SUSTAINABILITY

NEWSLETTER – NOVEMBER 2024

CONTENT

EU SUSTAINABILITY REGULATION
UPDATE FOR NOVEMBER

01 The EU Council Greenlights New Regulation for ESG Ratings

The EU Council adopted a new regulation on ESG rating activities in on the 19th of November. The rules aim at making ESG ratings in the EU more **consistent, transparent, and comparable** to boost investor confidence in sustainable financial products.

- ESG rating aim to provide an opinion of a company's impact on society and the environment and its exposure to ESG risks.
- The new rule will require ESG rating providers to be authorized and supervised by the European Securities and Markets Authority (ESMA).
- Rating providers will need to comply with transparency requirements regarding their methodology and sources. In addition, ESG rating providers outside of the EU will need to obtain an endorsement by an authorised ESG rating provider to operate in the EU.
- The regulation also introduces as a principle a separation of business and activities to prevent conflicts of interest.

Go to the press release →

02 EU Insurance Regulator Calls for Higher Capital Requirements for Fossil Fuels

The European Insurance and Occupational Pensions Authority (EIOPA), released a new report, **recommending the European Commission to implement additional capital requirements for fossil fuel assets on European insurer's balance sheets** to address the industry's **high exposure to transition risk.**

- The report's findings on climate transition-related market risks found that fossil fuel-related stocks and bonds have greater exposure to transition risks than other assets and that insurers should set aside sufficient capital to withstand potential losses from investments in these assets.
- Specifically, EIOPA recommends raising capital requirements by up to 17% for fossil fuel-related stocks and a charge of up to 40% for bonds.
- Fossil fuel assets are exposed to transition risks, notably stranded assets for economic activities unable to adapt their business models to align with the decarbonization of the real economy.

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EU SUSTAINABILITY REGULATION
UPDATE FOR NOVEMBER

03 ESMA announces the 2024 European Common Enforcement Priorities for Corporate Reporting

ESMA and European enforcers will focus on the following key topics in 2025: (i) IFRS financial statements, (ii) sustainability statements, notably materiality considerations under ESRS, scope & structure of sustainability statements, and disclosures related to Article 8 of the Taxonomy regulations, and (iii) European Single Electronic Format (ESEF) digital reporting.

The statement highlights **the importance of connectivity between financial and sustainability statements.** Specific areas of focus for sustainability reporting include:

- Double materiality assessment in alignment with EFRAG's Implementation Guide on Materiality Assessment.
- The impact materiality process should be based on the results of sustainability due diligence, including engagement with affected stakeholders.
- Extension of information in sustainability statements to cover material impacts, risks, and opportunities (IROs) related to the undertaking's value chain.

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04 EU Lawmakers Approve Regulation to Establish Carbon Removal Certification System

The EU Council gave **final approval for a regulation establishing the first EU-level certification framework for permanent carbon removals, carbon farming, and carbon storage in products.**

This voluntary framework will facilitate and encourage high-quality carbon removal and soil emission reduction activities in the EU, as a complement to sustained emission reductions. **Carbon removal activities will have to meet four overarching criteria to be certified:**

- They must bring a quantified net carbon removal benefit or net soil emission reduction benefit.
- They must be additional, meaning that they go beyond statutory requirements and that they need the incentive effect of the certification to become financially viable.
- They must aim to ensure long-term storage of carbon while minimizing the risk of carbon release.
- They should do no significant harm to the environment and should be able to result in co-benefits to one or more sustainability goals.

Go to the full press release →

GLOBAL SUSTAINABILITY REGULATION
UPDATE FOR NOVEMBER – APAC & UK

05 HKMA Unveils New Sustainable Finance Action Agenda

The Hong Kong Monetary Authority (HKMA) launched the Sustainable Finance Action Agenda on the 21st of October. The Agenda seeks to further consolidate Hong Kong's position as the sustainable finance hub in the region. The Agenda includes eight goals in four key areas: **(I) Banking for net zero, (II) Investing in a sustainable future, (III) Financing net zero, and (IV) Making sustainability more inclusive.** Specific goals include:

- Support banks' efforts in the preparation of transition plans by providing further guidance, support, and tools (i.e., taxonomy for green and transition activities, seminars & workshops).
- Actively expand the scope and variety of HKMA's sustainable investments and incorporate ESG factors, with a specific focus on climate change and forward-looking transition considerations, into every investment decision.
- Make sustainability more inclusive by equipping Hong Kong's banking practitioners with the relevant sustainable finance knowledge.

Go to the press release →

06 FCA publishes disclosure examples for the SDR and Investment Labels Regime

The Sustainability Disclosure Requirements (SDR) and investment labels regime enters into force on 2nd of December 2024. **The new regime defines a set of criteria and disclosure requirements for financial products with sustainability-related labels.** The example disclosures set out a series of good and poor disclosure practices:

- **Good practices for Sustainability Focus label:** define an explicit sustainability objective as a part of the investment objectives that is clear, specific, and measurable, having at least 70% of the gross value of the product's assets invested in alignment with the sustainability objectives, and identifying KPI to demonstrate progress towards the sustainability objective.
- **Poor practices:** Not linking the asset selection process to the fund's sustainability objective, not including an explanation or evidence as to why the scoring / threshold is appropriate for defining sustainability, and failure to disclose short-term and medium-term targets for Sustainability Improvers label.

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ESG MARKET INSIGHTS
DECARBONIZING PRIVATE MARKETS

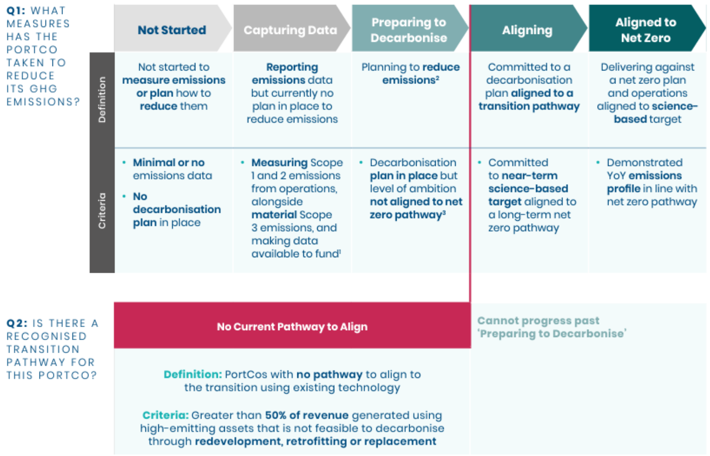
01 iCI and the Sustainable Markets Initiative's Private Equity Task Force release an updated version of the Private Markets Decarbonization Roadmap (PMDR)

The updated version of the PMDR (the Roadmap), developed with the support of Bain & Company, incorporates key insights and feedback from adopters and industry stakeholders. **The Roadmap provides a common language for private market firms across asset classes to disclose their decarbonization progress**.

Since its initial launch in 2023, the Roadmap has been widely adopted across private markets. **PMDR 2.0 addresses feedback from 40+ adopters, while maintaining the core framework**. Enhancements to the Roadmap include:

- Further asset-class specific considerations for Growth, VC, and Real Estate.
- Process refinements such as simplifications to the categorisation flow of Decarbonization Enablers (assets with activities enabling the net zero transition)
- A new PMDR Support Tool that enables portfolio classification and disclosure of key insights internally and/or externally through automated visualisations directly in Excel or through PowerPoint templates. The tool also provides flexibility on Scope 3 data, allowing GPs the option to communicate initial progress based on Scope 1 & 2 emissions.

Decarbonization Alignment Scale for Growth Funds



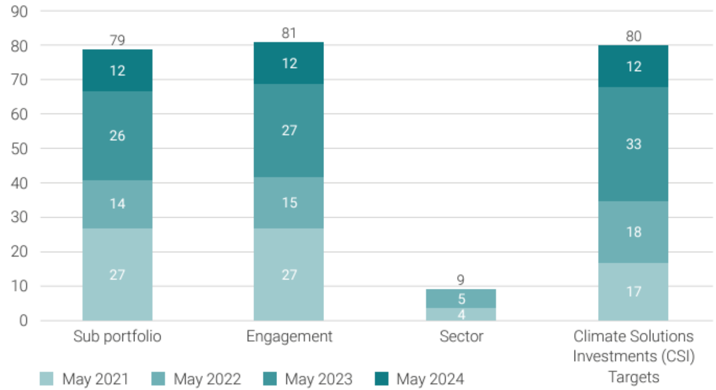
Source: Private Markets Decarbonization Roadmap 2.0 (November 2024)

Click to access the guidance →

ESG MARKET INSIGHTS
NET ZERO ASSET OWNERS

02 Net-Zero Asset Owner Alliance sets the pace on climate ambition, action and transparency in latest Progress Report

Total number of NZAOA members' intermediate targets set across the four target types



Source: Demonstrating 1.5°C-Aligned Decarbonisation, The fourth progress report, October 2024, UNEPFI, PRI.

The Net-Zero Asset Owner Alliance's (NZAOA) Progress Report presents its members' efforts to achieve net-zero GHG emissions by 2050. Key findings from the Progress Report include:

- 81 members, with a combined AuM of US$9.4 trillion (98.9% of the Alliance's total AUM) have now set intermediate decarbonization targets.
- Nearly all members (79 out of 81) have chosen to set sub-portfolio targets, which covers 48% of the members' total AuM. On average, members targeted a reduction of 26% by 2025 for bonds, equities, real estate, and infrastructure.
- Members' investment in climate solutions as grown from US$380 billion in December 2022 to US$555 billion in December 2023.
- However, real-economy decarbonization is not currently one of the driving actors of portfolio decarbonization. Action in the real economy is lagging what is needed to limit global warming to 1.5°C.
- The Report calls on policymakers to deliver reductions for oil & gas, design and implement carbon pricing mechanisms, develop a detailed and credible transition plan, phase out all unabated coal-fired electricity generation, and scale blended finance for investment in emerging markets.

Click to read the full progress report from NZAOA

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ESG MARKET INSIGHTS

03 Four Key Trends Shaping the APAC ESG Landscape

Responsible Investor identified **four key trends that will shape ESG for investors in the APAC region:**

1. **APAC can lead the way in setting the agenda for many issues in sustainable finance**. Historically, ESG has been critiqued as a Western-centric concept; APAC plays a key role in developing country-specific ESG approaches for sustainable development.

2. **Decarbonization remains a core challenge in the region.** Given that Asia is a global hub for manufacturing industries, scaling renewable energy and phasing out fossil fuels is vital to reaching net-zero carbon emissions.

3. Asia has emerged as **the leading force in the global market for green bonds**, with India launching its sovereign green bond last year, while Indonesia launched a 'coral bond' to finance the conservation of reefs. Japan is currently leading the institutionalization of transition bonds, to finance grey-to-green transition activities.

4. **India has been slow to embrace ESG**; the biggest pension funds have displayed limited appetite for ESG mandates, and only 11 ESG strategies have been launched by Indian managers. Support from large investors is necessary to drive the green transition.

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04 BCG Publishes their 2nd Annual Sustainability in Private Equity Report

The report draws upon data from **the ESG Data Convergence Initiative (EDCI) to assess how sustainability in private markets has evolved over the year.** Analysis of the data showed that **private markets have significant potential for lasting impact** on portfolio companies' sustainability practices.

The report also highlights LP views on sustainability, with the following key findings:

- **85% of the surveyed LPs** said they expect to increase their prioritization of sustainability-relate topics over the next 3 years.
- Almost **70% agreed that companies that consider and manage sustainability factors warrant a valuation premium** to peers that do not. This is aligned with a survey conducted by PESMIT and BCG, **which found that 70% of private company leaders expect to be paid a premium** upon exit for companies effectively decarbonized during holding period.
- The **key reasons for collecting ESG data from GPs include understanding portfolio ESG performance and engaging with GPs constructively on their ESG priorities**, while only a few report using the data for investment allocation decisions.

Go to the full report

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NEW IN RESEARCH
COMPARING PORTFOLIO NET-ZERO APPROACHES

01 The CFA Institute Research & Policy Center Study Comparing Frameworks for Aligning Investments with the Paris Agreement

The study examines **two strategies to align portfolios with net-zero targets: the Net Zero Achieving, Aligned, Aligning (NZ:AAA) screens**, which promote engagement with high emitters, and **the Paris Aligned Benchmarks (PAB),** which seek to shift capita, away from carbon-intensive companies.

- The NZ:AAA framework is **based on a forward-looking approach recommended by the IIGCC**, and prioritizes investing in companies already achieving net zero, those with credible net-zero commitments, or companies contributing to climate solutions, even if they are high-emitters today.
- The NZ:AAA also prioritizes engagement with high-emitting companies, rather than excluding them, with the goal of supporting the transition of sectors with high carbon-intensity.
- **The PAB framework is an EU Commission regulated approach that emphasizes reducing carbon intensity** by excluding carbon-intensive companies. It is used for passive strategies or for benchmarks.
- PAB is focused on **immediate carbon reduction** rather than a forward-looking assessment of a company's decarbonization plans; the approach lacks an effective mechanisms for engaging with high-emitting companies.

Strengths & Weaknesses of the NZ:AAA and PAB Net Zero Frameworks

	Achieving, Aligned, Aligning			Paris Aligned
	A	AA	AAA	PAB
Probability of alignment of portfolio with net zero by 2050	High	High	Medium	High
Exposure to net-zero risk premium	High	Medium	Low	Low
Ability to diversify portfolio	Weak	Medium	Strong	Strong
Immediate decarbonization of portfolio	Weak	Medium	Medium	High
Account for the varying efforts of companies to reach net zero	Yes	Yes	Yes	No
Focus on funding the energy transition	Strong	Medium	Medium	Weak
Forward-looking approach to net zero	Yes	Yes	Yes	Partial
Ability to engage and support stewardship with higher-impact companies	Strong	Strong	Strong	Weak
EU Taxonomy exposure	Strong	Medium	Medium	Weak

Source: CFA Institute, Aligning Investments with the Paris Agreement: Frameworks for a Net-Zero Pathway, October 2024.

Click to read the report from the CFA Research & Policy Center →

NEW IN RESEARCH
NET ZERO TOOLS, SOLUTIONS, & BENCHMARKS

02 CFA Institute Study on Tools Used by System-Level Investors for Net Zero

System-level investors believe that a majority of their returns (75% - 94%) result from the general price level of capital markets rather than individual asset performance. A study by CFA Institute on system-level investor approaches to net zero found that:

- **System-level investors draw a direct connection between climate change, transition risk, and financial impact.**
- They view addressing climate change as **an obligation that is an integral part of their fiduciary duty.** System-level investors emphasize that it is simply not enough to decarbonize their portfolios – they consider **active participation in reducing the impacts of climate change** as necessary to fulfilling their responsibilities.
- System-level investors have a long-term focus, enabling them to prioritize sustainable returns over immediate gains.
- Traditional institutional investing tools – including asset allocation, manager selection, and engagement – are adapted by system-level investors to achieve climate-related objectives.
- They see collaboration and active engagement with public policymakers as a vital part of driving broader systemic change.

Click to read the full report

03 Net Zero Investing: Solutions for Benchmarks, Incentives, & Time Horizons

The CFA published a new report discussing **the challenges and solutions to integrating net-zero objectives and climate-risk considerations to traditional investment programs.** The report provides guidance for choosing relevant benchmarks, incentivizing actions needed to achieve net-zero objectives, and determining appropriate time horizons. The report's key take aways include:

- **Net zero goals should coexist with an asset owner's risk, return, and actuarial targets** without compromising them.
- Current **climate risk management tools are insufficient** to for measuring climate risk; asset owners should take practical steps to reduce these risks in the interim as frameworks for climate-risk management evolve.
- Effective net-zero programs should **include incentives that encourage portfolio decarbonization and investment in climate solutions**. This includes asset manager performance incentives and goals (internal) as well as net-zero compensation structures set by **asset owners for specific mandates (external) to motivate behavioral change.**

Go to the full report

NEW IN RESEARCH
UN EMISSIONS GAP REPORT 2024

04 The UN Emissions Gap Report for 2024 Finds That Nations Must Deliver Dramatically Strong Ambition and Action or the Paris Agreement's 1.5°C Goal Will be Gone

Likelihood of warming exceeding a specific temperature limit (%)

Scenarios	1.5°C	2°C	3°C
Current policies continuing	100% (85–100%)	97% (28–100%)	37% (1–80%)
Unconditional NDCs continuing	100% (86–100%)	94% (28–100%)	22% (1–75%)
Conditional NDCs continuing	100% (77–100%)	79% (19–100%)	10% (0–69%)
Conditional NDCs + all net-zero pledges	77% (64–97%)	20% (64–97%)	0% (0–6%)

Source: UNEP, Emissions Gap Report 2024: No more hot air… please!, October 2024.

The fifteenth Emissions Gap Report from UNEP has one core message: ambition means nothing without action. The Report evaluates what is required from Nationally Determined Contributions (NDCs), commitments made by countries to reduce GHG emissions, to limit global warming to 2°C. Key findings include:

- GHG emissions set a record of 57.1 $GtCO_2$ in 2023, a 1.3% increase from 2022 levels.
- There is a significant disparity between the current, per capita, and historic emissions of major emitters and world regions; **GHG emissions across the G20 members accounted for 77% of global emissions in 2023**. In comparison, if all African Union members are added to the G20 total, total emissions increase by just 5%.
- Implied emissions trajectories of the G20 members towards net zero show reason for concern. The full implementation of unconditional and conditional NDCs reduces expected emissions in 2030 by 4% and 10%, respectively, whereas **a 28% reduction is needed for 2030 emissions to be aligned with 2°C and a 42% reduction for 1.5 °C.**
- **Immediate action matters:** temperature projections based on the conditional NDC scenario are 0.5°C lower than those based on existing policies.

Click to read the full report from the UN →

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IN FOCUS: REFLECTIONS ON COP29 AND COP16

COP 29 OVERVIEW (1/3)

COP29 Climate Change Summit – Overview of the Key Topics for Negotiation & Outcomes

COP29, the United Nations Climate Change Conference, took place in Baku Azerbaijan from the 11th of November to 22nd of November 2024. Key topics negotiated at COP29 include:

- **Setting the New Collective Quantified Goal (NCQG**) for climate finance. The framework is designed to provide financial resources for mitigation, adaption, and loss-and-damage measures. Despite progress, there is a significant gap between the pledged and delivered funds from high-income countries.
- **Reforming fossil fuel subsidies,** which totaled $1.7 trillion globally in 2022. Negotiators have called for a clear timeline for phasing out these subsidies to prioritize investment in renewable energy and just transition measures.
- **Strengthening National Contributions** which are due February 2025. The emphasis on **economy-wide and investable NDCs** aims to attract private-sector participation.
- **Addressing climate justice and indigenous rights**, including the legal recognition of climate migrants to address growing displacement.

OUTCOMES OF COP29

- Negotiation of a new climate finance goal ended with developed countries **pledging US$300 billion a year by 2035** to support developed countries with their climate transition, mitigation, and adaption.
- However, **the NCQG falls short of the estimated US$1.3 trillion needed by developing countries**. A roadmap to scale up finance towards US$1.3 trillion was added to the text, but there is little confidence that this level of finance will be delivered.
- **Parties failed to agree on how to take forward COP28's energy package**, an agreement to transition away from fossil fuels, triple renewable power and double energy efficiency by 2030.
- The outcome further failed to **explicitly call on nations to phase out fossil fuel subsidies**, and a draft text calling on nations to reduce investments in fossil fuel infrastructure and to develop 'polluter pays' instruments was rejected.
- **The National Adaption Plan (NAP)** assessment was tabled to 2025 for further consideration, as countries failed to meet the deadline that was set back in 2021. The Parties did reach an agreement on the Baku Adaption Road Map, which sets forth means of implementation indicators, highlighting the importance of finance, technology transfer, and capacity building for adaption.

Click to read more about the outcomes of COP29

IN FOCUS: REFLECTIONS ON COP29 AND COP16
COP 29 OVERVIEW (2/3)

On the Importance of Just Transition & Lack of Representation at COP29

Although some progress was made at COP29, the summit lacked representation and failed to make progress on human rights and gender. **Only 8 out of 78 of the world leaders that participated in COP29 were women**, although women, girls, and gender-diverse individuals are disproportionately impacted by climate change.

- **Due to existing inequalities**, such as lack of income and access to information, women, girls, and gender minorities are increasingly vulnerable to acute and long-term climate impacts.
- Climate-related threats also disproportionately impact women's health. For example, studies have linked high temperatures to adverse birth outcomes. Moreover, **numerous studies highlight that gender-based violence is reported to increase during or after extreme events, as was seen during covid-19**.
- More **equitable inclusion of women has also been linked with transformative policymaking across social and political systems and environmental policy** (e.g., greater number of women in national parliaments is associated with increased ratification of environmental treaties and more stringent climate policies).

The Lancet Planetary Health journal published an article on [Bridging the Gender, Climate, and the Health Gap: the Road to COP29]. The key findings included:

- Both slow-onset environmental changes (e.g., sea level rise, increasing temperature, droughts) and sudden-onset events (e.g., storms, floods) caused by climate change exacerbate systemic inequalities and disproportionally impact marginalized populations.
- Gender-specific health outcomes impacted by climate change include challenges in accessing health-care services, particularly for reproductive and maternal health, barriers to information regarding early warning systems or weather alerts, and disproportionate access to nutrition.
- 80% of people displace by climate change are women, and as climate-related hazards intensify, women risk being left behind, burdened with the responsibility of taking care of households. Moreover, sociocultural norms often restrict women's mobility and freedom to movement, limiting their ability to adapt to disasters.
- Meaningfully integrating gender-specific considerations into climate policy and practices is crucial to addressing gender-specific risks and vulnerabilities through programs and policies. This requires investment in enabling conditions (i.e., inclusive governance structures, gender-responsive budgeting, etc.)

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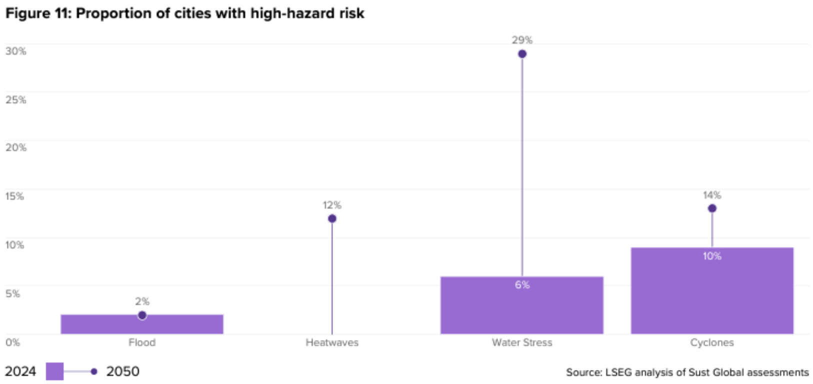
COP 29 OVERVIEW (3/3)

Implications of Transition & Physical Climate Risks on Investors

LSEG's latest Net Zero Atlas published prior to COP29 aims to provide investors with an outlook of physical and transition climate risks across the G20 based on the current 2035 targets for GHG emissions reductions. Key findings include:

- **The next round of 2035 emissions targets, 'NDCs 3.0', will shape the trajectories of G20 economies in the 2030s**, and determine the transition and physical risks faced by companies.
- Physical risks related to climate change **will put major cities at risk across G20 as natural hazards intensify.** Forecasts suggest that **annual climate damages could reach $38 trillion under a 2°C warming scenario**.
    - The share of major cities with high-risk exposure to flood, heatwaves, water stress, and cyclones would **increase from 18% to 47% under a high emission scenario**, with the average number of extreme heat days doubling across major cities.
    - Even in a low emission scenario, **large-scale resources are required to adapt cities** to shifting physical climate risk profiles. This is particularly urgent in Middle East and Southeast Asia.

Proportion of cities with high-hazard risk (2024 to 2050) – Flood, Heatwaves, Water Stress, and Cyclones



Source: LSEG, COP29 Net Zero Atlas (2024)

Click to read the full COP29 Net Zero Atlas from LSEG

IN FOCUS: REFLECTIONS ON COP29 AND COP16
COP 16 OUTCOMES (1/2)

Reflections on COP 16 – What are the Outcomes and Implications for Biodiversity?

Between October 21st and November 2nd, political leaders from nearly 200 countries joined representatives from Indigenous communities, youth groups, business leaders, and NGOs in Colombia for COP 16. The summit offered a chance to implement concrete action plans for halting biodiversity loss and protecting 30% of the world's land and water by 2030, an agreement reached in 2022. The first official progress report on the 30x30 goal was also published in 2024 as a part of the Protected Planet Report (The Report).

Biodiversity is also vital for mitigating climate change through natural carbon sinks and nature-based solutions for risk mitigation and resilience to natural disasters.

SO, WHAT WERE THE OUTCOMES OF COP16 AND WHERE ARE WE TODAY?

Progress towards the summit's core objectives came up short with many countries lagging in ambition and no agreements reached on key issues.

- The Report found that **just over 17% of the world's land area and 8% of marine and coastal areas are currently protected.** Much of the discussion at COP16 focused on how to pay for conservation and restoration at the speed and scale required to reach the goal of 30% by 2030 (requiring countries to protect another 16.7 million km^2 of land and over 78 million km^2 of marine and coastal areas.
- **In 2022, developed nations promised $20 billion per year by 2025 to support developing countries' biodiversity efforts.** They delivered $15.4 billion that same year (latest data available), but the additional pledges at COP16 total in the millions, not in the billions.
- A key point of discussion was whether companies should have to pay countries for **digital genetic information ('DSI')** used to develop vaccines, medicines, and other products, if it originally came from organisms within their boarders**. While they succeeded in creating a new DSI fund (the Cali Fund) at COP16**, **contributions were made voluntary.** 50% of the funds raised will be spent on activities linked to Indigenous Peoples and local communities.

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IN FOCUS: REFLECTIONS ON COP29 AND COP16
COP 16 OUTCOMES (2/2)

Reflections on COP 16 – What Is Needed to Meet Biodiversity Targets on Time?

Countries are **nowhere near closing the $700 billion annual gap in finance** for nature which is urgently needed to protect and restore our ecosystems. **All 190+ countries represented in COP29 were expected to submit National Biodiversity Strategies and Action Plans** (NBSAPs) by the end of the summit, but **only 44 did**.

In addition to closing the financing gap for biodiversity, global leaders need to:

- **Boost conservation and restoration**, especially in countries with megadiverse ecosystems.
  - 70% of the world's biodiversity is found in 17 megadiverse countries, a country with at least 5,000 plants that occur naturally only within its borders, as well as a marine ecosystem.
  - These include the tropical rainforests of the Amazon, Congo Basin, and Southeast Asia, as well as the coral reefs in the Pacific's Coral Triangle. Countries need to focus their conservation efforts on these areas as they have an outsized impact on species health and survival globally.
- **Fulfil promise to support traditional land management**.
  - Indigenous communities manage some of the most biodiverse areas in the world, yet few have seen their customary land tenure rights reflected in law.
  - Countries agreed to create a new body to ensure these groups' participation in the negotiations moving forward and must ensure that Indigenous and local communities have a say in national conservation policy and enshrine their traditional land rights into law.
- **Support biodiversity efforts through economics, policy, and data.** Implementing successful action plans will require the support of policy makers and enforcement.
  - Governments must shift to economic models that work with rather than against nature, including fulfilling their promise to **reform $500 billion per year in nature-harming subsidies (e.g., unsustainable farming and fishing practices)**, on which almost no progress has been made so far.

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