Written evidence submitted by Grantham Research Institute on Climate Change and the Environment

Response to the Environmental Audit Committee's Call for Evidence on 'The financial sector and the UK's net zero transition'

About the Grantham Research Institute

The Grantham Research Institute on Climate Change and the Environment was established in 2008 at the London School of Economics and Political Science. The Institute brings together international expertise on economics, as well as finance, geography, the environment, international development and political economy to establish a world-leading centre for policy-relevant research, teaching and training in climate change and the environment. It is funded by the Grantham Foundation for the Protection of the Environment, which also funds the Grantham Institute – Climate Change and the Environment at Imperial College London.

Author's note

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The views in this submission do not necessarily reflect those of the Institute or its funders. Any errors or omissions remain those of the author. The author declares no conflict of interest in the preparation of this submission.

Summary

- This submission highlights the 'just transition' efforts of the financial sector in decarbonising the UK economy. The just transition is an inclusive policy approach to ensure that workers, suppliers, communities and consumers affected by transition measures are considered in shaping the shift to net zero.
- The financial sector has a crucial role to play in reaching net zero targets, and in ensuring a just transition. As demonstrated through examples specific to the fossil fuel industry, efforts towards this are underway through the incorporation of just transition principles into elements of strategy, corporate engagement, policy dialogue, capital allocation and measuring contribution.
- The responsible retirement of fossil fuel assets must consider impacts on livelihoods and energy supply. Business and finance have a role to play in delivering a just transition through the energy sector. Examples from Royal London Asset Management (RLAM), Friends Provident Foundation (FPF) and Bridges Evergreen Holdings demonstrate this. Interventions in the real economy through corporate engagement and capital allocation can be helpful in mitigating the risk of stranded communities[1] and worsening fuel poverty.
- This submission focuses on the following themes outlined in the inquiry document:

[1] Stranded communities constitute those communities reliant on fossil fuel industries which will be left behind economically if they are not supported through the transition away from fossil fuel reliant industries to other economic opportunities in greener sectors.

a. The potential effectiveness of the financial sector, including through alliances such as GFANZ, in encouraging the decarbonisation of the economy in time to limit global temperature rise to 1.5°C.
b. Likely pathways to the responsible retirement of fossil fuel assets in a way that is compatible with the UK's national interest, reducing the risk of stranded assets and meeting the UK's international climate obligations.

I. About the just transition

1. The just transition recognises that the transition to a net zero economy needs an inclusive policy approach that considers those affected by net zero measures. The International Labour Organization published its *Guidelines for a just transition* in 2015 (ILO, 2015) and the concept was later incorporated into the goals of the 2015 Paris Agreement (UNFCCC, 2015): "Taking into account the imperatives of a just transition of the workforce and the creation of decent work and quality jobs in accordance with nationally defined development priorities,…". Ensuring that the priority groups; workers, suppliers, communities, and consumers, are involved in shaping the shift to net zero, have access to reskilling and accessible financial sources to succeed in this transition is crucial (Robins et al., 2021).

2. This submission responds to the themes of the potential effectiveness of the financial sector to decarbonise and likely pathways to the responsible retirement of fossil fuel assets. We recommend that both themes adopt a just transition lens to ensure that the transition is delivered in as efficient a manner as possible.

II. The potential effectiveness of the financial sector to encourage the decarbonisation of the economy through a just transition

3. There is a differentiated responsibility in the delivery of a just transition: governments hold primary responsibility while financial sectors play a supporting role. Financial institutions can encourage decarbonisation by incorporating just transition principles into elements of strategy, engagement, policy dialogue, capital allocation and by measuring their contributions (Robins et al., 2021).

4. Financial institutions can play a significant role by fully integrating the social dimension into the way they allocate capital for net zero. The just transition is a relatively new concept for many in the financial sector, but the case for action is clear:
   - It is the right thing to do and is fully consistent with longstanding commitments to social and human rights standards and the Sustainable Development Goals.
   - It is the necessary thing to do to ensure long-term public support for rapid and potentially disruptive change.
   - It is the smart thing to do because it will minimise transition risks and strengthen the human and social capital needed for long-term investment. It is a material issue for all financial institutions.

5. Efforts from the financial sector to support the just transition of fossil fuel industries are already underway. One such recent example is the pensions industry; the Scottish Widows' report, *The case for a just climate transition,* stated that they believed the just transition was fundamental for long-term investment and to societal prosperity for all their pension members.

6. Table 1 below shows some excerpts from UK financial institutions' published references to the just transition through their strategy and corporate engagement:

Table 1: Financial institutions' references to the just transition

Institution	References to the just transition
Aviva	Climate transition plan: In recommendations to governments: "Set economy-wide net zero targets for 2050 or (ideally) earlier", which includes to "set phase-out goals for fossil fuels and fossil fuel subsidies in line with the science and ensure that these subsidies are redistributed to support the 'just transition' for all."
Citigroup	"Initial" transition plan: Under the 'Social Responsibility' principle: "Strive to ensure that our net-zero transition is consistent with other sustainable development objectives. We will also assess how our financing decisions could affect lower-income communities, developing countries and communities dependent on carbon-intensive sectors, balancing the need for carbon reduction with the potential negative impacts on access to energy and economic dislocation."
abrdn	Climate Change, Our Approach to Investment 2021: "We strongly encourage companies to consider the social dimensions of the energy transition to ensure it is inclusive and 'just'. This means worker and community needs are considered on the path to a low-carbon economy so they are not left stranded. Other social aspects, such as affordability and reliability of energy supply are also important."
Royal London Asset Management (RLAM)	Stewardship and Responsible Investment Report 2021: "A just transition strategy for the energy utility sector requires companies to assess the social impact of their decarbonisation plans. Utilities should aim to engage extensively and creatively, bringing the following key stakeholders with them on the journey to net zero in a way that addresses the trade-offs and maximises its benefits."

7. Policy dialogue is a lever of influence for financial actors and can have a multiplying effect. Financial institutions that are part of the Powering Past Coal Alliance (PPCA) have achieved significant progress in enabling the transition from unabated coal power to clean energy that is sustainable and economically inclusive. The PPCA's Finance Taskforce, launched in June 2020, brings together members of government and the finance sector to halt new investments in coal-based power plants and increase clean energy-related investments. The Alliance also works as an enabling platform for sharing best practice and adopting practical initiatives to guide others in the process of transitioning (Muller and Robins, 2021).

8. By integrating just transition principles through capital allocation measures, financial actors are strategically pairing decarbonisation with powerful social benefits. An example of this is the Friends Provident Foundation's (FPF) investments in community-owned renewable energy. Small and medium enterprises (SMEs) in community energy initiatives contribute to decarbonisation and bring about place-based social and economic benefits (Robins et al., 2021). FPF has committed 10% of its endowment to impact investments like community-owned energy. In 2020, FPF invested in 'Riding Sunbeams', a joint venture between Community Energy South, Possible and Thrive Renewables, to decarbonise the transport system. They are developing community-owned renewable energy sources and making them commercially available to large regional energy users like railway networks, in this way contributing to carbon reduction and adding value to the communities they operate in.

9. The effectiveness of the financial sector in supporting the just transition is contingent on pricing social risks into investment and lending decisions. Many international initiatives are underway to integrate the just transition into the assessment and rating of companies by investors, banks, and

financial institutions (Muller and Robins, 2021). Examples include the Climate Action 100+ and the World Benchmarking Alliance (WBA). The WBA has developed a methodology to assess companies on the just transition and used it to assess 180 companies across the oil and gas, utility and automotive sectors. The WBA has also published the methodology for its Just Transition Assessments (WBA, 2021). Widespread adoption and scaling of these methodologies are key to measuring contributions.

III. Pathways to the responsible retirement of fossil fuel assets

10. The responsible retirement of fossil fuel assets is dependent on the inclusion of workers, suppliers, communities and consumers when transitioning away from high-carbon activities and towards a green economy. The *Workforce Report 2021* from Oil and Gas UK estimated that 195,900 jobs (direct, indirect and induced), will be supported by the UK offshore oil and gas industry in 2021 (OGUK, 2021). The report also found that, in 2020, 44.7% of the workforce was comprised by those aged 30–44 and 37.2% by those aged 45–-59. As the sector transitions, these workers will still be of working age and therefore will require measures to support them into other employment. To successfully follow through on this would require efforts such as social dialogue with stakeholders, and reskilling will be required where possible.

11. Fuel poverty is another risk posed to communities and consumers. In 2020 it was estimated that 3.16 million UK households are classified as 'fuel poor' (BEIS, 2022). In a green economy, clean energy must be delivered affordably. Hence, consideration of social risks and their mitigation through transition plans is essential for decarbonisation targets to succeed. By executing the just transition as a means to the responsible retirement of fossil fuel assets, the risk of assets and communities being stranded can be mitigated.

12. In the Grantham Research Institute's research through the Financing the Just Transition Alliance (FJTA), engagement with portfolio companies and clients have yielded successful results in corporate action. For instance, Royal London Asset Management (RLAM) and Friends Provident Foundation (FPF) have been engaging with energy utility companies to address the social implications of their decarbonisation goals (E.ON, EDF, National Grid, SSE and Scottish Power). As a result of this engagement, SSE became the first company in the world's utility sector to publish a just transition strategy in 2020. Following feedback from RLAM, FPF and the London School of Economics, SSE stablished 20 principles to incorporate fairness into its decarbonisation plans while transitioning out of high-carbon activities and towards net zero emissions (Robins et al., 2021). In 2021, five more companies published just transition plans (RLAM, 2021a):
    - E.ON published a section on just transition in its climate transition plan in March 2021.
    - National Grid committed to addressing the just transition in its Responsible Business Charter in August 2021.
    - Centrica published its just transition plan in September 2021.
    - EDF published its just transition plan in October 2021.
    - Scottish Power published its just transition plan in November 2021.

13. Mitigating the risk of worsening fuel poverty is an area in which the financial sector can take action. One example is Bridges Evergreen Holdings' investment into Agility Eco Services Ltd. AgilityEco runs affordable warmth and retrofit services across Britain in partnership with energy suppliers, the public sector and third sector partners. Bridges Evergreen provides financial, strategic and operational support to AgilityEco for scaling up the business. Since the company's launch in 2013, nearly 45,000 low-income households have been supported, resulting in lifetime savings of

over £200 million. This translates to an annual saving of £543 per household and contributes significantly to reducing fuel poverty (Robins et.al., 2021).

June 2022

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