بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

# FAB ESG WEEKLY UPDATE

05 August 2022

This week, we identified the following events of significance within sustainability and their respective business implications.

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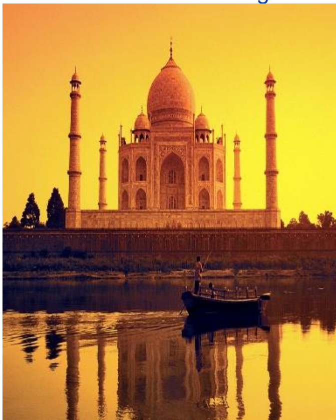
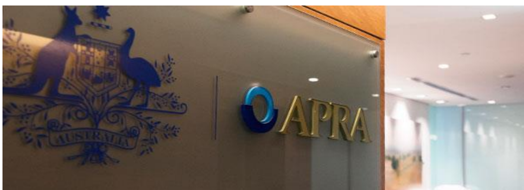
## REGULATORY

**1.** The **Reserve Bank of India (RBI)** released the **first major climate-related policy document published by the Indian central bank**. The paper outlines its approach to managing climate and other environment-related risks. It offers guidance largely aligned with the recommendations of the Taskforce on Climate-related Financial Disclosures (TCFD). According to the RBI, governance of climate risk management should be at board level, while including development and implementation of a strategy to embed climate and environment considerations into the organisation.



- Banks and other regulated financial institutions are asked to develop policies and procedures to identify, assess, monitor, and mitigate climate and environmental risks, and to issue timely and regular reports on their climate-related risk exposures. The use of forward-looking tools such as stress testing and climate scenario analysis is also encouraged. A recent report on the RBI's response to the climate crisis found that Indian fossil fuel extraction and other high-carbon sectors account for approximately 40% of bank lending to large corporations, representing a major transition risk to India's financial system.
- The **Government of India** announced the approval by cabinet of a **new series of 2030 climate commitments**, including a pledge to reduce emissions intensity by 45% and to transition to approximately 50% electric power from non-fossil-based sources. India established a long-term goal to reach net-zero emissions by 2070.




**2.** The **Australian Prudential Regulation Authority (APRA)** concluded that **financial institutions are still at early stages of integrating climate risk**. The Australian financial regulator based this assessment on the findings of its latest climate risk self-assessment survey conducted across the banking, insurance, and superannuation industries.

- The APRA-regulated entities are generally aligning well to APRA's guidance, especially in the areas of governance and disclosure. Climate risk, however, remains an emerging discipline compared to other traditional risk areas, with only a small portion of survey respondents indicating that they have fully embedded climate risk across their risk management framework. According to APRA, 4 out of 5 boards oversee climate risk on a regular basis, while just under two-thirds of institutions or 63% have incorporated climate risk into their strategic planning process.
- Also, almost 40% of institutions said climate-related events could have a material or moderate impact on their direct operations. Nearly three-quarters or 73% of the institutions had one or more climate-related targets in place, however 23% do not have any metrics to measure and monitor climate risks. Over two-thirds of institutions or 68% have publicly disclosed their approach to measuring and managing climate risks, with 90% of those aligning their disclosure to the Taskforce for Climate-related Financial Disclosures (TCFD) framework.

**3.** The **Monetary Authority of Singapore (MAS)** unveiled **new reporting and disclosure requirements for ESG funds targeted at retail investors**. The central bank and financial regulator of Singapore added that the requirements were aimed at enabling investors to better understand the ESG aspects of the funds they invest in, and to reduce the risk of greenwashing, or the exaggeration or misrepresentation of the sustainability attributes of the funds. A practice in line with recent frameworks launched by major regulators such the U.S. Securities and Exchange Commission (SEC), the European Union (EU) and the U.K. Financial Conduct Authority (FCA).

- Reporting requirements introduced in MAS' new guidelines include disclosures on details of funds' investment strategies, criteria and metrics used to select investments, and risks and limitations associated with the funds' strategies. The new guidelines are expected to take effect from January 2023.
- The new rules come as investor interest in ESG has undergone significant growth, driving a proliferation of investment products and services marketed as 'green' or 'sustainable,' but without clear rules communicating to investors the actual ESG-related attributes, methodologies and criteria that are being considered in the funds.

## RESEARCH

**1. Mastercard** updated its new payments index 2022 survey with the conclusion that the **majority of UAE consumers used a new digital payment method in 2021**. About 88% of consumers in the UAE have used at least one emerging payment method in the past year as the move towards a digital economy accelerates. Also, 33% of respondents considered social and environmental benefits when choosing a payment method.

- According to the survey, 39% of UAE residents used a tappable smartphone mobile wallet, while 29% recurred to the buy-now-pay-later (BNPL) services, 20% used cryptocurrency and 18% turned to payment-enabled wearable tech devices. While traditional payment methods continue to be used in the country, 29% of respondents to the MasterCard survey said they used less cash over the past year.
- In contrast, 66% of UAE consumers increased their use of at least one digital payment method in the past 12 months, including digital cards, SMS payments, money transfer apps and instant payment services. About 64% of generation Z in the Emirates are likely to have obtained a new digital payment alternative, compared with 22% of baby boomers.

**2.** The **University College of London (UCL) Institute for Innovation and Public Purpose** issued a **paper** focused on **aligning finance with the green transition**, from a risk-based to an allocative green credit policy regime. The study proposes an allocative green credit policy approach, whereby incentives and targets are deployed to align the financial sector with governments' decarbonisation plans.

- The paper distinguishes its approach from the risk-based framework that currently dominates financial policy related to the green transition. It offers a critique of the existing approach, highlighting that it has not succeeded in shifting financial flows from transition-incompatible activities, particularly given bank credit to carbon-intensive sectors has continued to increase in the nearly seven years since the Paris Agreement. The study characterised the risk-based approach as being primarily focused on policies such as disclosure, taxonomies, scenario analysis and stress testing, which amounts to outsourcing the pace and nature of decarbonisation to private finance.
- Instead, the paper advocates an allocative credit policy regime which places greater emphasis on environmental outcomes as a justification for policy intervention. It proposes a framework that includes both incentive tools, like climate-adjusted capital requirements, and coercive tools such as outright bans on financing certain sectors. Such policies would target both the banking system and market-based finance to ensure the entire financial system is aligned with green transition objectives. They would be dictated by the green industrial strategy, the need to develop green infrastructure, and the need to downsize transition-incompatible sectors as defined by a public taxonomy.

**3. Sustainable Fitch** published a **report** with insights from Fitch's inaugural ESG ratings, providing a quantitative and qualitative assessment of **the impact an issuing entity and associated financial instruments have on the environment and society.**

- Frameworks score higher than entities. This indicates that issuers of labelled bonds are doing a good job at aligning their ESG labelled bonds to international best practice, but their business activities only have average sustainability performance. Entities from EMEA have slightly better sustainability profiles than those in Asia-Pacific and the Americas.
- Issuers in essential services have most ESG-aligned business activities. Public entities, all involved in affordable or social housing, have the highest average scores for business activities, which evaluates the environmental and social impacts from core operations.

## COMMERCIAL

**1. Lufthansa** and **Shell** reached one of the **largest-ever sustainable aviation fuel (SAF) deals**. The supply agreement for 1.8 million metric tons of fuel represented the largest SAF deal for either of the companies to date and largest SAF commercial deal to date. The fuel will be produced by up to four different approved technology pathways and a broad range of sustainable feedstocks, while most current SAF is produced from biogenic residues, such as used cooking oils.

- Shell will supply as much as 594 million gallons to Lufthansa at airports around the globe. The deal will contribute to Shell's ambition for at least 10% of its aviation fuel sales by SAF by 2030, and to Lufthansa's goal of promoting availability, market ramp-up and use of SAF as an essential element for a carbon-neutral future of aviation.
- The agreement is reached while the aviation industry faces increasing scrutiny as a significant source of greenhouse gas emissions, responsible for 2% to 3% of global emissions, with that figure set to rise dramatically over the coming decades if no action is taken. SAF is seen by market participants as one of the key tools for the industry to address its climate impact, as it generates significantly lower lifecycle carbon emissions, up to 80% lower relative to conventional jet fuel.

**2. Hilton** announced the **enhancement of ESG targets to drive climate action and social impact**. The commitments including goals to significantly cut the emissions footprint of its portfolio of hotels, along with social impact pledges to support inclusive growth.

- Hilton's new climate goals include reducing greenhouse gas (GHG) emissions intensity by 75% in its managed hotels, an acceleration from its prior 61% target, and by 56% in its franchised hotels by 2030. The company stated that its upgraded GHG emissions targets have been validated by the Science Based Targets initiative (SBTi), as aligned with a trajectory to hold global temperature rise to 1.5°C.
- Hilton's social impact commitments include a target to create 5 million learning and career growth opportunities for employees and communities with a focus on underrepresented groups by 2030, meaningfully impact 20 million community members through local support, economic opportunities, and disaster relief by 2030, and promote responsible and inclusive conduct across 100% of its value chain operations.

**3. Carlyle** launched a **decarbonization-linked finance program for private credit market.** The global private capital investment company's program is among the first of its kind in the US private credit market.

- Under the new program, borrowers will receive a pricing benefit based on the achievement of decarbonization targets or other climate-related Key Performance Indicators (KPIs). Carlyle will work with borrowers on the assessment and monitoring of appropriate KPIs, and that the firm's ESG team will provide support and expertise to help borrowers achieve climate-related goals.
- The launch of the new program follows the establishment earlier this year by Carlyle of a commitment to achieve net zero greenhouse gas emissions by 2050 or sooner across its investments, along with interim emissions reduction targets for its majority-owned corporate private equity, power and energy portfolio companies and a goal to have 75% of its portfolio companies' scope 1 and 2 emissions covered by Paris-aligned climate goals by 2025.