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Marketing material for professional/qualified investors only **March 2022**

We need financial institutions to fight climate change

It was the single-minded greed of the finance industry and those who operated it that caused the Financial Crisis. Well, that was the story we were told.

Whether this is a fair assessment is irrelevant. Perception is everything.

Trust was lost in financial institutions. And it could not have happened at a worse time. Repairing that damage is needed because the survival of the human race may now depend on it.

We need financial institutions to fund our fight against climate change. There is a huge investment gap that governments cannot fill.

Insurance companies will benefit from the low-carbon transition because companies across every sector will require insurance to protect new assets and projects.

Through better funding, banks could actually cause the cost of generating renewable energy to fall even further and speed up the transition to a low-carbon world.

This is where we as investors can make a difference.

Governments can no longer afford to battle climate change alone

Many governments are highly indebted (see chart 1). They have been taking on huge amounts of debt ever since the Financial Crisis 14 years ago. This accelerated during the pandemic, when they were forced to spend to avoid a brutal economic depression.

Subsequently, tackling climate change is now financially a lot harder than before. Unfortunately, the need to act has become even more urgent. And our governments simply cannot afford it.

According to the think tank Climate Policy Initiative we will need to spend globally at least USD 4.1 trillion every year by 2030 if we are to succeed in transitioning to a low carbon world (see chart 3). This is necessary to prevent the planet from warming more than 1.5 degree Celsius.[1]

Right now, we are nowhere near that amount. In 2019/2020 we only invested USD 632 billion in fighting climate change globally (see chart 2). The public sector bore the burden, financing USD 321 billion (51.0%), while financial institutions only funded USD 130 billion (20.6%). Yet, with burgeoning budget deficits and increasing government indebtedness, financial institutions will need to pick up the slack and raise the bar to fund the energy transition.

[1] Climate Policy Initiative. (10 February 2022). Global Landscape of Climate Finance 2021. CPI. https://www.climatepolicyinitiative.org/publication/global-landscape-of-climate-finance-2021/

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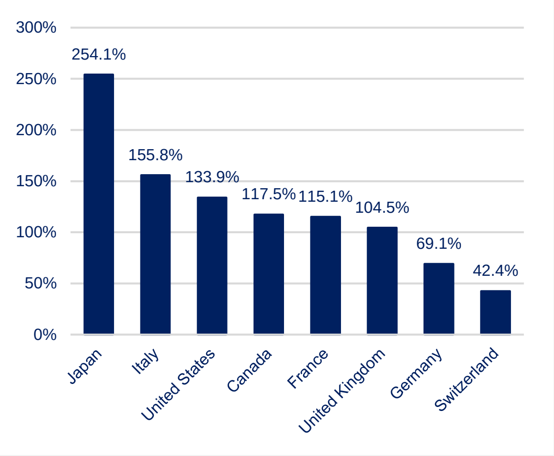
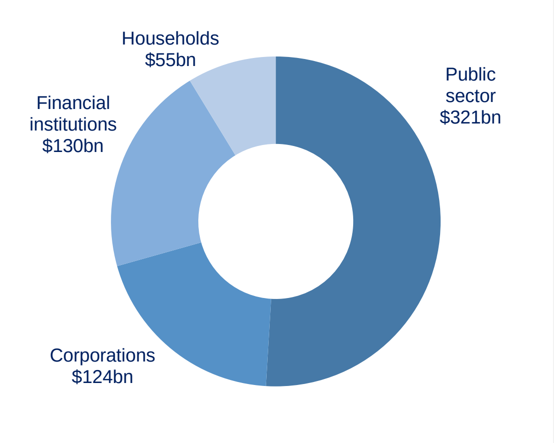
Chart 1: Government debt-to-GDP



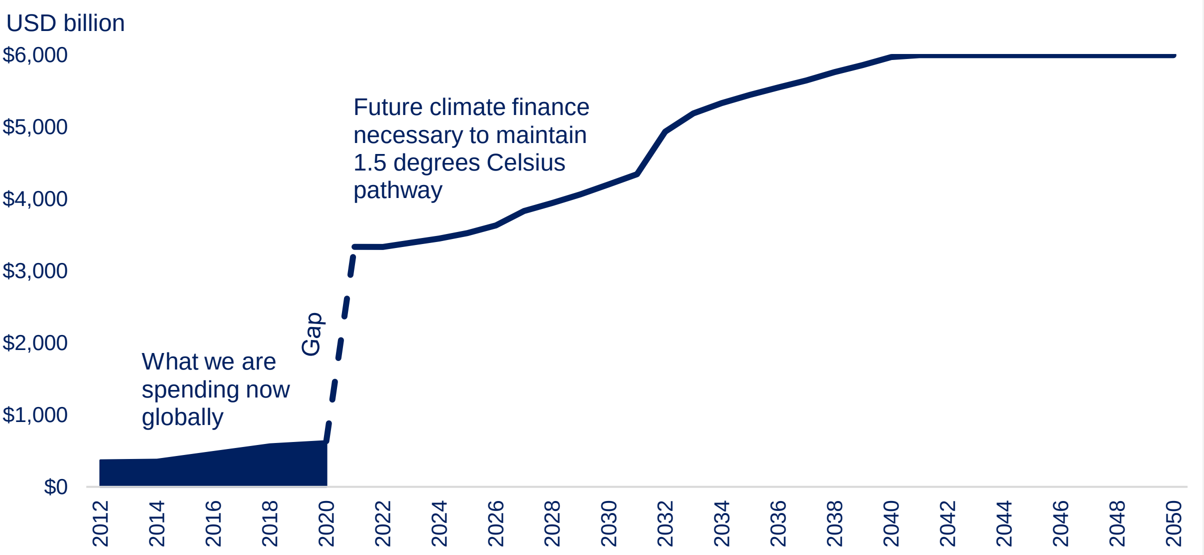
Source: IMF, 2020.

Chart 2: Who is financing the climate transition



Source: The Climate Policy Initiative, "Landscape of Climate Finance 2021".

Chart 3: Tracked climate finance flows and estimates for what is needed until 2050



Source: The Climate Policy Initiative, "Landscape of Climate Finance 2021".

The finance industry will have to fund the low-carbon transition

If the whole world wants to reach net-zero by 2050, USD 90 trillion of infrastructure investment is needed over the next 15 years.[2]

This funding gap can easily be filled by global financial institutions who already have access to USD 404 trillion in assets. Each of these institutions are unique in the way they operate, but they all can play a crucial role in helping us reach a low carbon world.

Insurance companies

Insurance companies will actually benefit from the low-carbon transition because companies across every sector will require insurance to protect new assets and projects. The premiums they earn are also likely to be invested over the long term in sustainable assets that aim to match their future liabilities.

They will be crucial in helping protect against climate catastrophes. The losses from perils such as severe convective storms or wildfires will need to be managed as their frequency increases with climate change. New innovative techniques will be needed to model these events and help insurers diversify their exposure.

The winners in the insurance sector are likely to be those groups with the right risk modelling, pricing and risk management at the heart of their business. It is these attributes amongst others that help them outperform.

Banks

Banks are very important in this fight against climate change. As lenders they can lower the cost of capital for building clean energy infrastructure. They can do this by simply facilitating the flow of money from the private sector into these projects. At present, deposits around the world are rising along with savings, which means banks have sufficient lines of funding to invest (see chart 4). In economics, savings equal investment, but in this case low-carbon investment.

Banks also work closely with fintech companies to provide new and innovative ways to raise finance that can help make renewable energy infrastructure affordable and bankable. They can help new initiatives overcome the institutional and financial barriers that fintech companies face.

Furthermore, through better funding, banks could actually cause the cost of generating renewable energy to fall even further and speed up the transition to a low-carbon world.[3]

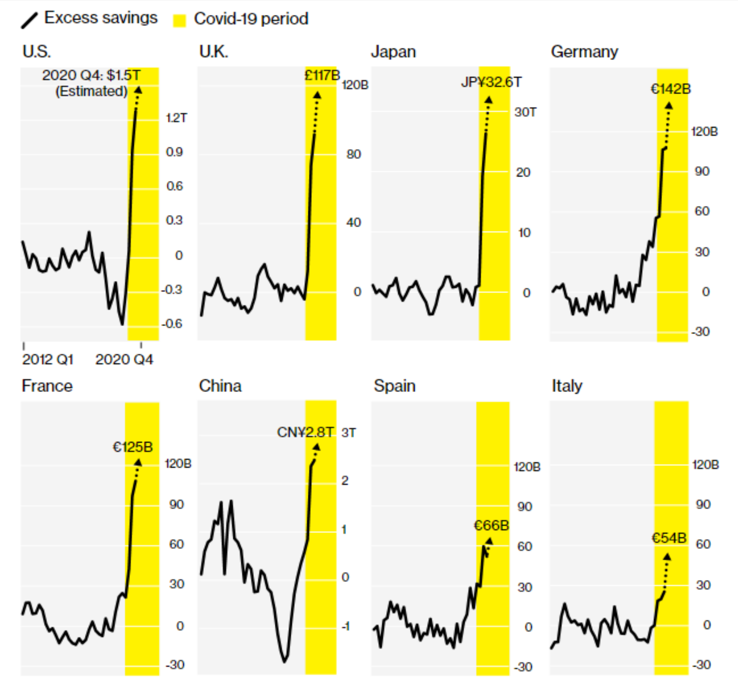
[2] Miller, G. (19 August 2021). Here's how to to bridge the net-zero funding gap. World Economic Forum. https://www.weforum.org/agenda/2021/08/nine-steps-to-bridge-the-net-zero-funding-gap/

[3] Schub, J. (27 August 2019). Why We Need Finance to Fight Climate Change. Yale Insights. https://insights.som.yale.edu/insights/why-we-need-finance-to-fight-climate-change

Chart 4: Savings equal investment

Savings to splurge

Lockdown barriers to spending combined with stimulus-boosted incomes have left consumers with massive pent-up savings



Source: National central banks and statistical agencies, Bloomberg Economics.

<u>Asset managers and wealth managers</u>

Asset managers will also provide important capital investment into sustainable projects and infrastructure on behalf of the investors they represent. Some of these flows will come from institutional investors, but they will also come from the wholesale market. This includes investments made by wealth managers on behalf of their high-net-worth client base. It also includes retail investors and those represented by financial advisors.

<u>Fintech and insurtech companies</u>

Fintech and insurtech companies will be vital for enabling sustainable investing through innovative digital technologies. These could be used to find alternative sources of funding and also help the wider industry quantify climate risks.

They will help measure and analyse the impact of climate change on the investment side, but also understand the risks and impacts of climate change on the liability side.

Data and automation will play a pivotal role by allowing them to help banks and insurers make smarter decisions. This includes loan book management, fraud reduction and overall risk management.

In addition to this, machine learning-based models developed by these companies may help the financial sector measure risk more accurately and at a much finer level.

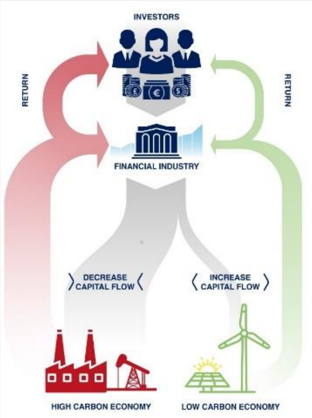
Our economy cannot transition to net-zero without the financial sector

This is something that is going to happen. Tackling climate change will be one of the biggest and most significant long-term structural trends that our global economy experiences this century. The investment opportunity is enormous. None of this can happen without the financial sector.

At present, capital is still flowing through our financial system to finance the high carbon economy (see figure 1). However, this is a transition and it is one where we will slowly see a decrease in capital flowing into high-carbon activities, as it increasingly flows into our new low carbon economy.

For investors, this is where the investment opportunity lies.

Figure 1: The great transition for high to low-carbon economy funding



Source: UNEP, Financial Institutions Taking Action on Climate Change, GlobeNewswire, March 2021.

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