ACCOUNTING FOR SUSTAINABILITY

REDUCING FINANCED EMISSIONS TO MEET OUR CLIMATE AMBITION

Case study: NatWest Group
NatWest Group is the largest business and commercial bank in the UK, with a significant retail business. Our ambition is to be a leading bank in the UK and Republic of Ireland (RoI) helping to address the climate challenge. Climate is a key area of focus in our purpose-led strategy, alongside Enterprise and Learning.

In February 2020 we announced our climate ambition, which includes the following:

1. At least halving the climate impact of our financing activity by 2030.
2. Supporting mortgage customers to increase their residential energy efficiency and incentivize purchasing of the most energy efficient homes, with an ambition that 50% of our UK and RoI mortgage customers’ homes are at or above Energy Performance Certificate (EPC) rating C, or equivalent, by 2030.
4. Making our own operations Climate Positive by 2025.
5. Stop lending and underwriting to companies with more than 15% of activities related to thermal and lignite coal, and major oil and gas producers; unless they have a credible transition plan in line with the 2015 Paris Agreement by the end of 2021. We plan a full phase-out from coal by 2030.

To support the delivery of our climate ambition, we are assessing the greenhouse gas (GHG) emissions associated with our loans and investments (financed emissions). To this effect, we have used available guidance eg the global GHG accounting standard of the Partnership for Carbon Accounting Financials (PCAF) – being the first major UK Bank to join PCAF – and have adopted the guidance methodology for financial institutions by the Science Based Targets initiative (SBTi). For year end 2020, we produced our first standalone climate-related disclosures report, which included preliminary estimates of our financed emissions.

Recently, NatWest Group became a founding member of the Net Zero Banking Alliance. This also confirmed our ambition to reach net zero carbon on our financed emissions by 2050.

We recognize that climate change is a critical global issue which has significant implications for our customers, employees, suppliers, partners and therefore NatWest Group itself. This motivated us to include climate in our purpose-led strategy. We recognize that a large share of our climate impact is beyond our direct operations; estimating our financed emissions gives us a way to understand that impact in more detail. Through this we can identify how we can accelerate the speed of transition and use the results in our decision making.

Climate change is also an area of increasing focus from policymakers and regulators, with the upcoming 2021 UN Climate Change Conference (COP26) a driving force for global action. Meanwhile, recent regulatory developments in the UK and Europe are showing a trend towards mandatory disclosures and new reporting frameworks. Although we were already working on climate-related disclosures, the expectation and pace of regulatory change is an incentive to accelerate this work.

Voluntary climate reporting was a natural direction for us to take. Having set our goal of reducing our financed emissions, we wanted to be transparent about our progress. There is also an expectation from the market to see how we are performing against our climate ambition. Our early reporting gives us the opportunity to play a part in industry discussions to support enhancements in emissions calculations and reporting.

Case study: NatWest Group
The announcement of our climate ambition in 2020 was a critical point in our journey to estimate financed emissions. We are working towards embedding climate into our decision making, governance and risk management, as well as our business plans. The link to our strategy has also been useful for staff engagement, establishing it as a key business priority.

Although the calculation of financed emissions started as a strategy-led programme, the involvement of the finance function now supports the review, analysis, development and embedding of measurement capabilities.

For our preliminary estimates of financed emissions, we focused on four sectors: residential mortgages, oil and gas extraction, agriculture (primary farming) and automotive manufacturing. We selected them based on a combination of the sector’s potential climate impact and their materiality to our loans and investments portfolio.

In finalizing our first focus sectors, we also reviewed whether appropriate methodologies existed for estimating their emissions and emissions intensity.

Having set the ambition and selected our focus sectors, we needed to start calculating our current financed emissions. We acknowledged from the outset that the analysis of financed emissions would be challenging with new and evolving methodologies. During 2020, we joined market-leading collaborative groups with the aim of supporting the development of market standards. For our preliminary estimates, we leveraged existing standards and learning across the industry. Amongst others, the PCAF standard was a useful starting point for methodologies that we could apply. More recently, SBTi published its guidance methodology for financial institutions, which we drew on as well. These approaches guided us in how we selected and analysed our data.

In the next sections, we explore our approach in more detail.

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2. See page 54 of NatWest Group’s Climate-related disclosures report 2020 for the full list of methodologies and standards used.
WORKING TOGETHER

Staff from finance, legal, risk, business, strategy and data functions were part of our core team for starting the process of calculating and reporting financed emissions. This team drove forward the agenda and spread awareness across other areas of the bank of what we were doing. As we expanded the work, other staff contributed key skills and knowledge and we will continue working collectively to improve our understanding, clarify roles and responsibilities and develop detailed plans to achieve our goals.

Finance plays a key role in holding the business to account, so engaging finance is important for developing measurement and supporting the business and other teams to make this business as usual. In 2020, finance mostly focused on developing the reporting process as well as supporting the on-going measurement work. As we mature our capabilities, finance’s role is evolving to include overall management of the measurement and reporting processes. This will include reviewing data and methodologies, developing management information and reporting, as well as incorporating financed carbon emissions into our financial processes.

More broadly, education amongst all colleagues has been a key focus of the bank during 2020 to help embed climate into our culture, including identification and management of climate-related risks and opportunities across NatWest Group. Approximately 800 colleagues participated in a 12-week programme launched during 2020, developed specifically for NatWest Group in collaboration with a UK-based university.

In addition, the finance team has established a climate technical forum attended by staff from various areas to support decision making and to enhance knowledge of financed emissions’ calculations and methodologies. We found it helpful to start by discussing the methodologies and calculations underlying the emissions data in advance of assessing impacts on various areas.
OUR DATA AND REPORTING

Data is central to calculating our financed emissions, so we needed to get our data processes set up quickly.

**Data**

Preparing the first calculations gave us useful experience in applying the PCAF approach and identifying our data gaps. Although there are many methodologies available, following one primary standard for measuring financed emissions, as much as possible, helped to focus our work as we moved from concept to practice. When we understood the data requirements for our sectors and methodologies, the data and analytics team led the work to source it. They aimed to get the best quality data that was feasible, guided by the PCAF data scoring methodology for data quality that is included within the PCAF standard.

For each sector, we used a mixture of sourced and extrapolated data to calculate our estimated financed emissions. In residential mortgages, for example, we used a government data source for EPC data, which was available for just under half of our portfolio. In cases where no data was available, we applied the average emissions profile based on the EPC data we did have. The next step was to review and challenge those calculations. We validated the results with our business colleagues to make sure that the financed emissions we had calculated seemed reasonable.

**Reporting**

The climate-related disclosures report explains our approach to financed emissions. For each sector we reported on how financed emissions were calculated and the types of publicly available and extrapolated data that we used. We also calculated and reported the weighted PCAF data quality score and dedicated a section of our report to the limitations of climate metrics and our estimates, including:

- Lack of reliable emissions and other important data
- Lack of standardization, transparency and comparability
- Reliance on assumptions and future uncertainty
- Variation in approaches and outcomes

Our auditors provided independent limited assurance over selected environmental, social and governance content (including climate-related disclosures) for the year ended 31st December 2020. We continue to engage with our auditors as we plan how to build on our current reporting.

3. For more detailed information on data availability and quality by focus sector, see sections 5.6.1 – 5.6.4 of NatWest Group’s Climate-related disclosures report 2020
4. For further details, see section 5.7 of NatWest Group’s Climate-related disclosures report 2020
A SECTOR-DRIVEN APPROACH TO REDUCING EMISSIONS

Understanding our financed emissions for specific sectors will enable us to set sector-specific targets that support our overall ambition and develop plans for reducing emissions.

We aim to engage and support our customers’ transition to a net zero economy, and we are committed to working collaboratively and exploring options with our partners, stakeholders and peers to deliver our climate ambition and achieve a better future for everyone.

**Automotive sector**

The automotive sector has some natural opportunities for emissions reduction. For example in the UK, our primary market, the government has announced plans to phase out petrol and diesel cars. A switch from internal combustion engine vehicles to electric vehicles can play a key role in achieving Paris-alignment in the automotive sector. To support this, we have partnered with Octopus Energy to support our customers’ transition to electric vehicles.

**Residential mortgages sector**

For residential mortgages, we know we can play an important role engaging with our mortgage customers to inform and increase awareness of the benefits and options available, helping them to improve home energy efficiency through making home improvements. Building on the launch of our Green Mortgage product, we will continue to develop green financial products to reward and incentivize the purchase of the most energy efficient properties, measured by their EPC, and also to allow customers to fund home improvements that increase the energy efficiency of existing properties. We will also take a proactive stance to sector engagement, working with government, as well as across the finance sector with non-governmental organizations (eg the Green Finance Institute) to align to industry standards and create consistency for customers regarding green financing.
NEXT STEPS

We are now exploring how to improve the calculations for our current focus sectors – by enhancing our data and further developing our methodologies – and plan to expand to other sectors. In particular, we will engage with customers, stakeholders, and participate in wider initiatives, to help enhance the availability of granular climate-related data for customers, with the aim to improve the quality of future estimates.

Using the preliminary financed emissions estimates, we are working with our business colleagues to set actions to support the transition to a net zero economy. In order to embed these actions into decision making across the organization, we are focusing on building our climate data capability, introducing new tools which integrate with financial planning, and also on education. Over time, we expect climate data granularity to improve as we move towards utilizing direct customer climate data. The financed emissions calculation will also help us with our customer engagement.

In the short term, we are focusing on building financed emissions into our regular management information so that users can start actively using this data.
TOP TIPS

START

Don’t be afraid to get started – just start. The data and calculations won’t be perfect, but the sooner you start to calculate your financed emissions the sooner you can plan to reduce them. That is something we need to do both as individual organizations and as an industry.

PLAN HOW YOU WILL USE FINANCED EMISSIONS ESTIMATES

It’s easy to get lost in the technicalities and the detail of the data, but avoid getting too embroiled. You need to use this information in your working practices: that’s how you create change. This is a big shift in culture and behaviour, so start planning for this early.

INTEGRATE FINANCED EMISSIONS INTO FINANCE

You will see very quickly how managing financed emissions links to finance’s work. Finance needs to have carbon in its language, alongside debits, credits, profit and loss. Make sure that you are training finance staff so they build their own knowledge of carbon emissions similar to financial metrics.

COLLABORATE WIDELY

There are many opportunities to collaborate with the industry, in particular as we go through the sector-by-sector analysis. We found it invaluable to work with PCAF and have conversations with other banks. As the banking corporate sponsor of COP26, we recognize the need for collaboration and cooperation that must take place between governments, businesses, regulators and society, and the key role of the finance sector to support the transition to a net zero economy.
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