A4S CFO LEADERSHIP NETWORK

DEVELOPING A NET ZERO TRANSITION PLAN – POLICY, PRODUCTS AND FINANCIAL PLANNING

Practical example: NatWest Group

NatWest Group

KING CHARLES III CHARITABLE FUND

WHAT

NatWest Group is a major UK-based relationship bank, with £366.3 billion of net lending to customers at the end of 2022. We aim to reach net zero greenhouse gas emissions by 2050 for our financing activity, assets under management and own operational value chain, supported by the following 2030 ambitions (all set against a 2019 baseline):

1. To at least halve the climate impact of our financing activity
2. To reduce the carbon intensity of our in-scope assets under management by 50%
3. To reduce emissions in our operational value chain by 50%

In February 2023, we published the initial iteration of our climate transition plan, which lays out the actions we are taking, and plan to take, to meet our net zero ambitions. Lending to customers drives the biggest part of our emissions, so our plan primarily focuses on how we can support our customers' transition.

While developing the climate transition plan has been a collaborative effort across the bank, the finance team drove and coordinated the process. A key principle for us in this process was aligning the transition plan with the financial forecast, which finance started to develop in 2022. This approach helps ensure that our transition plan is aligned with our overall strategy and forward-looking balance sheet changes.

"Finance has access to the financial plan and the future balance sheet … Starting with the financial forecast will be really helpful in developing a transition plan."

Supriya Sobti, Climate and Purpose Lead, NatWest Group plc

WHY

Having set our ambition to be a leading bank in the UK in helping to address the climate challenge, the next question was how we would achieve this. We had already done a lot of work in 2020 and 2021 on measuring our financed emissions baseline and understanding the climate impact of our financing activities. Once we had that starting point, it was important for us to turn our focus towards being able to plan and track progress from that baseline to our ambition.

We recognized that to meet our climate ambitions, we needed to define the tangible actions we would take, measure them and ensure these actions aligned with our strategy. In our plan, we wanted to be specific and proactive about how we intended to reduce our emissions and support our customers to transition.

A transition plan also gave us a structure for examining the expected impact of planned activities on our emissions so we could identify our progress against our climate ambitions. We also wanted to understand how that impact could be affected by the external environment. Focusing on impact enabled us to look beyond our own organization to ways that we could engage constructively with industry forums and regulators on climate.

HOW

Our approach is based on three interconnected layers that we considered in our planning (see page 28 of our 2022 Climate-related Disclosures Report for more detail):

1. **The policy environment** – broader government policies, including the UK's statutory commitment to achieving net zero by 2050, shape the environment in which both we and our customers operate.

2. **Business operations, products and services** – through working closely with our customers, product and service offerings can be designed to accelerate our customers' transition to net zero.

3. **Financial planning** – changes to the emissions on our forecast balance sheet show whether our plans put us on track to meet our climate ambitions and enable us to consider the cost of delivering our transition plan.

Supporting our customers' transition is key to our approach – a focus that is also reflected in our overall climate strategy. Throughout the process of developing our transition plan, we made sure that the plan would align with this broader climate strategy. The strategy also includes a target to provide £100 billion of climate and sustainable funding and financing between 1 July 2021 and the end of 2025, which will be an important enabler for supporting our customers' transition.

We started work on the transition plan by setting up sector-level working groups, focusing on the most significant sectors for us, based on their emissions and balance sheet materiality. We also prioritized sectors for which we have science-based targets in place. The working groups included staff from finance, risk, our Climate Centre of Excellence – an internal team set up to help us deliver our climate ambition – and sector specialists from our business teams.

"We have focused the initial iteration of our Climate transition plan on developing plans to support the transition of our customers in key sectors linked to property, energy, mobility and food systems as these have most impact on the UK's carbon footprint and our customers' day to day lives."

NatWest Group plc, 2022 Climate-related Disclosures Report

GOVERNANCE

In 2022, our board took an advisory climate resolution to the AGM: our ‘Say on Climate’. Shareholders had the opportunity to vote on our proposal to put in place a transition plan and to report on our progress each year. The resolution was a way for us to be transparent with shareholders about our climate ambitions and get feedback that we could bring into our work to develop the transition plan. Shareholders showed strong support, with over 92%[1] of votes cast in favour of the resolution.

This meant that the transition plan became a strategic focus area for us. Our board and board committees provided oversight during the development of the transition plan, supported by our Climate Change Executive Steering Group. Our Sustainable Banking Committee had a dedicated session to discuss progress on the transition plan, including the plans we had developed for different sectors. The board received updates in July, October and December 2022 and approved the initial iteration of our transition plan in February 2023.

We incorporated the climate metrics and initial climate transition plan outcomes in the financial planning governance and approvals process.

1 Votes cast with regard to the Say on Climate resolution (whether for or against) represent 85.96% of NatWest Group’s Total Voting Rights.

Figure 1: NatWest Group’s board-level governance (extract from 2022 Climate-related Disclosures Report)

GUIDANCE

As we started developing our climate transition plan in early 2022, the timing meant that much of our work on the transition plan took place before most guidance or frameworks existed. Early in 2022, the Glasgow Financial Alliance for Net Zero (GFANZ) was still developing its recommendations on net zero transition plans for financial institutions. The Transition Plan Taskforce (TPT) was established in the month our Say on Climate took place, and its proposed guidance wasn't released for consultation until late 2022.

We were keen, though, to use the best available external guidance as it developed. The Task Force on Climate-related Financial Disclosures (TCFD) had already released its guidance on transition plans, which gave us a useful starting point. We noted the recommendations from GFANZ and TPT as they developed – and, at the same time, took part in the discussions that helped to shape them. We used the essence of all the available guidance, aiming to find a balance between them, to make sure our transition plan was heading in the right direction.

"The initial iteration of our climate transition plan has been informed by the available guidance. We are aware that this guidance and standards will continue to develop, and we will continue to evolve our climate transition plan alongside these developments."

Supriya Sobti, Climate and Purpose Lead, NatWest Group plc

CONSIDERING THE POLICY ENVIRONMENT

We wanted to understand the external landscape to guide our internal actions. We have continued to consider the impact of UK policies since defining our climate ambitions in 2020, and this is one of the dependencies in our climate transition plan.

Government policies play a major role in incentivizing customer behaviour. So from the first meetings of our sector-level working groups, we wanted to understand the policies operating in the relevant sector and use this understanding to inform our discussions and plans. For example, knowing there was a transport policy to drive uptake of electric vehicles meant we could think about how to support our customers in making that transition.

We also needed to evaluate how changes to the UK government's policies between now and 2030 could affect our planned activities and expected results. The finance team worked with our Climate Centre of Excellence, who are internal policy experts in this area. Based on the expected policy trajectory outlined in the [Sixth Carbon Budget] from the Climate Change Committee (CCC) and the findings of the [Skidmore review], we identified relevant policies by sector – supplemented by the CCC's most recent progress report.

In its progress report, the CCC had assessed the credibility of the UK government's policies and plans. We used this to calculate an estimated delay to the policies. Where the CCC had identified some risks or significant risks, we estimated a delay of three to five years. For policy areas where the CCC considered that there were insufficient plans, we estimated a delay of ten years.

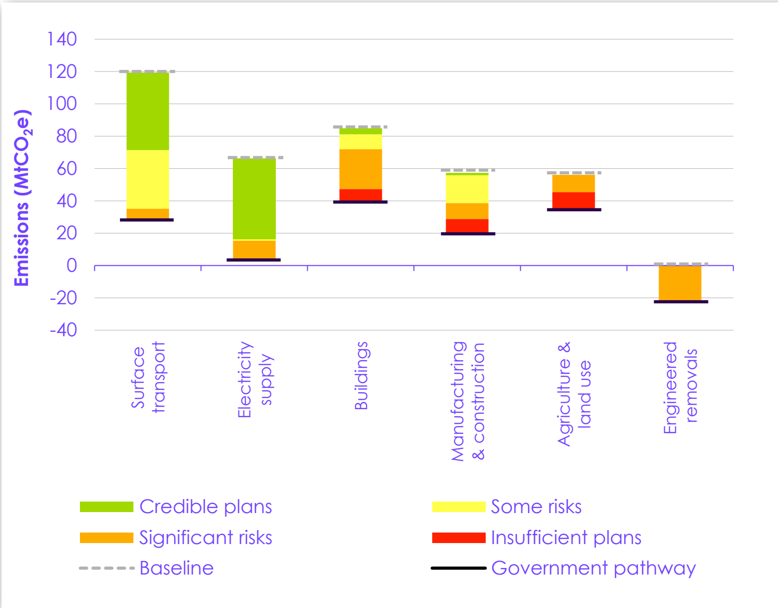

Figure 2: Assessment of policies and plans in 2035 for key sectors (extract from the CCC's Progress in Reducing Emissions report, 2022)

We then evaluated the effect we would expect the estimated delays to have on customer behaviour and financial planning. We used the results to model downside sensitivities and refine our transition plan.

DEVELOPING PRODUCTS AND SERVICES

Our sector-level working groups started by identifying the existing products and services that support the transition and have an impact on it. With this understanding of the current situation, we then explored how to expand those products and services. We wanted to understand our current position and impact, then consider how we could meet our ambitions and go further.

In this process of working at a sector level, we realized the extent to which sectors are interdependent. This prompted us to start thinking about products and services in the context of their wider systems. For example, retrofitting existing homes is important for reducing emissions in the mortgage sector, but it relies on the availability of contractors who can do the work and materials with which they can work. So when planning retrofitting-focused mortgage products, we also needed to consider the construction and manufacturing sectors. We are now using this understanding of the broader property system to plan actions and partnerships across the value chain that would help us maximize our impact.

FROM SECTOR TO SYSTEMS THINKING

No single sector – even with the best products – can achieve net zero alone. The upstream and downstream elements of a sector's value chain can either constrain or enable its plans for reducing emissions, and the best results are likely to be achieved when the full value chain is working towards the same goal. This showed us that we needed to think about reducing emissions from a system-wide perspective as we move beyond the initial iteration of our transition plan.

To start our system-focused work, we brought together the existing sector-level working groups so we could explore solutions in a more collaborative way. We aimed to find the key levers of change that would enable us to support decarbonization of those broader systems. This approach guided our work for the rest of 2022 and 2023, with our focus being on the property, mobility, energy, food and financial systems. We discussed our understanding of systems thinking in our 2022 Climate-related Disclosures Report and will use this structure as we continue to evolve our transition plan and climate reporting.

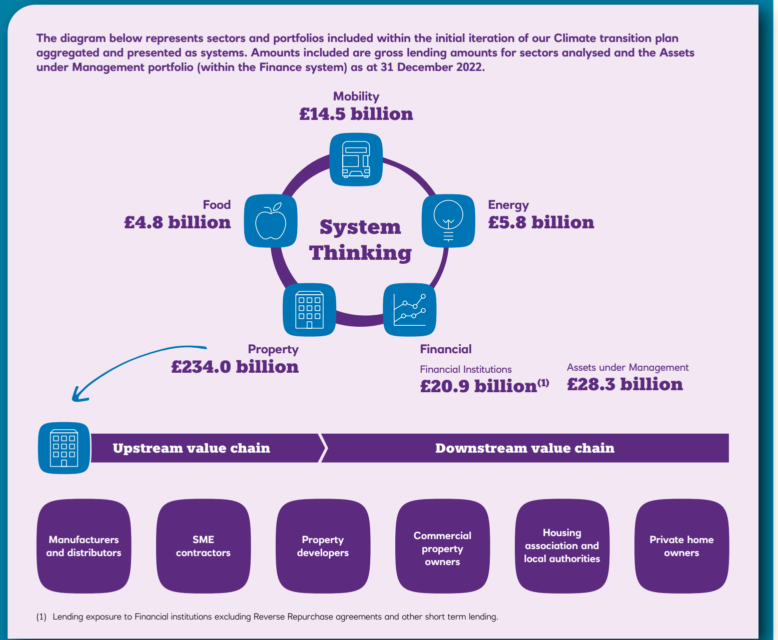

Figure 3: Systems thinking at NatWest Group (extract from 2022 Climate-related Disclosures Report

ENGAGEMENT WITH OUR VALUE CHAIN: THREE TOOLS TO SUPPORT THE TRANSITION

To support our customers' transition and embed climate in decision making, we are developing three tools:

- **Customer Transition Plan Assessment** – through this assessment, we can learn more about our customers' transition plans, the status of their transition and how we can provide support. This is a relationship manager-led process, and we are working to tailor the assessment for different customer segments and sectors so that the assessment better reflects the customer and sector context. We are also working on gathering information on the maturity of our customers' transition plans through our existing engagement with them.
- **Climate risk scorecards** – we were already using qualitative climate risk scorecards, and these new scorecards aim to introduce a more quantitative approach to assessing customers' climate risk. Drawing on the information we get from the Customer Transition Plan Assessment, the scorecards will enable us to assess the physical and transition risks faced by our customers. This will help us to determine how we – and our customers – can best mitigate the climate risks identified.
- **Internal carbon price** – we are working to develop an internal carbon price framework, for use alongside our other tools to inform decision making. When fully developed, we expect the internal carbon price to incorporate customer emissions profiles and information from our Customer Transition Plan Assessment.

FINANCIAL PLANNING

The next step was to understand whether our planned products and services would have the impact that we needed by bringing them into the financial forecasting process. By this point, we had developed specific actions that we felt were realistic given the policy environment, sector trends and expected customer behaviour. This included a list of products and services as well as enabling actions that were about influencing and educating our customers. Now we needed to align the transition plan with financial forecasts to ensure it was realistic and deliverable.

First, we wanted to see how the proposed actions from our transition plan were driving change on the balance sheet. We looked at how much of the forecast balance sheet came from climate-related elements, such as lending that supports the transition. Then we could compare the forecast proportion of climate-related elements to both our current balance sheet and future forecast.

To achieve this, we set up a finance working group, which included staff from the financial planning, climate and business finance teams. Collaborating with finance teams across the business meant that we could reflect a strong understanding of all our products and services in our planning.

> "One of the things we've been keen to do is make sure that our initial climate transition plan aligns with our financial forecast. We made a start in 2022 and will continue to enhance this alignment during 2023."
>
> **Supriya Sobti, Climate and Purpose Lead, NatWest Group plc**

To ensure that business teams were comfortable with the shape of the initial climate transition plan, we had a continuous loop of review and challenge with them throughout the development of the transition plan. We found that this was a powerful way to illustrate what the proposed business activities really meant for our climate ambitions. With that understanding, we refined the plans as needed, which included identifying areas where we needed to take more action, including education, promotions, partnerships, products and services, and business model changes.

More information on our approach to financial planning can be found on page 31 of our 2022 Climate-related Disclosures Report.

NEXT STEPS

Now that we have published the initial iteration of our transition plan, we will continue to iterate and enhance this to ensure it is relevant and meaningful, while applying a systems-thinking approach. We will continue to monitor the policy environment and broader social context, consider how this will influence customer behaviour, and think about what this means for our own plans. Guidance on transition plans will also be evolving over the next few years, and we will adapt and update our transition plan to align with the spirit of that guidance.

As we develop future iterations of our transition plan, we will continue to work on the alignment with our financial planning processes. This will include business teams considering their climate impacts as they prepare their financial plans, and we plan to model emissions alongside the financial forecast. This will strengthen the embedding of our climate ambitions within decision making and existing planning processes. We will continue to enhance the tools and methodologies we use for estimating financed emissions as well as the transition plan.

Supporting customers' transition will remain at the heart of our climate strategy and our transition plan. Another focus for us now that we have the plan in place is to continue to build customers' awareness and understanding of the tools and products available to them.

Beyond this, we will continue to establish partnerships and be involved in industry discussions around standards and guidance for transition plans. We hope that the industry will converge around one standard, and we will contribute to working towards that goal.

TOP TIPS

USE YOUR STRENGTHS

Bring your finance skills and expertise in analysis into the process. Start with what you know – products and services, financial forecasts and data analysis – and while methodologies are still developing, don't wait to make a start.

FIND INTERNAL ALLIES

Having allies in the organization can help you build momentum. It is especially useful to have allies at senior executive level, who can provide a top-down push to get things moving.

ALIGN WITH STRATEGY AND FINANCIAL PLANNING

Make sure that your transition plan is consistent with the direction of travel of your organization and an integral part of its strategy, not treated as a separate approach. Fully integrate your transition plan into your financial planning and budgeting processes.

TAKE ADVANTAGE OF AVAILABLE RESOURCES AND INSIGHTS

Many more resources and guidance are now available – so use them. The whole industry is still learning, but you can learn a lot from what's already out there. Work collaboratively with others to share and develop your approach. Engage in industry forums.

DON'T EXPECT PERFECTION

Your transition plan won't be perfect first time. Even the guidance and expectations are still developing. Do what you can, use it to inform your work and refine the transition plan over time.

GET IN TOUCH OR FIND OUT MORE

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Important information