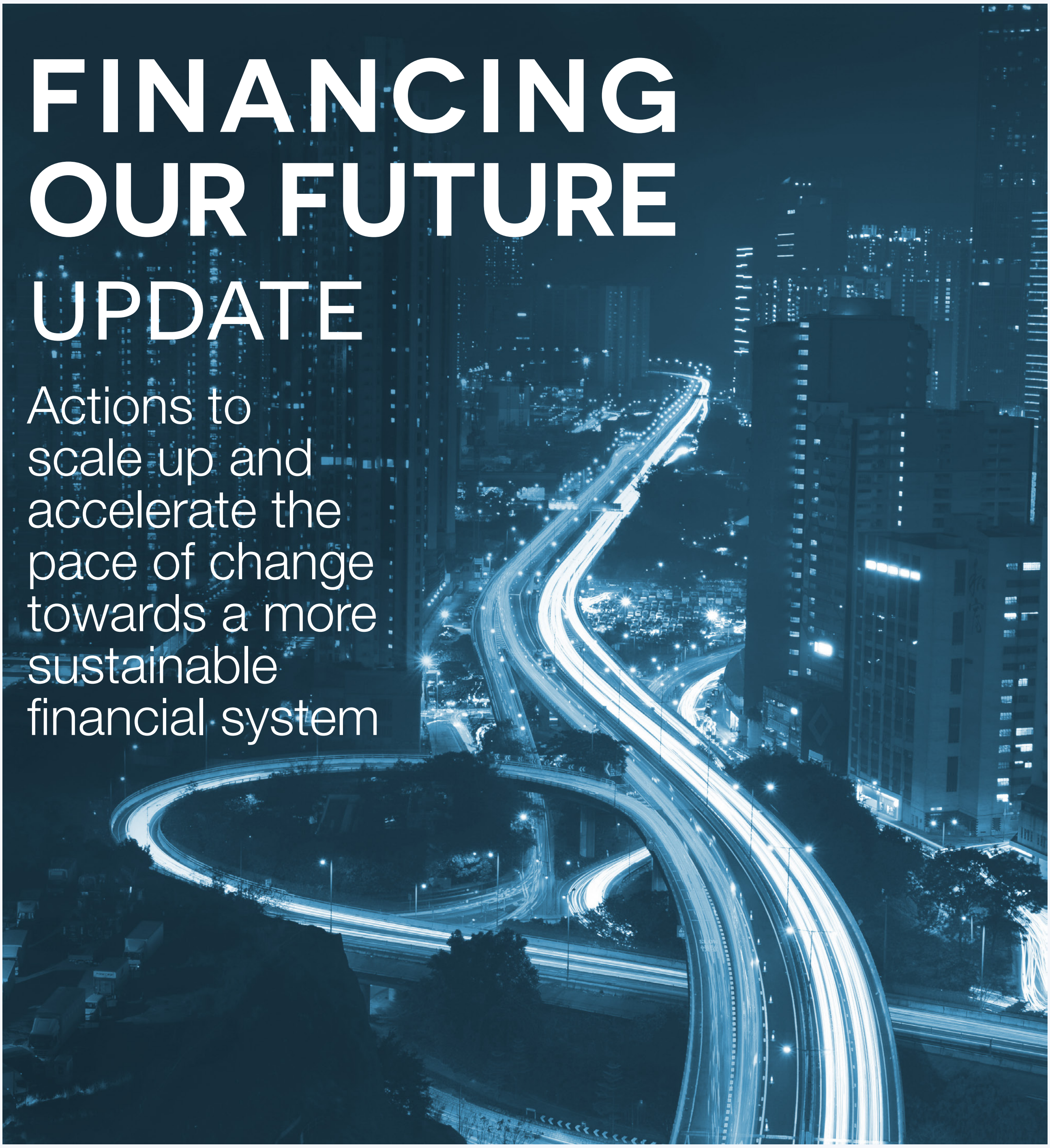
FINANCING OUR FUTURE

UPDATE

Actions to scale up and accelerate the pace of change towards a more sustainable financial system



A4S ACCOUNTING FOR SUSTAINABILITY

THE PRINCE OF WALES'S CHARITABLE FUND

AVIVA INVESTORS

The Finance Leader's Summit was hosted at St. James's Palace by HRH The Prince of Wales in 2018. The original Financing our Future report was produced following the discussions from the day. The pictures within this report are from that meeting of global financial leaders.

Published December 2019

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FOREWORD

Over the next 10 years, a rapid transformation of the global economy is needed if we are to address the current climate and nature emergencies, and create a sustainable future.

Our economic prosperity – and financial success – is dependent on a thriving society and a healthy planet. The reality is that environmental and social risks have a direct bearing on the sustainability of financial returns – this view is gaining ground, but too slowly to deliver the transformation required.

Successful organizations will need to redefine their business models if they are to continue to prosper in this very different world. Those who find ways to use natural resources in a sustainable way, and whose purpose is defined by the contribution they make to society, will find themselves uncovering new sources of innovation, reducing the risks they face and increasing their competitive advantage.

The pressure to deliver financial returns in the short term can make it seem challenging to respond to issues such as climate change, the full consequences of which are still to be felt. And yet the actions we take now are the ones which will determine our future economic, environmental and social wellbeing.

A growing number of leaders from each part of the investment chain and wider capital markets community are taking action to direct finance towards sustainable outcomes. It is only through collective leadership and by reconnecting with individual savers, investors and beneficiaries, that we will find solutions to the barriers which remain.

Last year, we brought together some of the largest and most influential representatives from across the capital market to define a set of actions that could deliver systematic change. 17 months on, this update of the Financing our Future report explores progress and commitments to action required.

As His Royal Highness has said, “There was a time when we could say that there was either a complete lack of knowledge, or at least room for doubt, about the consequences for our planet of our actions. That time has gone. We now know all too clearly what we are actually doing and that we need to do something about it urgently.”

The time to act is now.

Jessica Fries
Executive Chairman
A4S

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FOREWORD

Maurice Tulloch
Chief Executive Officer
Aviva

AVIVA

What each of us chooses to do today shapes what is possible for everyone tomorrow.

The nature of our business means that Aviva has long recognized the importance of thinking for the long term. Simply put, an unsustainable planet is an uninsurable one.

We also recognize that as part of the world's financial system we have the ability – and the responsibility – to help shape that system for the better. Our world is facing unprecedented pressure. If we cannot come together to find a more sustainable path, then the future looks bleak.

This is why the actions set out in this document and at the event it accompanied in July 2018 are so important. By offering practical steps for each part of the investment chain, they give clear direction to the choices all of us need to take. It is only by taking coordinated action that the enormous power of the world's financial resources can be directed towards investing in a future that works for everyone.

This document demonstrates the extent to which the current regulatory incentives are contributing to an unsustainable future, but also ways in which the system is beginning to change. A year on from the Finance Leaders' Summit, we have seen considerable progress on these recommendations. But our work is by no means done.

I want to pay tribute to His Royal Highness The Prince of Wales for his leadership on this most important of issues. Aviva is committed to continuing doing what we can to make a difference. As part of the group of Global Investors for Sustainable Development, convened by the United Nation's Secretary General, I look forward to sharing the content of this report with my fellow members as we promote the changes needed to build the future that we all wish to see.


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INTRODUCTION

In 2015, governments around the world committed to a sustainable and inclusive global economy through the Sustainable Development Goals (SDGs) and the Paris Agreement. These global goals provide a focus to develop solutions and channel investment towards areas such as decent work and economic growth, the provision of clean water and sanitation, reducing inequality, developing sustainable cities, and tackling climate change.

Nearly five years on from these commitments being made, and despite growing leadership across business, finance and government, the current trajectory remains an unsustainable one. Time is running out.

The most recent global data shows that financial flows are not yet moving in the right direction. Global fossil fuel consumption continues to increase, as do carbon emissions, almost half the world's population lack access to clean fuel, and nine out of ten people living in urban areas do not have clean air to breathe. Extreme weather events cost hundreds of billions in damages and billions of individuals across the world are exposed to water stress.

Last year, the United Nations (UN) highlighted that global emissions need to be reduced by 45% by 2030, and reach net zero by 2050. These dramatic reductions are vital if we are to have a chance of keeping the increase in global average temperatures to 1.5 degrees celsius, and of avoiding the worst impacts of climate change. At the same time, and in part driven by climate change, we are seeing a collapse in biodiversity, with severe consequences for humanity.

In July 2018, finance leaders from around the world gathered at St. James's Palace, London to commit to action. Included were representatives from each part of the investment chain, and they agreed to a set of five cross-cutting recommendations. These represent the actions needed to deliver a sustainable financial system that is supportive of the SDGs and puts us on a pathway towards achieving the goals of the Paris Agreement.

In September 2018, during the UN General Assembly, the Financing our Future Report was released, setting out these five recommendations, and the actions that need to be taken to achieve them, broken down by each actor in the financial system.

17 months on, this update summarizes the key findings in the original report, highlighting examples of progress made, and renewing the recommendations for action across all actors. The report is broken down into four sections:

1. An overview of the financial system, showing the connections between each actor
2. A summary of the five overarching recommendations
3. Indications of change and current actions, barriers and recommendations for each actor
4. A summary of the actions needed to underpin the five overarching recommendations

These actions will form the focus of our work in the coming year, helping to transform our economies and avert climate crisis.

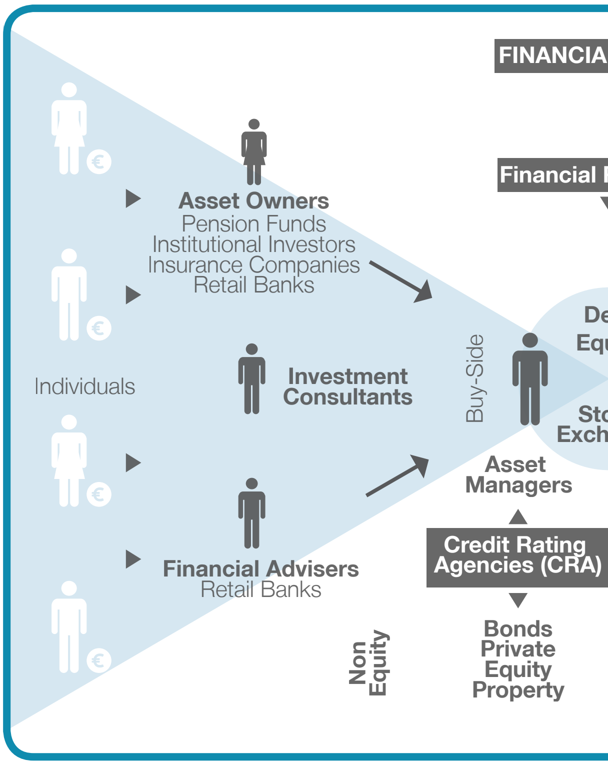
THE FINANCIAL SYSTEM

How all actors play a bigger role in delivering sustainable outcomes

Individuals are crucial and often overlooked participants in the financial system. Their savings fund investments in companies, who in turn are their major employers. Awareness of the impacts of the economy on society has increased dramatically in the last year and we now need to make the connection for people to help them understand their role in the financial system, its impact on the world around them and how they can have an influence, including through ensuring their sustainability and ethical preferences flow throughout the system.

Asset owners such as pension funds, insurers and sovereign wealth funds control a large proportion of global assets. If asset owners use their influence (often exercised via asset managers) to invest more sustainably, demand better information and practices from companies, as well as educate and consult their ultimate beneficiaries about the sustainability impact of the investments they make on their behalf, this would have a significant impact on sustainable development.

Investment consultants play an increasingly important role in advising asset owners on their investment strategies, including recommending asset managers. They should inform and educate clients about sustainable investing and provide solutions to address social and environmental risk and opportunity.

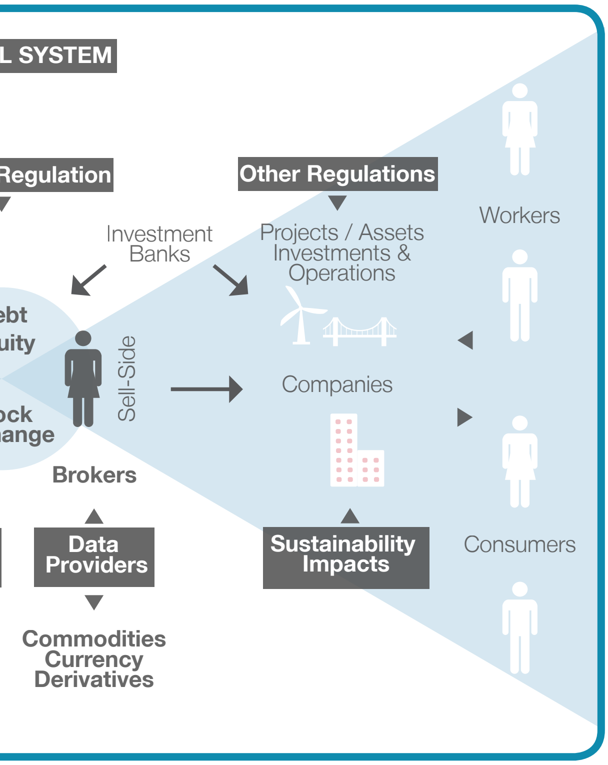


Source: Aviva Investors, European Political Strategy Centre

Asset managers should proactively engage with clients on the benefits of integrating environmental, social and governance (ESG) factors and develop comprehensive investment, engagement and voting strategies to deliver client preferences. They should use their influence to encourage companies to disclose sustainability information of better quality, including adopting the recommendations of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD), and hold them to account on the adoption of sustainable business models.

Credit rating agencies should continue to improve the integration of sustainability issues into their assessments of credit risk when material, and be transparent about the approach they take. Capacity building is needed within the sector to create more competition and widen the market for independent ESG ratings.

Regulators and policymakers have a duty to correct market failures, such as a tendency toward short termism, which cannot be solved by market participants. They should align incentives in financial services with the sustainability outcomes agreed by national governments, making sure they can manage and mitigate the long-term financial sustainability risks they are increasingly identifying. This includes supporting the recommendations of the TCFD.



Companies should disclose consistently and transparently on the alignment of their activities with internationally and nationally-agreed sustainability objectives, following international best practice where possible. On climate change, this would include following the recommendations of the TCFD. They should seek to engage with their investors, clients, customers and employees on sustainable values and integrate them into their practices.

Stock exchanges should encourage companies listing with them to disclose consistent, comparable and high-quality sustainability information, working with regulators and standard setters in instances where they cannot ask for this information directly. They should help promote sustainable financial products and educate companies, investors and individuals on the merits and advantages of sustainable finance.

Banks, both retail and investment, should embed sustainability throughout their business models, including (depending on the type of bank) by ensuring their own loans and investments are sustainable, asking their clients about their sustainability preferences, helping companies issue green bonds and other sustainable products, and delivering unbiased, long-term financial analysis and advice that integrates ESG factors.

KEY RECOMMENDATIONS

1. Build and disseminate a compelling evidence base, and empower people to act

For many, there is already compelling evidence that social and environmental issues can present material financial risks and opportunities, in addition to the moral imperative to act. According to recent research by HSBC, however, there are still significant numbers in the finance and business worlds who are not yet convinced that sustainable business can be good business. Although their Financing and Investing Survey pointed to many positive trends, HSBC's research showed that almost 40% of investors believe that sustainable investing sometimes involves accepting lower returns or higher risk, while only 42% of issuers see a potential financial gain from acting responsibly.[1] This is contrary to a growing body of academic research which suggests that embedding ESG can lead to outperformance. This implies that: a) gaps remain in the research undertaken to date; b) existing research is not being disseminated effectively; and/or c) the evidence base that does exist is not yet changing underlying beliefs.

There not only needs to be compelling evidence of the importance of integrating ESG into investment and business decisions – individuals from across the finance community need to be convinced and to want to act. Surveys increasingly show that, when asked the question, a significant proportion of people – of all ages, across the world – would like to put their savings and investments to better use and invest more responsibly. Furthermore, climate activism in 2019 has demonstrated powerful and growing peer influence of individuals, such as Greta Thunberg, mobilizing younger generations to challenge the status quo.

The case for action is growing but a concerted effort is still needed to dispel any remaining myths that ESG is a luxury rather than a necessity.

2. Set ambitious targets and embed them into strategy and decision making

Companies, investors and other organizations are increasingly recognizing the need to set ambitious targets to drive the transformation needed to tackle climate change and other significant ESG-related risks, and to align strategies, business models and finance with the achievement of these targets.

Tackling short termism and setting targets that will build long-term resilience is the smart decision for organizations seeking to create value that will endure. A key first step is to commit to a net zero emissions target.

3. Allocate funds to deliver sustainable outcomes

To support a rapid transition to a net zero carbon economy and to achieve the SDGs, there needs to be a significant increase in the volume of finance directed towards activities which will deliver these outcomes. This is likely to require both increased allocation of funds towards explicitly sustainable products, for example social or green bonds, as well as the integration of ESG considerations into all aspects of financing and investment decision making.

An additional US$4 trillion a year is needed between now and 2030 if we are to achieve the SDGs, but the benefits far outweigh the costs. We need to get money flowing in the direction of long-term value and reap the multiple benefits of a sustainable future.

1 Sustainable Financing and Investing Survey 2019, HSBC https://www.gbm.hsbc.com/insights/sustainable-financing/sustainable-financing-and-investing-survey-2019

4. Adopt global reporting standards and use consistent terminology

Without the information needed to provide insight into sustainability factors, users across all parts of the system cannot properly assess the performance or prospects of companies or funds. According to Morgan Stanley research, 70% of surveyed asset managers felt that the industry lacks standard metrics to measure nonfinancial performance of sustainable investments.[2] This hinders their ability to quantify impact. Some of the common issues faced by those seeking to incorporate a better understanding of sustainability risk and opportunity into investment decisions include: 1) a lack of common frameworks, standards and definitions leading to a lack of consistency, including in the labelling of products; 2) significant data gaps through failure to disclose, in particular where reporting is left to voluntary approaches rather than mandatory; and 3) a lack of enforcement of existing requirements. Joint action is required to close the information gap, a prerequisite for effective integration and alignment of sustainability and finance.

Action is starting to be taken, by regulators, standards setters and market participants, to drive convergence and adoption of global standards. All actors should come together to accelerate this process.

5. Price externalities to accelerate integration into decision making

Social and environmental risks are starting to have short-term financial impacts, however, the full consequences are only likely to impact over the longer term. Added to that, the costs will not necessarily fall on those with the greatest need to act. Finding ways to price in the risks faced is therefore vital to accelerate action. Some steps have been taken by regulators around the world to put a price on carbon. At the same time, companies and investors have started to embed a shadow price on carbon, water and other externalities in an attempt to 'future proof' decisions. Natural, social and human capital accounting also plays an important role in pricing the true cost of decisions, helping organizations to understand their impacts and dependencies.

Leaders are beginning to price externalities into decision making in order to future proof their organizations. This needs to become the norm.

2 Sustainable Signals: Growth and Opportunity in Asset Management, 2019, Morgan Stanley Institute for Sustainable Investing and Bloomberg L.P. https://www.morganstanley.com/assets/pdfs/2415532_Sustainable_Signals_Asset_Manager_2019_L.pdf

ACTORS

In 2015, the UN SDGs and the Paris Agreement set out an ambitious vision for the future. The economic and financial community have a central role to play in achieving this vision. Without sufficient financial flows, the majority of which will have to come from private sources, the world remains on course for a dangerously risky future. The current trajectory is creating significant financial risks for business and the finance sector, when many would in fact stand to benefit from the opportunities that a sustainable pathway offers.

Despite the opportunities and the risks, capital markets have been slow to respond, although there are clear signs that this is starting to change. To deliver the SDGs and the Paris Agreement, we must go beyond a niche of green or social finance: mainstream finance must be made sustainable.

To connect finance and sustainability, a wholesale rethinking of behavioural incentives for all actors who influence the flows of global capital in financial markets is required: from individual investors putting money in their pension funds to sovereign wealth funds investing billions, or legislators and regulators setting and enforcing the rules that govern the financial system.

A DECADE OF DELIVERY

It is estimated that achieving the SDGs will cost between US$5 trillion and US$7 trillion a year. Having found approximately US$3 trillion so far, the UN predicts that we need to find an additional US$2 trillion to US$4 trillion a year between now and 2030. While an objectively large figure, this amount constitutes just a small fraction of the US$87 trillion in gross world output, according to figures from the International Monetary Fund (IMF). There is also a significant upside. In studying four sectors – food and agriculture, cities, energy and materials, and health and wellbeing – WRI found that achieving the SDGs will create US$12 trillion of new market opportunities by 2030. They also predict the creation of 380 million new jobs by 2030, 90% of which are expected to be in developing countries.

With the fifth anniversary of both the Paris COP Agreement and the launch of the SDGs falling in 2020, we are entering a decade that needs to mark the turning point in global sustainability. Time is running out. We need transformational change of the finance system and each actor on the capital markets stage must play a role.

The following sections give example indicators of change and summarize the actions we are currently seeing within each constituency, as well as the barriers they face and our recommendations for action. We also reference a few examples of specific work that we and others are undertaking across the system.

INDIVIDUALS

The financial system exists to serve the needs of individual people. People invest their pensions and other savings via financial intermediaries. These intermediaries then put this money to work through loans and investments that make a real-world impact. In turn, people are employed by, and purchase products and services from, companies – and the actions of those companies impact the wider world in which people live.

However, few people feel that they understand how the financial system works or, therefore, the connection between their savings and the wider environment. Consequently, too often the role of the individual in the financial system is forgotten or disregarded by those who direct much of the flows of finance.

INDICATIONS OF CHANGE

2019 has seen a shift in the attitudes of individuals to the effect that the economy is having on the natural world. The increasingly evident impacts of climate change, publicity around the damage created by plastics in our oceans, and actions such as the Fridays for Future school strike movement, have made the sustainability of our economy a mainstream issue for the first time. The UK Government's Department for International Development conducted a survey[1] regarding investment to finance the SDGs. The results of the survey, published in September 2019, showed that 68% of UK savers want their investments to consider impact on people and the planet alongside financial performance. This aligns with research by Morgan Stanley in the US which found that 75% of individual investors surveyed were interested in sustainable investing, rising to 86% for millennials.[2] More work is needed to help people make the connection back to their own investments and actions.

EU rules for financial advisers and portfolio managers are being revised. They will include a mandatory requirement to ask clients if they have ESG preferences that they want reflected in the recommendations made as part of the "suitability" test. The new rules are expected to apply from early 2021.

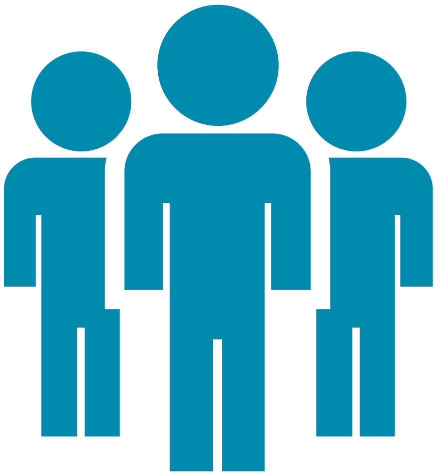
1 Investing in a Better World: Understanding the UK public's demand for opportunities to invest in the Sustainable Development Goals, 2019, Department for International Development https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/834207/Investing-in-a-better-wold-full-report.pdf

2 Sustainable Signals Whitepaper, 2018, Morgan Stanley https://www.morganstanley.com/pub/content/dam/msdotcom/ideas/sustain¬able-signals/pdf/Sustainable_Signals_Whitepaper.pdf

RECOMMENDATIONS

Many of the recommendations for the financial system actors in the sections that follow focus on empowering individuals to understand their role in the financial system, so as to express more fully their preferences about how investments are made on their behalf to influence the wider world around them.

The financial advisory community have a particularly important role to play to help individuals understand the impacts of their investment choices, ESG risks and opportunities, and the options available to them.



MAKE MY MONEY MATTER

In September 2019 at the UN General Assembly, Richard Curtis, film maker and one of the Secretary General's Advocates for the Sustainable Development Goals, announced the formation of a new coalition and a public campaign called Make My Money Matter. The campaign has been formed to channel the additional funds needed to deliver on the SDGs focused specifically on individuals and their pension funds. Based on the campaign's early analysis, they found that many people don't realize that their money, especially their pension fund money, is invested – let alone often in an unsustainable way.

The coalition behind the Make My Money Matter campaign intend to mobilize public awareness and support for sustainable investing, in particular, motivating individuals to demand that their pension be sustainably invested.

WORLD BENCHMARKING ALLIANCE

Following its launch in September 2018, the World Benchmarking Alliance (WBA) is undertaking work to rank the 3000 global companies with the greatest impact on achievement of the SDGs. Over the course of the next three years, the WBA will produce a series of indices enabling investors and other stakeholders to align their decisions with delivery of the SDGs. The first index of seafood companies was released in October 2019, and the second, focused on automotives, was released in December.

ASSET OWNERS

Asset owners are both highly exposed to the risks of an unsustainable future and in a strong position to influence a more sustainable outcome.

INDICATIONS OF CHANGE

It is becoming more and more accepted that ESG factors can have a material impact on investments, and regulators are beginning to act. The EU's Action Plan for Financing Sustainable Growth includes proposals for changes to "fiduciary" (or "investor") duties of asset owners and asset managers, as well as enhanced disclosures of the sustainability characteristics of firms and their products. In 2019, the International Organization of Pensions Supervisors issued guidelines for regulators on the integration of sustainability factors into the investment and risk management of pension funds, stating that to do so is in line with fiduciary duties. The UK Government has set out an expectation that TCFD disclosures will be mandatory for large asset owners, as well as listed companies, from 2022. And last year, the Australian Council of Superannuation Investors launched Australia's first Stewardship Code for asset owners, setting out six principles for signatories to commit to on an 'if not, why not?' basis, underlining asset owners' responsibility for promoting sustainable value creation.

CURRENT ACTIONS

1. Investors are increasingly signing up to global initiatives (such as Climate Action 100+) to promote sustainability within their investee companies.
2. Asset owners are more routinely assessing sustainability risks, opportunities and potential impacts on their portfolios, and adjusting investments accordingly.
3. The UN convened "Net Zero Asset Owners' Alliance", with members representing almost US$4 trillion (as at December 2019), have committed to transitioning their investment portfolios to net zero greenhouse gas emissions by 2050, consistent with limiting global temperature increase to 1.5 degrees celsius.
4. Some are introducing low-carbon or SDG funds and are committing a percentage of portfolio allocation to investments with positive social and environmental impacts.
5. Some pension funds have sought to embed ESG risk into their defined contribution default fund.
6. Asset owners are taking steps to influence others, for example, building sustainability into investment mandates, engaging with the sponsor, and engaging directly with companies, for example at Annual General Meetings.

A4S ASSET OWNERS NETWORK – 10 ACTION AREAS

The A4S Asset Owners Network brings together just under forty chairs of pension funds, their pooling partners, investment committees and endowments to explore the relevance of material ESG risks and opportunities with peers. The Network has identified ten action areas, summarized below, on which individual members are either wholly or selectively focused to help to deliver a sustainable financial system capable of supporting achievement of the SDGs and the Paris Agreement.

Allocating funds to deliver sustainable outcomes

1. Making Defined Contribution pension scheme default funds sustainable
2. Assigning a percentage of Defined Benefit pension scheme assets to sustainable investments
3. Integrating ESG considerations into wider investment decision making
4. Moving beyond equities to identify opportunities for climate and ESG risk management through debt, real estate and infrastructure investments

Influencing others

5. Engaging with pension scheme beneficiaries
6. Engaging with pension scheme sponsors
7. Engaging with investment consultants and asset managers
8. Engaging with companies in which pension schemes are invested at Annual General Meetings
9. Signing up to the Transition Pathway Initiative (TPI)

Adopting global reporting frameworks

10. Implementing the TCFD recommendations

BARRIERS

1. Fiduciary duties are still poorly understood and the belief that social and environmental issues can be financial in nature is not consistently held.
2. Information about ESG risk and performance of assets is not readily available and what exists may be of a poor quality.
3. Beneficiaries' sustainability preferences are seldom collected or reflected in the investment mandates asset owners give to asset managers, and beneficiaries frequently may not have the confidence or expertise to express those preferences.
4. There are regulatory disincentives to long-term sustainable investments for insurers.
5. There is insufficient transparency in the investment chain for asset owners to have confidence that their mandates have been reflected in votes cast.

RECOMMENDATIONS

1. **Upskill board members and management** with the necessary sustainability competencies and embed ESG considerations into governance, staff recruitment, training, remuneration, and board discussions.
2. **Build ESG requirements and performance metrics into the instructions given to investment consultants and the mandates given to asset managers**, and ask tough questions.
3. **Engage with beneficiaries**, who increasingly want to know where their money is being invested.
4. **Create an ESG decision-making framework** through which to govern and justify all investment decisions.
5. **Evaluate and reallocate investment portfolios** across all asset classes (fixed income, equity, etc) towards investments in climate solutions and away from those with high carbon exposure, in particular for default funds.
6. **Allocate a percentage of funds** to products specifically targeting sustainable outcomes.
7. **Implement the TCFD recommendations**. Integrate climate change into governance, strategy, risk and metrics. Ask investees to evaluate and disclose their exposure to – and strategies for managing – their climate-related financial risk.
8. **Call for the adoption of global sustainability reporting standards**, mandating asset managers to use voting, engagement and investment powers to influence corporate behaviour.
9. **Work actively with other stakeholders** to call for sustainable finance regulation at the national, regional and international level.

MAKING THE DEFAULT SUSTAINABLE

Assets held in passive funds by pension schemes will grow by around six per cent a year over the rest of this decade according to a survey by Create Research. Even when funds are actively invested and managed, they are extremely unlikely to be aligned with the outcomes agreed in the Paris Agreement.

The default fund is where 95% of workers leave their money and it is in the interest of both the pensions industry, and its beneficiaries, for default funds to be properly screened for climate risk and for pension funds to take full advantage of the emerging opportunities presented by low carbon transition. With Willis Towers Watson estimating that the top 300 pension funds worldwide represent US$18.1 trillion in assets under management, an industry-wide shift towards greener options would represent a significant step on the pathway to zero carbon.

A4S's Asset Owners Network has been working with this theme over the course of 2019, sharing best practice examples, experience and challenges where schemes have been working to make their default fund the sustainable option. Some fund providers have launched sustainable default options, such as Aviva's "Silver" default, which integrates ESG considerations, and its ethically screened "Stewardship" default.

ASSET MANAGERS

With the size of the global asset and wealth management industry expected to grow to US$145.4 trillion by 2025, asset managers have significant influence over how capital is directed.

INDICATIONS OF CHANGE

In 2018, at a World Bank coordinated Investor Forum in the lead up to the G20 summit in Buenos Aires, managers of over US$20 trillion, together with heads of state, finance ministers and leaders of global development organizations, issued a "Call to Action", building on the 2018 Financing our Future report which included that regulators should clarify that integration of ESG into investment processes is consistent with fiduciary duties.

Based on current European Commission proposals, asset managers, in common with other financial market participants, will have to disclose and report upon how they integrate sustainability risks into their investment processes and risk management. The European Commission is also proposing complementary amendments to key regulation to make integration of ESG a requirement. The development of an EU taxonomy for sustainable investments aims to promote consistency of terminology and assessment of investments, to support these initiatives. Changes to the Shareholder Rights Directive will mean that within the UK and EU, asset owners and their asset managers will need to disclose and report annually on their stewardship activities, and how their remuneration policies are consistent with a long-term investment approach for equities.

CURRENT ACTIONS

1. Using engagement with companies and voting to encourage more sustainable practices and disclosures.
2. Increasing evidence of integrating sustainability criteria into investment decisions as business as usual.
3. Undertaking thought leadership and engagement to reform markets.
4. Creating investment products and services specifically aimed at helping clients to avoid ESG risks and/or have a positive ESG impact through their investments.

BARRIERS

1. A lack of clear mandates from clients.
2. Fiduciary duties do not always explicitly reference the need to account for ESG issues, although this is beginning to change.
3. Leadership from the top doesn't always translate into action by individual fund managers.
4. A lack of comparable, consistent and timely corporate disclosure on ESG risk and opportunity.
5. A lack of transparency and accountability over voting and engagement on ESG issues.
6. An increasing shift towards passive investing, without effective integration of ESG.
7. Incentives to focus on the short term.
8. No commonly agreed ESG index, standard or approach on which to base responsible investment product ranges; impact and quality can vary considerably.

RECOMMENDATIONS

1. **Ensure that client preferences are captured and acted upon**. Make the inquiry about clients' sustainability preferences a standard part of getting to know the client. Inform and advise clients on long-term systemic threats and opportunities, including ESG issues, as well as those relating to overall economic development, financial market quality and stability.
2. **Upskill boards**. Ensure that boards have the required knowledge of sustainability and ESG issues.
3. **Develop technical knowledge of ESG**. Develop internal competence on matters related to sustainability so as to exercise stewardship in an effective manner. Integrate long-term sustainability considerations into risk modelling and investment strategies, starting with the application of the TCFD guidelines.
4. **Embed sustainability across all products, including passive funds, and incorporate performance updates into fund reporting**. Ensure that there is a sufficient level of senior oversight and accountability in relation to integration of ESG.
5. **Analyse climate risk exposure of all funds**, both in terms of the physical risks and transition risks, for example undertaking a carbon pathway analysis to compare whether the emissions from portfolio holdings are aligned with 1.5°C, and reporting on the results in terms of 'level of warming' by fund or asset class.
6. **Have transparent engagement and voting practices**. Update and publish voting policies to reflect ESG considerations and long-term sustainability risks and opportunities. This should include a commitment to engage investee companies and demand from them transparent reporting of relevant and material sustainability factors in relation to their business strategy, operations and risk, including the most significant parts of their supply chain. Disclose proxy votes publicly and report back to clients on the specifics and impact of the engagement that has been undertaken on their behalf.
7. **Work with other investors to engage effectively with companies and drive action on climate change**, for example through groups such as Climate Action 100+.

CLIMATE ACTION 100+

CA100+ is an investor initiative to ensure the world's largest corporate greenhouse gas emitters take necessary action on climate change. The companies include 100 'systemically important emitters', accounting for two-thirds of annual global industrial emissions, alongside more than 60 others with significant opportunity to drive the clean energy transition.

Launched in December 2017 at the One Planet Summit, to date, more than 370 investors with more than US$35 trillion in assets under management have signed on to the initiative. In September 2019, Climate Action 100+ released a progress report that showed more investors are mobilizing across dozens of countries to drive corporate action on climate change and that the target engagement is starting to have results. Companies on the initiative's focus list have started to make progress towards its goals, including a trebling in support for the recommendations of the TCFD and taking action such as setting reduction targets and aligning with executive remuneration.

INVESTMENT CONSULTANTS

In their role advising pension funds and other asset owners, investment consultants influence the allocation of trillions of dollars of assets.

INDICATIONS OF CHANGE

The Association of Member Nominated Trustees (AMNT) and UK Sustainable Investment and Finance Association (UKSIF) have secured a public commitment from 16 investment consultants to bring the UK Pension Regulator's ESG guidance to their client base. In July 2018, AMNT and UKSIF wrote to the 16 investment consultants asking for details on how they had sought to meet their commitments. 15 replied and key findings released in December 2018 were that:

- Consultants are at a different stage in their journey with respect to their ESG advice. Some of the larger consultants have been in ESG for many years and thus have had more time to develop a more sophisticated approach.
- Over 80% indicated that some type of training programme on ESG was provided to their clients. However, overall, there was a general lack of any indication that this training had led to any change in the advice demanded by asset owners of their consultants.
- A few investment consultants noted the inclusion of ESG within board meeting packs or as agenda items and some noted the creation (or pre-existence) of some type of internal governance committee.
- Many responses focused on one-off or ad-hoc external publications dedicated to ESG issues.
- A few investment consultants had integrated ESG issues into their strategic planning and their staff performance evaluation processes and approximately 75% had either created new ESG training programmes for their employees or were updating their existing training programmes on ESG issues.
- Very few consultants provided numbers to substantiate the scale and impact of their responsible investment efforts.

CURRENT ACTIONS

1. Membership of global industry groups to promote action.
2. Thought leadership on ESG topics across different asset classes and portfolios as a whole.
3. Advice provided to clients to assist them in steering assets in a more sustainable direction.
4. New advisory propositions for clients (eg by integrating ESG metrics into liability-driven investment models).

BARRIERS

1. There is currently no regulatory requirement for investment consultants to incorporate sustainability issues in advice and many are still not considering ESG issues as part of "business as usual".
2. Limited explicit demand from asset owners for investment consultants to integrate sustainability issues into their advice.
3. A lack of availability of comparable, high-quality, long-term data on sustainability performance of individual assets and asset managers.
4. Fee structures can disincentivize integration of ESG into advice.
5. ESG knowledge and understanding is still not mainstream.

RECOMMENDATIONS

1. **Embed into interactions with asset owners**. Proactively ask asset owners if they have ESG preferences as part of the standard service. Share analysis with asset owners demonstrating that ESG integration can improve performance.
2. **Embed into interactions with asset managers**. Proactively assess prospective asset managers' ESG credentials as part of selection/recommendation process, including in relation to the management of climate risk.
3. **Build internal knowledge and incentivize integration**. Integrate ESG into the recruitment criteria for new hires, and incorporate into mandatory training for existing team members to build internal capacity. Ensure all consultants are well informed about recent developments in the ESG space, for example the work of TCFD.
4. **Adopt leading practice in relation to role as fiduciary managers**. Support the establishment of a finance product standard to provide clear signalling to institutional and retail investors. Expand the evidence base and literature around ESG challenges and opportunities of new and different asset classes.
5. **Show leadership**. Join industry groups to learn about and contribute to ESG integration.

BANKS

Banks' triple role of adviser, facilitator, and market player makes them critical in aligning finance with sustainability. Their sheer size also means that decisions made have significant impact on outcomes achieved.

INDICATIONS OF CHANGE

The UN Principles for Responsible Banking were launched by 130 banks from 49 countries, representing more than US$47 trillion in assets, on 22 and 23 September 2019, during the annual UN General Assembly. More than 45 CEOs together with the UN Secretary General attended the launch ceremony. Signatories have committed to a set of six principles including alignment of the business strategy with the SDGs, setting and publishing targets, engaging with clients and customers, consulting stakeholders, embedding in governance and culture, and being transparent about progress made.

The Climate Bonds Initiative is showing year-on-year growth in the green bonds market from US$171bn in 2018 to an estimated US$250bn in 2019, highlighting the continued rapid growth in sustainable products, albeit from a low base.

In relation to sell-side research at investment banks, research commissioned from EXTEL by Aviva Investors found that mainstream analysts spend nearly 90% of their time focused on a time horizon of 12 months or less, when many sustainability risks are material over a much longer period. Regulators, including the EU, are focused on steps to address this issue.

CURRENT ACTIONS

1. Conducting their own research into the connection between sustainability issues and finance.
2. Incorporating sustainability risks and opportunities into their analysis of loan portfolios and stress testing.
3. Incorporating sustainability risks and opportunities into banks' own lending and broader practices and facilitating financing towards sustainable investments and away from unsustainable investments.

BARRIERS

1. Sell-side research has a short-term focus and analysts often face conflicts of interest.
2. Lack of comprehensive, robust, comparable data on corporate sustainability performance.
3. The impact of sustainable investments is not always tracked.
4. Market failures prevent a proper reflection of sustainability risks in decision making.

RECOMMENDATIONS

1. **Build ESG into governance**. Establish clear policies that will direct capital towards sustainable outcomes covering both corporate and other forms of lending – making it clear when targets relate to a bank's own lending. Allocate board-level responsibility, upskilling board members as needed.
2. **Engage with clients to encourage action on ESG**. Proactively ask about both retail and corporate clients' ESG preferences. Engage with customers, and in particular smaller companies, to support them to move towards more sustainable business models. Ensure that the capital markets team provides advice to companies that reflects a need to integrate ESG risks, including within marketing materials, and engage investors on the need for ESG risks to be included.
3. **Develop products and support their rapid adoption**. Identify opportunities that help accelerate flows of finance towards sustainable outcomes and away from unsustainable ones.
4. **Properly assess and price ESG risk**. Ensure the bank's and its clients' material exposure to sustainability risks and opportunity is properly assessed and disclosed, including the use of scenario analysis and stress testing. Consider mechanisms to set a differentiated pricing structure to reflect risks associated with ESG. Set loan covenants relating to sustainability performance. Consider challenging house brokers to integrate ESG into their own ratings. Make ESG a formal part of all term sheets.
5. **Build the evidence base**. Increase long-term research and analysis. In conjunction with academia and policymakers, assess the extent to which commonly used valuation metrics, for example discounted cash flow, incentivize unsustainable investments, and develop and utilize alternative metrics.

UK BANKING SECTOR

In 2019, the Bank of England surveyed UK banks and found that almost three-quarters are beginning to treat climate risk in a similar way to any other financial risk. They found that banks have started to assess both transition and physical risks and analyse the resulting exposures. This includes exposure to carbon-intensive sectors, consumer loans for diesel vehicles, and mortgages for rental properties, given new energy efficiency requirements. In relation to physical risks, examples include exposure of their mortgage book to flood risk and of sovereign debt to extreme weather events.

The Bank of England has also set out changes to the supervisory regime in the following areas:

- **Governance**: Firms will be expected to embed the consideration of climate risks fully into governance frameworks, including at board level, and assign responsibility for oversight of these risks to specific senior managers.
- **Risk management**: Firms will be required to consider climate change in accordance with their board-approved risk appetite.
- **Regular use of scenario analysis**: Firms will be required to use scenario analysis to test resilience.
- **Disclosure of climate risks**: Firms will be expected to develop and maintain methods to evaluate and disclose climate risks.

CREDIT RATING AGENCIES

Credit rating agencies play a central role in determining the cost of debt. The integration of ESG into ratings processes therefore is a major influence on corporate behaviour and on investment allocation.

INDICATIONS OF CHANGE

The three largest credit rating agencies have all now taken steps to embed ESG into the rating process or provide a separate ESG rating for debt. There has also been an increase in transparency to show how ESG is taken into account. In May 2019, the European Securities and Markets Authority issued guidance for credit ratings that called for greater transparency around whether ESG factors were a key driver of the credit rating given.

CURRENT ACTIONS

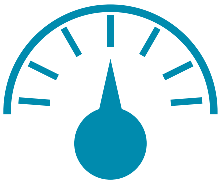
1. Integrating ESG factors into ratings.
2. Providing information (distinct from standard credit ratings) on ESG performance.

BARRIERS

1. Short-term time horizon over which risk is assessed.
2. The way ESG issues are considered in credit rating is unclear to market participants.
3. Credit Rating Agency regulation has yet to be updated to reflect sustainability considerations.
4. Lack of consistency in the way different credit rating agencies incorporate and weight different ESG data points into a final rating.

RECOMMENDATIONS

1. **Continue to increase transparency**. Disclose whether and how ESG issues are being considered in existing credit rating methodologies, governance and disclosure. Disclose whether and how new disclosure data (for example TCFD) are considered in credit ratings.
2. **Take a longer-term view**. Extend the time horizon of the credit risk analysis to reflect better the investment time horizon of the underlying assets and the time horizon of investors. Consider ways to signal the time horizon implicit in the analysis undertaken.
3. **Influence issuers**. Systematically demand increased and better ESG risk disclosure from issuers, highlighting where a lack of substantive ESG data has prevented comprehensive consideration in the ratings process.
4. **Define fair commercial offerings**. Work with users of ESG ratings and assessments so that the integration of ESG considerations does not negatively impact performance and promotes greater integration of ESG factors into investment decision making.
5. **Work with regulators** to establish greater consistency and transparency in ratings and assessment methodologies, adopting common terminology and utilizing publicly available information.



STOCK EXCHANGES AND SECURITIES REGULATORS

"Securities regulators have a responsibility to ensure that risks are appropriately evaluated, which includes climate… A framework needs to be adopted, disclosure needs to be made, and we don't have forever for this to happen." – Mary Schapiro, 29th Chair of the US Securities and Exchange Commission

INDICATIONS OF CHANGE

In October 2018, the World Federation of Exchanges (WFE) released the WFE Sustainability Principles, a formal declaration by the WFE and its membership to take on a leadership role in promoting the sustainable finance agenda. As the introduction states, "WFE member exchanges hereby acknowledge their role in fostering and promoting the development of a sustainable financial system, making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development, and promoting the transition towards an inclusive, and sustainable economy. They recognize the importance of integrating the long-term perspective into financial markets to reduce socio-economic and physical risks, and to contribute to enhanced financial stability." Since the establishment of the principles, WFE has worked with the UN Sustainable Stock Exchange initiative to release additional guidance supporting implementation of the principles.

Action is also being taken by international securities regulators, with the International Organization of Securities Commissions (IOSCO) launching a Sustainable Finance Network and releasing a statement on disclosure.

In Europe, the European Commission has issued, through their Technical Expert Group on Sustainable Finance, a proposed methodology for Paris-aligned and low-carbon benchmarks, to ensure consistency and comparability of index calculation. They will also require all administrators of substantial equity and credit benchmarks to publish the implicit degrees of warming for the benchmark from 2021.

CURRENT ACTIONS

1. Developing and promoting green products, services and indices, facilitated through the acquisition of ESG data, analysis and expertise.
2. Encouraging better quality disclosure.
3. Creating sustainable finance platforms and forums such as the IMF's international platform on sustainable finance which aims to scale up mobilization, strengthen international cooperation and coordinate taxonomies, disclosures, standards and labels.

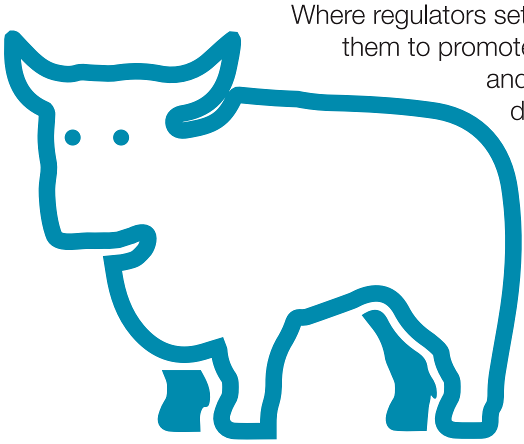
BARRIERS

1. There are challenges to establishing global regulatory requirements that are consistent but take local differences into account.
2. The quality and impact of sustainable finance product offerings vary.
3. Competition between individual exchanges can hamper the adoption of ESG standards.

RECOMMENDATIONS

For stock exchanges:

1. **Mainstream ESG risk into conventional indices**. Incorporate ESG factors into mainstream indices, making them sustainable by default.
2. **Widely promote sustainable indices**. Develop segments to promote sustainable finance investment and ensure that sustainable products listed are promoted and easily found, using globally consistent definitions and terminology.
3. **Engage with companies on sustainable finance**. Provide guidance to listed companies on sustainability disclosure requirements, starting with the TCFD recommendations.
4. **Use influence**. Where there is stock exchange control over listing requirements, use this to ensure that sustainability disclosure is mandatory, explicit, regularly updated and regularly enforced. Where regulators set requirements, engage with them to promote integration of sustainability, and adopt international standards as the default approach.



For securities regulators:

1. **Develop a sustainable finance strategy**. Build on the work being done through IOSCO's Sustainable Finance Network.
2. **Endorse the TCFD**. Support the global, mandatory adoption of the TCFD recommendations to accelerate uptake, at a speed propotionate to the scale of the climate crisis and urgency of action needed in response.
3. **Adopt global reporting standards**. Building on IOSCO's work, consider the formation of a grouping of those securities regulators who either have or are planning to mandate improved disclosures to work together to improve comparability and consistency of information on a global basis, for example, acting in concert to facilitate adoption of a single global reporting standard.
4. **Form a sustainable finance committee**, charged with informing IOSCO on how it can: 1) embed sustainability considerations throughout its work; 2) support IOSCO in its efforts to provide the necessary guidance and standards to its members when it comes to sustainability disclosure; and 3) support work to update IOSCO's Strategic Framework for Investor Education and Financial Literacy to take account of sustainable finance issues.

IOSCO SUSTAINABLE FINANCE NETWORK

In January 2019, the International Organization of Securities Commissions (IOSCO) announced the creation of its Sustainable Finance Network and released a statement on disclosure, emphasizing that "ESG matters, though sometimes characterized as non-financial, may have a material short-term and long-term impact on the business operations of the issuers as well as on risks and returns for investors and their investment and voting decisions."

Ashley Alder, Chairman of the IOSCO Board said in a statement to the SSE, "IOSCO is monitoring developments in this area closely, given the growing importance of ESG matters to investors, and the continuing need to enhance transparency in the capital markets. IOSCO's statement reminds issuers of their obligations to consider the disclosure (voluntary or otherwise) of the potential impact on their businesses of ESG-related risks and opportunities when these are material. IOSCO established its Sustainable Finance Network, under the leadership of Erik Thedéen of Finansinspektionen of Sweden, to enable IOSCO members to share their experiences and monitor ESG developments."

On 19th June 2019 in Stockholm, IOSCO held its first Sustainable Finance Network Stakeholder Meeting as an interchange between securities regulators, standard-setting bodies and the market on sustainable finance.

EU TAXONOMY

In committing to the SDGs and climate-related goals through the Paris Agreement, the EU and its Member States endorsed a direction for sustainable growth. These goals provide signals to corporations and investors about future economic trends, investment opportunities and risks, but it is only the alignment of public policies to the goals that will encourage capital markets to re-orient capital flows.

Through financing or investments and through the stewardship of investments, investors will influence the decisions taken by corporations and other entities. This chain of influence requires translation of policy goals into frameworks that the investors and managers of capital can respond to. The EU Taxonomy is one example of such a framework: a list of economic activities assessed and classified based on their contribution to EU sustainability-related policy objectives.

The EU Taxonomy will be a disclosure-based implementation tool that can enable capital markets to identify and respond to investment opportunities that contribute to environmental policy objectives. Decisions by investors to allocate capital or influence company activities based on these objectives has the potential to make a substantial contribution to climate goals and to the related SDGs.

A4S CFO Leadership Network and Salesforce ring the NYSE opening bell during Climate Action Week NYC September 2019

COMPANIES

"Your company's strategy must articulate a path to achieve financial performance. To sustain that performance, however, you must also understand the societal impact of your business as well as the ways that broad, structural trends – from slow wage growth to rising automation to climate change – affect your potential for growth." Laurence D. Fink, Chairman and CEO, BlackRock

INDICATIONS OF CHANGE

A growing number of companies from around the world are adopting leadership positions to tackle climate change and to support achievement of the SDGs. In August 2019, the Business Roundtable released a Statement on the Purpose of a Corporation signed by 181 CEOs who commit to lead their companies for the benefit of all stakeholders – customers, employees, suppliers, communities and shareholders. In September 2019, companies with a market capital of US$2.3 trillion pledged to set targets aligned with 1.5 degrees, a number which is set to grow over the coming year. Nearly 900 organizations now publicly support the TCFD recommendations and research from the Governance and Accountability Institute indicates that 60% of Russell 1000 and 86% of S&P 500 Index companies were publishing sustainability reports in 2018. There is still, however, a long way to go before these actions become the norm.

CURRENT ACTIONS

1. Collaborating with others to promote sustainable markets.
2. Committing to net zero emissions targets and embedding into strategy and decision making.
3. Adopting global reporting frameworks and accounting standards, for example, the TCFD.
4. Developing and adopting sustainable finance frameworks to align investment plans and budgets with sustainable outcomes.
5. Engaging with the capital markets to highlight the importance of sustainable business, including as part of investor roadshows, capital raising activities and by engaging with their own corporate pension schemes.

BARRIERS

1. Corporate boards and teams lack knowledge and understanding of ESG issues.
2. Challenges remain for companies to know how to integrate the SDGs into strategy and decision making.
3. There are mixed demand signals from lenders and investors. For example, the market expectation of quarterly reporting drives short termism.
4. There is often a focus on reporting metrics rather than also focusing on how underlying strategy, business model and management quality can deliver sustainable outcomes.
5. There is a lack of transparency in sustainability ratings.
6. Companies are faced with an increased fragmentation in reporting requests and requirements, despite the widespread adoption of a small number of recognized global frameworks.
7. The understanding of how to measure impacts and dependencies across natural, social and human capital is still developing.
8. Policies, incentives and subsidies can conflict with achievement of sustainable outcomes.

RECOMMENDATIONS

1. **Assess the sustainability of your business model**. Use scenario analysis, such as that recommended by the TCFD, to assess your current business model. Identify opportunities to rethink your purpose and align with delivery of the SDGs.
2. **Set ambitious targets and align strategy and decision-making processes with their achievement**. Set an 'integrated' strategy with sustainability at its heart. Adopt a net zero emissions, science-based target consistent with 1.5 degrees. Use resources such as the A4S Essential Guide series to embed into strategy, management and decision making.
3. **Embed sustainability into your governance arrangements**. Integrate ESG into the recruitment criteria for new directors, and incorporate into mandatory training for board members to build internal capacity.
4. **Align remuneration and performance management with the achievement of your sustainable strategy**. Consider in house training for investor relations and treasury teams to meet changing skills requirements, and work with key industry providers to integrate within core modules of professional qualifications.

5. **Engage with others, including the capital markets, to drive change**. Ensure investors and debt providers have sufficient and appropriate access to material sustainability information, incorporating into roadshows, presentations and issuance documents. Include ESG criteria as part of the selection process for banking and other financing or procurement relationships. Examine how to encourage integration of sustainability within corporate pension scheme arrangements.

6. **Adopt recognized, global standards for reporting to investors and other stakeholders, and support the call to achieve global adoption**. Adopt best practice sustainability disclosure guidelines, including the TCFD recommendations. Participate in benchmarking efforts that will help them put their performance in perspective and understand better where improvements can be made. Consider how to contribute to achievement of the SDGs and extend reporting to cover impacts and dependencies.

THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES

In June 2017, the TCFD released its final recommendations (2017 report), which provide a framework for companies and other organizations to develop more effective climate-related financial disclosures through their existing reporting processes.
Support for the TCFD has grown to 898 organizations as of September 2019.

In its 2019 update the TCFD identified the following four key takeaways:

- Disclosure of climate-related financial information has increased since 2016, but is still insufficient for investors.
- More clarity is needed on the potential financial impact of climate-related issues on companies.
- Of companies using scenarios, the majority do not disclose information on the resilience of their strategies.
- Mainstreaming climate-related issues requires the involvement of multiple functions.
- There is now significant support for increasingly mandatory disclosure.

In November 2017, CFOs from the A4S CFO Leadership Network and wider global community signed an A4S Statement of Support for the TCFD recommendations. Two years on, there are 43 signatories from across the globe with total assets of over US$2.1 trillion, and growing. A4S is working with these organizations to support implementation, and found the following from a recent survey:

- **58%** of organizations have committed to adopting the TCFD recommendations in full by a set date between 2020 to 2022
- **100%** of CFOs are involved in assessing and managing climate-related risks and opportunities for their organization
- **75%** are assessing the financial impact and **92%** are reflecting the impact in the organization's businesses, strategy and/or financial planning
- Scenario analysis remains one of the most challenging areas to implement

REGULATORS

"The good news is that governments are now establishing the policy frameworks, and the private sector is beginning to allocate capital accordingly. Our efforts (as central banks and supervisors) will help smooth the transition prompted by these actions." – Mark Carney, Governor, Bank of England

INDICATIONS OF CHANGE

The European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority issued technical advice to the European Commission in 2019 that set out how sustainability risks might be incorporated into firms' risk management, as well as investment decision making. The UK Prudential Regulation Authority set up a number of climate risk working groups, utilizing industry expertise and the Bank of England's "climate hub" to develop practical recommendations. In 2019 the UK's Department of Work and Pensions introduced mandatory inclusion of ESG statements in Statements of Investment Principles.

As highlighted in the section of this report on individuals, the European Commission is proposing changes to financial advice and distribution to require clients' sustainability preferences to be taken into account as part of financial advice and portfolio management, expected to take effect from 2021.

In Australia, the Australian Accounting Standards Board (AASB) and Auditing and Assurance Standards Board (AUASB) issued a joint statement underlining the expectation that climate risk should be considered when preparing and auditing financial statements.

CURRENT ACTIONS

1. Regulators are beginning to show thought leadership.
2. They are promoting disclosure of sustainability risks by companies and providing guidance on the need to include ESG factors in fiduciary duty.
3. There is a significant international collaboration across the regulator community.
4. Regulatory tools are being used to drive change.

BARRIERS

1. Regulators' mandates limit the role they can sometimes play.
2. Funding and expertise are lacking.
3. Perception that using regulatory tools to manage sustainability risks could distort financial markets.

RECOMMENDATIONS

How policy makers need to support regulators:

- Give regulators a clear and explicit mandate to incorporate relevant sustainability issues into their preservation of financial stability, and provide them with adequate funding and expertise to do this effectively.
- Ensure financial regulators have the expertise to enforce this regulation appropriately.

How policy makers and regulators can mobilize other constituents:

Individuals:
- Governments should work with multilateral institutions, industry, educational and consumer groups to design and deliver ambitious financial literacy programmes delivered in secondary, tertiary and professional education.

Asset owners:
- Clarify in relevant legislation/regulation and guidelines that the duty of pension funds includes a duty to incorporate material ESG issues into how pensions are invested, and to consult end beneficiaries on their preferences.
- Ensure pension funds and insurers are disclosing granular, comparable, consistent data on the ESG performance of their assets.
- Ensure the prudential framework for insurers adequately incorporates climate risks, including in capital requirement differentiation.

Asset managers:
- Make it explicit that the consideration, evaluation, and disclosure of long-term sustainability risks and opportunities are an integral part of an asset manager's fiduciary duty to its clients.
- Establish an equivalent of France's Article 173, or the EU's Regulations for Sustainability-Related Disclosure by Financial Market Participants. These regulations create an obligation for asset managers to disclose how sustainability is taken into account in their investment strategies and product offerings, and report on the resulting performance.
- Require the boards of asset managers develop competence on sustainability and governance issues, as well as establish organizational principles and reward structures that encourage long-term oriented behaviour.

Investment consultants:

- Incentivize investment consultants to integrate ESG in their processes as set out above, including proactively raising ESG issues with clients.
- Clarify that fiduciary duty for asset managers includes ESG issues.

Banks:

- Ensure the prudential framework for banks effectively incorporates long-term sustainability risks to financial stability such as climate change.
- Ensure that banks track, assess and disclose their alignment with sustainability objectives, starting with climate change. Support the adoption and implementation of the TCFD guidelines, including the use of scenarios and stress tests.
- Consider ways to encourage long-term ESG research under research payments and direct fund managers to raise this issue proactively with their clients.
- Explore the establishment of a requirement for all sell-side company research to include a section that looks beyond 12 months and to include a specific ESG performance analysis section.
- Put in place appropriate regimes in relation to the expected expertise and the advice provided by banks and independent financial advisors to retail clients.

Credit rating agencies and other rating providers:

- Provide regulation and guidance for credit rating agencies to integrate material sustainability risks and opportunities within ratings.
- Develop and require adoption of globally consistent definitions and terminology to enable users to have clarity on products.

Stock exchanges:

- Ensure that sustainability disclosure is mandatory, explicit, regularly updated and regularly enforced through mechanisms such as the TCFD framework.

Companies:

- Implement mandatory reporting in relation to sustainability disclosures, adopting common global sustainability accounting standards to enable robust, comparable information to be available to investors, and embedding reporting frameworks such as the TCFD recommendations into financial reporting regimes.
- Promote improved corporate sustainability performance by making alignment to the SDGs a precondition to accessing public procurement tenders.

NETWORK FOR GREENING THE FINANCIAL SYSTEM

At the Paris “One Planet Summit” in December 2017, eight central banks and supervisors established the Network of Central Banks and Supervisors for Greening the Financial System (NGFS). Since then, the membership of the Network has grown dramatically and, as of November 28th 2019, the NGFS consisted of 51 members and 12 observers. Members represent jurisdictions which account for more than half of global emissions.

The Network’s purpose is to help strengthen the global response required to meet the goals of the Paris Agreement and to enhance the role of the financial system to manage risks and to mobilize capital for green and low-carbon investments in the broader context of environmentally sustainable development. To this end, the Network defines and promotes best practices to be implemented within and outside of the membership of the NGFS and conducts or commissions analytical work on green finance. Three workstreams have been agreed as follows:

1. **Microprudential and supervision**, structured around the following three main topics:
   - Mapping current supervisory practices
   - Encouraging climate-related risks disclosure
   - Considering the extent to which a financial risk differential exists between ‘green’ and ‘brown’ assets

2. **Macrofinancial**, structured around the following three main topics:
   - Sizing the impact of climate-related risks on the economy both in the central case and in the event of tail scenarios
   - Assessing transmission channels of climate-related risks to the economy and the financial system
   - Identifying areas where further research is needed

3. **Scaling up green finance**, structured around the following three main topics:
   - Leading by example and greening the activities of central banks and supervisors
   - Understanding and monitoring the market dynamics of green finance
   - Being catalysts for a sound scaling up of green finance

As an example of action by members, the Bank of England, which chairs workstream two, is stress testing the UK financial system under various climate pathways, including the current high emissions business-as-usual scenario and the transition to net zero by 2050. The test will integrate climate scenarios with macroeconomic and financial models, an approach being developed in consultation with insurers and other stakeholders.

SUGGESTED ACTIONS PER KEY RECOMMENDATION

1. Build and disseminate a compelling evidence base, and empower people to act

1.1. **Establish a global research fund** to identify critical gaps and commission research to close identified gaps from both the academic and investment research communities.

1.2. **Extend existing analysis to include ESG considerations** and provide an outlook over longer time horizons than is currently the norm.

1.3. **Engage with key industry publications and the financial media** to support dissemination of research.

1.4. **Engage with individual savers and pension fund beneficiaries** to support alignment of investments beliefs, working with corporate sponsors and the investment community as relevant.

1.5. **Review incentive structures** to ensure that sustainability performance outcomes are part of short and long-term remuneration.

1.6. **Incorporate sustainability into professional codes of ethics and qualifications** to provide the necessary culture, tools and knowledge for finance and accounting professionals to act.

1.7. **Ensure that trustees, board members, and key decision makers are 'sustainability competent'**, for example, through dedicated training programmes such as those run by the University of Cambridge Institute for Sustainability Leadership (CISL).

1.8. **Consider the need to strengthen regulatory guidance** to reinforce the need to consider ESG matters. In particular as part of fiduciary responsibility as seen in actions taken and recommendations made by the International Organisation of Pensions Supervisors (IOPS), the EU Commission, and the Department for Work and Pensions in the UK.

2. Set ambitious targets and embed them into strategy and decision making

2.1. **Commit to a net zero emissions target**, for example, setting a 1.5 degree Celsius-aligned science-based target, and consider adoption of other business-relevant targets linked to delivery of the SDGs.

2.2. **Embed sustainability into board strategy sessions and regular board reporting**, using the SDGs to explore the organization's purpose and challenge its business model.

2.3. **Provide the board with robust information on sustainability** for use in decision making and executive remuneration.

2.4. **Conduct scenario analysis for climate risk** to test the resilience of your business model and strategy.

2.5. **Build a long-term investment plan** incorporating climate change mitigation and adaptation measures.

2.6. **Adopt the guidance within the A4S Essential Guides series** to integrate sustainability into strategy and decision making.

3. Allocate funds to deliver sustainable outcomes

3.1. **Map the impact of investments on the SDGs and climate change**, developing a strategy to align investment policies and decisions with these outcomes.

3.2. **Analyse your investments** to assess whether they are compatible with limiting global warming to 1.5°c.

3.3. **Set a target percentage allocation** to investments with positive social or environmental impact.

3.4. **Provide a defined contribution default fund** that incorporates steps to reduce exposure to climate-related risks and increases allocation to solutions.

3.5. **Support steps to embed ESG into passive funds**, considering ways to make sustainable funds the norm.

3.6. **Adopt a sustainable finance framework** to allocate capital towards sustainable outcomes.

4. Adopt global reporting standards and use consistent terminology

4.1. **Accelerate adoption of the TCFD recommendations** by committing to report against the recommendations and encouraging others to report, for example investors can exercise voting powers where there is a failure to provide adequate disclosures, and asset owners can consider inclusion as part of the selection process for managers.

4.2. **Integrate sustainability information into core business decisions and client interactions**, whether it be guiding investments, providing analysis of companies or rating bonds, and make it clear to preparers how the information is being used.

4.3. **Work with other interested regulatory authorities around the world to provide the mandate to an independent global body with appropriate competence**, oversight and accountability mechanisms to set sustainability standards, and provide incentives for existing standard setters to work together to drive greater convergence. Make disclosures mandatory, both by companies and by funds. For companies and investors, join forces to provide regulators with a clear call to action.

4.4. **Consider the potential for the SDGs to improve reporting on sustainability impacts** by investors and companies, for example by using the SDGs as a framework for strategy development, target setting and reporting, and through support for the World Benchmarking Alliance (WBA).

4.5. **Support efforts underway at national and international levels to develop clear labels for products**, with the aim of delivering globally consistent standards, for example by working with the International Organization for Standardization.

4.6. **Adopt existing best practice standards** where they exist, for example, the green bond principles and the social bond principles.

4.7. **Report on outcomes** – both financial and non-financial – in a transparent manner to enable retail and institutional investors to assess performance.

5. Price externalities to accelerate integration into decision making

5.1. **Adopt a shadow price on carbon** within analysis and investment decision making, for example through joining the Carbon Pricing Leadership Coalition (CPLC), aligning the price with the latest analysis (for example, the CPLC's Stern-Stiglitz report of 2017 suggests a price on carbon of US$100 by 2030).

5.2. **Support efforts to internalize market externalities into the price signal at a level sufficient to affect investment decisions**. This could include effective carbon pricing at an impactful level, and with clear signals setting out future increases, as well as eliminating fossil fuel subsidies.

5.3. **Undertake a natural, social or human capital assessment** across your business/portfolio to understand impacts or dependencies.

A4S

The Prince's Accounting for Sustainability Project (A4S) was established by HRH The Prince of Wales in 2004. Our aim is to make sustainable decision making business as usual.

We work with the finance and accounting community to:

- Inspire finance leaders to adopt sustainable and resilient business models
- Transform financial decision making to enable an integrated approach, reflective of the opportunities and risks posed by environmental and social issues
- Scale up action across the global finance and accounting community

A4S has three global networks: the Chief Financial Officers Leadership Network, a group of CFOs from leading organizations seeking to transform finance and accounting; the Accounting Bodies Network whose members comprise approximately two thirds of the world's accountants; and, the Asset Owners Network which brings together Pension Fund Chairs to integrate sustainability into investment.

www.accountingforsustainability.org

AVIVA

Aviva provides life insurance, general insurance, and savings and investments to 33 million customers across the world, helping people save for the future and manage the risks of everyday life. Aviva is the UK's leading insurer, serving one in every four households, and has strong businesses in selected markets in Europe, Asia and Canada. Aviva's asset management business, Aviva Investors, manages over £331 billion in assets. Aviva aims to serve its customers well, building a business which is strong and sustainable, which people are proud to work for, and which makes a positive contribution to society.

Aviva was:

- the world's first carbon neutral insurer in 2006;
- a co-founder of the World Benchmarking Alliance;
- a founding signatory to the UN Principles of Investment, the UN Environment Programme Finance Initiative and their Principles for Sustainable Insurance, and is a signatory to the Net Zero Asset Owners' Alliance;
- a member of the FSB's Taskforce for Climate-Related Financial Disclosure (TCFD) and the EU's High-Level Expert Group on Sustainable Finance; and
- the first asset manager to formally incorporate corporate responsibility formally into its voting policy, and the first to announce that it would vote against companies not providing TCFD disclosures.

www.aviva.com

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