Danone S.A.

France, Consumer Goods & Services

Accounting		Climate Assumptions		Audit		Date of analysis: April 20 2021
Judgements	Consistency with other reporting	Visibility	Paris alignment	Visibility in KAMs	Consistency check	Year end: December 2020 Report date: March 18 2021 AGM: April 29 2021
Significant concerns	Some concerns	Significant concerns	Significant concerns	Significant concerns	Some concerns	Climate Action 100+ company, so seen by investors as key to driving global net zero emissions.

Summary view:
- Over 76% of the company's total emissions are from the purchase of goods and services, largely milk, dairy ingredients, and packaging. The company aims to be carbon neutral by 2050, with interim targets set for 2030.
- Extensive discussions of climate considerations and commitments outside of the financial statements stand in contrast to little discussion of associated financial costs or assumptions within the financial statements, and no mention in the joint audit report. Additional disclosure could help investors to assess the impact on financial reporting amounts.

Background

The Business.

- Danone is a French food group, operating through three product-based global entities: Essential Dairy & Plant-based (EDP), Specialized Nutrition, and Waters. From 2021 its operations will become geography-led, with the change being made 'in light of the global spread of the Covid-19 health crisis and the emergence of a radically changed environment'.
- In 2020, Danone become the first listed company to adopt the *Entreprise à Mission* model.[1] Four of its 2030 Company Goals became its mission and were integrated into its by-laws. One of these is climate-related: "to preserve and renew the planet's resources, by supporting regenerative agriculture, protecting the water cycle and strengthening the circular economy of packaging, across its entire ecosystem, in order to contribute to the fight against climate change". 32 of Danone's entities are certified B Corp™, covering 50% of its sales.[2]
- The Company confirms that its peak GHG emissions were in 2019. Emissions totalled 26.1mTCO2eq. in 2020 (down 1m). These amounts relate to entities consolidated for financial reporting purposes, as permitted by the GHG protocol. Over 95% is scope 3, with 76% relating to purchased goods and services, largely milk, dairy ingredients, and packaging.

Approach to climate change.

- Danone has an ambition to achieve carbon neutrality by 2050, and has signed the Business Ambition for 1.5°C pledge. It has two 2030 science-based targets (vs a 2015 baseline): to halve CO2 emissions intensity per Kg products sold, and to reduce scope 1 and 2 emissions by 30% in absolute terms. All electricity is to be renewably sourced by 2030. Environmental targets also focus on regenerative agriculture, water stewardship, and the circular economy.
- Climate risk is considered low impact in the short term but high in the long-term. The transition risk of a shift to plant-based alternatives and of growing customer engagement in fighting climate change, are rated as having high probability of occurring from 2020-2030, and medium to high in financial significance depending on climate scenario analysis.
- Danone's strategy is based on (i) reduction of carbon emissions, (ii) fostering soil carbon sequestration and (iii) compensation of remaining emissions through carbon positive actions.
- In February 2020 Danone announced a €2bn accelerated investment plan for 2020-2022, to 'future-proof' and upgrade the competitiveness of its business model. The plan has 3 pillars: regenerative agriculture, sustainable packaging and connected end-to-end operations. It includes €600m operating costs, €1bn capex, and €500m (2020) 'other operating expenses'.

---

[1] An *Entreprise à Mission* has its social, and environmental objectives aligned with its purpose, and set out in its by-laws.

[2] Certified B Corporations are a new kind of business that balances purpose and profit. They are legally required to consider the impact of their decisions on workers, customers, suppliers, community, and the environment.

- The company participates in The Livelihoods Carbon Fund, an investment fund dedicated to restoring ecosystems and carbon assets. Carbon credits generated are certified, then allocated to its investors in proportion to their investments. Danone has pledged funds of €38.8m.
- Starting in 2019, Danone discloses a 'carbon-adjusted' recurring EPS that takes into account the financial cost of the GHG emissions of its value chain, estimated at €35 per ton of carbon. Reductions in 2020 emissions contributed a 4.1% decrease to the cost of carbon per share. The 'carbon-adjusted' recurring EPS decreased by 19% in 2020 (vs 13% before adjustment).
- Fulfilment of climate goals has a bearing on executive remuneration (based on ratings by CDP) and awards to officers and senior executives (based on the carbon footprint reduction).

Accounting: judgements and consistency with other reporting

Accounting judgements		Significant concerns

- Danone's accounts are prepared under IFRS as adopted by the European Union.
- Intangible assets at December 2020 were €23bn, 98% of which are not amortised (goodwill and intangibles with indefinite lives). Impairment charges were €363m, €288m of which related to brands in EDP and Specialized Nutrition, in light of new assumptions made in the strategic plan. Future cash flows used in impairment testing are amounts in budgets and strategic plans for 2 years, extended to 3-5 years for Waters/EDP and 9 years for Specialized Nutrition, and extrapolated beyond this using growth rates. 2020 changes in assumptions relate to discount rates, not growth. There is no apparent mention of climate change risk or related plans.

Consistency with other reporting		Some concerns

- Other operating income(expense) captures 'items that, because of their significant or unusual nature cannot be viewed as inherent to Danone's recurring activity and have limited predictive value, thus distorting the assessment of its recurring operating performance'. Other views could be taken on this, however separate disclosure can be helpful. Costs of €163m (€114m 2019) are shown as 'related to the transformation of Danone's organizations and operations', mainly attributed to the transformation of EDP's operations.
- Such costs may represent lower-than-anticipated 2020 spend on the €2bn plan, but given the significance of climate risk and commitments, it is concerning that there is little apparent disclosure of associated investment, costs, or impacts on margins.

Climate assumptions in accounts: visibility and Paris alignment

Visibility of climate assumptions in accounts		Significant concerns

- There are no apparent climate-related assumptions. There is thus no sensitivity analysis.
- However, outside of the financials, the annual report discloses that Danone has developed three climate change scenarios to assess the resilience of its activities, its strategy and the related financial risks. The assumptions do not appear to be specified in the report.

Paris alignment		Significant concerns

- With no visibility, there can be no alignment with the goals of the Paris Agreement.

Audit: visibility in KAMs and consistency check

Audit firm: joint auditors Ernst & Young Audit, and PricewaterhouseCoopers Audit	Responsible partner: Gilles Cohen Responsible partner: François Jaumain
Audit standards: professional standards applicable in France	

Visibility in Key Audit Matters		Significant concerns

Stripes image credit: Prof. Ed Hawkins www.showyourstripes.info

- There appears to be no explicit reference to climate change in the joint auditors' report.
- KAMs identified are: Revenue recognition, Goodwill, brands and investments in associates, Tax assets and liabilities. Both the goodwill and tax items contain an element of recovery through future cash flows. These KAMs refer to the Covid-19 pandemic, but neither appears to consider climate risks. Only tax specialists are mentioned as having been utilised.

Consistency check		Some concerns

- The auditors state that they have performed specific verifications of the Group's information given in the management report of the Board of Directors, and had no matters to report as to their fair presentation and their consistency with the consolidated financial statements. Given the climate targets set and activities undertaken to meet them, the limited coverage in financial disclosure and lack of discussion in audit considerations stands in contrast to this.
- The PwC partner responsible for the audit also provided assurance on the consolidated non-financial information statement in the management report. The assurance opinion was also signed by a PwC Sustainable Development Partner, Sylvain Lambert.

The Climate Accounting Project is an independent investor-led project to reinforce the statements of the IASB and IAASB that material climate change issues are incorporated within their standards. This analysis seeks to understand the extent to which companies and auditors are delivering against this aspect of these standards and similar local standards.		**Key**
		Good practice
		Few concerns
		Some concerns
		Significant concerns

Terms, conditions and disclaimer

The information contained in this document is for general information and educational purposes only.

Nothing in this document constitutes investment, legal, accounting, tax or other professional advice, or any recommendation to buy, sell or hold any security or other financial instrument, nor to exercise voting rights in any particular way. The information contained in this document is not intended to form the basis of any investment or voting decision, it does not constitute any form of investment recommendation or investment research and has not been prepared in accordance with any legal requirements designed to promote independence or objectivity. The authors of this report are not regulated by the Financial Conduct Authority or any other financial regulatory authority. You should make your own independent assessment and seek your own professional advice.

No representation or warranty is made that any of the information contained in this document is accurate or complete and no responsibility or duty of care of any kind is assumed by any person for errors or omissions in the contents or for the fairness of the opinions given. The authors do not accept any liability whatsoever for any direct or consequential loss howsoever arising, directly or indirectly, in connection with the use for any purpose of the information contained in this document.

You expressly agree that you use the information in this document at your own risk.

All information in this document is believed to be current as of the date of publication. Information may have been updated subsequently. The authors may make additions, deletions, or modifications to the contents at any time without prior notice.

This document reflects the authors' own interpretation and opinion of accounting and auditing standards and how companies and their auditors have applied those standards. No representation or warranty is made that any interpretation or opinion of International Financial Reporting Standards, International Standards for Auditing, other financial reporting and regulatory requirements or the application of these standards or requirements by individual companies or their auditors is correct, complete or fair, nor that they are incorrect, incomplete or unfair, or that the same views would or would not be arrived at by others. You should seek your own professional advice if making decisions that depend on the interpretation of any standards related to financial reporting or auditing, or other regulatory requirements.

The views expressed in this document reflect the personal opinions of the authors and not those of any other companies, organisations, committees or persons with which they may be associated.

Stripes image credit: Prof. Ed Hawkins www.showyourstripes.info