

LENDING FORESTS A HAND

RESULTS FROM THE CDP FINANCIAL SERVICES
CLIMATE CHANGE AND FORESTS PILOT 2020

EXECUTIVE SUMMARY

Limiting global temperature rises to well below 2°C will require both deep de-carbonization and, crucially, a halt to deforestation. The financial services sector will be critical in achieving the transition to a low-carbon, deforestation-free economy. Currently, the forces driving climate change and ecosystem destruction are deeply intertwined with our financial system. However, there are opportunities for the sector to be a key driver of change. Achieving net-zero will require massive investment in low-carbon technologies and sustainable agriculture, which only the financial sector can provide.

CDP aims to expand its questionnaires to cover a full range of environmental factors. For financial institutions, that means covering the impacts they have through their lending, investments and insurance underwriting. As a step towards that goal, and building on its existing work on climate change management within financial services, CDP worked with stakeholders to develop forests-related metrics for the financial sector, with a particular focus on the sector's funding of forest risk commodities (FRCs), which are the single largest cause of deforestation and forests degradation globally.

CDP has piloted the forests-related metrics with a select number of banks during the Financial Services Climate Change and Forests Pilot. The project was geographically focused on Southeast Asia – a high-risk global region for deforestation which lost 12% of its total previously forested area from 1990-2010; but also a region in which momentum is building behind the sustainable finance agenda.

The capital markets are a key audience for environmental data, but they also provide environmental disclosures. In 2020 CDP launched its first reporting framework specifically for the sector, focused on climate change portfolio impact. In delivering this pilot project, CDP integrated forests-related metrics into the existing reporting framework for financial services, rather than creating a standalone forests questionnaire. In doing so, CDP created the first structured, self-reported disclosure framework for forests-related information for banks.

The goal has been to involve the most significant lenders to the FRC sectors, harnessing our previous research on the topic. Out of the target group of banks invited, the response rate was 24%, resulting in a sample of 10 banks disclosing (seven ASEAN and three global). The participating banks are significant financial players, collectively holding loans of more than \$2.5 trillion, and accounting for over 19% of all lending to the FRC sectors in Southeast Asia. Five of the ASEAN banks had not previously reported to CDP, demonstrating that the project helped develop and deepen engagement, extending the benefits of environmental disclosure to the financial sector in a region expected to contribute significantly to global economic growth in the future. CDP used the reporting framework to engage with banks, using methods throughout the project which were collaborative and focused on awareness raising and capacity building.

KEY FINDINGS

Key findings from the pilot project:

Banks in the sample are aware of climate change and deforestation as issues that could impact their business...

They are already integrating environmental concerns into governance structures, financing policies, risk processes and engagement with clients.

There are areas that ASEAN banks can improve to catch up with their global peers...

They could aim to replicate best practices already implemented by leading global banks.

Banks tend to view the topics of biodiversity and nature holistically, rather than seeing deforestation as a standalone topic...

There is interest in tools that would allow banks to assess their environmental risks and for a more rounded environmental reporting framework for the financial sector.

Scope 3 portfolio emissions are the most significant source of GHG emissions for banks.

Portfolio emissions were over 400 times higher than operational emissions for the only participating bank able to disclose its portfolio emissions.

...although they focus mostly on one side of the 'double-materiality approach'.

The participating banks generally assess how environmental issues could affect their portfolios; they are less likely to assess environmental impact, particularly on forests.

...but disclosure on forests must improve overall, especially relating to the financing of forest risk commodities.

Only one bank disclosed their financing of key FRCs, as most do not yet conduct analysis on how their portfolios impact forests.

...however, their focus is often on upstream clients that have direct impacts on nature.

By using narrow definitions, some banks may overlook indirect deforestation risks in their clients' supply chains.

There are substantial opportunities for banks in financing the transition to a low-carbon, deforestation-free future.

The disclosure of potential financial impacts of environmental opportunities outweighs the disclosure of potential risks (including the anticipated costs to realize those opportunities).

Based on the findings CDP has directly drawn conclusions and recommendations for banks, as well as for investors and policy makers. In particular, CDP calls on banks to:

- ▼ Consider both sides of the ‘double materiality’ issue; in addition to assessing how environmental issues might affect their portfolios, banks should assess how their portfolios impact the environment, including forests.
- ▼ Assess their portfolio’s impact on deforestation throughout the supply chain (producers, processors, traders, manufacturers, retailers).
- ▼ Pro-actively engage with their clients to hold them accountable and guide them in their transition towards sustainability.
- ▼ Strengthen their reporting framework and fully disclose their lending practices, including their financing of FRCs.

There is an ever-greater need for robust, timely and actionable environmental data that the market can use to inform decisions. CDP intends to expand its questionnaires beyond its current questions on carbon emissions, deforestation and water security to include a full range of environmental factors as we are committed to accelerating global environmental ambition and driving action. For financial institutions, this means covering all environmental risks, opportunities and impacts driven by their lending, investments and insurance underwriting. The Financial Services Climate Change and Forests Pilot was a step towards that goal. As a next step, critical metrics will be included in our mainstream reporting framework for financial services companies in the future.





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