



The Road to Net Zero: The Role of Data

A SIX Special Report

Introduction

COP28 made it crystal clear: achieving net zero carbon emissions by 2050 through decarbonization and transition finance cannot be done without the commitments and actions from the financial services industry.

Sparked by a wave of new regulations and growing pressure from shareholders and end investors, financial institutions - including banks, asset managers and asset owners - are playing a vital role in supporting the transition to net zero.

Financial market participants are changing their business practices and disclosing more information about climate risk to clients, shareholders and regulators alike. However, in order to manage climate risks appropriately, companies, banks and investors require access to clear, consistent, and comparable data.

Financial Institutions Are Starting to Evaluate Climate Change and Transition Risks

Climate change is something which financial institutions are taking increasingly seriously.

Inflows into climate change focused funds - namely funds that invest into and help finance companies which are supporting the climate transition - are on the rise. Analysis from Morningstar found that climate funds now collectively manage US\$534 billion, representing 20% of all global sustainable fund assets.¹ Since 2018, assets under management (AUM) at climate funds have increased by 14-fold, while the number of funds with climate related strategies has jumped by 30% over the last 18 months.²

But, what is driving this activity?



¹⁺² Morningstar – September 26, 2023 – Assets in global climate funds march steadily higher.

Regulators Get Serious on Climate Change Rules

With most governments having pledged to reach net zero by 2050 under the Paris Agreement agreed in 2015 and ratified in 2016, regulators are doing their part to drive positive change within all sectors of the economy, including financial services.

ESG Book reported (2023) that there are now more than 1,255 ESG policy interventions that have been introduced worldwide since 2011, compared to just 493 regulations published between 2001 and 2010 with many of them focusing on climate risk.

Martina Macpherson highlights that “most of the existing climate risk disclosure frameworks since the announcement of the Kyoto Protocol, which operationalizes the United Nations Framework Convention on Climate Change (1997), the Paris Agreement (2015-2016) and the Task Force on Climate-Related Financial Disclosures (TCFD) framework (2017) have focused predominantly on issuer, i.e., company-related, reporting”.

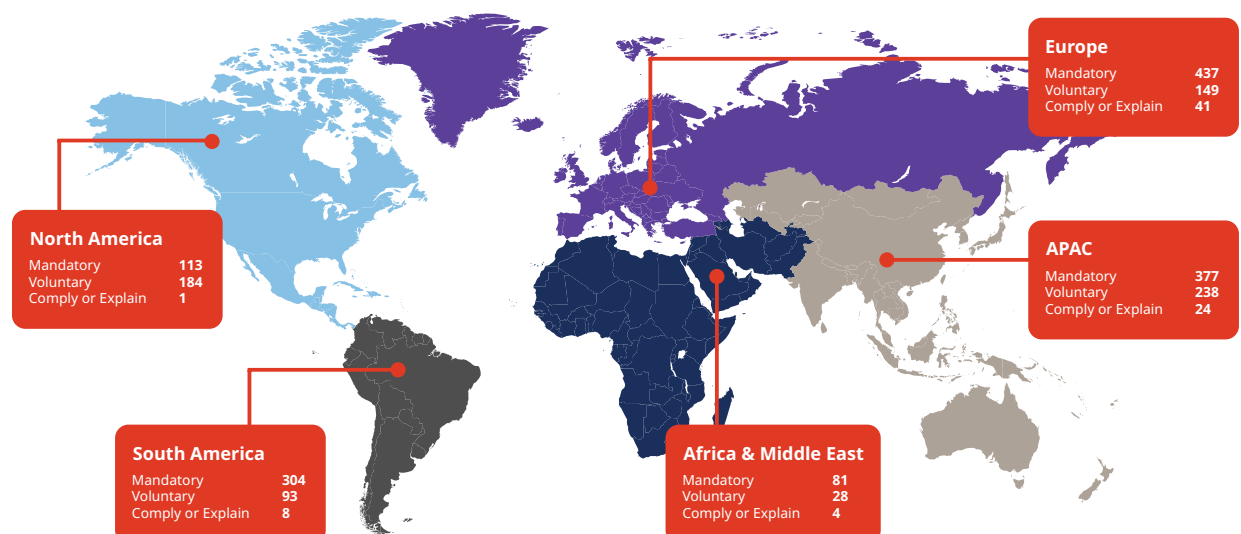
Today, the TCFD's recommendations have been adopted by companies in many jurisdictions, including the UK, Hong Kong, New Zealand, Singapore and Switzerland. In contrast, investor-related climate risk reporting is slowly gaining pace, and is finally being incorporated into ESG regulation, such as the European Union's (EU) Sustainable Finance Disclosure Regulation (EU SFDR).

As a result of the Paris Agreement, which aims to limit global warming to within a 1.5-2°C trajectory, climate risk management frameworks and regulations are focusing on climate risk and valuation assessments or, most recently, and with the launch of the Swiss Climate Scores and the Transition Pathway Initiatives in the UK, on transition trajectories and impact.

Martina Macpherson
Head ESG Product Strategy
and Management at SIX

Regional Breakdown of ESG Regulations

Regional Regulations from 1980 to present day.



Source: ESG Book, Regional Breakdown of ESG Regulations, 2023

Climate Disclosure Rules for Investors Are Becoming More Common-Place and the Swiss Climate Scores Are in Pole Position to Drive Actions and Stewardship

Following the commitments of a total of 196 nations who signed the Paris Agreement, Switzerland has pledged to reduce its GHG emissions by 50% compared to 1990 levels by 2030 and become climate-neutral by 2050. This has been anchored in Swiss law since a public vote was held on the "Climate and Innovation Act" in June 2023.

On climate disclosures for investors, Switzerland forms part of a small handful of countries that have developed specific, though self-regulated, disclosures for financial products. The six criteria of the Swiss Climate Scores (SCS) were launched in 2022. They have been designed to help Swiss financial institutions quantify and disclose climate related risks, impacts and alignment so as to support compliance with the "Strategy" and "Metrics and Targets" pillars of the TCFD framework.

Noting that whilst the creation of the SCS was informed by the TCFD, they are not one and the same: the SCS

can be seen as a means for financial institutions to fulfil certain requirements of the TCFD but not the other way round. This divergence between frameworks can cause some complexity for actors in the company and investor reporting value chain. Some countries, such as the UK (and if and once passed also the US), have tried to avoid fragmentation risks by closely aligning their reporting rules with the TCFD's reporting requirements. Meanwhile, the EU is currently facing increasing pressure from all actors to review the EU Sustainable Finance Disclosure Regulation (EU SFDR) and to simplify and align the current framework with other regulatory reporting and disclosure regimes.

To ensure that the SCS indicators enjoy a high degree of international interoperability, compatibility and consistency with existing climate risk disclosure frameworks in accordance with the Paris Agreement, Switzerland's Federal Council is working in close collaboration with international bodies such as the G20, the Organisation for Economic Co-operation and Development (OECD), the International Platform for Sustainable Finance (IPSF) as well as in bilateral financial dialogues.

Climate Risk Disclosure Frameworks at Investor / Financial Product Level

	Frameworks		Law / Regulations		
Organisations					
Title	Task Force for Climate Related Financial Disclosure Recommendations	Swiss Climate Scores	Enhancing Climate-related disclosures by Asset Managers, life insurers and FCA-regulated pension providers	The Enhancement and standardization of Climate-related Disclosures for Investors	Sustainable Finance Disclosure Regulation
Focus	Climate	Climate	Climate	Climate	Sustainability
Regulatory Status	Voluntary	Self-regulated	Required	Pending	Required
Effective Date	2017	2022	2022	NA	2022

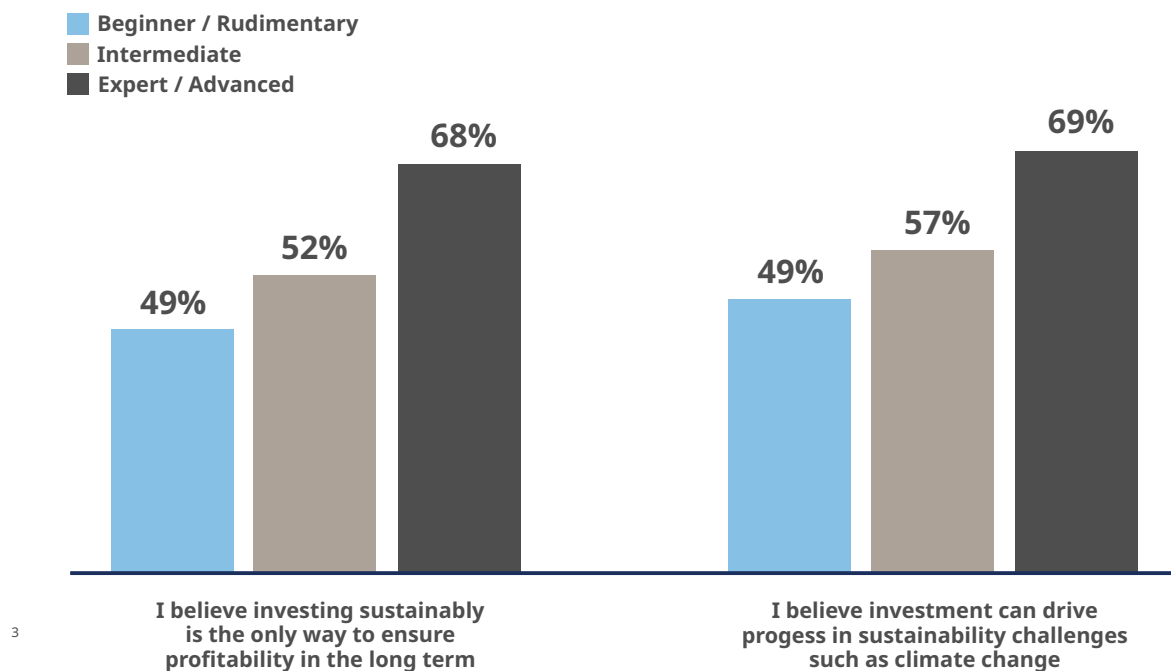
Adapted from "TCFD 2023 Status Report"
[Financial Stability Board \(FSB\)](#), [TCFD Status Report, September 2023](#)

Investors Take on the Climate Change Mantle

Regulators and investors alike are asking that financial firms take action relating to climate change.

In addition to financial returns, institutional and retail investors also want their asset managers to embrace sustainability. According to a survey by Schroders, 61% of investors favor funds that deliver good performance, but which also integrate sustainability factors³ (see chart below).

Most Investors Believe a Sustainable Approach is Key to Long-Term Returns



In some instances, however, investors are open to sacrificing returns in exchange for managers delivering on their sustainability objectives.

Data from U.S. Bank found two thirds of Generation Z investors want to allocate to funds whose strategies are aligned with their values, while four fifths of Generation Z and millennial investors would tolerate underperforming the S&P 500's 10 year average return of 12% to ensure that the companies they have exposure to are aligned with their core beliefs.⁴

There is also growing empirical evidence suggesting women are more attuned to sustainability issues than men. For example, a survey of its clients by RBC Wealth Management found women are twice as likely as their male counterparts to say that it is important for the companies they invest in to integrate ESG into their policies and decision-making.⁵

Many of these investors are pushing managers for detailed reporting about their ESG and climate- related activities.

³ Schroders – September 27, 2022 – Schroders Global Investor Study 2022

⁴ NBC – August 27, 2023 – 'Not just money and math' – Young people are willing to sacrifice returns for ESG

⁵ RBC Wealth Management – As women gain power, interest in ESG investing grows

Stranded Asset Risks Become a Key Issue for Investors

Climate change is also a strategic risk management issue for asset managers and asset owners, from a mitigation and an adaptation standpoint. A number of institutions are demanding that asset managers divest from greenhouse gas emitting industries as they are concerned that these holdings could eventually become stranded assets, and potentially worthless over the long term, as consumer buying habits evolve and environmental regulations start to bite around the world.

Oil and gas companies, for instance, could become obsolete, i.e. “stranded assets”, as consumers increasingly eschew petrol and diesel cars, more governments introduce measures to encourage a wider adoption of hybrid and electric vehicles or look for alternatives to phase out their old oil and gas boilers for heat pumps.

Changing consumer behaviours and spending, as well as policy and tax incentives mean that financial institutions also need to think carefully about how they manage their climate risks in portfolios or on their balance sheets when investing or supporting lending activities.

Data Is Key, but There Are Challenges

Financial institutions need access to robust, “high-integrity” data to manage ESG and climate risks, to define their impact, to provide climate metrics to clients and regulators, and to comply with regulations on climate risk disclosures and sustainable finance frameworks such as EU SFDR, EU GAR and EU BTAR.

However, accessing high quality, consistent sustainability and climate data is not always straightforward. Firstly, there are a lot of data gaps and biases as information may be reported by some companies, or other public sources, but not by others.

Next, there is limited standardization around sustainability and climate data, which can make reporting a time consuming complexity management exercise.



This lack of harmonization is not helped by the sheer volume of industry standards, reporting frameworks and regulations although efforts to bridge some of these divergences and to establish more interoperability between corporate reporting disclosure frameworks such as EFRAG’s^a EU ESRS^b and IFRS’ ISSB^c are currently underway.

^a EFRAG = European Financial Reporting Advisory Group

^b EU ESRS = European Sustainability Reporting Standards

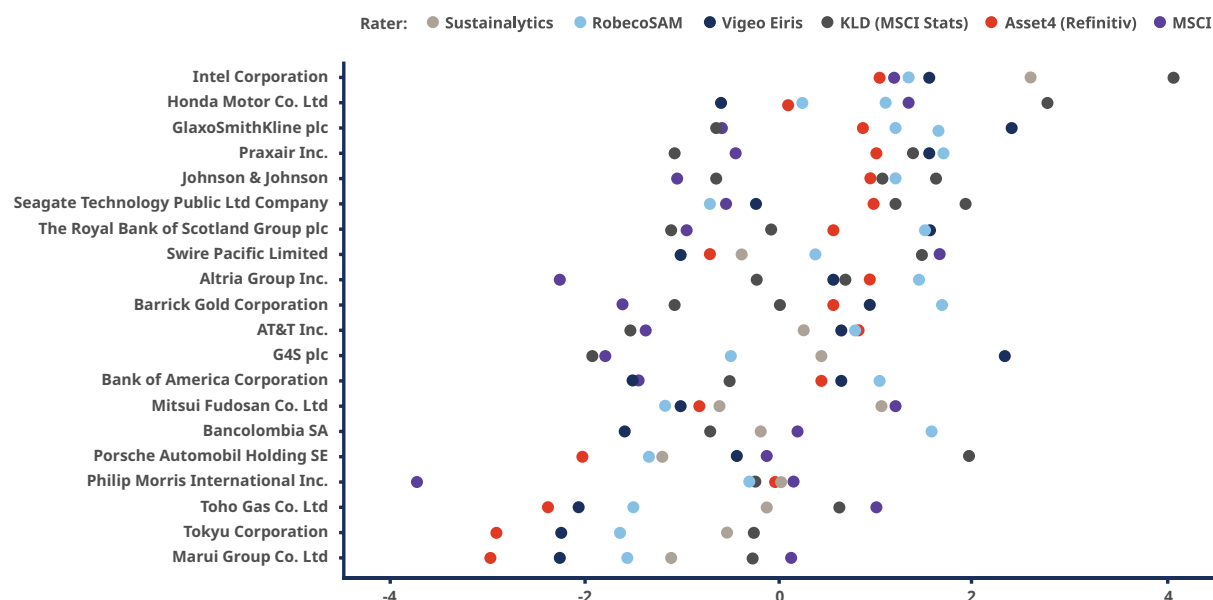
^c IFRS’ ISSB = International Sustainability Standards Board (IFRS) International Sustainability Standards Board (ISSB)

A number of asset managers and asset owners often rely heavily on ESG ratings for investing, risk management and reporting purposes, but even here, there are challenges, as the different ratings agencies will use their own proprietary methodologies when scoring companies on climate and sustainability risks. These different approaches can lead in turn to the phenomena often classified as “the aggregate confusion”, as ESG ratings for companies are at most correlated at around 60%.

The Aggregate Confusion: The Divergence in ESG Ratings, MIT Sloan (2019)

Challenges – ESG Ratings Divergence

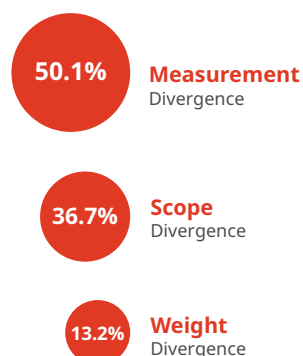
Correlation among ESG Ratings 0.61 vs. 0.99 on Credit Ratings



Source: [MIT Sloan Business School, Aggregate Confusion: The Divergence of ESG Ratings, 2019](#)

Overcoming data challenges and ratings and scores divergences will be critical if companies and investors are to meet their sustainability and climate related goals and portfolio management trajectories in line with regulatory parameters. As climate and sustainability data-related complexities become even harder to manage, many organizations are looking to third parties for support in data management and end-to-end analytical capabilities, for example in portfolio monitoring and reporting.

Three Main Sources of Divergence



How SIX Supports Its Clients

Through its new “Climate Data” offering, SIX supports clients globally with their climate related investment and risk decisions, as well as with the monitoring of climate risk factors. The data can also be used in investor reporting and supports investors’ compliance with climate-related backward and forward looking frameworks and regulations.

The new thematic data sets come as an addition to the existing ESG and sustainability-related datasets that SIX offers at a company and at a financial instrument level.

SIX identifies, aggregates, normalizes and distributes climate data sets from leading providers (e.g. MSCI, Inrate, CDP) through a data feed. With the Climate Data from SIX,

clients can rely on complete, clean, enriched and high quality information.

This specific data can help financial institutions meet their increasing disclosure requirements around climate, but also reduces complexity as firms have access to high quality data via a single access point.



Making a Difference
with Data

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