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GLOBAL BANK REVIEW: ESG PERSPECTIVES

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With ESG edging into finance's mainstream, the Global Bank Review canvassed three senior figures on how climate change and rising social obligations are impacting their institutions. Green Investment Group Asia head Ivan Varughese, UBS global head legal, sustainable finance Aleksandra Schellenberg, and Barclays' sustainable finance leader Marco DeBenedictis share their insights.

This article is part of our *2021 Global Bank Review – ESG: Creating a purposeful future*, an annual publication by our Global Banks Sector Group which brings together our people who live and breathe banks.

IV - Ivan Varughese (Head of Asia, Green Investment Group, Macquarie Group)
MD – Marco DeBenedictis (Head of Sustainable & Transition Finance, Barclays Corporate Banking)
AS - Aleksandra Schellenberg (Head Legal, UBS Global Wealth Management, Chief Investment Office Research; Global Head Legal, Sustainable Finance, UBS)

How have attitudes, policies and operations shifted on ESG factors in the last three years?

IV: On climate there is now broader consensus on the need to act and so the focus has shifted to how we come together to deliver this action. Corporates and financial institutions are seeing further growth in demand for environmental and social finance, often associated with infrastructure and energy. ESG factors are increasingly taking centre stage within investment strategies, with Asia set to become the next frontier for sustainable investing.

MD: Over the last three years, we've seen a hyper-growth period in awareness towards ESG. We're observing much more development in corporate strategies as the market matures. The governance, the way businesses look at their supply chains has been enhanced. There's also the well-being perspective. What was previously accepted as an employee may no longer be – something employers have to consider in a post-Covid world.

AS: It's changed significantly. Sustainability became a boardroom topic. This shift not only impacts policies on corporate governance, it impacts investment decision making. One of the reasons behind this shift is the rapidly growing awareness of sustainability among clients. European asset holders already predict systematic environmental risk will be more important than financial risk within three-to-five years. Covid plays an important role. It sharpened understanding of the importance of sustainability and accelerated the discussion with our clients because they now understand the risks of not addressing the topics.

Banking is historically pretty hard-nosed, are young bankers looking to sustainable lending as a place for ambitious professionals?

MD: Sustainability strategies are definitely top-of-mind for many young professionals, and this is understood by employers. Combining traditional lending practices with the opportunity to create something new is certainly a talent empowerment tool. Graduates, Gen Z – they think about the mission of the company.

What are your greatest ESG concerns or risks to manage?

MD: A lot stems from reputational impact – positive and negative. The positive side is: what is your role as a thought leader? How consistent are your external messages with your policies? That has a second-order effect on things like share price and shareholder expectations. A lot of progress has been made in consistency and transparency. Go back to fundamental economic principles, the more transparent and liquid the market, the narrower the spread and more visibility on the value of assets you hold. That's critical from an ESG perspective.

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Marco DeBenedictis

AS: My biggest concern is that ESG risk is discussed mainly as reputational risk and seen as ring-fenced. When speaking to members of various industry associations I often hear that ESG risk will not impact financial institutions´ bottom lines because it's just reputational risk. There is still not enough awareness how connected the risks are. We shouldn't look at this as reputational risk without significance for the financial performance. This is my personal mission to get this message across the industry.

The EU Taxonomy is a major shift in the environment. Any thoughts on how that plays out?

MD: This is a great step as it's more robust for all stakeholders, following a market standard. If our borrowers have four banks and are all talking the same language around sustainability, then it's clear there is consistency and you can compare like-for-like.

AS: The Taxonomy can become a very powerful tool to eliminate the confusion around sustainability-related terminology. It's not likely to happen short-term though. It is very complex and prescriptive. In addition, sufficient ESG data is not available. I expect many financial institutions will struggle to report the alignment of their investments with the Taxonomy until that improves.

"[World Economic Forum] research shows Millennials and Generation X will in the next 30 years potentially inherit US$40 trillion – they want to invest this sustainably and banks need to have solutions for them or they will go elsewhere."

Aleksandra Schellenberg

How will ESG impact investment and business strategies in the next three-to-five years?

IV: We're likely to see this impact increase significantly – you only have to look at the progress over the past 12 months to see the shift taking place in boardrooms and right through organisations.

Macquarie announced it will become a member of RE100, a global corporate leadership initiative bringing together businesses committed to 100% renewable electricity, and will source all the energy supplying its premises and data centres from renewable sources by 2025.

MD: Continued standardisation and transparency, for sure. We often hear investors and lenders talking about embedding ESG into everything we do and I expect this trend to continue. Through the 2020s we'll see each loan over a certain size, or for businesses over a certain size, to have some form of sustainability metrics attached.

AS: Sustainability will move from being seen as "going an extra mile" to becoming the norm. The current generation of clients are demanding the priority of banks should not only be financial performance of their products, they should also have positive impacts on the planet and people. [World Economic Forum] research shows Millennials and Generation X will in the next 30 years potentially inherit US$40 trillion – they want to invest this sustainably and banks need to have solutions for them or they will go elsewhere. Therefore, I expect more banks will:

- Redefine their strategic initiatives and, as UBS, apply long-term lens that not only focuses on financial targets but equally considers positive impacts on the planet;
- Expand their sustainable product shelf. We will see more sustainable mortgages, loans and saving accounts;
- Start a dialogue with clients about the importance of ESG considerations; and

We can expect more rules and regulations, in particular in the lending space and ESG ratings.

Greenwashing is much discussed, how difficult is it for a bank to manage conflicting pressures in the area?

MD: It's appropriate to have a glide path to assess our clients' transition. We feel it is right to have taken an engagement strategy for those businesses. We know these businesses care about sustainability and we believe they also hold many of the resources to unlock how to get to a net-zero world. We're adopting a transparent engagement model, as we recognise the cost of getting it wrong is high.

Any thoughts on how to rebut greenwashing claims or be clear you have a robust process?

MD: The key thing we've had to define is: "What does net zero mean for a bank?" Barclays has a large capital markets franchise – that doesn't sit on our balance sheet – and so how do we have a responsible strategy around our financing, when we are not holding many of these assets? As such, we've invested resources into a model, publically available, as we believe transparency is the only way we can make real progress.

How much momentum is there in sustainable lending and are there barriers that would be helpful to remove?

MD: Momentum is really high. A lot of volume is driven by capital markets and there's a trickle-down effect in syndicated loans, then trade finance and the SME market. What happens in the SME space will drive large corporate behaviour tomorrow. The barrier is often time and education.

Any advice in trying to build a sustainable finance business or tackle any other aspect of ESG?

MD: Consistency with your external messaging is key because stakeholders can see through any inconsistency. You also have to develop an ESG strategy based on your strengths as an institution, so you can ultimately give shareholders the return they expect.

What is your bank's general approach and priorities regarding ESG?

IV: The organisation as a whole views the commitment to ESG performance as part of our broader responsibility to clients, shareholders and the communities in which we operate. Macquarie’s ESG approach is structured around eight focus areas considered material to our business. The eight focus areas include environmental and social risk management; environmental and social financing; climate change; sustainability in direct operations; client experience; people and workplace; business conduct and ethics; as well as the community.

AS: For over two decades now, sustainability has been one of the top priorities for UBS. Our CEO makes it clear: sustainability must be part of our DNA, a core part of our purpose: reimagining the power of investing; connecting people for a better world. We aim to pro-actively help clients transition to sustainable ways of doing business, to ensure their long-term success and support them in fulfilling their responsibility to society. Ninety percent of wealthy investors want to align their investments with their values – UBS will continue to lead in sustainable finance.

How much momentum is there in green investment and lending currently?

IV: The Asian region is predicted to see up to US$250 billion of new investment flow into utility scale renewable energy projects by 2025. Offshore wind energy is reshaping local industries and revitalising economies across Asia.

AS: Over the past few years, sustainability has been moving into the mainstream, driven by increased transparency, regulation and investor demand. Globally, [sustainability] focused funds have reached a record high, exceeding the US$2 trillion mark in 2021. We believe this will keep gaining momentum.

“The important work in achieving a shared commitment to net zero has been done. The challenge for the rest of this decade is on advancing the practical solutions we need to get there."

Ivan Varughese

What's your advice to peers for managing ESG risks or opportunities?

AS: Talk to your clients. Make them aware of the impact of their investment decisions on ESG factors. Talk to other banks – talk about disclosures and reporting standards and what really works and what doesn't work. Talk about solutions that would be helpful to manage ESG risk. Also, talk to regulators. Understand what regulators want to achieve and suggest ways you can give it to them. That way it's a win/win solution.

What are your big predictions for how investment and finance will evolve to respond to the ESG agenda during the 2020s?

IV: The important work in achieving a shared commitment to net zero has been done. The challenge for the rest of this decade is on advancing the practical solutions we need to get there. To date, much of the investment into renewables has been supported by governments, either through feed-in-tariff regimes or reverse auctions. Going forward, we expect to see increasing demand come directly from the customer side as corporates take the initiative to procure zero-emission solutions for their own needs. We will also see new markets emerge for technologies such as storage.

MD: We are reaching a very different level of maturity and it's ingrained into every conversation. Each product you have as a bank will have a sustainable variant – it might not be priced the same but there will be a version so there's consumer choice. Particularly in my area of syndicated lending, it will be the rule rather than the exception to have some kind of sustainability performance targets in financing.

AS: Sustainability will become the norm. Clients will realise sustainability doesn't mean charity and investments in such products yield comparable returns to traditional investments. There will be an increase in the number and variety of ESG-purposed products across the banking sector. Rating agencies will become new, strong players. And greenwashing disputes will lead to clearer taxonomies and transparency where clients are able to better distinguish the quality of sustainable products.

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