BUSINESS ENVIRONMENT COUNCIL
商界環保協會

Responsible Investment Workshop: How Investors and Corporates Can Manage Climate Risk

Workshop Report

Workshop held 14 March 2018
Report published 5 June 2018

Supporting Organisations

Asia Investor Group on Climate Change

CDP
DISCLOSURE INSIGHT ACTION

International Capital Market Association

PRI Principles for Responsible Investment

Key Messages

1. The investor community is increasingly conscious of climate-related financial risks. There is greater recognition that climate risk poses a fundamental threat to economic stability. 237 firms managing a combined US$81.7 trillion have pledged to regularly disclose their business' exposure to climate risk and to implement initiatives in line with the Task Force on Climate-Related Financial Disclosures recommendations.[1] 280 investors managing US$30 trillion in assets have signed on to the Climate Action 100+ initiative to engage companies to improve governance on climate change, reduce emissions and strengthen climate-related financial disclosures.[2] Action to take on board climate risk is no longer regarded as an optional nice-to-have consideration for ESG funds only, and the need to integrate climate change into decision making to ensure the resilience of funds is becoming mainstream.

2. Many investors are taking action – establishing the relevant governance structure and internal policies, researching into the ESG and climate-related performance of companies, utilising tools and indices to assess companies, integrating climate considerations into allocation decisions, and engaging companies to encourage ESG excellence and disclosure.

3. However, issues still arise as to how best to take climate risk on board. Analytical frameworks and information are being developed and improving. This workshop was about not only why it is important to factor in climate risk but also how to do so.

Introduction

4. Business Environment Council (BEC) Climate Change Business Forum Advisory Group (CCBF AG) organised a workshop on 14 March 2018 through BEC Institute of Environmental Education. It brought together both corporates and investors. The aims were to:
   - build capacity amongst the investor community on how to integrate climate risk into investment-related decisions, and
   - support corporates in using these tools and frameworks to manage climate risk and for disclosure purposes.

[1] http://www.businessinsider.com/blackrock-jp-morgan-banks-factoring-climate-risks-into-decisions-2017-12

[2] http://www.climateaction100.org/

5. The background to this is that climate change – in terms of physical risks as well as policy changes – is and will increasingly disrupt business operations, supply chains, and impact asset values. It has become apparent that risks to the financial system as a whole are high as a result of incorrect assessment of risk. The Financial Stability Board (FSB) therefore set up a Task Force on Climate-related Financial Disclosures (TCFD) to identify means of managing this risk. The Task Force made recommendations as to a framework for investors to use in their decision-making. In addition, banks and other financial institutions have been developing tools and setting up information databases to enable such decisions as well as effective active engagement with corporates. Though some parts of the Hong Kong financial sector are well aware of these developments, to many the reasons for and ways of implementing this risk-management approach are unfamiliar.

6. BEC CCBF AG promotes awareness of, and builds capacity in relation to, climate mitigation, adaptation and resilience activities amongst the BEC membership and generally amongst the business community in Hong Kong. This workshop follows on from work began several years ago on increasing the climate resilience of key sectors of Hong Kong's economy, including the corporate and financial services sector. Please see the *Hong Kong Climate Resilience Roadmap for Business*[3] for more background information.

7. This report summarises the presentations given, the key findings from the group discussion and highlights key findings and messages that emerged. We hope that by consolidating this information we will inspire continued action on the part of investors and corporates.

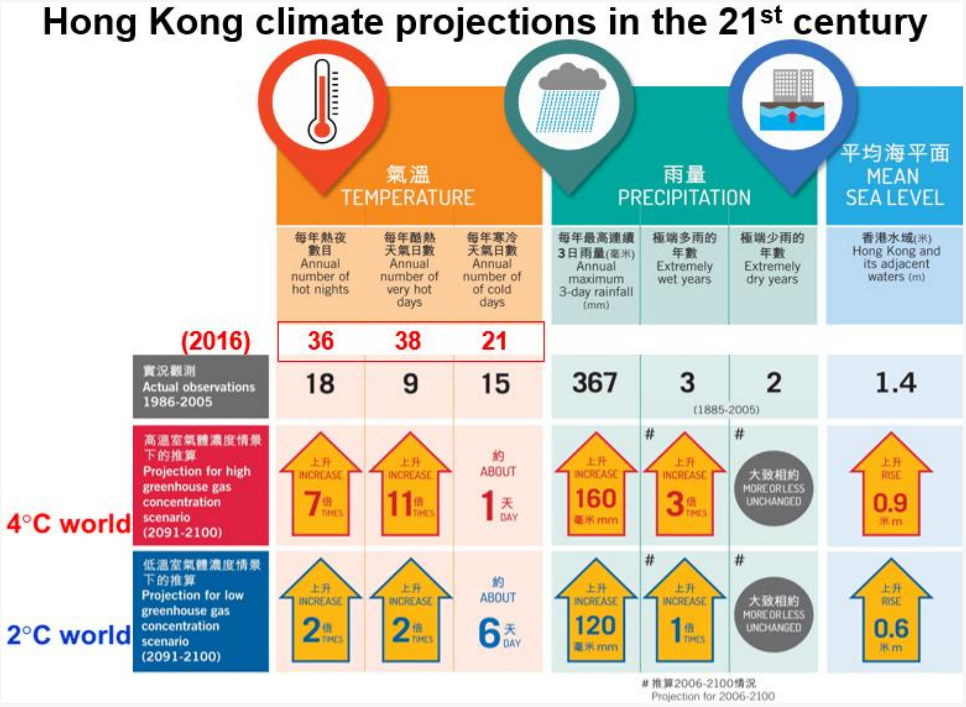
What is Climate Risk and Why Should Investors and Corporates Care?

Ms Maya de Souza
Assistant Director – Policy Research, Business Environment Council Limited

8. The climate is changing. Temperature is increasing, patterns of precipitation are shifting, and sea level is rising. These factors, known as climate variables, lead to

[3] http://bec.org.hk/files/images/Resource_Centre/Publications/BEC_Hong_Kong_Climate_Resilience_Roadmap_for_Business_report.pdf

direct and indirect risks to businesses. Physical risks include direct impacts such as damage to infrastructure and assets, heat stress and health impacts affecting the workforce, water scarcity, and indirect impacts such as a compromised supply chain and disease. These risks are explored in depth in BEC's *Hong Kong Climate Resilience Roadmap for Business*.



9. In addition to physical risks, there are transition risks to consider. These range from new developments in international agreements and domestic policy, changes in business and investor practice and expectations, to the emergence of new and disruptive technology. Overall, the landscape for businesses is shifting. While there are risks, there are also new opportunities businesses can capitalise on.

10. In order to assess the vulnerability of a company to climate risk, investors should consider four aspects of a company, as put forward by the TCFD: governance, strategy, risk management, metrics and targets. This is a high-level over-arching framework. Other tools and information sets are also important for effective management of climate risk.

Responsible Investment & Climate Change: Introduction and the TCFD Recommendations

Mr Lorenzo Saa
Director, Global Networks & Outreach, PRI

11. Responsible investment is a process that involves active consideration of environmental, social and governance (ESG) issues in investment decision-making and in engaging with companies as an owner of equities or bonds. The underlying recognition is that ESG issues are a fundamental part of understanding the value of an investment, and that ESG factors can have a material effect on investment value.

12. Supported by the United Nations, the PRI was established by institutional investors to support the development and implementation of the six Principles for Responsible Investment[4] – an aspirational set of investment principles focused on the incorporation of ESG issues into investment processes and engagement practices. Since the launch in 2006, the number of signatories has grown from 100 to almost 2,000 across the globe, with a total combined assets under management of over US$70 trillion.

13. At the core, responsible investment is about good investment – using more information, taking a longer-term perspective, emphasising risk management, upholding fiduciary duty and ultimately delivering better outcomes. Responsible investment is about enhancing performance, not about philanthropy. It improves rather than sacrifices returns. But of course, a key benefit of responsible investment is it also can drive sustainable outcomes.

14. There are different ways to practice responsible investment, and may include negative or positive screening, engaging companies on ESG issues, or integrating ESG issues into investment analysis. ESG integration should be a natural progression in the investment research process. It gives better understanding of a company or industry and how ESG factors may impact it. ESG research and integration incorporates long-term material factors for more informed decision making. An increasing number of funds investing in listed equities (80%) and in fixed income assets (76%) now integrate ESG considerations into their investment decisions, with 45% and 44% respectively undertaking a screening process.

[4] https://www.unpri.org/pri/about-the-pri

15. The FSB TCFD report reiterated the message that climate change is a global challenge and is material to businesses and investments. It published its recommendations to promote more informed investment, credit, and insurance underwriting decisions, and to enable investors to making informed decisions as to exposure to climate-related risks.

16. The TCFD recommendations relate to climate-related financial disclosures across sectors and jurisdictions to ensure that investors are fully informed on climate risk. They are structured around four thematic areas which are core elements of how organisations operate – governance, strategy, risk management, metrics and targets. The Task Force encourages forward-thinking through scenario analysis, a tool useful for assessing the resilience of an organisation's strategies to climate risks.

Governance	Strategy	Risk Management	Metrics and Targets
Disclose the organization's governance around climate-related risks and opportunities.	Disclose the actual and potential impacts of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning where such information is material.	Disclose how the organization identifies, assesses, and manages climate-related risks.	Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.
Recommended Disclosures	**Recommended Disclosures**	**Recommended Disclosures**	**Recommended Disclosures**
a) Describe the **board's oversight** of climate-related risks and opportunities.	a) Describe the **climate-related risks and opportunities** the organization has identified over the short, medium, and long term.	a) Describe the organization's processes for **identifying** and **assessing** climate-related risks.	a) Disclose the **metrics** used by the organization to assess climate-related risks and opportunities in line with its strategy and risk management process.
b) Describe **management's role** in assessing and managing climate-related risks and opportunities.	b) Describe the **impact** of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning.	b) Describe the organization's processes for **managing** climate-related risks.	b) Disclose **Scope 1, Scope 2, and, if appropriate, Scope 3** greenhouse gas (GHG) emissions, and the related risks.
	c) Describe the **resilience** of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario.	c) Describe how processes for identifying, assessing, and managing climate-related risks are **integrated into the organization's overall risk management.**	c) Describe the **targets** used by the organization to manage climate-related risks and opportunities and performance against targets.

17. Implementing the TCFD recommendations is a process of learning by doing. Many organisations are already taking action. For example, the City of London Green Finance Initiative and China Green Finance Committee are partnering to pilot reporting against the TCFD recommendations in 2018, with many investors and corporates from the UK and China participating.

18. PRI is working to support its signatories implement the TCFD recommendations across a range of work-streams, including introducing climate-related disclosure indicators for signatory reporting, developing tools (such as the TCFD Recommendations Country Reviews[5] and Asset Owner Guide on Implementation[6]), engaging initiatives and other activities. Implementing the TCFD recommendations should be seen as a tool for integrating climate-related considerations into the mainstream financial system, rather than viewing it as additional component.

Responsible Investment – Managing Climate Risk

Ms Emily Chew
Global Head of ESG Research & Integration, Manulife Asset Management
Chair of Working Group, Asia Investor Group on Climate Change

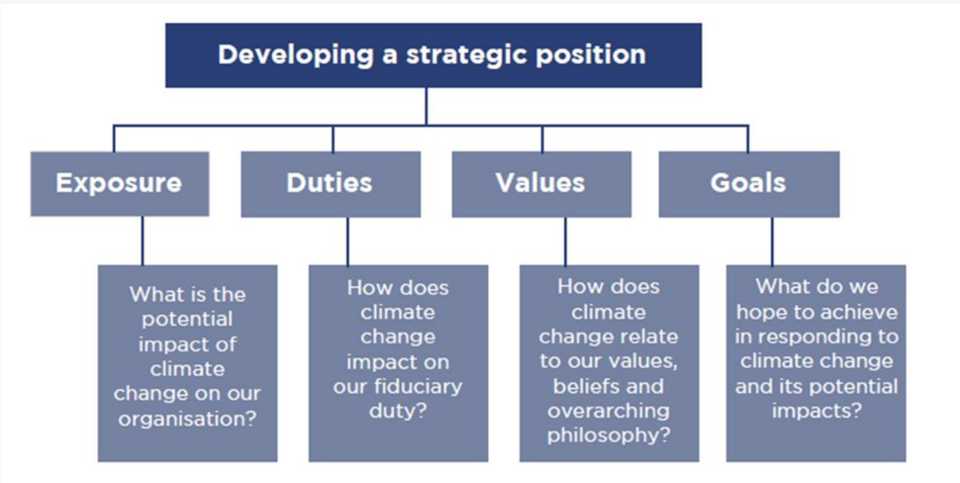
19. Manulife Asset Management (MAM) adopted an ESG policy in 2015. The reasons are: MAM has fiduciary duty to be responsible stewards of client capital; ESG integration support active management which is ultimately about fully

[5] https://www.unpri.org/18.tag
[6] https://www.unpri.org/download?ac=4652

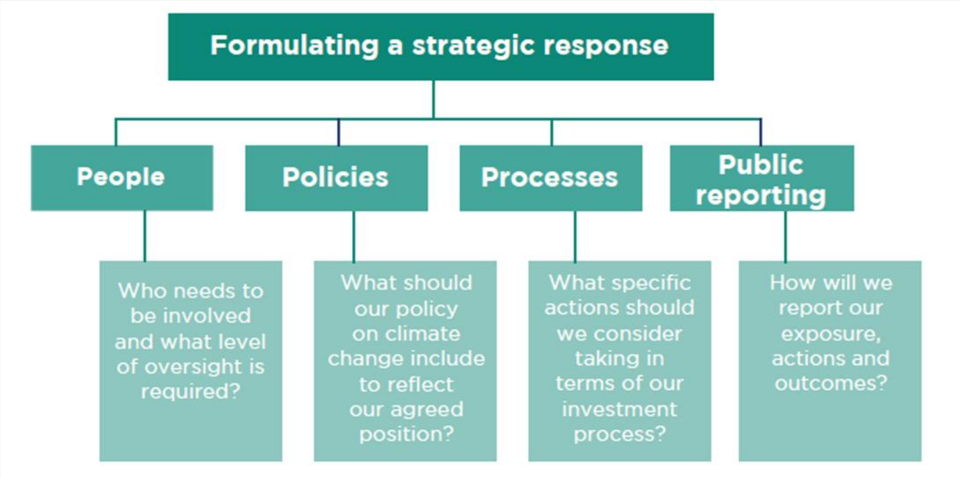
understanding the risk/return profiles of investments; stakeholders and investors are increasingly expecting ESG integration and consideration; and ESG supports industry innovation. The social license to operate is shifting. Investors seek investment outcomes that not only deliver long-term wealth, but leave behind a desirable world for beneficiaries.

20. ESG integration can be complex. But for MAM being part of the Asia Investor Group on Climate Change (AIGCC) is helpful, as the group provides a platform to engage peers to collaborate, co-learn, and share best practices and resources. Working collaboratively with peers – knowing that your organisation is not alone in this endeavour – is important to tackle the “tragedy of the horizons”.

21. AIGCC’s *Integrating Climate Change into Investment Strategy: A Guide for Investors*[7] provides guidance in developing strategic position and response to climate change. In developing a strategic position, investors should recognise climate risk, understand the organisation’s exposure, and bear in mind the long-term welfare of stakeholders. Once a position is established, the organisation should assess what are the people, policies, and processes necessary to operationalise a strategic response. Public reporting is an important element of an organisation’s strategic response, and the TCFD recommendations provide a framework to do so. Actions such as reviewing asset allocation, conducting scenario analysis, divesting, engaging policy makers, exercising right to vote on climate resolutions, collaborating, and disclosure could be part of executing a strategic response.



[7] http://aigcc.net/wp-content/uploads/2017/12/AIGCC-CC-Guide-Design-Final.pdf



22. MAM has begun to embed ESG factors into investment operations. Initiatives include proactive and in-depth ESG research and analysis, utilising ESG scoring and benchmarking to aid decision making, regular ESG risk reviews, engaging and building a sense of ownership within different teams internally, working collaboratively with companies, and establishing a governance structure for strategic oversight to support ESG integration.

23. MAM is taking part in Climate Action 100+, an initiative led by investors to engage corporates to improve governance on climate change, curb emissions and strengthen climate-related financial disclosures. Current corporate disclosure of targets and goals still fall short of the Paris Agreement ambition. But through this initiative, a united investor community is setting a new level of expectation on corporate disclosure, and working constructively with businesses to manage climate risk and to strive for the Paris Agreement goal.

Measuring Climate Change Risks and Opportunities in Institutional Portfolios

Mr Mervyn Tang
Vice President, Head of Asia Pacific ex Japan, ESG Research, MSCI

24. MSCI provides ESG ratings for over 13,000 issuers (including subsidiaries) linked to more than 590,000 equity and fixed income securities globally. The firm also provides various other tools to support investors' ESG needs, such as sustainable

impact metrics for impact investment, and company screens in relation to specific issues such as CO_2 emissions.

25. This work reflects increasing consciousness of climate risk by investors. They have responded to the agenda by taking action to understand, measure and manage exposure to market and regulatory risks associated with climate change and carbon, and to communicate climate change impacts to asset owners and others. Events and initiatives such as the Portfolio Decarbonization Coalition[8], Montréal Carbon Pledge[9], and more recently the release of the TCFD recommendations helped raise the profile of the issue amongst the investor community.

26. The first step to addressing climate risk is assessing the carbon footprint of a portfolio. This may involve measuring emissions, analysing and benchmarking exposure, evaluate stranded asset risks, and tracking performance. Carbon footprinting sets a baseline to inform future action such as reporting, engagement, integrated risk management, and decarbonisation. Relevant guiding metrics and indexes may include company activity types, revenue source, carbon intensity per unit output, GHG emissions, fossil fuel reserves ownership, utilities and fuel mix.

27. Following assessment, the next step is to transition towards decarbonisation. Actions may include: screening out worst performers, allocating to assets aligned with a low carbon future, tilting and optimisation, setting carbon reduction targets, and taking on board MSCI Low Carbon Target indexes[10]. Metrics, indexes and analytics can help to guide this process. When making decisions regarding screening or allocating, investors should not only consider a company's current ESG performance, but also the momentum of how quickly it is improving.

28. The third is to align portfolio construction with a 2C pathway. This is about transformative action.

29. In assessing a company's overall climate-related risk, one should consider a company's policies and oversight, targets and programs, and performance metrics. As to the risks a company may be subject to, it is important to consider both direct and indirect physical and transition risks and the ability for the company to mitigate and adapt. It is useful to note that some companies with high risk exposure may have the ability to easily and substantially reduce its risks – so it is important to

8 http://unepfi.org/pdc/
9 http://montrealpledge.org/
10 https://www.msci.com/msci-low-carbon-indexes

assess companies in multiple dimensions. Beyond risks, investors should also consider new opportunities that a company may be well positioned to capture.

30. Scenario analysis is an emerging approach for assessing climate risk and stress testing, and can provide a more comprehensive view of how asset allocations are affected by different climate shocks. It moves beyond simply carbon footprinting individual companies to provide a system-level analysis. Scenario analysis will take into consideration the difference in trajectories by geography, as well as different impacts to asset classes.

Our Approach to Address Climate Change in Our Investments

Mr Paul Milon
ESG Integration & Sustainability Specialist, Asia Pacific; Consultant Relations & Investment Specialist, BNP Paribas Asset Management

31. BNP Paribas Asset Management (BNPP AM) has a number of ambitious achievements and targets to its name including: reaching carbon neutrality by 2017, committed €20 billion for renewable energy financing by 2020 and €100 million in energy efficiency/clean tech start-ups, and divestment from coal and unconventional oil & gas-related activities. BNPP AM believes the finance sector should be a key engine to drive the energy transition for a sustainable future.

32. The motivation to address climate change in investments is the belief that climate change will have significant direct and indirect impact on the value of investments in the long-run. It has identified the activities it considers to be most at risk in terms of tighter regulation, higher costs, or physical damages.

33. As an asset manager, it is BNPP AM’s duty to protect the value of its client’s investments, and it has developed a 3-fold strategy to do so: allocation of capital, responsible stewardship, and transparency.

34. In order to assess the climate risk BNPP AM and its investors may be subject to, it is key to understand how companies manage their climate risks, their level of climate-related performance, and the rate at which their performance is improving. BNPP AM expects companies to disclose according to the TCFD recommendations as far as possible. BNPP AM also has established sector-specific thresholds at which it will screen out companies from allocation.

35. As a signatory of the Montreal Carbon Pledge, BNPP AM publishes the carbon footprint of many of its equity funds. BNPP AM aims to progressively publish the carbon footprint of all equity funds, this however is subject to data availability from companies. BNPP AM expects companies to disclose in line with its commitment to publicly report carbon footprint of portfolios, have sound environmental performance, and have clear plans to align themselves with the goals of the Paris Agreement. BNPP AM has developed a methodology for measuring the carbon footprint of funds.

36. BNPP AM assesses company alignment with the transition pathway, for example an assessment of utilities. BNPP AM has adopted a carbon-free policy for their Sustainable and Responsible Investment funds, establishing sector-specific thresholds and standards.

37. Where corporate performance or disclosure is lacking, BNPP AM may engage companies to encourage uptake of enhanced practices, strategies and disclosure. BNPP AM engages companies through dialogue, by exercising voting rights as a shareholder, and through membership of various initiatives and coalitions. They

favour constructive engagement and do not always adopt a divestment strategy.

Questions & Answers

38. **Question:** Climate-related policies vary across jurisdictions. China is an example in which policy can be changed quickly with little or no prior consultation. How can we take into account the different transition risks across geography?

    Answer: A policy mapping exercise first has to be done to assess the transition risk across regions. This then needs to be related back to the characteristics of a portfolio. This is a complex exercise, but the investor community should let data and service providers know that there is such demand, and to work with them so that this service can be scaled up quickly.

39. **Question:** Are there any assessments for PRI signatories to ensure they are investing responsibly?

    Answer: Each signatory is required to report annually to PRI, and there are assessments based on that report. PRI acknowledges that different organisations are at different levels in terms of awareness and capability to address climate risk. PRI welcomes those who may just be starting this journey. However, if the signatory still falls below standards after 3 years, PRI will engage the company to understand which areas it may need help in. There is a possibility that organisations can be delisted if they remain below standards afterwards.

40. **Question:** Is disclosure from companies keeping pace with the expectations of the investor community? Are the disclosures being verified?

    Answer: In Asia, many companies are still at the stage of just beginning to disclose. So at the moment, there is not the luxury of verifying disclosures in a robust way. However, since disclosure is done as part of a company's financial reporting, it should be done with integrity and professionalism. So it should be reliable. On the other hand, voluntary disclosure still varies greatly between companies. There needs to be consensus amongst investors on specifically what type of data is most helpful. The Global Reporting Initiative standards and TCFD recommendations is taking us towards that direction, and given these already existing frameworks, corporates should be prepared to respond accordingly.

A group exercise was also undertaken. Key points emerged are shown in the Annex.

Acknowledgements

BEC is grateful for the generous support of member companies[11] of the Steering Committee of BEC CCBF AG, who have provided financial support for the workshop and report.

BEC thanks the supporting organisations of the workshop: Asia Investor Group on Climate Change, CDP, International Capital Market Association, and PRI (acknowledged in alphabetical order).

BEC also thanks the speakers for contributing to the workshop and the development of this report. BEC staff Ms Maya de Souza and Mr Jonathan Ho led the workshop organisation and report writing.

About BEC & BEC CCBF AG

Business Environment Council Limited ("BEC") is an independent, charitable membership organisation, established by the business sector in Hong Kong. Since its establishment in 1992, BEC has been at the forefront of promoting environmental excellence by advocating the uptake of clean technologies and practices which reduce waste, conserve resources, prevent pollution and improve corporate environmental and social responsibility. BEC offers sustainable solutions and professional services covering advisory, research, assessment, training and award programmes for government, business and the community, thus enabling environmental protection and contributing to the transition to a low carbon economy.

BEC Climate Change Business Forum Advisory Group ("BEC CCBF AG") promotes awareness of, and builds capacity in relation to, climate change mitigation, adaptation and resilience activities amongst the BEC membership and generally amongst the

[11] http://bec.org.hk/about-us/bec-climate-change-business-forum-advisory-group

business community in Hong Kong. It also aims to provide a platform for BEC to engage relevant regulatory bodies on climate change related matters, and forge collaboration links between local and global expertise on climate change.

Disclaimer

Annex: Group Exercise

The Workshop involved a group exercise with six groups considering the following scenario and working through the questions below. Key points made are set out below.

Scenario: You are managing a fund which invests in real estate in Asia. After the devastating impact of Typhoon Hato on Macau, hurricanes and power outages in Puerto Rico, floods in Taiwan and bush fires in California, you have been asked to re-evaluate the investments held by the fund taking on board “climate risk” and to ensure that there is a clear understanding of the range and severity of risks involved as well as the opportunities that will arise.

Question 1: In terms of establishing whether relevant climate risks have been properly mitigated or opportunities taken on board by the relevant companies, what aspects of the company and its practices do you consider to be of greatest importance having regard to the TCFD approach and your own knowledge and experience?

Answers:

- As well as the four parameters in the TCFD recommendations, should look at whether the company has insurance coverage, and whether it has done a risk assessment to assess if the extent of insurance coverage is sufficient.
- Look at the company's risk awareness, whether it has a plan to manage and monitor risks, whether it has a governance structure for strategic oversight and to capitalise on opportunities.

Question 2: What information would you hope to find within the sustainability report or company annual report to investigate these issues? How confident do you feel in relying on the data provided by the company in their reports? What are the key performance indicators you would ideally disclose against to give an indication of your company's climate resilience? What metrics/units of measurement would you use?

Answers:

- Where are the assets located geographically – are those areas prone to disaster?
- Are there historical cases of extreme events and how did the company respond?
- What is the company's energy consumption, carbon intensity, and what climate actions are being taken?
- What is the company's risk assessment approach?
- How the company would perform in a stress test against IPCC scenarios?
- Would like the company to disclose possible opportunities and financial returns, in addition to risk.
- Third party verification of data would be beneficial.
- What are the company's KPIs? Are there business continuity plans?

Question 3: What would you do if you cannot find this information or need more or better information? What sort of questions would you consider putting to the relevant companies? What issues would you raise with them? Which other tools would you use to help with your analysis e.g. MSCI tools?

Answers:

- Will use MSCI tools for analysis, and refer to CDP reports for more information.
- Understand their governance structure. Is there strategic oversight regarding long term risks?

- How are they doing their sustainability materiality assessments? Are they taking on board evidence?
- What policies does the company have as to climate more generally?
- Has the company done stranded assets scenario planning? How reliable are the assets and what is their lifetime?
- How is the company transitioning more generally? Shouldn't look at climate risk in isolation from other issues.
- And investors should consider the whole value chain, beyond the company's own operations.