

ADVANCING THE UK TRANSITION

On 25 June 2024, the PRI hosted a conference dedicated to investing for sustainability impacts (AM session) and advancing the UK transition (PM session) as part of London Climate Action Week. The PM session brought together UK policymakers, regulators, and investment industry stakeholders to discuss sustainable finance policy priorities for an incoming UK government, with a focus on priorities which can facilitate a successful transition to a sustainable and equitable economy that benefits natural and social systems.

The sessions delved into key policy developments related to the UK's transition, including:

- a stocktake of the UK landscape and trajectories;
- a discussion on the place of regulation; and
- market leading practice and policies on the transition.

The discussions showcased policies and signals to make the UK an attractive destination for investment, rooted in overcoming perceived or existing barriers and drawing on best practice across the globe. The value of a transition planning ecosystem in building momentum for the transition was emphasized, with crucial roles for both investors and policymakers in this ecosystem. A dive into the place of regulation responded to the important question of how policymakers and investors can work together to create a positive, sustainable regulatory environment and support the transition.

This document presents a summary of the points raised throughout the PM session. The views presented in this summary do not represent the positions of PRI.

STOCKTAKE OF THE UK LANDSCAPE AND TRAJECTORIES

This session began with a factual overview of the UK's sustainable finance architecture, pointing to the key policy developments that have taken place to date. Whilst there has been some progress towards a green economy, market perception is that there is still a lack of clarity on what this entails. The UK has seen the Financial Conduct Authority's (FCA) Sustainability Disclosure Requirements (SDR) and investment labels regime finalised, alongside the FCA's anti-greenwashing rule; publication of the Transition Plan Taskforce (TPT) guidance and plans for bringing the International Sustainability Standards Board (ISSB) framework into UK law. More broadly, the UK has decarbonised its power sector faster than many other major economies.

The UK as an attractive place for investment

The panel discussion then turned to making the UK an attractive destination for green investment. The ability to deliver on returns and the availability of capital was highlighted as a strong prerequisite for this. Solvency UK and Mansion House Compact were noted as important first steps. With private capital still not flowing at the necessary pace in the UK, and in the context of the US' Inflation Reduction Act directing capital towards the US, a point on failing to create the UK as an investment destination on par with other countries was raised. Equally, changing targets, such as the recent rollback of net zero policies, has led to some distrust from industry in the government's ability to create a sustainable investment destination.

To make the UK a more attractive place for green investment, panellists pointed to the need for a broad direction of travel towards net zero, with the right policies and regulations that investors can trust to meet net zero. Subsidies pledges were also flagged as a crucial tool. Whilst a sustainable finance architecture is broadly in place in the UK, real economy policies to stimulate and fast track sustainable investment will be important to shift capital.

Overcoming barriers

The UK has already pledged to be a world leading green finance hub and should maintain this ambition. However, research by the Climate Change Committee (CCC) shows that the transition is not on track, and coupled with misaligned incentives, such as North Sea oil and coal mine licenses, the policy framework is out of sync with the transition to net zero. Panellists emphasised that the UK government should address this by with a clear industrial strategy that indicates what a net zero future looks like and where the investment opportunities are. This strategy should build consensus around a long-term stable plan to reach net zero and to rebuild investor confidence. Moving from commitments to delivery was a common thread throughout the discussion, with a need/ask for clear decarbonisation roadmaps across the next 10-15 years, along with investment plans for investment in priority sectors. In terms of policy engagement, it was highlighted that regulators would work faster and better with market support, with policy reforms geared towards the investable universe and the revival of

industrial policy. Policy interventions on transition plan requirements will be required for investors to meet their objectives for long-term returns and to succeed on their transition plans.

The UK could learn from other geographies on accelerating the transition. Australia has taken Net Zero Economic Authority [budgetary measures](#) dedicated to priority transition industries, and intended to support workers, regions and communities in the economy-wide net zero transition. The Australian government has also worked with investment community to identify investment opportunities, increasing confidence on capital flow for these areas, and with a clear risk return.

Addressing social inequalities

In response to concerns on the cost of the transition for the taxpayers and impacts on communities, panellists noted that investment in the transition will create growth in the economy. The UK's [Social Factors Taskforce](#) was also raised as an example of breaking down barriers to investment. Social factors are no less material, but harder to measure than climate factors. The Taskforce delivered a report which produced a materiality analysis of social factors to be implemented and used by industry. The FCA could support this by looking into mandatory social impact measurement.

Taking this further, to best ensure that workers share the benefits of the transition, Australia have set up the Net Zero Authority on just transition and Scotland have a just transition Commission in place.

THE PLACE OF REGULATION

Over the past few years, sustainable finance regulations have increased significantly across the world, including new and revised/updated policies on disclosures, labelling, taxonomies and non-financial disclosures amongst others. This reflects a welcome focus from governments in ensuring that financial entities play an active role in the transition, as well as creating the right policy environment to ensure a shift towards net zero financial centres. However, discrepancies in approaches across jurisdictions, asset classes or a lack of coordination with the private sector can sometimes create issues in implementation of these regulations and create unintended, adverse consequences.

The objective of this second panel was to engage on the role of regulation in driving the UK's transition to net zero, and looking at how policymakers and investors can work together to create a positive, sustainable regulatory environment and support the transition.

The regulatory landscape

The panel began with an assessment of the UK's regulatory approach to the transition. The panel discussed the limits of voluntarism, with a purely market-led approach lacking the power to compel alignment. Therefore, the role of regulatory intervention should be considered where there are risks to the public interest. In the UK, the FCA's mandates on market integrity, competition and consumer protection offer a case to consider regulatory intervention.

The ESG landscape is dynamic, fast-evolving, and innovative. In such a context finding the right balance between principles and prescription was emphasized for sustainable finance policy development. Here, a case for a conveyor belt approach to regulation was made, which would link different types of governance tools together to help create a high-integrity governance ecosystem around net zero. This approach can start with the market and voluntary measures, then progressively building into regulation.

Investors subject to UK regulation then explained their experience of complying with the Taskforce for Climate-related Financial Disclosures (TCFD), Stewardship Code, SDR, and the anti-greenwashing rule. The notion of proportionality and fairness for smaller asset managers and asset owners was raised, with smaller organisations spending more time on compliance than investment decisions and engagement. The consistency of regulation was also raised, posing the question of whether high carbon sectors are regulated as much as those producing transition plans.

Spotlight on pensions

Two thirds of UK pensions funds have committed to a net zero target and would take action without regulation because of two key concepts – fiduciary duty and investment freedom. Fiduciary duty is the legal responsibility to act solely in the best interest of members, whilst investment freedom relates to the freedom to choose investments which secure the interest of their members.

More broadly, the panel considered the intentions of regulation, and whether it was achieving these aims. For TCFD application to pension schemes, the intentions were better training and education at the investment decision-making level, better risk management, a nudge for capital allocation towards climate solutions. Currently, investor education and understanding are high. However, capital allocation towards climate solutions have not flowed. Long-term climate risks are still being analysed as immaterial, with poor data, which called into question the utility and value of climate scenario analysis. To resolve this gap, intention must be matched with delivery, with a frequent self-assessment on whether regulation is achieving its aim.

The way forward for regulation

Panellists indicated that it was crucial for regulators to engage deeply and actively with market participants – bilaterally, through trade associations, membership bodies and beyond. Such engagement ensures that regulators develop a comprehensive and usable sustainable financial framework that responds to industry needs. This accelerates progress by leveraging insights from the market and leads to better policy outcomes, consistent with the conveyor belt approach.

The Transition Plan Taskforce (TPT) serves as a strong model for how public and private sectors can come together to decipher what constitutes as a credible and effective transition plan that can be regulation ready and rolled out across the economy. There was strong support for this work, which will now be taken forward by the IFRS Foundation, expanding the remit of the TPT's work globally.

FIRESIDE CHAT – ACTORS OF THE TRANSITION

A fireside chat between actors of the transition drew upon insights from the Transition Plan Taskforce, IOSCO, and the Transition Finance Market Review. The discussion emphasised the importance of building momentum on the transition planning ecosystem.

Recognising that momentum on the transition has built over the last few years, the strategic benefit of transition planning and turning targets into concrete, costed implementation actions has become increasingly accepted. The TPT has played a huge role alongside GFANZ to bring transition planning into the mainstream and provide guidance.

Transition Finance Market Review

The Transition Finance Market Review sought feedback on how to create a leading market for high quality transition finance in the UK. It looked at how to optimise opportunities for UK financial and professional services and build on the TPT by thinking about how transition plans can assist the flow of capital to hard to abate, high-emitting sectors.

The Review's proposed approach was sector and asset class agnostic, with a focus on high-emitting sectors. There was strong support that transition plans will constitute a helpful cornerstone of high-quality transition finance, with an important role at the organisational level as a strategic action plan to turn targets into concrete actions built into business planning. In comparison, a taxonomy would have more relevance at the activity level. Feedback from the Review also highlighted that national sectoral pathways were crucial, given that there is no one-size-fits-all approach to transition planning. Lastly, blended finance and sequencing came through as strong enablers of the transition, with the possibility of scaling up blended finance through greater interaction with multilateral development banks.

A transition planning ecosystem

Next, the speakers discussed the transition planning ecosystem. They highlighted that the shortfall in transition finance was less about a scarcity of available capital, and more about the scarcity of commercially viable, scalable investment opportunities. In the UK, it was noted that there is a lack of planning and certainty, with an absence of sufficient targeted catalytic blended finance or use of guarantees. This speaks to the need for national transition planning to sit above private sector transition plans, with transition finance to leverage these plans.

The development of a national transition plan or strategy was raised as an evolution of government's existing commitments under the Paris Agreement. A national transition plan would build on the pillars of the TPT's framework, supporting private sector transition plans. Providing a clearer direction of travel and offering incentives for the transition will be at the core of an integrated transition planning ecosystem, and leveraging the pillars of TPT's framework was noted as critical. An emphasis on engagement was noted, allowing private sector actors to highlight policy and technology barriers as well as inform a costed action plan for government.

On a more granular level, condensing high-level government strategies down to where capital needs to be spent across different sectors of the economy would create a strong foundation to identify the capital required from the public sector and from the private sector. This would also shine light on the barriers that need to be overcome to create an enabling environment for private capital to flow.

From an international perspective, there are increasing calls for national transition plans across the globe. Looking ahead, the next round of nationally determined contributions (NDCs) should serve as investment plans for the future. Here, there is an opportunity to embed this thinking within a developed framework and engage with multilaterals.

MARKET-LEADING PRACTICE ON THE TRANSITION

Beyond financial regulation, real economy policies and whole of government integration of sustainability targets are crucial to achieving a just transition, bringing along industry and communities alike. As financial institutions, academics and governments grapple with this topic, this panel looked at market and policy tools to accelerate the transition and high-integrity capital raising, and how to ensure strong and effective cross-sector collaboration.

This panel was intended to provide the audience with an understanding of what is needed to bring the private sector along with policy developments, and how the UK can establish its role as a market leader on the transition.

Securing a just transition

The LSE and Transition Pathway Initiative (TPI) have developed Assessing Sovereign Climate-related Opportunities and Risks (ASCOR), an investor-led framework of indicators to assess how countries are mapping the low-carbon transition and the impacts of climate change. Amongst other elements, the indicators cover: whether the country has ratified fundamental human, labour, and indigenous rights; an inclusive and institutionalised approach on just transition; a green jobs strategy; and integration of just transition into carbon pricing.

Whilst the UK has developed a Green Finance Strategy, this analysis confirms that an inclusive and institutionalised approach is lacking. The closure of two major steel plants in Port Talbot, the UK's largest single emitter of carbon dioxide, putting 3,000 jobs at risk, was set out as an example of a case where the impact of the transition on local communities has been overlooked. Panellists highlighted good examples from Scotland, South Africa, and Spain where just transition planning has been prioritised and resulted in positive outcomes.

The investor angle

On metrics, some investors clarified that whilst they were in the process of gathering emissions and human rights data, there was lack of robust data on transition metrics. Additionally, this data was often only examined on a case-by-case basis.

Investor action on the transition to date has focused predominantly on engagement strategies and initiatives. A measured and achievable approach, with consensus from stakeholder was highlighted as a standard for best practice for engagement. For example, from a social impact lens, considering a disproportionate amount of household income will go on energy bills, exploring social housing projects offers an opportunity for investors to take action in securing cheaper energy with greater investment renewables. A further example was given on engaging with companies to disclose scope 3 emissions alongside scope 1 and 2, in order to bring the whole value chain along to act on net zero.

Additional levers such as setting ambitious goals for climate change; capital allocation to companies aligned with the transition, contributing to climate solutions and innovation; engagement with every company invested in; and policy advocacy to shift norms were also discussed. An investment framework that enables investors to consciously allocate capital was highlighted as a key enabler.

Solutions

Panellists agreed that current financial regulation alone is not successfully shifting financial flows towards the transition at the pace and scale required. Instead, as mentioned in previous panels, real economy policies were needed, with clear market signals making a significant difference. Regulatory stability was also noted as an important driver of investor behaviour.

Whilst the UK has been a pioneer in developing robust climate legislation and early investment into renewables, recent government rollbacks on climate policies have undermined the UK's progress to date. Panellists suggested the focus should now be on energy efficiency, carbon pricing, and fossil fuel phase-out. Energy efficiency was showcased as a win-win, considering the potential for lower energy costs, a way to drive the just transition, and secure greater energy security. On carbon pricing, whilst the level of carbon price is important, the coverage of carbon price was also important to consider, such as the percentage of national emissions this represents. Carbon pricing should also be complements by subsidies. Finally, on fossil fuel phase-out, to date, new licences have continued to be granted for oil and gas exploration. Other countries, such as Spain, France, and Colombia have banned or set deadlines for exploration.

Ultimately, for the investment industry to support the transition, the risk and return calculation must be viable for investors. Currently, systemic climate risks are not being systemically considered under fiduciary duties. Managing systemic issues demands a wide range of tools to be deployed.