. Access to safe, sufficient and resilient water, sanitation and hygiene and the sound management of freshwater ecosystems are essential to economic prosperity, health and development outcomes, and to environmental sustainability. Yet, the world is not managing water well or making the most of it.

Water security represents one of the greatest challenges that businesses, investors, governments and citizens will face in the upcoming decades. Parts of Europe are heavily affected by water-related hazards, and disclosers to CDP make this clear in reporting the extent to which their vulnerability to water risks influences their actions. **Broader action, better risk assessment and strengthened cooperation among the public and private sectors** are crucial steps to manage water risks, protect citizens and seize the opportunities arising from a better water stewardship.

Water Security: The reliable availability of an acceptable quantity and quality of water for health, livelihoods, environment and production, coupled with an acceptable level of water-related risks¹. It is realised to the degree that water scarcity is non-existent, or has been decreased or eliminated, and to the degree that floods and contamination of freshwater supplies are non-threatening.

Key actors to achieve the EU water goals

- ▼ **Companies in the most water impactful industries**, in particular, those involved with the finance, food, energy, industrials, textile and material systems. Companies in the food, textile, energy, industrial, chemicals, pharmaceuticals and mining sectors account for and wield influence over **70% of the world's freshwater use and pollution**. In almost all cases, their business models, practices and products do not align with a water secure future, a future in which SDG 6 has been achieved.

¹ David Grey & Claudia W. Sadoff (2007-09-01). "Sink or Swim? Water security for growth and development". Water Policy. Iwaponline.com. 9 (6): 545–571. Retrieved 2014-08-16.

- ▼ **Cities, States and Regions:** sufficient water supply, water quality and water security are sine qua non for communities to live and thrive. As water demand is growing and climate change is increasing the frequency of severe weather events from droughts, extreme rainfall and flooding also in Europe, urban water challenges are now as urgent as ever. European cities, states and regions are called to play a major role planning and managing water supply, building water efficiency, strengthen climate resilient infrastructures and smart water grids, with the ultimate aim of protecting citizens and business in short and long-term. Better monitoring and strengthened transparency will allow local authorities to catch opportunities to rethink the way that water is addressed in city design, policy and infrastructure development, and enhance their dialogue with investors and corporations.
- ▼ The **financial market** which powers the economic activities that affect our freshwater, can work to protect it. By increasing the transparency of this sector, and other high impact sectors, as it relates to the transition to a water secure future, the flow of capital can be redirected away from those businesses, products and practices that deplete freshwater resources, towards those that protect them. This can catalyse a desire to grow differently amongst the private sector and its extensive supply chains, sparking transformations and innovations that decouple production and consumption from the depletion of water resources.
- ▼ The **EU and the European national governments** can enact new minimum requirements and standards in policy, based on best market practice and in line with the EU goals on water security and quality. Governments can better understand and link the water actions of the 3 key stakeholder groups - corporates, cities, states and regions and investors and banks. Qualitative and quantitative information regarding water stress, usage, efficiency, targets and impact of business operations and cities' populations on water resources along their supply chains can be used to inform policies targeting the financial market to ensure that capital is allocated in line with the protection of water resources in Europe and globally. Lastly, governments can use their own spending power by integrating water stewardship at the heart of their public procurement decisions.

Our input focusses on four areas.

▼ **Corporate disclosure and action**

Strengthening the corporate reporting framework by specifying disclosure requirements of corporates on water security throughout their entire supply chains, notably considering the Non-Financial Reporting Directive.

▼ **Cities, States and Regions disclosure and action**

Enabling cities, states and regions disclosure of risks associated with water security, supporting them assessing their climate-related vulnerability and developing plans for

increasing resilience; and assisting cities in showcasing projects they are pursuing across water and climate to investors and in working with corporations in a meaningful way.

▼ Sustainable Finance

Integrating water risk assessment into policy measures targeting investors and banks, notably considering the legislative and non-legislative measures of the EU Action Plan on Sustainable Finance.

▼ Public and private procurement

Encouraging better management of water-related impacts of suppliers and act as a driver of positive action on water stewardship in supply chains; and embed sustainability criteria into procurement standards.

1. Corporate disclosure and action

The [CDP Europe report 2018](#) reveals that 183 companies responded to CDP's water questionnaire, with 11 companies having achieved an A score.

- ▼ 62% of European companies identify water-related risks to their direct operations or wider value chain
- ▼ European companies estimate €4bn of financial impact from water-related issues in the past year
- ▼ 80% of European companies state that the availability of sufficient good quality freshwater is important or vital to their direct business operations
- ▼ 92% of European companies have a water-related target or goal in place
- ▼ 30% of European companies with targets are looking at water quality issues

A majority of European companies admit that their **business models are highly dependent on water availability and quality**. Four-fifths (80%) claim that having access to sufficient good quality freshwater is either important or vital for their own direct use, and two-thirds (64%) believe the same is true indirectly in areas outside of their operational control. The scale of this dependence exposes the risks that these businesses will face in a world with greater water scarcity and degraded freshwater quality.

Indeed, a fifth of European companies (22%) reported suffering from some sort of water-related issues in the past year, with a **total estimated financial impact of around €4 billion**. Drought and flooding are the most prominent of these, resulting in serious disruptions to production capacity, increased operating costs, and directly impacted company assets.

As multinational businesses, these **water-related impacts have been felt around the world**: from droughts in the Cape region of South Africa impacting agricultural supply chains; to heavy

rainfall and flooding in India damaging infrastructure and shutting down manufacturing facilities; through to dangerously high pollution levels in the Yangtze river in China. The insurance industry is also facing the costs of remedying damage, with premiums in many industries rising to reflect more frequent incidents of extreme weather.

A majority of companies (62%) have identified that they face some sort of **water-related risk**, which could occur in **direct operations or the wider value chain**. The risks most commonly identified are physical impacts, particularly water scarcity or droughts and flooding.

A quarter of respondents also disclosed that they are subject to **regulatory risks**, such as tighter water discharge rules related to quality and volume. For example, in some markets such as India and Thailand, companies report that they are now required to evaporate wastewater instead of discharging it. And this results in **increased operational costs**, due to additional energy requirements for evaporation compared to discharge.

Across the 183 European businesses reporting on water this year, they assess a **total financial value at risk of €16.4 billion from water-related risks**. A number of respondents also reported difficulties in providing a standalone figure to quantify their water risk, suggesting that the true financial impact could be far higher. And significantly, these companies also assess that the cost of responding to their water-related risks is around €6 billion, highlighting that inaction could be substantially more expensive than the costs of action.

Companies also point to the fact that they have a number of **positive water-related business opportunities, amounting to a total estimated financial value of €58 billion**. The most commonly identified this year were improvements to water efficiency (38%) including 34% resulting in cost savings, opportunities to increase sales of products and services (29%), and an increase in resilience (15%).

Addressing more complex water risks and opportunities can pose a particular challenge, as issues frequently centre around an entire river basin relied upon by multiple communities and businesses. The ability for individual actors to make a difference by themselves can be limited. Many businesses in Europe are exposed to water risks through their supply chain, or operations in regions outside of Europe. In cases such as shortages in the Rio Grande - relied on by Mexico and the USA - these challenges can become politically charged.

However, some of these difficulties are being overcome through **collaborative action and engaging with global supply chains**. For example, in Bangladesh the IFC leads the Partnership for Cleaner Textile (PaCT). This brings together development funding and support from some of the world's large clothing brands and retailers – including the governments of Denmark and the Netherlands, and a number of major European businesses – helping transform approaches to water and wastewater management across the country's textile industry.

Solving these challenges also offers business **benefits beyond overcoming the more immediate or obvious risks**. Improving freshwater availability, taking pressure off groundwater reserves, and reducing pollution can benefit the health, wellbeing and wider economic success of local communities and ecosystems. In turn this can help local industries to thrive, strengthening supply chains and supporting sustainable development.

The **environmental and financial impact resulting from water management issues is being increasingly recognized as a crucial topic for companies** to address, across their own operations and supply chain. And of the 183 companies responding this year to the CDP water questionnaire, 65% demonstrate that they have taken this into account in their business through having a publicly available water policy setting out a clear position on water management. Almost all respondents (92%) have some sort of water-related target and goal in place, most with targets at several levels. This represents a substantial increase from the 61% of companies doing the same last year. Although it should be noted that the comparison relates to an expanded set of disclosures, particularly with this year's CDP Europe report including for the first time business in the UK and Ireland.

And while the **majority of targets (81%) are fixed at a company-wide level**, 17% are only at a site level. The increase in companies disclosing that they now have water-related targets and goals this year suggests the profile of these issues are continuing to increase. The most frequently cited motivations behind taking action appears to be some combination of a desire to reduce the environmental impact of a business, demonstrate good water stewardship, mitigate risks, and deliver cost savings. It is also of note that where companies have used a scenario analysis approach to understand their climate related risks and opportunities, over half (56%) identify some sort of water-related outcomes that could affect their business.

Companies have largely **aligned their water targets and goals with the achievement of some of the specific targets sitting under the UN's Sustainable Development Goal (SDG) 6 on Clean Water and Sanitation**. Most companies with targets focus on improving water efficiency (88%), along with a sizeable number (30%) looking at water quality issues. However, very few are setting out specific goals that would directly contribute to some of the more systems-level SDG 6 ambitions such as the protection and restoration of water ecosystems, or access to water and sanitation. There is an increasing adoption of market-based approaches to drive action in companies, reflecting a growing recognition that the business costs related to water and wastewater could increase steeply as regions face water scarcity and quality issues, which could be exacerbated by climate change. There are now 13% of responding companies implementing an **internal water pricing mechanism**, with a further 30% are currently exploring **water valuation practices**.

Looking at the longer term, **water-related issues are being integrated into the planning and strategy of a majority of disclosing companies**: 63% of companies integrate water-related issues in their financial planning, 71% into their long-term business objectives, and 74% in their strategy for achieving long-term objectives. Although of those companies including

water in their long-term strategies, the time horizon considered is most commonly between 5 and 10 years, still not fully factoring in the SDG timeframe out to 2030.

Conclusions for Corporates

- ▼ CDP's water [A List 2018](#) features eleven European companies. Just 31 companies globally achieved an A score for water, a significant drop from last year's total of 74. The 11 European companies on the water security A List represent 35% of the global total;
- ▼ Scale and urgency of the environmental challenge posed by water security is huge and European companies can show global leadership by increasing in discloser numbers and by intensifying engagement with their supply chains on water stewardship.

2. Cities, States and Regions disclosure and action

- ▼ Over 160 European cities out of 628 cities globally disclosed to CDP in 2018
- ▼ 53 European states and regions out of over 120 globally disclosed to CDP in 2018
- ▼ 34% of European regions see substantive risks to their water supply in the short or long term, mainly increased water stress and scarcity, declining water quality, flooding and inadequate or aging infrastructures
- ▼ The top risks to water supply reported by cities are increased water stress and scarcity, flooding, and declining water quality
- ▼ Most commonly reported climate hazards by European cities and regions are extreme temperature (mainly heat), floods, droughts, precipitation, mass movement. These risks are addressed by adaptation measures such as policy, mapping and modelling, biodiversity, engagement, infrastructure, planning, awareness campaigns.

Often climate related activities in cities are isolated from economic development outreach, creating communication and **information barriers between cities and potential investors**. The [Matchmaker](#) project bridges this divide by working with cities to highlight **projects in flood control**, waste management, sustainable transportation, renewable energy, **water management**, and energy efficiency. Matchmaker serves as a clearinghouse for cities to showcase planned projects to the finance sector and better position them to mitigate against and adapt to climate change.

In 2017, European cities identified USD 21.360.703 total cost of water management projects, with 27% of projects either in scoping, pre-implementation or operational implementation phase².

² <https://www.cdp.net/en/cities/matchmaker>

Conclusions for Cities, States and Regions

- ▼ Include water security in vulnerability assessment and adaptation plans;
- ▼ Set ambitious water efficiency and reuse targets;
- ▼ Capitalize on opportunities to reduce and recycle water;
- ▼ Invest in water management and river basin projects;
- ▼ Attract private sector finance for water smart urban projects.

3. Sustainable Finance

Finance enables agribusinesses to pump ever increasing amounts of non-renewable groundwater, it enables tailings dams to be constructed at the heads of free-flowing rivers and enables chemical companies to release toxic pollution, but it can also be the key to changing all of this. **Failures of leadership in markets and governance** cause systemic and pervasive water insecurity issues: from lack of access to safely managed drinking water for more than 2.1 billion people to water pollution caused by wastewater discharge, 80% of which re-enters the water cycle untreated, and even untimely death, with a staggering 850,000 people dying each year of preventable diseases such as diarrhoea (UNICEF, 2016). The tug of war between scarce supply and increased demand, driven by economic growth and exacerbated by climate change could cost some of the world's regions up to 6% of GDP by 2050 and lead to sustained negative growth in some regions of the world, spur migration, and spark conflict³. The world is not on track to meet SDG 6, and this significant flow of capital is greatly undermining our ability to change course.

The ways in which businesses affect freshwater resources, is enabled by banks and institutional investors. In the absence of effective global corporate governance, **commercial banks and their institutional investors can offer unique incentives for change** by ensuring their investment and lending practices drive improvements in water security.

As water crises worsen, banks and institutional investors will become increasingly exposed to risks that could threaten their reputations, revenue and financial stability. Concurrently, as governments around the world move to address this issue and achieve SDG 6, banks, and the companies within lending and investment portfolios, face substantial risks of stranded assets if they fail to move with the times. Yet, a recent CDP survey suggests that **awareness of these issues is low**: while 70% of responding financial institutions regard climate change as an important issue for their institution, this number drops to just 22% for water security. The perception of materiality of the issue within banks appears to be at odds with reality. This is worrying given the recent report⁴ from the Dutch Central Bank warning that the Dutch financial services sector is exposed to €97billion of risk due to water scarcity.

³ SDG6 Synthesis Report 2018 on Water and Sanitation

⁴ Values at risk? Sustainability risks and goals in the Dutch financial sector

The **lack of water risk awareness** means that banks often fail to undertake adequate due diligence on their lending as it relates to water security. Moreover, the policy, regulatory and supervisory structures that dictate how capital is allocated within the financial sector, do not mandate any consideration of water security issues in lending decisions. Thus, a **policy vacuum compounds the lack of awareness and accountability** among commercial banks. It is clear that the policies set by central banks on macroprudential and microprudential issues are critical for system change.

Conclusions for Investors

- ▼ Institutional investors with assets of US\$96 trillion support the CDP Water Disclosure Request. As a first step, seek to understand the extent and nature of their exposures to water risk. CDP water data offers essential insights in this regard;
- ▼ European banks hold an amount of 42.89 trillion of total assets⁵ which can be leveraged to drive water stewardship in companies' business models by integrating water security in lending criteria;
- ▼ Scale and urgency of the environmental challenge posed by water security is huge. Just 31 companies globally achieved an A score for water, a significant drop from last year's total of 74. The 11 European companies on the water security A List represent 35% of the global total. Investors and banks should strengthen engagement on water with their investment and lending portfolio companies.

3. Public and private procurement

With public procurement accounting for about 14% of European GDP, **public authorities' buying can play a key role in positive environmental action by driving suppliers** to act on water security.

Activities causing harm to freshwater resources can often be hidden in complex supply chains, which is why it's important that **public buyers engage with their suppliers**.

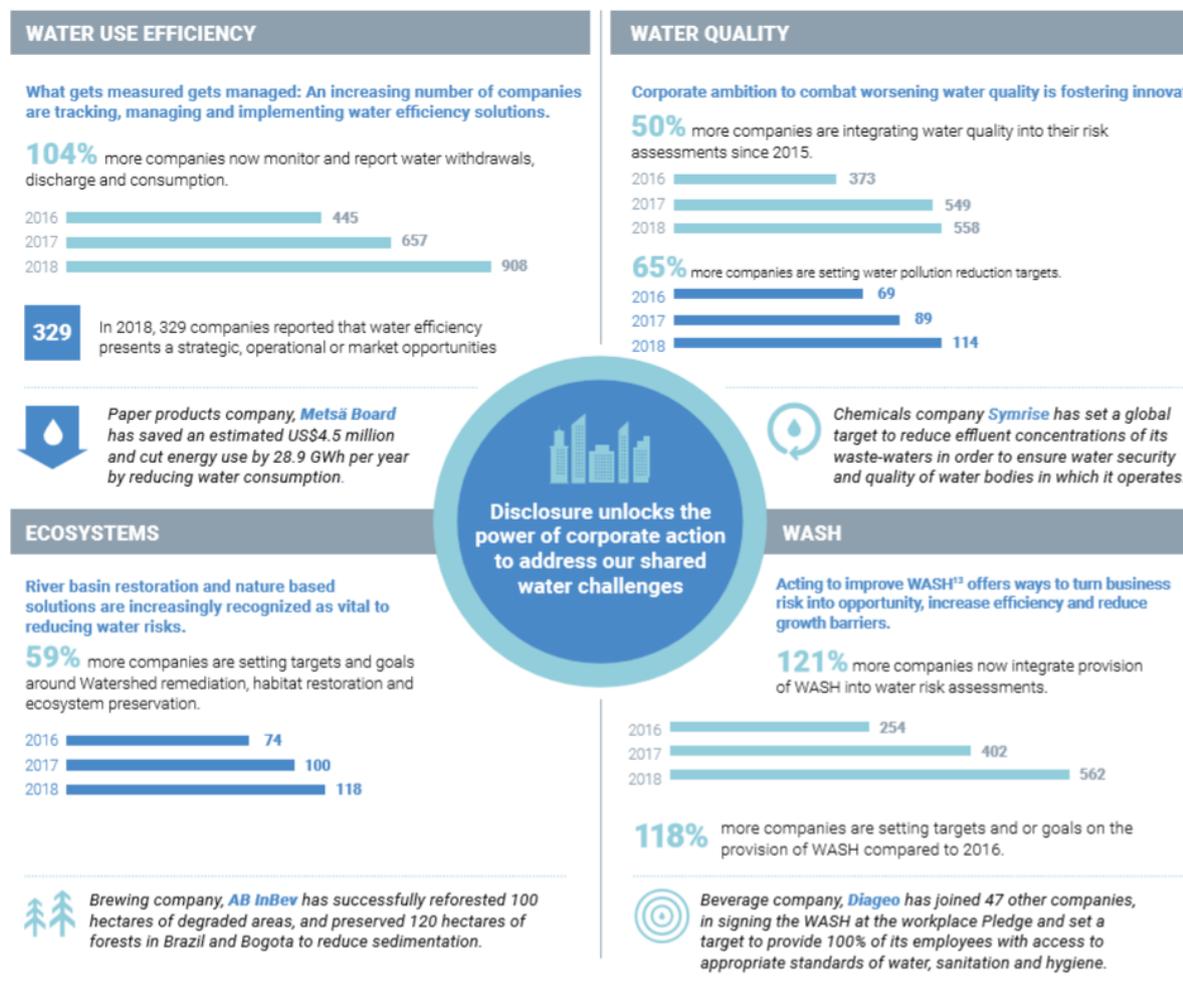
Water is the life blood of the global economy. A secure supply is essential for many industries, ranging from agriculture and manufacturing, through to power generation and hospitality. However, without a radical improvement in water management and stewardship across the economy then the World Bank predicts that water scarcity, exacerbated by climate change, could cost some of the world's regions up to 6% of GDP by 2050⁶.

⁵ <https://www.ebf.eu/wp-content/uploads/2018/09/Banking-in-Europe-2018-EBF-Facts-and-Figures.pdf>

⁶ World Bank (2016) High and Dry: Climate Change, Water, and the Economy.

Even worse, a failure to protect freshwater resources can prove disastrous to communities and ecosystems. And where water sources and drainage basins are badly managed, this can exacerbate the impact of natural disasters such as flooding.

Corporates highlight the enormous **importance of addressing water security issues**. A total US\$62 billion of revenues are currently associated with identified areas of water risk within direct operations, that have the potential to have a serious financial or strategic impact on businesses. They ask their suppliers to report separate **data on water withdrawal, consumption and discharge**. Each of these categories saw an increase from 2017, demonstrating ongoing progress in the collection of **important monitoring and transparency metrics, allowing businesses to better manage their freshwater use**.



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⁷ [CDP Supply Chain report 2019](#)

There is huge power in the scale of procurement spend. But with great power comes great responsibility. And over the past 10 years we have seen a fundamental shift in expectations around business action on climate change and other environmental sustainability issues. Subnational actors – particularly large corporates, but also some large public sector organizations – have started to play an increasingly important role driving water security internationally. In many cases they are moving considerably faster and further than governments have required.

Over the past decade, as CDP's remit has expanded beyond climate change to encompass other urgent sustainability issues, the Supply Chain program has similarly expanded to address these areas. **Water was introduced in 2013, to address scarcity and stewardship issues around this critical resource.**

- ▼ More than 1.300 disclosing suppliers in Europe and 5.562 suppliers globally, providing information about their efforts to manage and govern freshwater resources.

Government members who want to leverage the power of public procurement to drive action on climate change and water security:

- ▼ Los Angeles Department of Water and Power
- ▼ California Department of General Services
- ▼ U.S. General Services Administration (GSA)
- ▼ Ministry of the Environment, Government of Japan

Yoshiaki Harada, Minister of the Environment, Government of Japan: *“By taking action along the supply chain, companies can send price signals that reverberate throughout the economy and embed climate action at all levels. Members of the CDP Supply Chain program have set an example here, showing other organizations how to effectively create sustainable change through supplier engagement. As part of our commitment to driving climate action the Japanese government will be joining the 115 CDP Supply Chain members asking a selection of suppliers to disclose their climate change information to us through CDP in 2019.”*

Conclusion for Public and Private Procurers

- ▼ Encourage better management of water-related impacts of suppliers of public and private procurement organizations and act as a driver of positive action on water security in supply chains;
- ▼ Embed sustainability criteria into procurement standards; [Public authorities can use their purchasing power](#) to influence suppliers to adopt more sustainable practices relating to their water impact.

Recommendations for Policymakers

1. Ensure integration of water security matters as much and explicit as possible in the legislative and non-legislative measures of the **EU Action Plan on Sustainable Finance**⁸:
 - ▼ Action 1: Establishing an EU classification system for sustainable activities
 - ▼ Action 2: Creating standards and labels for green financial products
 - ▼ Action 3: Fostering investment in sustainable projects
 - ▼ Action 4: Incorporating sustainability when providing financial advice
 - ▼ Action 5: Developing sustainability benchmarks
 - ▼ Action 6: Better integrating sustainability in ratings and market research
 - ▼ Action 7: Clarifying institutional investors' and asset managers' duties
 - ▼ Action 8: Incorporating sustainability in prudential requirements
 - ▼ Action 9: Strengthening sustainability disclosure and accounting rule-making
 - ▼ Action 10: Fostering sustainable corporate governance and attenuating short-termism in capital markets
2. **Strengthen disclosure requirement of companies.** Governments should implement a fit-for-purpose framework of corporate reporting that delivers **decision-useful information on water security to financial markets**, and which ensures that companies comply with best practices regarding transparency on water management and water resource protection throughout their supply chains (see Action 9 above: Strengthening sustainability disclosure and accounting rule-making).
3. Recognize and monitor **impacts of water-related risks on urban communities**; capitalize on opportunities of water smart cities and regions and ensure **vulnerability assessments include water risks in order** to deliver fully-fledged long-term water security, resource management and resilience strategies in cities, states and regions. Recognize the links between water, energy and climate impacts and move towards a natural capital approach.
4. Encourage better management of water-related **impacts of suppliers of public and private procurement organizations** and act as a driver of positive action on water security in supply chains.
5. Embed **sustainability criteria into procurement standards** and use public and private purchasing power to influence suppliers to adopt more sustainable practices relating to their water impact.

We are at the European Commission's disposal to provide further evidence.

⁸ https://ec.europa.eu/info/publications/180308-action-plan-sustainable-growth_en

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