

Bank Investor Engagement Project

July 2022



Improving climate transition planning communications

The Bank Investor Engagement Project (BIEP) was launched in 2021 by Tapestry Networks and the High Meadows Institute to address communication challenges between large banks and their investors. Its primary focus is to establish key priorities and identify gaps and good practices for effective communication and engagement between institutional investors and banks on environmental, social, and governance (ESG) issues. On June 22, 2022, BIEP participants met virtually to discuss investor expectations regarding bank climate transition plans, and what effective communication and engagement on climate transition entails.

The last 12 months have marked an inflection point for banks committing to and articulating plans to transition their businesses in response to climate change. In the lead up to and following COP26 in November 2021, nearly 100 large banks globally joined the Net-Zero Banking Alliance. Even many of the holdouts have now made commitments. As large banks subsequently published climate transition methodologies and plans, they also confronted new headwinds to transition efforts. The Russian invasion of Ukraine heightened sensitivity around energy security and affordability as gas prices around the world surged, contributing to inflation with the prospect of a global recession looming. Talk of a “just transition,” that is, one that does not disproportionately impact low-to-moderate income people or those in emerging markets, and the need to balance priorities around energy security and cost, have altered the discussion around climate transition in national capitals and boardrooms.

Discussion on June 22 highlighted that investors are looking for both more specifics about implementation plans and interim targets, but also greater transparency and candor about the challenges in achieving them.

This *ViewPoints* synthesizes perspectives emerging from the session and discussions in preparation for the meeting. It is organized around the following sections:

- **Investors expect banks to actively facilitate the transition to a greener economy**
- **Investors are looking for greater detail and transparency in transition plans**
- **Banks are managing a range of challenges to improve planning and communication**
- **The road ahead: improving engagement through ongoing discussion**

Investors expect banks to actively facilitate the transition to a greener economy

Banks play a unique role in supporting economic growth in the markets they serve. Stakeholders look to banks to shift financing from carbon-intensive activities to sustainable ones. An investor said, *"We see them as engines of economies. As this massive transition happens in economies, they need to make sure they're on top of it."* Another stated, *"We expect to hold their feet to the fire on it. They have to play a central role."* BIEP participants discussed the role investors expect banks to play:

- **Investors want to see evidence that banks are acting on their commitments.** Investors want banks to translate statements of intent into demonstrated action. One said, *"It's committing to Net Zero by 2050, and putting out interim targets. Those are the basics of what I'm looking for from the large banks that I cover."* While investors increasingly recognize that Net Zero plans will be iterative, they expect them to be credible and authentic. *"We don't want to see any gaming because we're already seeing the ability for people to arbitrage between balance sheets, etc. And we're of the view that you have to commit to a 1.5-degree scenario. Anyone who doesn't use a 1.5-degree scenario is not serious. The difference between 1.5 and 2.0 degrees is life or death for millions of people."* Investors are also looking for greater transparency about banks' lobbying activities and those of industry groups *"and the extent to which these are aligned or not with their commitments."*
- **Banks should engage with policymakers, but not wait for regulatory clarity to establish standards.** Investors want banks to proactively engage in developing standards and frameworks rather than waiting for the regulators to take charge. According to one investor, *"I think there should be an expectation on the banks that they are engaging with their regulators to ensure that the regulatory environment encourages and enables change."* Another encouraged banks to lead: *"Hopefully, banks will not wait for the regulator to come up with standards; banks are driving standards, which is good, through all of these industry initiatives, like the Net-Zero Banking Alliance."* Another investor suggested banks continue to engage with regulators as well: *"How can you engage with policymakers and regulators to make sure that the incentives are there for companies to decarbonize because, if incentives aren't in place, it's not going to happen. And banks are more bound than most industries by the regulatory environment."*
- **The largest global banks face heightened expectations.** Investor expectations vary based upon a bank's size and where they operate. One investor acknowledged, *"As investors, we have to look at the overall regulatory regime and also regulatory constraints or operating environments that banks have."* As a result, most investors distinguish between banks with operations concentrated in single geographies and the regulatory environment there and

those that operate across multiple jurisdictions. The global banks are generally held to the highest standard. An investor said, “*I think what I would expect from a global financial institution is some of that sharing of knowledge across jurisdictions, which would help them to understand the risks that they're taking at a different level.*” Another explained, “*We focus only on the largest and global banks, because ultimately, they will have the biggest impact on global emissions reductions.*”

Investors are looking for greater detail and transparency in transition plans

Many banks have only just published their first climate transition plans, and some are still developing their first draft. To date, banks have used different formats, different methodologies, and different climate scenarios in their plans. As a result, meaningful analysis and comparison across banks is challenging: one investor suggested the industry is “*at a stage of commitment and process and calculation improvement, rather than at a data comparison stage.*” Investors are looking for some common components, however. One said, “*You begin to look for three dimensions of key first principles that you'd expect to be there: 1. How are you as an institution helping your customers get to Net Zero through your lending and challenging of them? 2. How will you yourself as an institution get to Net Zero in terms of your world footprint or your use of energy and travel and buildings? And 3. How are you building capability both internally and externally to help develop solutions?*” All participants noted that the process will be iterative, as bank plans develop over a three-to-four-year timeline. Participants highlighted some areas where banks can enhance communication:

- **Key targets and timelines on the path to Net Zero.** An investor called for banks to include “*a plan of action, a rollout, and a timeline.*” Another stated, “*We appreciate that many banks have established long term targets and credible long-term goals, but we want to see more disclosure from banks about interim targets, especially to 2030.*” An investor explained, “*Realistically, we know, for example, that we are not going to be able to get rid of coal-fired steel plants by 2030. So, by extension, certain parts of real estate are not going to meet near term alignment, or midterm alignment with Net Zero. It's going to come later. Acknowledging that those things will come is really important in building out that timeline.*” Investors would also like more information about how banks are engaging with clients: “*In order for banks to set these targets, they have to engage with industry clients, their biggest clients, but they're opaque on the timeline for that, and we want to more disclosure about this.*”
- **More transparency around challenges to achieving commitments.** “*We'd welcome banks being very transparent about challenges that they face. Perfection shouldn't be the enemy of the good ... We recognize that there are significant challenges,*” said one investor. Another noted, “*People have shied away from really talking about the potential financial*

tradeoffs of Net Zero, but it's not all going to be good in terms of profitability, and that's a discussion that needs to be had transparently."

- **Greater insight into the full extent of carbon-related financing activities.** While investors are not pushing for divestment from oil and gas companies or other high-emitting sectors, they would like to better understand the full range of bank exposures and support for those sectors and activities. An investor said that includes not just financed emissions, but "*facilitated emissions*," through things like bond underwriting that may not end up on bank balance sheets. One investor said this represents "*a blind spot in most of the plans that I have seen.*" They would also like better transparency into not just outstanding loans, but the total "*undrawn commitments; everything that's potentially available to a client.*"
- **Further details on how banks are managing to a just transition.** Investors are increasingly conscious of the need to ensure the transition to a sustainable economy does not have a disproportionately negative effect on those least able to absorb additional costs. One said, "*We have to be honest. When we talk about transition, we have to talk about a just transition in the same sentence; they're indivisible.*" The same participant asserted, "*We need to be really thoughtful about what happens over the next couple of years in terms of capital allocation and what transition means: does it mean more natural gas or more nuclear or doubling down on renewables? Because the cost of energy has gone up so much. But the key thing is being transparent and honest about it. We want to see that people are grappling with the issue, not using it as an excuse to duck the issue.*" This also means clearly connecting social issues to climate transition planning, such as ensuring "*resilience and adaptation,*" for those already being affected by climate change.
- **Shifting more focus to advancing sustainable finance.** Much of the focus on transition planning is on how banks are reducing their financing of brown activities. Investor participants are looking for more attention as to how banks can increase sustainable finance. One investor said, "*We've been asking banks to talk more about the green side of the equation ... I think that the banks have an opportunity to be the solution to the problem of providing financing to green industries and renewables and helping that way.*" Many banks have made green financing commitments, but what is included in those commitments varies by institution. Investors would like to see more "*frequent reporting updates on progress against those targets.*" As one bank participant noted, "*If we simply constrain supply without simultaneously addressing demand, what we will see is, in effect, a much worse version of what we're already seeing, which is a huge consequence for energy affordability for industry and for households, which is a very disorderly transition.*" Another observed, "*I see a lot of focus has been put on phasing out bad stuff. There are shiny headline figures about what's being done in primary investment positions for green finance, and there are a lot of unknowns about the impact of that. Helping stakeholders*

understand what the banks are really doing more than just as a headline number to really encourage that energy transition would go a long way.” Ultimately, investors and banks are looking for ways to find a balance between the more mature focus on climate and sustainability risk and the nascent measurement and reporting on opportunities for banks investing in transition. A bank executive suggested investors could also do more: “This is transforming our business, and yet activists just want to get a sound bite. We need to get off the incessant oil and gas focus and focus on the investment in the systems change we need. We need investor pressure to transform the system by doing more to support new technologies ”

- **Linking climate transition to incentive compensation.** Investors expect banks to align executive compensation with meeting climate targets. According to one, “*That's certainly something we're very focused on in discussions: getting climate targets, and key materiality and sustainability targets reflected in executive compensation.*” And yet, the same investor noted, “*Everybody claims they're doing it in one way or another. But I think best practice is miles apart from what the majority of the space is doing.*”
- **Increasing third party assurance.** Climate reporting remains a long way from the maturity of traditional financial reporting, making auditing and assurance difficult. But investors would like additional third-party assurance to get comfortable with the information banks are producing. An investor said, “*Moving towards assurances around your mathematics, how do you do it? I was never trained to do that. And I'm not a climate scientist; I'm going to assume that your math is correct, but I would like someone else to vet it. I think that's really important for us.*”

Banks are managing a range of challenges to improve planning and communication

Banks are learning as they go through a complex process that touches on virtually every aspect of their businesses. They emphasize the importance of investors developing a better understanding of those complexities as they assess banks’ planning and reporting efforts. A banker stated, “*I'm really interested in making sure that investors understand how to read banks' Net Zero plans and interpret them, because I feel like we've learned so much through this process, and it's a super technical exercise. But what I've noticed is that there seems to be a default among at least activist investors that it's too hard and there's too much homework required to understand what we report. So, you have this reversion to, ‘You didn't commit to phase out fossil fuel expansion’ ... It's not necessarily grounded in climate science.*”

Bank participants identified some of the challenges they confront in the transition planning process:

- **Accessing data remains a central constraint.** A bank participant said, *"The data issue is the biggest tangible issue that we're facing. It's emissions from clients that we never thought about or collecting production data on barrels of oil or megawatts of energy as an output. It's all the way down to things like system records of the square footage of buildings that we're financing."* Estimating Scope 3 emissions across their portfolios, particularly financed emissions, presents banks with perhaps their biggest obstacle. Future regulation requiring public companies to disclose their emissions could help but may not be a panacea. A banker explained, *"The fossil fuel companies have been doing this for a while. It is more of a challenge for the smaller companies who have lower emissions; it's not on their radar. They are smaller in impact but in aggregate they could really be material, and many of our clients are not even public companies."* An investor predicted, *"A lot of institutions are going to have to do a sort of mark-to-market or a reevaluation over time as tech and data improve. We want to see that happen. We don't want you to rest on assumptions, even if they prove correct. And frankly, I don't think we would punish institutions for digging in and redoing their data the way they should."*
- **Forecasting over long time horizons.** Trying to forecast the impact of climate change across a bank's portfolio by 2050 is not only a difficult exercise, but one that relies on a range of unknowns and assumptions regarding issues outside the banks' control. A bank executive commented, *"There is not going to be a very clear year-by-year linear path. It's getting incredibly hard to predict just what the milestones will be year to year."* Scenario planning is an important aspect of long-term planning, but some banks have played "choose-your-own adventure," by using bespoke scenarios. Some activists and others are pressing banks to use a single, sector-agnostic scenario. As one participant noted, *"Scenarios are not forecasts. A scenario is a just a version of the possible future, to offer a narrow, but achievable path to Net Zero."* In response, an investor said, *"There is no scenario; there are scenarios, and we think these scenarios are industry specific. The effort by some groups to impose one scenario on banks are just wrong, and we're pushing back."* Ultimately, these scenarios provide carbon budgets required to meet temperature goals within a probabilistic determination. As a result, a bank executive noted, *"At the end of the day, regardless of which scenario you use, you have to get within that budget, and that is going to require significant reductions of carbon in each of those sectors, significantly moving away from the trajectories today."*
- **Navigating an uncertain, sometimes contradictory, regulatory landscape.** Banks and investors have had to understand and navigate an emerging "alphabet soup" of frameworks, standards, raters, and stakeholder groups as the ESG agenda has matured.

While industry efforts and new reporting requirements suggest convergence is coming, one bank director warned, *“it’s going to take longer than people expect based on my experience.”* In the meantime, as some jurisdictions move forward with stress tests, taxonomies, and legal action to combat greenwashing, some states in the US are moving in the opposite direction. Texas and West Virginia, for example, recently adopted laws designed to limit state business with any financial firm that boycotts fossil fuel companies.¹ At the same time, banks are looking for greater policy clarity from governments that have made their own Net Zero commitments. A banker said, *“Almost every government in the world has set Net Zero related ambitions. Timeframes can vary from jurisdiction to jurisdiction, but only about a quarter of those have enacted laws on the back of those.”*

- **Grappling with issues beyond their traditional mandates.** In the absence of clear public policy, banks feel as though they are being asked to make decisions best left to elected policymakers. *“These are really complex issues that affect geopolitical issues and our national and regional energy security,”* a bank executive observed, *“And I think it is very challenging to ask banks to take a bilateral position on an aspect of what is an incredibly complex energy transition.”* As long as banks are compelled to deal with this situation, one bank executive advised, *“The only way to navigate that is to have a very clear policy and to be consistent about it ... You can’t try to cater to all sorts of different audiences.”*

The road ahead: improving engagement through ongoing discussion

As banks refine and implement transition strategies, some view investors as potential allies in driving progress. One bank participant said, *“You do need to hold us accountable and to hold our clients accountable to following through on the commitments that we’ve made.”* Banks and investors see value in informal engagement to identify *“the redline issues”* and the *“areas of real complexity that we could explore together and try to be thoughtful about how we address them.”* Participants identified the following areas for further exploration:

- **Diving into sector-focused transition planning.** A bank participant said it would be helpful to get *“into the weeds of specific sectors and what investors are expecting from us.”* Bringing carbon-intensive sectors into these discussions could help to *“manage aspirations with where our clients are today.”* An investor observed, *“We’ve seen some banks compare the mix of their portfolios to the broader global economy and sort of laying out some differences in climate exposure in that regard. Those comparisons have been interesting in terms of lending to heavy carbon emitting sectors.”*
- **Engaging more effectively with policy.** Some participants see potential to share case studies and specific examples of areas where banks have worked proactively to shape the climate policy discussion in an open and transparent manner.

- **Providing opportunities for candid discussion on climate transition planning.** A participant noted the value of ongoing, informal discussions among banks and investors to complement the many industry efforts, frameworks, and protocols already available. A participant said, *"The white papers are already out there, and there are the official groups, but the value of this group is that it is more honest. So, I think it's helpful to have an informal report, but it's really the continuing sharing of perspectives as we build this up."*

As we look ahead, we invite investor and bank feedback on climate transition plans and on bank ESG communications more broadly as we explore future opportunities for banks and investors to engage.

About the Bank Investor Engagement Project (BIEP)

The Bank Investor Engagement Project addresses communication challenges between complex banks and their investors. Its primary focus is to establish key priorities and identify gaps and good practices for effective communication and engagement between institutional investors and banks, especially around matters not covered in existing financial communications. The BIEP is organized and led by Tapestry Networks, in partnership with High Meadows Institute. *ViewPoints* is produced by Tapestry Networks and aims to capture the essence of the BIEP discussions and associated research. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of senior management, advisers, and stakeholders who become engaged in this leading-edge dialogue, the more value will be created for all.

About Tapestry Networks

Tapestry Networks is a privately held professional services firm. Our mission is to help the leaders of the most important institutions in the world do their work more effectively and with greater confidence. We create an environment where directors, executives, regulators, and policymakers learn from one another, explore new ideas, and collaborate to solve problems, working across the public and private sectors. Our work creates value for those who participate, for those who sponsor it, and for society. Since 2003 we have helped groups of leaders deal with difficult problems, all material to the success of their organizations.

About High Meadows Institute

High Meadows Institute is a think tank and policy institute focused on the role of business leadership in creating a sustainable society. High Meadows Institute conducts research, leads programs, and develops frameworks to increase private sector contribution in addressing the challenges of the 21st century. High Meadows Institute sponsors the BIEP as part of its continuing commitment to drive positive change.

Appendix

The following individuals participated in these discussions:

Participants

- Galina Alova, Vice President, Sustainable Investing, JPMorgan Asset Management
- Charlotte Apps, Sustainable Investing (ESG) Associate, Fidelity International
- Jeff Barbieri, Vice President, Corporate Governance/ESG Research, Wellington Management
- Drew Barker, Head of Climate, Risk Management, Truist Financial
- Laura Barlow, Group Head of Sustainability, Barclays
- Kim Croucher, Director, Sustainability and ESG, Barclays
- Stu Dalheim, Executive Director, Calvert Investments
- Lara de Mesa, Global Head of Responsible Banking/ESG, Santander
- Benjamin Friedrich, Director, BlackRock Investment Stewardship
- Drew Hambly, Executive Director, Global Stewardship, Morgan Stanley Investment Management
- Bob Herz, Audit Committee Chair, Morgan Stanley and Fannie Mae
- Carolyn Hewitt, Senior Investment Strategist, Responsible Investment, Newton Investment Management
- Tori Kaplan, Head of Corporate Responsibility, Truist
- Christian Leitz, Managing Director, Head Corporate Responsibility, UBS
- Andrew Mason, Stewardship Director, Abrdn
- Beate Muenstermann, Senior Financials Analyst, Managing Director, JP Morgan Asset Management
- Marty Pfinsgraff, Risk Committee Chair, PNC Financial
- Alan Smith, First Church Estates Commissioner, Church of England
- Val Smith, Managing Director and Global Head, Corporate Sustainability, Citigroup
- Matthew Vahidi, Vice President, BlackRock Investment Stewardship
- Tim Whitehead, Head of Sustainability Risk, Goldman Sachs

- Tim Youmans, EOS North America Engagement Leader, Hermes

High Meadows Institute

- Allison Kosta, Communications and Operations Manager
- Chris Pinney, President, and CEO

Tapestry Networks

- Dennis Andrade, Partner
- Eric Baldwin, Principal
- Tucker Nielsen, Principal
- Andre Senecal, Associate

Endnotes

¹ “State Bank Regulations Become New Front in the Fossil Fuel Wars,” *JDSupra*, May 5, 2022.