BANK OF ENGLAND

Speech

The Road to Glasgow

Speech given by

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Introduction

Sir David Attenborough's prophetic introduction has exposed the scale of the challenges and hinted at the enormous opportunities before us. And the Secretary of State has just described the prospect of a lasting COP 26 legacy and the opportunity for finance to be the force for good we know it can be.

Now is the time to answer these calls to action. Private finance will have a critical role to play in a successful transition to a net zero carbon economy. With the UK COP26 Presidency, in partnership with Italy, the world is watching.

Today is all about action. The actions the private financial sector can take to support a whole economy transition. The actions that regulators, governments and countries will take to catalyse your efforts. The actions that our fellow citizens are demanding, and that future generations deserve.

And you have already begun. Private finance is now increasingly focused on the opportunities and risks in the transition. Every major systemic bank, the world's largest insurers, its biggest pension funds and top asset managers are calling for the disclosure of climate-related financial risk through their support of the Taskforce for Climate-related Finance Disclosures (TCFD).[1] Investors controlling over $40 trillion in assets (across Climate Action 100+, UN PRI, and the Net Zero Asset Owner Alliance) want to see transition plans to a low carbon world from their portfolio companies.[2] This is backed by the critical roles that Multilateral Development Banks, Development Finance Institutions and National Development Banks are playing to accelerate their support to low carbon growth.

Achieving net zero will require a whole economy transition—every company, every bank, every insurer and investor will have to adjust their business models. This could turn an existential risk into the greatest commercial opportunity of our time.

As the Secretary of State said, finance is the COP 26 deliverable that "makes all the others - adaptation and resilience, nature, energy transition and clean road transport- possible."

The scale of these requirements are enormous: $3.5 trillion in infrastructure investment alone every year for decades.[3] All forms of finance: public, private and blended finance will play a part. Public finance to support a fair and inclusive transition across our economies. Development and blended finance to support adaptation and resilience. And mainstream private finance to help all companies realign their business models for net zero.

The objective for the private finance work for COP 26 is simple: ensure that every financial decision takes climate change into account.

[1] The full list of current TCFD supporters is available at: https://www.fsb-tcfd.org/tcfd-supporters/.
[2] See https://www.unpri.org/signatories, http://www.climateaction100.org/investors, https://www.unepfi.org/net-zero-alliance/.
[3] https://www.iea.org/news/deep-energy-transformation-needed-by-2050-to-limit-rise-in-global-temperature.

To do so, we will work with you – the private sector – to put in place the frameworks so that you can do what you do best – allocate capital to manage risks and seize opportunities across the economy.

Determining who's ready for the transition and who's not requires:

1. Disclosure of climate financial risk to become comprehensive;

2. Climate risk management to be transformed; and

3. Investing for a net-zero world to go mainstream.

On the road to Glasgow, we will focus on the three Rs: reporting; risk management; and return - to help unlock the private financial flows that are vital to the transition. This will support a wider shift to Paris alignment and be underpinned by public finance efforts to deliver $100bn.

To succeed we will need your support and your action. We will publish the strategy and how you can get involved when I formally assume my new roles, but following Sir David's lead, I wanted to offer you an exclusive preview today.

Reporting: improving the quantity and quality of climate-related disclosures by implementing a common framework built on TCFD

An old adage is that which is measured can be managed.

For COP 26 we want you to help refine and implement TCFD disclosure; and we will work with authorities to commit to pathways to make climate reporting mandatory.

We will build on existing good work. Catalysed by the G20 and the Paris COP, the private sector has already led the development of a framework for climate financial reporting through the TCFD.[4] The TCFD has become the go-to standard for consistent, comparable and decision-useful and efficient information. It is comprehensive, encompassing recommendations on governance, strategy and risk management, as well as metrics and targets.[5] And most importantly, it represents the best views of the private sector of what is decision useful, capturing the opinions of both the companies that must access finance and of the providers of capital from across the financial system.

[4] The 2017 recommendations report is available at https://www.fsb-tcfd.org/publications/final-recommendations-report/.
[5] The TCFD is the only reporting framework to all each of these strands for both banks and investors: https://carbonaccountingfinancials.com/files/downloads/Overview-Initiatives-Shaping-Climate-Action-Journey-for-FIs.pdf.

The TCFD has widespread public backing from across the financial sector.[6] Every major systemic bank, nine of the ten top asset managers, all the credit rating agencies, all major accounting firms and shareholder advisory firms back the TCFD. In January this year, the International Business Council (IBC) of 140 CEOs published a report on a common set of metrics that IBC members signed up to, which included TCFD.[7] And the UNPRI announced that all 2,275 signatories must make TCFD disclosures or risk ejection from the group.

The institutions like yours will be the main users of this information. You have the opportunity to shape these disclosures as they become market standards. We encourage the private sector to:

1. **Contribute to the review of the current TCFD framework that Mary Schapiro is leading.** Tell her what's important, what's less so, what should be refined to ensure disclosures are decision-useful, comparable, consistent and efficient before they become mandatory.

2. **Commit to reporting a full set of TCFD disclosures in the 2021/22 reporting round:** The self-help community for TCFD is considerable. Through multi-sector TCFD summits and more focused TCFD industry preparer forums, companies can continue to share knowledge to improve disclosure practices.[8] Full disclosure encompasses scope 1, 2 and 3 emissions and includes a strategy for managing these down, embedded through appropriate board-level governance structures and linking outcomes to compensation.[9]

3. **Demand TCFD-consistent disclosures from your borrowers and the portfolio companies.** In the process, you will unleash tremendous value and be better able to manage embedded risks.

For COP 26 we will work to develop pathways, in consultation with international standard setters - such as the FSB, IFRS and IOSCO – and national authorities to determine the best approaches to making climate disclosure mandatory.

Risk management: ensuring firms and investors can measure and manage the risks in the transition to a net zero world.

The second step on the path to a sustainable financial system is better climate risk management.

Managing climate-related financial risks requires disclosure to go beyond the static (a company's carbon footprint today) to the strategic (their plans to manage down their emissions). Risk management means assessing the forward-looking disclosures to judge the resilience of firms' strategies to the transition.

[6] The full list of current TCFD supporters is available at: https://www.fsb-tcfd.org/tcfd-supporters/.
[7] https://www.weforum.org/press/2020/01/measuring-stakeholder-capitalism-world-s-largest-companies-support-developing-core-set-of-universal-esg-disclosures/.
[8] https://www.wbcsd.org/Programs/Redefining-Value/External-Disclosure/TCFD.
[9] Scope 1 means all direct emissions from the activities of an organisation.
Scope 2 means indirect emissions from electricity purchased and used by the organisation.
Scope 3 means all other Indirect emissions from activities of the organisation, occurring from sources that they do not own or control.

To this end, the Bank of England will become the first regulator to stress test its major banks and insurers against different climate pathways, including the catastrophic business-as-usual scenario, the ideal - but still challenging - transition to net zero by 2050, and the late policy action - or climate Minsky moment – scenario that could bring a sudden recognition of the scale of stranded assets and the economy-wide disruption that a delayed and disorderly transition will bring.[10]

Our stress test of the world's leading international financial centre will show how major financial firms expect to adjust their business models, as well as the potential collective impact of these responses on the wider economy.

The stress test will reveal the financial firms - and by extension the companies - that are preparing for the transition, and it will expose those that have not.

The Bank's stress test will build on the scenarios being developed by the Network for Greening the Financial System (NGFS) – a coalition of over 50 central banks, representing half of the world's emissions.[11] This spring, the NGFS will make these scenarios open source and publicly available, so that any company, in any sector, can use them to assess their strategic resilience.

To embed climate-risk management, we're encouraging the financial sector and our international peers to:

1. **Help shape the climate stress testing framework, which Sam Woods will describe later this morning,** by sharing your expertise and responding to the approach that the Bank has put forward in its discussion paper.[12]

2. **Start building capability within your firms.** Expertise in managing the physical and transition risks associated with climate change will be a core competency for banks and insurers.

3. **Share knowledge and expertise.** Climate risk management is a nascent field, and we all need rapidly to improve our skills. That's why the Bank and the FCA have established the Climate Financial Risk Forum (CFRF) to publish the sector's collective view of risk management and scenario analysis best practice.[13]

4. **Run stress tests in other jurisdictions.** Already, 15 other authorities have committed to run stress tests. Through the NGFS, the Bank of England will share our experience so that others can conduct stress tests for their own financial systems. This will help improve and refine the methodology.

[10] https://www.bankofengland.co.uk/news/2019/december/boe-consults-on-proposals-for-stress-testing-the-financial-stability-implications-of-climate-change.
[11] https://www.banque-france.fr/en/financial-stability/international-role/network-greening-financial-system.
[12] https://www.bankofengland.co.uk/paper/2019/biennial-exploratory-scenario-climate-change-discussion-paper.
[13] CFRF members include banks, insurers, asset managers, and other organisations with a strong interest. The working groups include industry groups to ensure a wide range of views is reflected. https://www.bankofengland.co.uk/climate-change/climate-financial-risk-forum.

5. **Embed assessment of climate risks into financial stability analysis:** where the FSB is taking forward work, drawing on the advances made by its members as well as the NGFS.[14]

Return: helping firms and investors identify the opportunities in the transition to net zero.

The transition to net zero will affect every sector of our economies, and all companies that are transitioning to net zero should be encouraged.

In parallel, with people increasingly demanding climate action, asset owners and managers will need to disclose whether their clients' money is being invested in line with their values—a point Richard Curtis will make much more eloquently and forcefully later this morning.

Thus far, the approaches to doing so have been inadequate. ESG metrics—while worthy—are dominated by the S and the G. Carbon footprints are not forward-looking. And the impact of shareholder engagement is hard to measure. Moreover, a whole economy transition isn't about funding only deep green activities or blacklisting dark brown ones. We need fifty shades of green to catalyse and support all companies towards net zero and be able to assess collectively whether we're "Paris aligned".

Given that net zero is both an imperative of climate physics and a commitment by 120 countries; companies, banks, insurers, pension funds and investors will increasingly be expected to develop and disclose their transition plans. For companies that could mean:

- Commitment to a net zero target (for scope 1, 2 and ideally scope 3 emissions) by a specific date;
- Assessment and disclosure of how the transition to a net zero business model will impact strategy;
- Short term milestones to track progress; and
- Details of governance, including whether executive compensation is tied to success and how risks are managed at the board level.

In turn, there are several possible ways for the providers of capital to assess the level of preparedness for the transition. To support the assessment of who is on the right side of history and therefore presents the most promising investment opportunities in the transition, providers of capital could measure and disclose:

1. **The percentage of assets that comply with TCFD disclosure;**
2. **The percentage of assets that are Net Zero-aligned ("Paris aligned");**

[14] See e.g. Giuzio, M. et al. (2019), *Climate change and financial stability* in the Financial Stability Review of the European Central Bank, May 2019; and Piera de Silva, L. A. (2019) *Research on climate-related risks and financial stability: An "epistemological break"?*, speech at at the Conference of the Central Banks and Supervisors Network for Greening the Financial System (NGFS), Paris, 17 April 2019.

3. **Progress on transition as assessed against industry-specific transition pathways** to help identify the leaders and laggards in the transition; and

4. **Degree warming potential of the portfolio**, which assesses the quality of transition plans relative to the Paris goals. Firms such as Aviva, Axa and Allianz have already voluntarily disclosed this information. They are now feeding into a TCFD group that is considering whether the warming potential, or any other metric, is the best way to measure the potential opportunities in the transition.

For COP 26, we intend to leverage the success of existing groups and coalitions, like the Net Zero Asset Owner alliance, Climate Action 100+ and the UN PRI to build a large coalition of asset owners and asset managers who expect their portfolio companies to become Net Zero aligned.

MDBs and Innovative Finance

The work on reporting, risk and returns will put in place the foundations for private finance to help drive the transition to net zero, but much more must be done across the full spectrum of the financial sector.

Multilateral Development Banks and Development Finance Institutions have essential roles in mobilising blended finance for adaptation, resilience and mitigation, especially in the communities most exposed to the devastating effects of climate change. As the Secretary of State noted, we will be asking these institutions to develop robust implementation plans for Paris Alignment in the run up to COP26.

We will also consider how to best channel the expertise, experience and ingenuity of the financial sector to develop innovative approaches to meet the biggest challenges in the transition to net zero. This will mean:

1. Understanding which new financial products, such as transition bonds and transition indices, can make a real difference to climate finance and support efforts to scale them up rapidly as needed.

2. Promoting the most promising climate innovations in insurance sector, such as contingent liability structures for climate policy risk and micro- insurance in emerging economies, drawing on the leadership of organisations such as the CCRI and IDF; and

3. Evaluating the prospects for private markets in carbon offsets and nature-based solutions, drawing on the sector’s expertise in creating and running efficient and transparent market infrastructure.

Conclusion

With sustainable finance moving from CSR to the C suite, the UK COP 26 Presidency in partnership with Italy will help build the foundations of a system that will be able to seize the opportunities of transitioning to net zero.

The UK has been at the forefront of innovation for centuries. It was the birthplace of the industrial revolution that brought unimagined progress. The City financed the steam engines, the railroads and the new energy sources that powered this transformation. And now – on the cusp of the sustainable revolution – the world once again needs your innovation, resources and leadership. Your actions can reinforce and amplify the efforts of development finance institutions, MDBs, and local and national governments spanning 195 countries.

Join the world on the road to Glasgow, and help create a path to a sustainable world.

COP26 private finance strategy to drive Whole Economy Transition

Overarching goal: Every financial decision takes climate change into account

Reporting	• Private sector to refine TCFD climate-related financial disclosure to increase quantity and quality of reporting	• Agree potential paths to mandatory reporting at domestic and international levels	• Build coalitions of countries who mandate reporting and companies committed to full climate disclosures
Risk Management	• Assess the resilience of firm's strategies to net zero transition through stress tests	• Develop open source, business-relevant reference scenarios for regulators, financial firms and businesses to test strategic resilience	• Establish coalition of central banks and regulators committed to issuing guidance on risk management and running stress tests
Return	• Enable investors to make informed decisions on whether companies and portfolios are transition ready	• Agree metrics to measure net zero/ alignment of investment portfolios	• Build coalition of financial institutions that commit to net zero alignment and measurement and disclosure of progress
MDBs/DFIs	• Encourage MDBs to report their own emissions and exposure to climate risks, in line with TCFD	• Realise MDBs' commitments to transition plans to achieve Paris Alignment	• Explore rapid expansion of blended financing for climate resilience, adaptation and mitigation
Innovative Finance	• Work with the private sector to promote the most promising and impactful financial innovations in sustainable finance (including transition bonds, contingent climate securitisations, and the scaling up of rapid private markets for carbon offsets and nature-based solutions)		