Legal & General
INVESTMENT MANAGEMENT

Net zero: banks and insurance

To prevent dangerous climate change, greenhouse gas emissions must reach net zero. What do **banks and insurers** need to do?

48% of global financial assets are in banking and insurance, with significant climate impact through their associated emissions

Sources of emissions

'Scope 3' Upstream

Indirect GHG emissions from a company's supply chain, employee travel etc.

'Scope 1'

Direct GHG emissions from companies' operations, including facilities and vehicles

'Scope 2'

Indirect GHG emissions from purchased electricity

'Scope 3' Downstream

Other **indirect** GHG emissions from lending, insurance, investment and advisory activities

Source: FSB (2020), data as at end-2018

Companies

Key levers

- Transitioning away from financing/underwriting high-carbon activities
- Building climate considerations into risk management frameworks to reduce and reprice carbon exposure
- Increasing intermediation of capital into low – carbon activities
- Climate-supportive products and advisory services; customer education

Governments

Key policies

- Carbon pricing
- Capital requirements and stress-testing aligned with rising carbon risks
- Use of incentives/subsidies to scale up sustainable products and activities
- Mandatory climate change disclosures

Challenges

- Data and compatibility with risk frameworks
- Mismatch of timings, incentives, maturity of investments
- Regulatory divergence and competing priorities
- Political and counterparty risk
- Fungible, fragmented sources of capital

Opportunities

- Anticipating - and benefiting from - future policy and regulatory action on climate
- Growth in demand for sustainable banking and insurance products
- Improved reputation and stronger relationships with customers/ governments

Other environmental considerations

- Pollution and impacts on biodiversity associated with financed activities

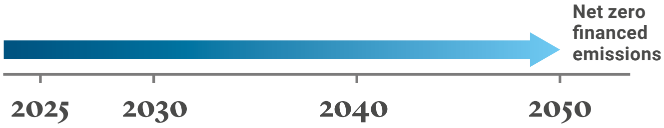
Social impacts and the just transition

- Access to finance linked to economic development; increased need to finance emerging markets and technologies
- Ending financing in certain sectors creates risk of job losses

Physical risk impacts

- Highest direct risks in property investments and insurance
- Indirect climate impacts on demographics and insurance liabilities

Decarbonisation effort



Easier to achieve

Transitioning away from projects/underwriting/ potential clients that are misaligned with the global direction of travel

Climate risk disclosure

Financing/intermediating low-carbon upgrades to existing and new infrastructure

Possible with effort

Changing the risk profile of 'green' vs. 'non-green' financial activities

Large-scale adoption of climate-friendly products and services

What is needed?

Company leadership

Alignment of investments/ financing with net-zero global trajectory, with targets for financed emissions increasing in stringency over time

Research and innovation

Investment innovations to allow capital flows at scale into low-carbon, including collaboration with regulators and development agencies

Consumer behaviour

Growing market for 'green' financial products

LGIM will vote and implement investment sanctions against companies falling short of our climate expectations.

How are we assessing companies' pathways to net zero?

Net-zero Commitment	• Does the company support the Paris Agreement target? • Does the company have a net-zero target for its investments, backed by clear milestones and strategy?
Strategy	• Is the company analysing the implications of climate change to its portfolio, and how they are integrated into its risk management frameworks? • Does the company clearly articulate its role in the low-carbon transition? • Is there evidence of company reducing involvement with high-emitting sectors?
Resilience	• Resilience of portfolio in – and alignment to – climate scenarios?
Targets	• Targets to grow revenue relating to 'green' financial products and services where there is clear alignment with existing business model
Collaboration	• Evidence of the company working collaboratively across its value chain to address climate financing challenges? • Evidence of the company advocating for meaningful policy action (e.g. carbon pricing)
Red lines	• Does the company have restrictions around underwriting/investing in thermal coal? • Does the company disclose scope 3 emissions associated with its investments?

For more information...

Please see: https://www.lgimblog.com/categories/esg-and-long-term-themes/climate-impact-pledge

Important information

Source: LGIM as at September 2020. The value of an investment and any income taken from it is not guaranteed and can go down as well as up, you may not get back the amount you originally invested. The above information does not constitute a recommendation to buy or sell any security

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