

25th April 2024

The Transition Finance Market Review team
c/o The Treasury Lords Minister and
the Minister for Energy Efficiency and Green Finance

Submitted by e-mail to: tfmr@cityoflondon.gov.uk

Dear TFMR team,

CFA UK letter in response to the TFMR's call for evidence dated 14th March 2024

The CFA Society of the UK (CFA UK) welcomes the opportunity to respond to the TFMR's consultation on Transition Finance (TF).

Given our purpose and relative focus, we are focussing our comments on the topic of "*Building the UK as a global hub for transition finance*", covered by Chapter 6 of your consultation, including Q's 33 and 36.

In addition, as the CFA Institute has just released an extensive research report on TF, we would like to draw your attention to it – key recommendations and cross references provided below, with a synopsis attached at Appendix 2.

OUR VIEW ON THE REQUIRED ECOSYSTEM FOR TF IN THE UK

We support the TFMR's desire to focus on how the UK can become a global hub for TF.

We however believe that the ecosystem required to grow this sector and the UK's prominence as a centre for TF should also:

- ***Emphasise the skills, knowledge and competencies required*** that enhance our relative standing, and
- ***Call out the Ethics and Professionalism focus*** embedded in the UK that will enable the sector to grow robustly yet safely

We outlined our view on sustainability training and competence in our response to the FCA's DP23/1 in May 2023.

The CFA Institute in its recent research on TF has also highlighted that "*Knowledge gaps in transition finance hinder mainstream adoption and create challenges in effectively communicating and implementing transition strategies*".

Our suggestions for consideration in this context are:

1. ***Developing a qualification or certification focussed on TF roles*** in affiliation with a credible educational body, which is in time seen as the benchmark for competence in the sector.

2. ***Energising thought leadership through collaborative initiatives*** that include public bodies, universities, and learning / development focussed bodies such as CFA UK and the CISI.
3. ***The development of case studies*** that demonstrate the end to end experience and success of TF within the UK ecosystem, for issuers as well as professionals. In our experience such case studies are best developed by practitioners with the relevant experience.

As flagged in the CFA Institute’s report, “*transition finance involves navigating a complex landscape of economic, regulatory, environmental, and technological considerations*”, which in our view underscores the opportunity to differentiate the UK ecosystem.

KEY POINTS FROM CFA INSTITUTE’S RECENT REPORT ON TF

The CFA Institute and CFA UK both provide certifications that include TF and to varying degrees support the attainment of competency in this area. We also generate thought leadership on many sustainability related topics.

The recent TF report advocates disclosure, clarity on transition plans, collaboration, and addresses key issues raised in your consultation.

- [Navigating Transition Finance | CFA Research & Policy Center \(cfainstitute.org\)](https://www.cfainstitute.org/research/policy-center/navigating-transition-finance)

The key recommendations are:

- Institutional investors that wish to intentionally incorporate net-zero considerations into their investment strategy and process should disclose both portfolio emissions and decarbonization progress (year-on-year reduction of portfolio emissions) and establish portfolio decarbonization targets.
- Corporations should provide feasible and credible transition plans and provide inflation- and forex-adjusted carbon intensity per revenue so investment managers can better measure the impact to the real economy of their portfolios and should include decarbonization targets in balanced scorecards for executive remuneration.
- Governments and regulators should work with industry stakeholders to develop transition taxonomies, harmonize transition plan disclosures, and require economic feasibility disclosures. They should also allocate additional public and blended finance, consider using reverse auctions/climate bad banks to manage phaseout, and use labelling to help individual investors navigate the investment product landscape.

The report includes topics raised in TFMR’s consultation, cross referenced below:

TFMR’s consultation questions	CFAI’s report coverage
Chapter 2 - Scope of TF	Section 2 - The current state of TF
Chapter 3 - Ensuring credibility & integrity of TF	Section 5 - Credible and feasible transition plans; and other sections
Chapter 4 - Barriers to application of TF	Section 3 - Challenges in TF

Chapter 5 - Opportunity for investments, products, services	Section 4 – Empower the TF storytelling (to an extent)
Chapter 6 - Building the UK as a global TF hub	Please see the first section above of this letter. Also Report Section 6 – Additional Govt support to derisk TF

CFA UK will be happy to meet and discuss our feedback and contribute as appropriate to developing the TF opportunity in the UK.

Yours sincerely,



Amit Bisaria

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With thanks for contributions from: Olivier Fines CFA, and the oversight of the CFA UK's Ethics & Professionalism Steering Committee.

APPENDIX I About CFA UK and CFA Institute



CFA UK serves nearly 12,000 members of the UK investment profession. Many of our members analyse securities, manage investment portfolios, advise on investments, or are in roles responsible for investment operations or oversight.

Our role is to help investment professionals build and maintain their skills and competencies so that they are technically and ethically competent to meet their obligations to clients. We advocate for high standards of ethical and professional behaviour and our work with regulators, policymakers and standard setters is focused on skills, knowledge and behaviour.

We are not a lobby group or a trade body. We are an independent, professional association whose mission is to ‘educate, connect and inspire the investment community to build a sustainable future.’

Founded in 1955, CFA UK is one of the largest member societies of CFA Institute. Most of our members have earned the Chartered Financial Analyst® (CFA®) designation. All our members are required to attest to adhere to CFA Institute’s Code of Ethics and Standards of Professional Conduct.

For more information, visit www.cfauk.org or follow us on Twitter @cfauk and on LinkedIn.com/company/cfa-uk/



CFA Institute is the global association for investment professionals that sets the standard for professional excellence and credentials. The institute is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Its aim is to create an environment where investors’ interests come first, markets function at their best, and economies grow.

It awards the Chartered Financial Analyst® (CFA) and Certificate in Investment Performance Measurement® (CIPM) designations worldwide, publishes research, conducts professional development programs, and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.

CFA Institute has members in 162 markets, of which more than 170,000 hold the Chartered Financial Analyst® (CFA) designation. CFA Institute has nine offices worldwide and there are 158 local member societies.

For more information, visit www.cfainstitute.org.

APPENDIX 2
“NAVIGATING TRANSITION FINANCE: AN ACTION LIST”
EXECUTIVE SUMMARY

The report

The research report (published on March 27th by the Research and Policy Center) examines the challenges and possible solutions to accelerate the development of transition finance for the decarbonization of high-emitting sectors. We incorporate opinions from market participants and suggest actions for stakeholders to enhance awareness, improve disclosure, and mitigate risks, emphasizing collaboration to support effective transition finance for net-zero goals.

Background

Transition finance is any form of financial support that helps decarbonize high-emitting activities or enables the decarbonization of other economic activities. The pivotal role played by transition finance in achieving net-zero goals, however, is not universally recognized. Currently, no standardized definition of eligible activities and entities exists, no international organization has endorsed transition finance instruments, and high-risk perceptions associated with the novel technologies involved in decarbonizing high-emitting sectors are common. Consequently, many investment strategies that incorporate net-zero considerations exclude or underweight high-emitting sectors for the creation of low-emission portfolios.

Navigating the complex landscape of economic, regulatory, environmental, and technological considerations, transition finance requires a collaborative effort for success. This report explores actions that investors, asset managers, corporations, and policymakers should consider enhancing awareness of the role of transition finance in achieving net zero; to improve the disclosure of credible transition plans; to provide clarity on transition activities and transition finance products; and to mitigate risks associated with transition finance.

Traditionally framed as green and clean, sustainability requires a significant paradigm shift to incorporate transition finance. All stakeholders in the transition finance system must cultivate new skills, establish fresh priorities, and, above all, embrace a new mindset. Collaboration synergy is crucial to achieving change and enabling transition finance to play a bigger part in supporting net-zero goals.

Recommendations

We make the following recommendations to advance transition finance.

- Institutional investors that wish to intentionally incorporate net-zero considerations into their investment strategy and process should disclose both portfolio emissions and decarbonization progress (year-on-year reduction of portfolio emissions) and establish portfolio decarbonization targets. Institutional investors could use a

dashboard with multiple metrics and attribution analysis to report to clients on how their investment strategies promote low emissions or emissions reduction. This approach would improve transparency and awareness of portfolio decarbonization goals.

- Corporations should provide feasible and credible transition plans to assure investors/financiers of their steadfast commitment to attaining transition targets. Further, corporations should provide inflation- and forex-adjusted carbon intensity per revenue so investment managers can better measure the impact to the real economy of their portfolios and should include decarbonization targets as part of a balanced scorecard for executive remuneration to incentivize accountability and intentionality.
- Governments and regulators should work with industry stakeholders to develop transition taxonomies, harmonize transition plan disclosures, and require economic feasibility disclosures. They should also allocate additional public and blended finance to better mobilize private sector investment, consider using reverse auctions/climate bad banks to manage phaseout, and use labelling to help individual investors navigate the investment product landscape, thereby creating a more informed and sustainable financial ecosystem.

What are the objectives of this report?

Transition finance plays a pivotal role in achieving net-zero goals, but it is not adequately recognized. Many investment strategies that incorporate net-zero considerations exclude or underweight high-emitting sectors for the creation of low-emission portfolios. The objectives of this report are to enhance comprehension of transition finance, pinpoint obstacles to widespread implementation, and explore collaborative initiatives required from the investment community, high-emitting corporations, and policymakers to overcome these obstacles.

How does this report incorporate the market participants' view?

We conducted intensive individual interviews with over 20 market participants representing various stakeholders in the transition finance system. These interviews aimed to explore perspectives on the challenges and solutions encountered in practice. Additionally, we invited volunteers to participate through an ESG virtual roundtable organized by the CFA Institute in May 2023.

Why is transition finance difficult to understand?

Transition finance is any form of financial support that helps decarbonize high-emitting activities (transitional activities) or enables the decarbonization of other economic activities (enabling activities). High-emitting sectors, such as cement, chemicals, fertilizers, steel, and transportation, collectively contribute to about one-third of global emissions. Achieving a net-zero world is unattainable without decarbonizing high-emitting industries. However, the eligibility for transition finance varies widely across different countries and regions, with

some having established taxonomies and catalogues of eligible activities, while others have no clear definition or scope of transitional and enabling activities. Additionally, no international organization has endorsed transition finance instruments (such as Transition Bonds).

What are the obstacles in practice?

Due to poor awareness, it is difficult to communicate transition strategy to individual investors. In some cases, transition finance is not sufficiently understood among institutional investors.

There is scepticism surrounding both the quantity and quality of transition plans. Transition plan disclosure is not mandatory, and there is no universally defined standard for what qualifies as a credible transition plan, which can lead to greenwashing concerns. An EY (2023) study found that only 5% of FTSE100 constituent companies disclosed sufficiently detailed transition plans. Additionally, the feasibility of achieving net-zero targets is not addressed in transition plans.

Furthermore, the risk/return profile of transition finance is perceived as unfavourable. Net-zero pledges raise operational challenges, particularly the trade-offs related to investments in hard-to-abate sectors where complete decarbonization remains unattainable based on current technologies. Governments rely on market forces to drive advancements toward decarbonization targets, but this process takes time, and consequently, the investable universe for transition finance has remained limited.

Why is collaboration important to Transition Finance?

Collaboration is vital for Transition Finance, as fragmented efforts have hindered progress toward common net-zero goals. Governments, corporations, and asset managers often lack coherence and consistency in their strategies: certain high-emitting countries/regions require transition finance from private sector but lack established taxonomies defining eligible activities, and high-emitting corporations seeking external financing for decarbonization often lack comprehensive transition plans. Despite numerous net-zero commitments from asset owners and managers, there is a notable absence of commitments to allocate a proportionate amount of capital based on real-economy impact.

Shifting towards transition finance necessitates a broader understanding of sustainability beyond traditional 'green' initiatives. The dynamic nature of climate challenges requires all stakeholders to adopt a collaborative and interdisciplinary approach and to redefine success metrics to encompass both financial performance and real-world impact.