FAB ESG WEEKLY UPDATE

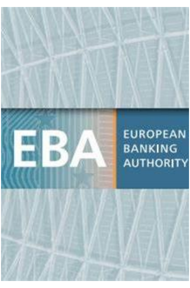
20 October 2023 – 82nd edition

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

For previous editions please refer to our website repository.

REGULATORY

1. The **European Banking Authority (EBA)** recommended **accelerating the integration of ESG risks into capital requirement frameworks**. EBA assessed the role of environmental and social risks in its prudential supervision framework for banks and investment firms. The regulator included recommendations for the acceleration of these risks across the pillar 1 framework, which defines banks' minimum capital requirements. Environmental and social risks are expected to become more prominent over time, changing the risk profile for the banking sector, across financial categories such as credit and market risk, as well as operational risks, and potentially affecting individual institutions as well as the overall financial system's stability.



- The regulator provided short-term actions recommended over the next 3 years, including incorporating environmental risks as part of stress testing programs, encouraging the inclusion of environmental and social factors as part of external credit assessments by credit rating agencies, and as part of due diligence requirements and valuation of immovable property collateral. Additional near-term recommendations include requiring institutions to identify whether environmental and social factors constitute triggers of operational risk losses, and to develop environment-related concentration risk metrics as part of supervisory reporting.
- On a longer-term basis, EBA presents possible revisions of the pillar 1 framework, in light of the increased importance of environmental and social risks, including the possible use of scenario analysis to enhance the forward-looking elements of the prudential framework, the role of transition plans as part of the development of further risk-based enhancements to the pillar 1 framework, reassessing the appropriateness of revising the internal ratings based supervisory formula and the standard approach for credit risk to better reflect environmental risk, and introducing environment-related concentration risk metrics under the pillar 1 framework.

2. The **European Commission** will **postpone the adoption of the European Sustainability Reporting Standards (ESRS) by 2 years**. The decision was made public as part of the 2024 Commission work programme, which sets out the list of actions for the upcoming year. One of the 2024 programme's priorities includes the reporting burden for companies, with the Commission including the postponement of the deadline for the adoption of sector-specific European Sustainability Reporting Standards (ESRS) as one of the key actions listed.

- The ESRS defines the rules and requirements for companies to report on sustainability-related impacts, opportunities and risks under the European Unions' upcoming CSRD. The postponement will allow companies to focus on the implementation of the first set of ESRS, while ensuring that EFRAG has time to develop sectoral ESRS that are efficient and limit the reporting requirements to the minimum necessary.
- The Commission's strategy on long-term competitiveness sets out the goal of reducing burdens associated with reporting requirements by 25%, without undermining the policy objectives of the concerned initiatives. To achieve this goal, the Commission has sought to simplify reporting requirements, for instance through the reform of the Union Customs Code, which will bring about around €2 billion in cost savings for traders. The proposed revision of rules on statistical surveys seeks to reduce costs, including for SMEs, by €450 million.

European Commission

3. The **Monetary Authority of Singapore (MAS)** proposed **a set guidelines on net zero transition planning for financial institutions**. The transition planning guidelines set out MAS supervisory expectations for financial institutions like banks, asset managers or insurers to have a sound transition planning process to enable effective climate change mitigation and adaptation measures by their customers and investee companies. A move focused on the global transition to a net zero economy and the expected physical effects of climate change.

MAS
Monetary Authority of Singapore

- The key expectations that MAS has set out for financial institutions are: engagement, rather than divestment, as the key lever for financial institutions to steward their customers and investee companies to transition in an orderly manner; a multi-year approach, beyond the typical financing or investment time horizons, to facilitate a more comprehensive assessment of climate related risks; a holistic treatment of risks enables better risk discovery; consideration of environmental risks beyond climate-related risks in their transition planning; and transparency to support accountability, while promoting credibility.
- The guidelines build on MAS' existing supervisory guidance to financial institutions and focuses on their internal strategic planning and risk management processes to prepare for both risks and potential changes in business models associated with the transition. While the underlying risk principles are similar, the guidelines were developed recognising the different business models and needs of financial institutions in banking, insurance, and asset management.

RESEARCH

1. The **World Economic Forum (WEC)** issued a report on **accelerating decarbonization and energy transition in the Middle East and North of Africa (MENA)**. The region has been heating up at twice the global average for the past 4 decades, and is projected to be 4°C warmer by mid-century. While governments are playing their part in setting up the net zero ambition and creating an enabling environment, companies need to shoulder the responsibility of delivering sustainability action to move the discourse on climate adaptation forward.

- MENA's commitment to the Paris Agreement, signed by all of its major economies, provides the pivotal foundation for climate action. In the past 2 years, an estimated 60% of the region's emissions and GDP have come under net zero pledges, and while this is a strong start, corporate climate leadership in MENA trails that of the region's global peers. The overall contribution of MENA countries to global emissions are relatively small at around 8% but these emissions have tripled over the past 3 decades, with an alarming 21% growth in just the past decade.
- A worrying 45% of MENA's agricultural land is already exposed to challenges such as salinity, soil nutrient depletion and erosion, while 60% of the population inhabits areas plagued by water stress, which is almost double the global average. In 2022 alone, the region saw the displacement of 14 million people due to catastrophic events. Climate change could slash MENA GDP by between 4% and 21% by 2050 due to a lack of climate action.

WORLD ECONOMIC FORUM

2. The **United Nations Framework Convention on Climate Change (UNFCCC)** published a report on the **global stocktake elements ahead of COP28**. The global stocktake is the key mechanism under the Paris Agreement to ratchet up climate ambition and accelerate implementation. The stocktake reviews the implementation of the Agreement and assesses collective progress towards achieving its purpose and long-term goals in mitigation, adaptation and means of implementation. It is carried out every 5 years. The first global stocktake commenced in 2021 and will conclude at COP 28.

UNFCCC

- The report is based on 24 joint submissions from 180 groups and 44 individual stakeholders. It reflects the views of governments and their perspectives on the main elements that will help them make decisions at the COP 28 global stocktake. The UNFCCC found that the past climate action has been insufficient and more needs to be done by governments to limit global warming to 1.5°C above pre-industrial levels, to avoid loss and damage, and to adapt to climate change.
- While there are divergent views on the details of how to reach the goals of the Paris Agreement, all parties agreed they need to take more action and support developing countries. Many non-Party stakeholders reiterated that the global stocktake outcome affirm that Parties will respect, protect and fulfil obligations on human rights including the right to a clean, healthy and sustainable environment, the right to health, the rights of indigenous peoples, local communities, migrants, children and youth, farmers, persons with disabilities, refugees, and people in vulnerable situations and the right to development, as well as gender equality, empowerment of women and intergenerational equity.

3. The **Task Force on Climate-related Financial Disclosures (TCFD)** authored a report illustrating a **sharp increase in company disclosure of climate risks and opportunities**. The publication describes companies' progress in making climate-related financial disclosures and highlights some of the challenges they face in making such disclosures. It is supported by a study, using artificial intelligence technology, of the publicly available reports of more than 1,350 large companies across a broad range of regions and sectors over 3 years.

- Companies in Europe saw the highest number of average disclosures at 7.2, while Middle East and Africa-based companies had the lowest at 3.8. Large cap companies with a market cap greater than $12.3 billion had much higher reporting rates than their smaller counterparts with 6.7 disclosures per company, compared with 3.9 for companies with market caps under $3.2 billion.
- The study found a significant increase in both the number of companies providing disclosure aligned with the TCFD recommendations, as well as an increase in the number of recommendations followed by the companies. According to the report, 90% of companies in 2022 provided disclosures in line with at least one of the TCFD's 11 recommendations, compared with 80% in 2021 and only 64% in 2020, and 58% of companies are now reporting on at least 5 recommendations, up from 40% last year and only 18% in 2020. Average disclosures per company reached 5.3 in 2022, up 66% from 3.2 in 2020.

TCFD

COMMERCIAL

1. The **United Arab Emirates** will host the **first-ever ministerial dialogue on building water-resilient food systems during COP28**. The ground-breaking session will take place on December 10th, 2023, and represents a partnership with Brazil. The initiative was made public by the UAE Minister for Climate Change and Environment Mariam Almheiri at the UN-organised World Food Day Conference in Rome.

- The Minister urged nations to sign the Emirates declaration on resilient food systems, sustainable agriculture and climate action. In doing so, nations would commit to aligning national food systems and agricultural strategies with nationally determined contributions, national adaptation plans and national biodiversity strategies.
- The initiative will bring together ministers, the private sector, international organisations and civil society to assess water and food resilience within national determined contributions and national action plans. Worldwide, agriculture is the single largest consumer of freshwater, while food production is responsible for up to 33% of total global emissions, according to FAO data.

2. **Masdar City** aims to **accelerate the United Arab Emirates' net zero transition**. Masdar City and Huawei signed a memorandum of understanding (MoU) at GITEX Global 2023 to promote knowledge-sharing and capacity-building in net zero development. Both parties also aim to help reduce the carbon footprint of Masdar City's information and communications technology (ICT) infrastructure, and promote the adoption of carbon-conscious ICT.

- In addition to optimizing existing ICT systems at Masdar City, Huawei will advise on Masdar City's upcoming command and control centre, which will feed data related to energy, water, and waste management in all Masdar City-owned buildings to a central location. This will allow facilities managers to monitor and improve building performance in real-time.
- Masdar City, already home to one of the largest clusters of LEED platinum buildings in the world, has 3 net zero energy buildings currently under construction, the first of which will be completed in October 2023. Huawei is already home to several low-carbon campuses and is creating new technologies to support sustainability as one of their strategic priorities.

3. **Abu Dhabi University (ADU)** inaugurated its **first on-campus inflatable and portable farm**. The inauguration is a result of a recent agreement signed between ADU, Midbar and RBK to establish a business framework for delivering supply and research and development solutions to the UAE market across several sectors.

- With this facility, ADU aims to maximise its innovation efforts to provide students, faculty and the wider UAE community with sustainable and inclusive solutions to overcome challenges and foster innovative thinking. The space will enable students and faculty with the opportunity to positively impact the UAE's community by providing practical learning opportunities, fostering interdisciplinary collaboration, promoting innovation and contributing to sustainable solutions in agriculture, which reflects with the country's commitment to a sustainable and innovative future.
- The project integrates various technologies, including the IoT and AI, in addition to more than 15 innovative solutions, to create a sustainable environment for food security and agriculture. Advanced smart farming solutions support the community by increasing crop yields by up to 30% and reducing labour costs by up to 80%, as well as the need for inputs such as water and fertiliser.