

Commercial Banks' Approach to Climate Change Management

Internal Taxonomy for Assessing Climate Change

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Disclosure: Chatham House Rules info disclosure, Presenter's personal view on issues/options to deal with climate change reporting and not that of his employer's, his view cannot be construed as investment/planning advice.

Agenda

- **What Banks have been doing on climate change**
 - Institutional set-up - Engagement from the top and communication across
 - Risk Control - Scorecard an internal climate risk taxonomy
 - Scorecard – tackling info challenges
 - Scorecard – integrating it into the credit process
- **What are the next steps**
 - Ways of assigning higher risk to unsustainable obligors

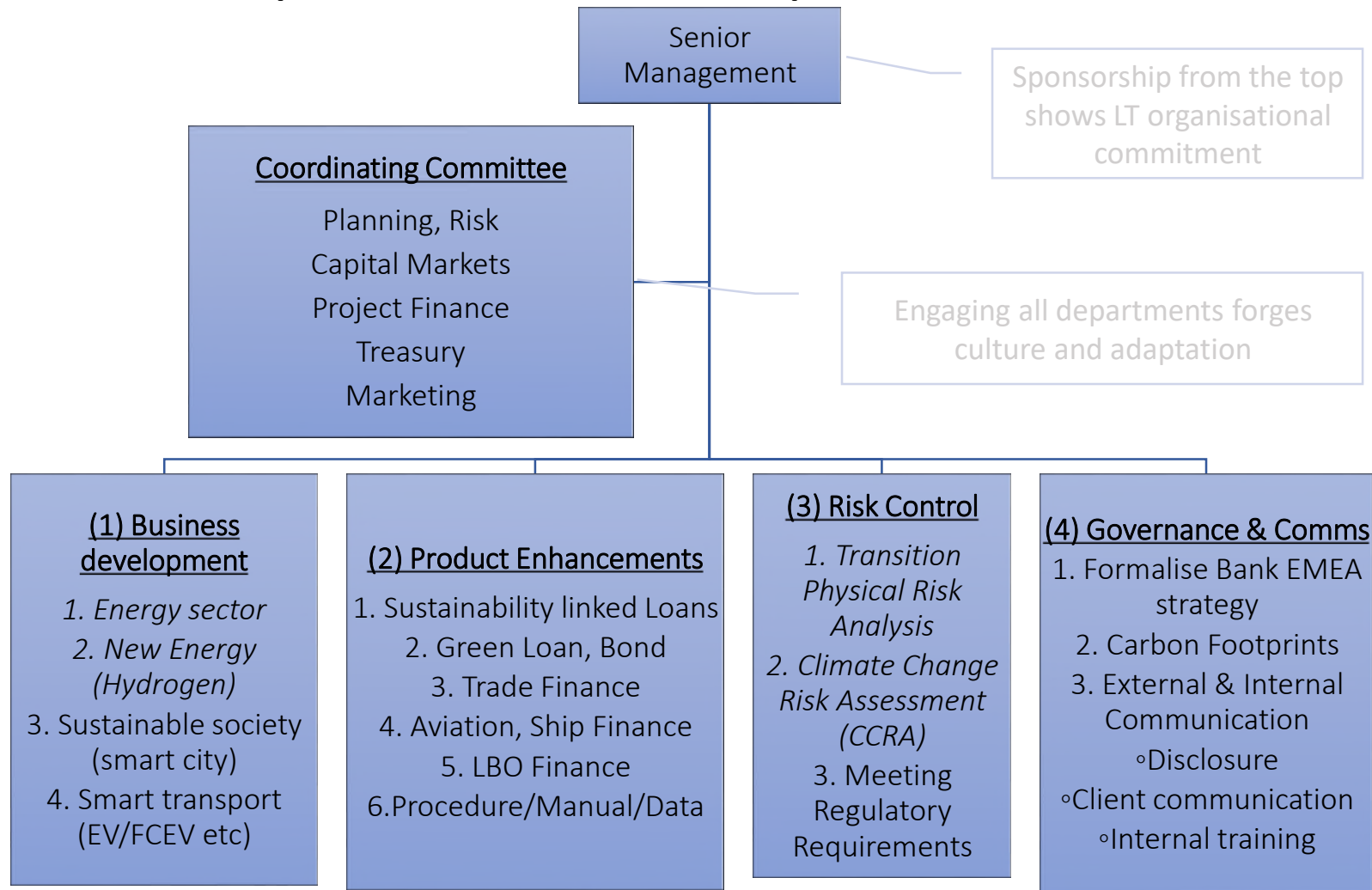
Appendix: ESG trend offers significant new business opportunities

Appendix: European Banks sustainability lending commitments

Institutional set-up - Engagement from the top and communication across

- Constant involvement from executives and collaboration across departments forges the right culture.

Institutional set-up – covers all TCFD focused requirements



TCFD Recommendations for Disclosure

Governance

- ✓ Board Oversight
- ✓ The role of Management

Strategy

- ✓ Identify and describe climate-related risks and impacts
- ✓ Organisational resilience

Risk Management

- ✓ Process for identifying, assessing and managing climate-related risks
- ✓ Integration of processes into overall risk management

Metrics/Targets

- ✓ Disclosure of metrics/targets
- ✓ Disclose Green House Gas emissions and related risks



Communication - collaboration, education, disclosure



Risk Control - Scorecard an internal climate risk taxonomy

- Screening obligors and portfolios to identify climate risk exposure.
- Initial objective to map all obligors and industries and assess revenues at risk.
- Each obligor is assigned a risk of 0-100 (0=high risk , 100=no risk),
- Goal is to migrate Bank's BS into greener/sustainable investments that meet the Paris Climate accord.

System for taxonomy of obligors



Sample result for obligor

Type of Risk	Factors	Explanation
Transition Risk	Obligor's Industry	Industry transition risk, 4+ categories based on CO2 emissions (scope 1,2).
	Carbon Intensity	4+ categories in CO2 distribution, No data is penalized.
	Strategy, Execution & Disclosure	Info on emissions and strategy on Corporate, PF level, basic and comprehensive
Physical Risk	Obligor Industry	4+ categories, nature of industry, location of assets, revenue impact of catastrophes, supply chain.
	Risk Country	HQ country?, past disruptions (deaths, GDP impact)

	Country	ind_nme	CountryRisk	Q_Disclosure Score.Score	Sector Transition	Physical	GHGScore.Score	ToTal Score
AIRBUS SE	NETHERLANDS	Aerospace & Defense	Medium Risk	Comprehensive Disclosure	High Risk	Low Risk	Top_25-50	LOW Risk



Sample result for industry

Frequency Distribution by Sector	0 - 10	11 - 20	21 - 30	31 - 40	41 - 50	51 - 60	61 - 70	71 - 80	81 - 90	91 - 100
Advertizing Agencies				2	10	1	1			
Aerospace & Defense			2	3	3	2	1			
Air Transport			10	5	5	10				
Auto Parts			10	5	10	10	2			

Scorecard – tackling the info challenges

- Front Offices will need to engage with clients and include their responses in credit applications.
- The following are a selection of key questions asked by colleagues to clients that have prompted discussion relating to climate change, and tangible opportunities for the Bank.

Not all companies are forthcoming

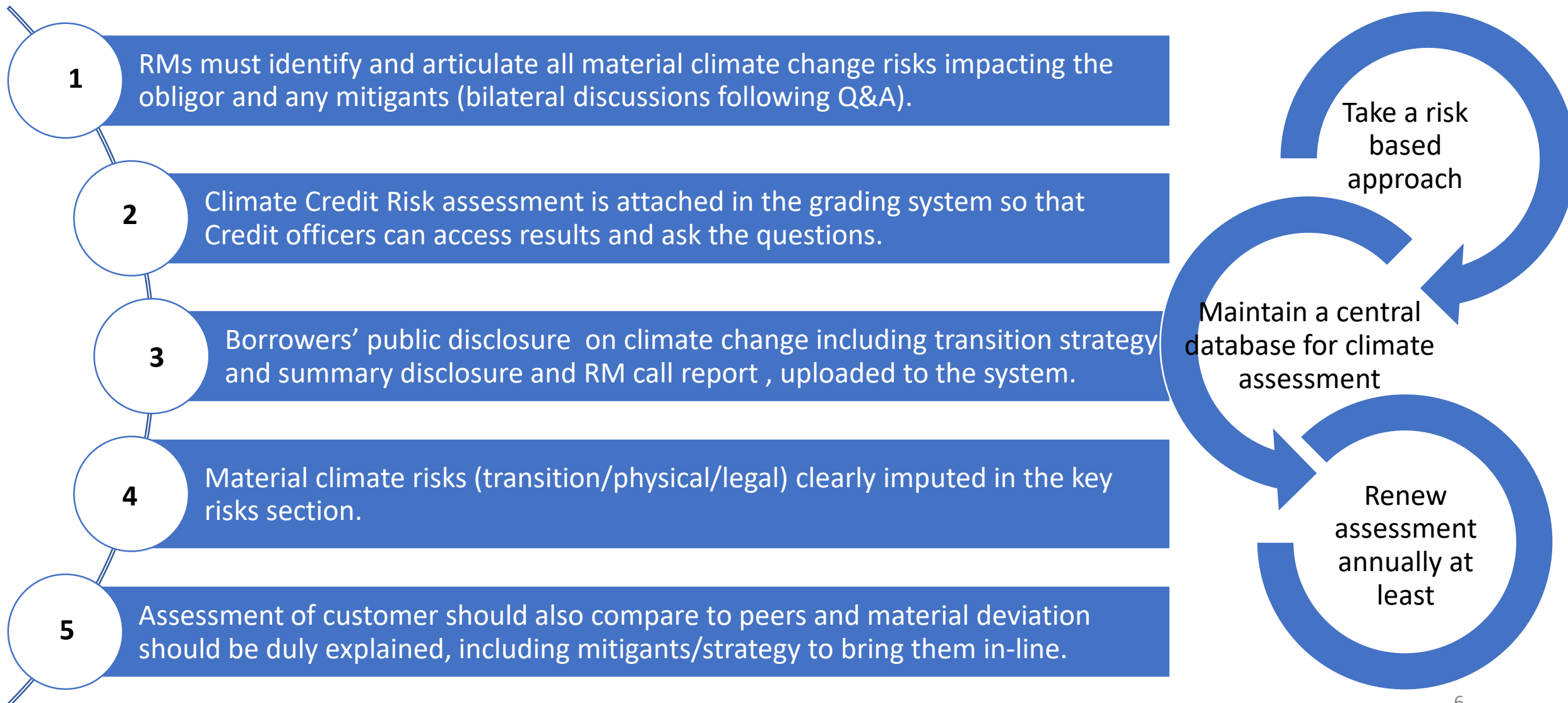
Company	CO2 Emissions Targets	Strategies for decarbonisation	CDP 2019	
Enel	Net zero emissions by 2050	Raise emission-free(e.g. renewables) production to 62% in 2021 vs 48% in 2018	A	Detailed disclosure
Iberdrola		Achieve 74% renewable generation share by 2030 by investing heavily in offshore wind	A-	
Tullow	No specific targets	Review the current process for analysis of climate risks & resilience of investment decisions to make it more robust	D	Basic disclosure
Novatek	No specific targets, only mention about specific target on gas flaring etc.	Take several measures, but difficult to understand how effective they are to reduce CO2 emissions	D-	

...What questions can I ask?

What does your organization see as the biggest risk in relation to climate change?	
What process do you have in place to identify, assess and manage climate related risks?	
What is your organizations' most senior level of oversight with regards to Climate Change?	
What accountability is associated with the oversight responsibilities?	
Does your organization have a heatmap/grading system for the various risks/parts of your business?	
Whom have you identified as relevant stakeholders (e.g. Shareholders, Clients, NGO's etc.)?	
Have you got a formal process to engage with various stakeholders?	

Scorecard – integrating it into the credit process

- An understandable, transparent process without ambiguity and subjectivity will ensure better adaptation in current credit systems.



Ways of assigning higher risk to unsustainable obligors

- Various ways to link the Climate Credit Risk assessment to capital allocation, more detailed/standardised disclosure will improve assessment and better differentiate among customers.

Qualitative input in grading

- Integrate qualitative CCRA into the grading methodology , eventually impact grading, PDs and return on investments.
- Qualitative adjustment and notches adjusted for ESG non-compliant customers.

Natixis – green weighting factor

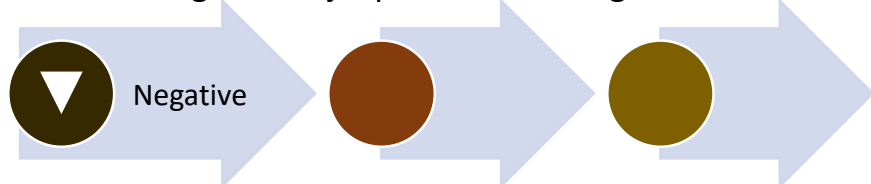
- Risk weights assigned to each colouration of assessment scale (24% penalty for Brown and 50% premia to dark green; favouring capital to green prospects)

End goal

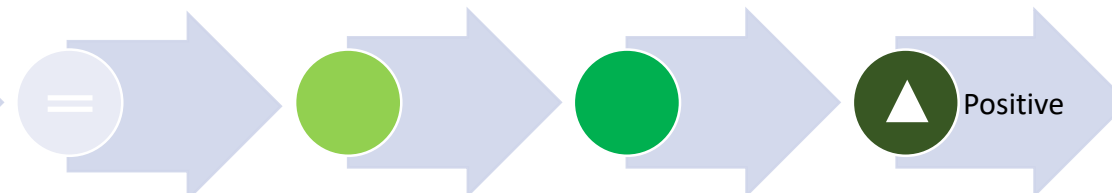
- As standards and disclosure is standardised, a more analytical approach can be developed per obligor and sensitivities run in confidence.

Green weighting factor, Natixis approach

Receive a negative adj. up to 24% of weighted assets



Receive a positive adj. up to 50% of weighted assets



Thank you for the time

- Happy to answer questions in the Q&A session

Appendix: ESG trend offers significant new business opportunities

- A race for the banks to innovate in climate change could see them capturing significant new profit centers.

ESG trends drive 2-3% ROE difference for leaders

	Leaders (%)	Laggards (%)
Risks Gradual reduction in revenues from energy sectors; increase in cost of risk	- 0.5	- 0.5 — 1
Opportunities Transition financing, green financing, ESG investing products, analytics and advisory	+ 1	- 1.5
Total impact on RoE	+1	-2

Source: S&P Global Market Intelligence

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ESG could drive \$150bn revenue opportunity in MT

	Sub-areas	Revenue potential	
Savings and investing	Impact investing Sustainable investing Integrated ESG investing	\$70-90 BN	- Asset and Wealth Management solutions and funds - Distribution opportunity to meet consumer demand - Product opportunity to expand into alternative structures focused on new investment propositions
Financing	Green bond Green lending Transition finance	\$20-40 BN	- >\$5 TN of financing required per year to meet the investment needs of climate change and energy transition - Much of this will be public, but huge opportunity for businesses and infrastructure providers to both adapt the existing and grow the new - Green bonds already growing rapidly; emerging opportunities in dedicated transition finance structures and (high margin) lending
Content and risk transfer	Data and analytics Advisory Insurance and risk transfer	\$10-20 BN	- Hedging opportunities for exposed companies and investors (both financing and climate linked) - Support in thinking through implications on the business and strategic mitigation (e.g. M&A, divestments) - Use of data and analytics to inform a richer client discussion

Appendix: European Banks sustainability lending commitments

- Coal and unconventional H/Cs low hanging fruits for financiers.
- Since it is important not to erode business, sustainability finance will gradually assist customers get on a sustainable track and also preserve banks' revenues.

Banks	Lending Commitments
SG	No financing of coal power plants, coal mining & associated infrastructure. A cap on coal in energy mix of power portfolio (19% by 2020)
	EUR100bn in energy transition funding
	Exclusion policy regarding financing of coal and related, extended to Arctic oil and oil sands.
	As of 2018 coal-related projects 16.4% vs 19% 2020 target
BNP	Reduce coal financing to 0% as of 2030, already no coal-related and unconventional H/C financing.
	Channeled 16bn in RWs in 2019 and increased target to 18bn by 2021end.
	Increase by €10bn/yr in average over 2019-2021 CF contributing to energy transition and sectors directly contributing to UN SDGs.
CASA	Double size of green loan to €13bn by 2022
	Exit of Coal financing in EU & OECD by 2030
	Incorporate ESG in 100% of large corporate financing and gradually on SMEs.
	Increase amounts invested to ESG to €20bn (x2) bt 2021
UBS	No PF on new coal-fired power plant globally.
	Only supporting existing coal-power (>30%) who have transition strategy aligning with Paris pathway
	Severely restricting lending and capital raising to coal mining.

Banks	Lending Commitments
DB	No financing new coal power facilities, reduction on existing to Power companies relying heavily on coal
	No coal mines, 20% reduction in 2020 vs 2016.
	Environmental and social due diligence, signed off by Group Sustainability for oil & gas, M&M, Utilities
	In 2019 concentration in Oil & Gas, utilities, steel, M&M was lowered, LT Climate risks taken into account.
BARC	Green Bond investment of £4bn over time vs £2.7bn in 2019
	Commit to net zero by 2050 and to facilitate £150bn of green finance by 2030
	Prohibit financing to clients with more than 50% coal revenues (30% in 2025, 10% in 2030), no Arctic Circle and fracking in Europe.
HSBC	2025 target to facilitate \$100bn of sustainable financing (\$52.4bn since 2017)
	Strengthened the energy policy not to finance coal-power (exception Bangladesh, Indonesia, Vietnam).