BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY

Mary Creagh MP
Chair, Environmental Audit Committee
House of Commons
London
SW1A 0AA

Sarah Breeden
Executive Director
International Banks Directorate
T 020 7601 4474
sarah.breeden@bankofengland.co.uk

1 February 2018

Dear Ms Creagh,

In light of the Environmental Audit Committee's (EAC) green finance inquiry, I thought it might be helpful to summarise the work the Bank of England has in train to ensure the UK financial system mitigates the climate-related risks associated with the transition to a lower carbon economy. As you would expect, our work is focused on those issues relevant to advancing our statutory objectives for monetary and financial stability.

Mitigating climate-related financial risks and greening the financial system

As we have set out, the Bank has taken a series of steps to mitigate the climate-related risks faced by the financial system.[1] This has focused on assessing the financial risks that might arise via two primary risk factors (or channels). First, the physical risks that arise from the increased frequency and severity of climate and weather related events. Second, the transition risks that can arise from the process of adjustment towards a lower carbon economy, such as shifting investor sentiment, new disruptive technology or developments in climate policy.

The Bank's work began with a PRA-led prudential review of climate-related risks to the UK's insurance sector, undertaken to coincide with the second round of DEFRA's climate change adaptation reporting.[2] The PRA is currently undertaking a review of climate-related risks to the UK's banking sector, to be published in the coming months. That will support the PRA's participation in the third round of climate change adaptation reporting.

Most recently, the Bank became a founding member of the Central Banks and Supervisors Network for Greening the Financial System.[3] The Network, announced at the One Planet Summit in Paris on December 12th 2017, consists of eight central banks and supervisory authorities, who have agreed to share experiences and best practice on the supervisory and macrofinancial dimensions of climate-related and environmental risks as well as on options to scale up green financing. The Network will hold a high level conference focused on climate risk management and supervision on April 6th 2018 in Amsterdam and conduct a stock-taking exercise during 2018.

As part of the Bank's efforts to ensure the transition to a low carbon economy is financed efficiently and prudently, the Bank, on behalf of the UK, has co-chaired – with the People's Bank of China – the G20's Green Finance Study Group (GFSG), which was established under China's G20 Presidency in 2016. The GFSG has a mandate to "*identify institutional and market barriers to green finance and, based on country*

---

[1] See Scott, van Huizen and Jung, (Q2 2017), *The Bank of England's response to climate change,* Quarterly Bulletin, 2017 Q2.
[2] https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/publication/impact-of-climate-change-on-the-uk-insurance-sector.pdf
[3] https://www.bankofengland.co.uk/-/media/boe/files/research/greening-the-financial-system-statement.pdf

experiences, develop options on how to enhance the ability of the financial system to mobilize private capital for green investment." A summary of the Group's work from its first year, the Green Finance Synthesis Report, was published and welcomed for the G20 Summit in September 2016.[4] The report identified seven options for scaling up green finance. The GFSG called for greater consistency and standardisation of terms and conditions for green bonds and facilitated development of a best practice document to support the widely-accepted Green Bond Principles, for example.[5]

The Bank has also sought to support a number of external initiatives to strengthen London's role as a global green finance centre. For example, the Bank co-chairs a bilateral working group on green securitisation as part of the UK-China Green Finance Task Force, focusing on commercial and operational solutions to help issuance of green covered bonds and other securitised structured bonds. The overall project is being led by the Chinese Green Finance Committee and the City of London's Green Finance initiative (GFI). In addition, the Bank attends the UK Green Finance Taskforce, established by the Department for Business, Energy and Industrial Strategy and HM Treasury, as an observer.

Enhancing climate disclosure

Through the Bank's membership of the Financial Stability Board (FSB), and Governor Mark Carney's role as Chair of the FSB, we have supported G20 work to mitigate climate-related risks to financial stability through enhanced disclosure.

Markets need the right information to manage the risks from, and to facilitate the transition to, a low carbon economy. Until now, that information has been absent. A minority of companies disclose climate-related metrics[6], and with over 400 competing disclosure regimes around the world, companies that wanted to disclose often did not know what to report or how to report it.[7] In April 2015, G20 Leaders called on FSB to consider climate risk. In December 2015, the FSB launched the industry-led Task Force on Climate-related Financial Disclosures (TCFD) to develop recommendations on voluntary climate-related financial disclosures.

The private sector industry-led Task Force, chaired by Michael Bloomberg, includes users and providers of disclosures, major companies, large investors, global banks and insurers, the major accounting firms and largest rating agencies. The TCFD has concentrated on the practical, material disclosures most relevant to investors and creditors and which can be compiled by all companies that raise capital. The Task Force's recommendations were published in July 2017 at the G20 Leaders' Summit in Hamburg.[8] They focus on four areas critical to how real-world businesses operate: governance, strategy, risk management, and metrics.

While the recommendations can be adopted by firms of any size in any sector, they also provide specific guidance to those industries most affected by climate change. They tackle not only the most obvious physical risks related to climate change but also the less straightforward financial risks that come from the transition to a lower-carbon economy. Importantly, they help investors understand how climate risk is likely to impact a business's strategy and operations in the future.

---

[4] http://unepinquiry.org/wp-content/uploads/2016/09/Synthesis_Report_Full_EN.pdf

[5] https://www.whitecase.com/sites/whitecase/files/files/download/publications/client-alert-green-bonds-an-introduction.pdf

[6] Sustainability Accounting Standards Board (2016), October Technical Bulletin

[7] OECD (2015) *Climate change disclosure in G20 countries*

[8] The final TCFD report can be found on the FSB website (https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Report-062817.pdf), as can additional annexes on implementation (https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Annex-062817.pdf), scenario analysis (https://www.fsb-tcfd.org/wp-content/uploads/2016/11/TCFD-Technical-Supplement-A4-14-Dec-2016.pdf).

The EAC has asked whether a voluntary approach to TCFD implementation is likely to be sufficient. The Bank is of the view that at this stage it is important for TCFD adoption to be voluntary. The TCFD designed their recommendations with the aim of creating a virtuous circle whereby firms voluntarily adopt the recommendations, investors respond by making clear which disclosures are of particular value, and firms learn by doing as good practice emerges. The Task Force intends to report on the first year of implementation to the G20 Leaders' Summit in Argentina in November 2018, including by identifying good practice which may have wider application. Good quality disclosures will ultimately be driven by firms innovating and investor pressure incentivising firms to take their lead from the best quality disclosures.

The area with the clearest need for further development is scenario analysis and planning. To support the conversation between scenario developers and potential scenario users, the Bank of England co-hosted a conference with the TCFD in November. This was attended by representatives from across the financial sector, industry, international organisations, civil society and academia and was the first step in sharing experiences and expertise on scenario analysis.

The TCFD recommendations have huge momentum and are bringing climate-related disclosures into the mainstream. The number of leading companies supporting TCFD had risen to over 230 by late 2017, with those companies having a combined market capitalisation of $6.5 trillion. Supporters range from consumer staples to industrial and energy giants, from transportation companies to the world's largest extractors. And they include institutions from across the full financial ecosystem, responsible for assets of over $80trn, and including 20 globally-systemic banks (and the six largest UK banks), 8 of the top 10 global asset managers, the world's leading pension funds and insurers, its largest sovereign wealth fund, all the major ratings agencies and accounting firms, and the two dominant shareholder advisory services companies.

Conclusion

Climate change and society's responses to it, presents financial risks which impact upon the Bank's objectives. The Bank is responding to these risks by engaging with regulated firms through prudential supervision. This includes refreshing earlier analysis on the insurance sector and expanding this to consider climate-related risks to the UK banking sector.

The Bank is also enhancing the resilience of the financial system by engaging with initiatives to support an orderly market transition to a lower-carbon economy. This includes taking a close interest in initiatives to enhance climate disclosure, and liaising with other Central Banks and financial regulators, for example, by playing an active role in the Network for Greening the Financial System.

We consider that this response to climate change helps ensure the Bank is playing its part, in line with its mandate, to address the financial risks from climate change.

Yours sincerely

Sarah Breeden
Executive Director