CONFERENCE OF PARTIES (COP 26) INSIGHTS

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> If climate disclosure and action fail to improve, then we risk blindly walking into a climate-driven collapse of global wealth, a so-called Carbon Crunch, which could prove ten times worse than the Credit Crunch.

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1. Overview of the COP

Globally, we are seeing the impact of climate change, and news about storms, floods, droughts, heat waves, species extinctions, and emerging pandemics among other catastrophes is overwhelming. Yet, perhaps the most frightening part is the fact that this chain of events is self-amplifying. Climate change is not theoretical anymore, and change is happening faster than expected, requiring desperate mitigation measures and effective action.

Since 1995, the United Nations Framework Convention on Climate Change (UNFCCC) has been holding a yearly Conference of Parties (COP). At the COP, global leaders gather to take momentous decisions to tackle climate change issues. The COP is considered as an opportunity for all climate change activists and leading players to come together, network, learn and eventually influence the decisions that the global leaders will take. Over the years, the COP has resulted in several global agreements that have shaped the world as we know it today, including the Kyoto Protocol, and the Paris Agreement. The ultimate objective of these agreements is to stabilize greenhouse gas (GHG) concentrations in the atmosphere at a level that will prevent dangerous human interference with the climate system, in a time frame which allows ecosystems to adapt naturally and enables sustainable development[1].

The year 2021 marks the 26th year for the COP, and it is being held in Glasgow, UK. Most experts believe COP 26 has a particular urgency, because countries are going to report on their 5-year Nationally Determined Contributions (NDCs) according to the Paris Agreement, which indicates that global GHG emissions should be limited to well below 2 degrees Celsius, aiming for 1.5 degrees Celsius. The Paris Agreement also aims to reach global net-zero emissions, where the amount of GHGs emitted equals the amount removed from the atmosphere, in the second half of the century. (This is also known as being climate neutral or carbon neutral.)[2]

In this insight, the major COP outcomes in relation to the goals will be summarized. In addition, it will highlight the importance and role of ESG/sustainability services in achieving global ambitions of GHG reductions.

2. COP 26 Goals

1.5^0

Net zero and 1.5 degrees

Countries are called on to reach **net-zero carbon emissions by 2050** and to keep global temperatures **below 1.5C**

Protect ecosystems and habitats

States are encouraged to **protect and restore ecosystems** and build resilient infrastructures to withstand climate change

Mobilise Finance

Developed nations are asked to mobilise **$100bn in climate finance** per year for poorer nations to tackle climate change

Collaboration

Parties at COP26 will need to **collaborate** to finalise the **Paris Rulebook**, which sets out the rules of the Paris Agreement

Source: UKCOP26 | Updated November 03, 2021

Goal 1

Secure global net zero by mid-century and keep 1.5 degrees within reach

Through accelerating the phase-out of coal, curtailing deforestation, speeding up the switch to electric vehicles and encouraging the investment in renewables.

Goal 2

Adapt to protect communities and natural habitats

Through protection and restoration of ecosystems. And building defenses, warning systems and resilient infrastructure to avoid loss of homes, livelihoods and even lives.

Goal 3

Mobilize finance

Through mobilizing at least USD 100 billion in climate finance per year by 2020.

Goal 4

Work together to deliver

Through finalizing the Paris Rulebook (the detailed rules that make the Paris Agreement operational). And accelerating action to tackle the climate crisis through collaboration between governments, businesses, and the public.

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3. COP 26 outcomes and pledges in-line with the Goals

Goal 1: Secure global net zero by mid-century and keep 1.5 degrees within reach

Some of the main highlights for achieving the first goal include:

- A methane pledge was signed by 100 countries, who committed to reduce global methane emissions by 30% by 2030
- Almost 90% of global emissions and over 90% of global Gross Domestic Product (GDP) is now covered by mid-century net zero or carbon neutrality commitments, which is 60% more than 2019 commitments
- More than 40 countries, including the UK, USA, India and China, as well as the European Union (EU), have backed the first international commitment to achieve "near-zero" emission steel production by 2030
- 42 countries have set coal phase-out dates and international public finance for coal will be coming to an end. The USA, UK, France, Germany and EU have announced they will help fund South Africa's transition away from coal

The International Sustainability Standards Board (ISSB)

When it comes to sustainability reporting, consistency is key. That is why a unified and globally consistent sustainability-related corporate disclosure, the International Sustainability Standards Board (ISSB), was established by the International Financial Reporting Standards Foundation (IFRS)[5] .

The IFRS also published two prototype disclosure-focused documents, including one focused specifically on climate-related disclosure, and another setting out general sustainability disclosures.

Goal 2: Adapt to protect communities and natural habitats

Some of the main highlights for achieving the second goal include:

- A pledge to end deforestation by 2030, was announced by around 133 countries[3]
- 32 countries have submitted their National Adaptation Plans, representing more than 2 billion people; this supports the sharing of best practice and mobilizing action
- A Forest finance pledge of allocated US$12 billion was signed by 12 countries, for forest-related climate finance between 2021-2025
- 10 global Mega Agriculture companies have committed to halting forest loss associated with agricultural commodity production and trade

Goal 3: Mobilize finance

A very important breakthrough for mobilizing finance is the launch of the Glasgow Financial Alliance for Net Zero (GFANZ) in April 2021. GFANZ is a pre-COP initiative, initiated by the COP Presidency, the UN High Level Climate Champions and Mark Carney. 450 firms have joined the initiative so far, responsible for assets beyond US$130 trillion, and they are leading net zero initiatives across the financial system. [4]

As part of GFANZ, the Net Zero Financial Service Providers Alliance (NZFSPA) was formed. The alliance is composed of several major financial service providers including Morgan Stanley Capital International (MSCI), Binder Dijker Otte (BDO), Ernst and Young (EY), and Price Waterhouse Coopers (PWC) among others. All are committed to align their relevant services and products to help enable investors and financiers achieve their net zero goals, and to set their own climate targets. All of this is in support of the goal of global net zero GHG emissions by 2050. These organizations will also set interim targets for 2025 within 12 months of joining, and they will set science-based targets to reduce their operational emissions.

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4. Environmental, Social and Governance (ESG) Raters' interest in climate change

What gets measured, gets managed. Here lies the importance of ESG raters in providing tools for companies to measure their carbon emissions and help them reach the 1.5 degree goal. For example, MSCI offers 700 climate change metrics including: Climate VaR, Low Carbon Transition Score, forward-looking indicators, emission data, fossil fuel exposure, and clean tech solutions to facilitate integration across the investment process[6].

The rater Refintiv has developed sophisticated carbon data and estimate models structured around four steps: Reported, used when emissions data is already available; CO2 model; Energy model; and Median model[7]. Refinitiv also has a low carbon select index[8].

Additionally, the rater S&P 500 has a Net Zero 2050 Climate Transition ESG Index. This is designed to measure the performance of eligible equity securities from the S&P 500, selected and weighted to be collectively compatible with a 1.5 degrees Celsius global warming climate scenario at the index level[9].

Another rater, FTSE Russel, has a Climate Risk-Adjusted Government Bond Index Series. This measures the performance of fixed rate, local currency, investment-grade sovereign bonds, and tilts index weights according to each country's relative exposure to climate risk, with respect to resilience and preparedness to the risks of climate change[10].

At a local level, Boursa Kuwait has environmental sustainability metrics related to climate change. These consist of: GHG Emissions, Emissions Intensity, Energy Usage, Energy Intensity, Energy Mix, Water Usage, Environmental Operations, Environmental Oversight, and Climate Risk Mitigation.

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5. The role of Environmental, Social and Governance (ESG)/Sustainability in addressing climate change

One of the most effective ways of addressing climate change is through ESG, which is a way of evaluating a firm's conscientiousness over social and environmental and governance factors. Historically, ESG/ sustainability services were exclusively provided for certain industries such as mining and coal, steel, oil and gas, etc. However, this is not the case anymore. ESG/sustainability is now mainstreamed into all industries across all sectors. In other words, any company, whether large or small, can benefit from being sustainable.

To put things in perspective, it's important to outline key aspects of ESG/sustainability services. The process begins by providing the company with a mature assessment of existing practices, identifying its strengths and areas of improvement. Based on the assessment, a budgetary plan is prepared. In order to assure actual implementation, the plan should have realistic applicable expectations. Implementation should start with the quick wins in order to build momentum and motivation. The company must also monitor all operations across the supply chain by defining or remapping stakeholders, and by aligning their policies and codes of conducts with their view of a sustainable supply chain. Moreover, capacity building is usually provided to stakeholders regarding necessary sustainability issues. Such capacity building will ensure stakeholder support and buy-in for the company's goals and proactively avoid any possible resistance from them.

Currently, less than 1% of managed assets are aligned with the ambitions of the Paris Agreement; it is estimated that less than 10% of large companies comprehensively measure and report emissions.[11] This means that there is a long way to go for ESG/sustainability implementation on a large scale, necessitating governmental buy-in and mandatory reporting of both public and private disclosure.

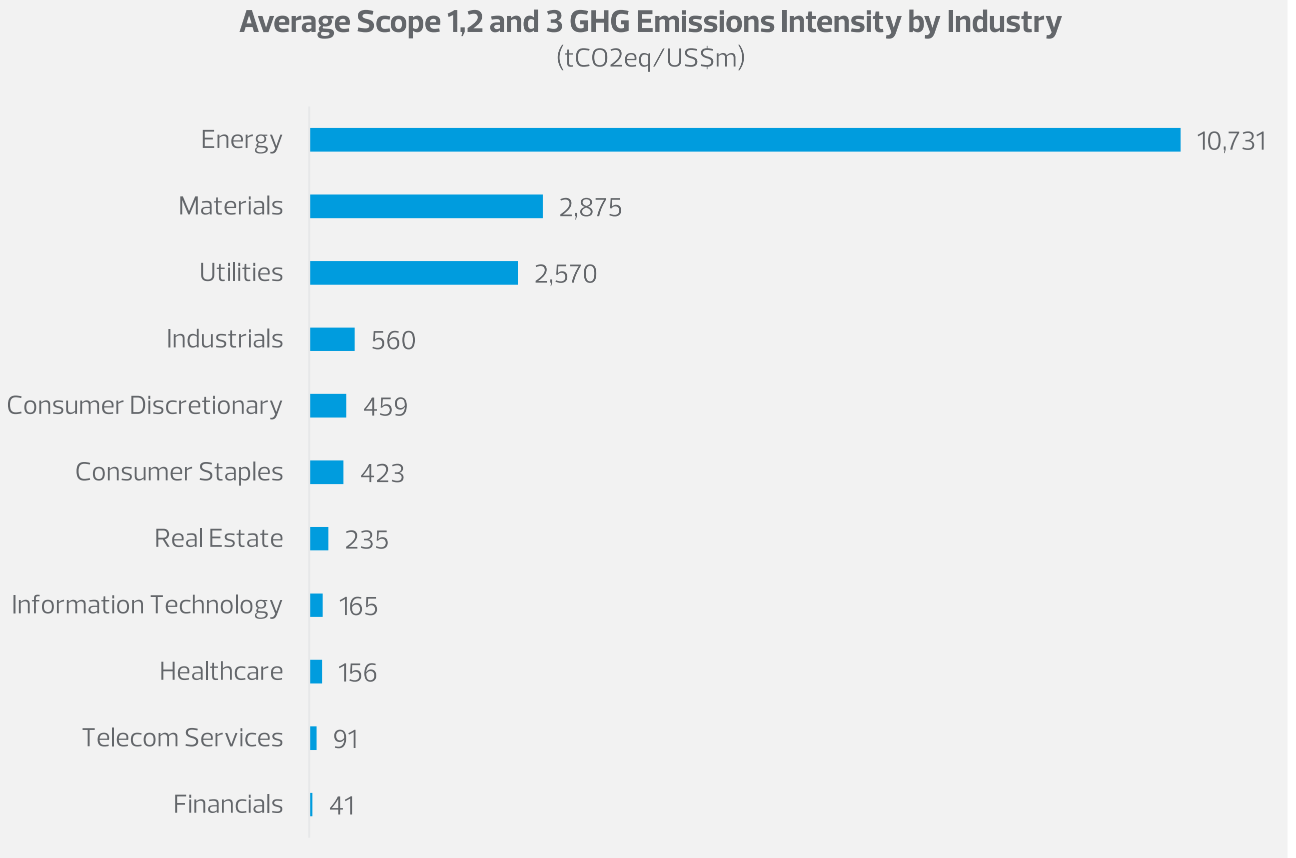
Furthermore, ESG/sustainability services nurture companies shifting to digitization. This includes digital wages, reduction of paper, holding online meetings etc. Digitization serves the environment greatly in terms of cutting down GHG emissions through reducing transportation, reduction of waste, as well as saving resources and biodiversity protection. Another interesting advantage of digitization is the fact that it increases a country's Gross Domestic Product (GDP) through reducing the time taken for money transfers down to zero. One study by PWC showed that an increase of 10 percent in a country's digitization score fuels 0.75% growth in its GDP per capita.[12]

Knowledge transfer is also one of the key outcomes of ESG/sustainability reporting. When companies communicate their best practices through ESG/sustainability reporting, they allow other companies and organizations to benchmark their performance, in turn motivating others to take environmentally responsible actions and prepare mitigation plans accordingly. All of this can be counted as indirect economic impact, with monetarized value of the non-financial elements.

Clearly, tackling climate change will not be possible without massive global action across all sectors. This means that companies, banks, insurers and investors all have to adjust their business models and develop credible plans for the transition to a net zero economy and then implement them. Herein lies the importance of ESG/sustainability services, and the transformation of ESG/sustainability agendas into clear implementation roadmaps. In this regard, RSM is delighted to provide support for addressing ESG/sustainability areas/ topics through our diversified skilled expertise and services.

To learn more please visit our website: https://www.rsm.global/kuwait/insights/sustainability-insights

5. The role of Environmental, Social and Governance (ESG)/Sustainability in addressing climate change



Source: Sustainalytics, as of October 2021

The figure above shows the average volume of direct (Scope 1) and indirect (Scope 2) GHG emissions from sources owned or controlled by each industry as well as from its value chain (Scope 3) per unit of revenue (million USD), according to research by Sustainalytics.[13]

References

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