Banking & Payments Federation Ireland

BPFI Sustainable Finance Paper

Continued Public-Private Coordination Central to Ireland's Transition to Net Zero

Introductory remarks from Banking & Payments Federation Ireland Chief Executive, Mr. Brian Hayes.

Economies and societies are increasingly facing the complex and severe consequences of biodiversity loss and climate change. Against this background, legislators in the European Union (EU) and around the world are taking actions to change economic activities that have significant adverse impacts on environmental, social and governance (ESG) factors and to alleviate the worst consequences. While these policies will be gradually introduced and take full effect for financial market participants over a longer time, it is crucial to develop strategies to be able to cope with such changes.

The critical role of private finance in limiting global warming to 1.5 degrees Celsius has moved to centre stage at a global level and in Ireland. In November 2021, COP26 demonstrated the dynamic transition underway in the banking sector. The Glasgow Financial Alliance for Net Zero (GFANZ) commitment means banks, worth $130 trillion (including Irish retail banks), will work towards a net-zero planet by 2050.

The IMF estimates that envisaged emission reduction target in Ireland will require investment of close to €20 billion per annum over the next ten years of which about one third would be public capital spending and the rest would have to come from private investment.

However, time is of the essence in addressing the climate crisis. Businesses in Ireland need capital to achieve the significant changes required and consumers need finance to support their private transition. This is why international and EU policymakers, in delivering on the objectives of the Paris Agreement, have focused on the crucial role of investors, lenders and insurers to provide such finance and to incentivise and support their clients and investee companies as they make the transition.

Irish retail banks are leading the way and are pro-actively driving the transition to a carbon-neutral economy. It is via the retail banking sector in Ireland, represented by BPFI, that business and wider society will achieve the goals necessary to protect our planet for future generations.

The objective of this paper is to articulate the work being undertaken by retail banks in Ireland in the sustainable finance space and the absolute imperative of effective government and private sector partnership to help reorientate capital flows and support consumer and business behaviour to achieving net zero. A brief overview is provided of the policy and regulatory context to which retail banks have responded in their strategic and risk management frameworks. Strategic action taken by retail banks, along with the ongoing engagement work of BPFI as the representative body for banks in Ireland, are summarised. Finally, pivotal public-private initiatives to deliver on environmental goals are highlighted.

Brian Hayes
Chief Executive
Banking & Payments Federation of Ireland
November 2022

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About Banking & Payments Federation Ireland

Banking & Payments Federation Ireland (BPFI) represents the banking, payments and fintech sector in Ireland. Together with its affiliates, the Federation of International Banks in Ireland, and the Fintech & Payments Association of Ireland, BPFI has 100 member institutions and associates, including licensed domestic and foreign banks and institutions operating in the financial marketplace here.

BPFI advocate at a domestic and EU level on all issues impacting the operating environment for our membership, and work to promote an environment that is as supportive as possible for our membership to maintain and grow their operations in Ireland.

Executive Summary

It is impossible for companies and society to ignore the tsunami-like emphasis on Environmental Social and Governance (ESG) issues in recent years. The science is indisputable, and the effects of climate change are already clear. Extreme weather events are becoming more frequent with devastating consequences. Indeed, the extreme heat that millions of Europeans have experienced this summer provides a tangible reminder of the need to address global warming.

Such evidence is testament as to why such ambitious and urgent targets have been set by the UN, the EU, and the Irish Government, all supported by an array of stakeholders from environmental organisations, scientists to investors, consumers, and society at large.

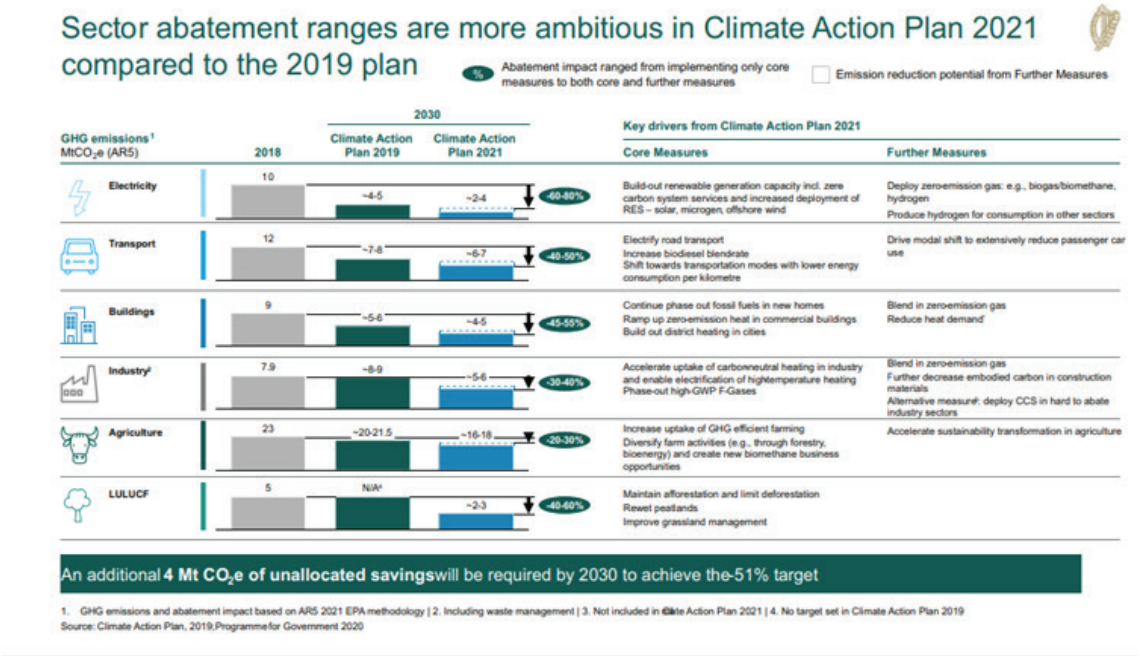
The Irish Government's Climate Action Plan 2021 reflects Ireland's commitment to achieving the 2030 Agenda for Sustainable Development. Ireland is working with its international partners to ensure that climate action remains a major policy priority, in recognition of the grave threat climate change poses to the achievement of the UN's Sustainable Development Goals globally.

The Climate Action Plan

The Climate Action Plan 2021 provides a detailed blueprint for taking decisive action to achieve a 51% reduction in overall greenhouse gas emissions by 2030 and setting Ireland on a path to reach net-zero emissions by no later than 2050, as committed to in the Programme for Government and set out in the Climate Act 2021. The Climate Action Plan lists the actions needed to deliver on our climate targets and sets indicative ranges of emissions reductions for each sector of the economy. This plan makes Ireland one of the most ambitious countries in the world on climate.

The Government's Climate Action Plan has made it clear that all sectors will be involved in the monumental transition that lies ahead. The figure below shows a sectoral split of the implied emission targets by 2030 and identifies the relevant core and further measures required.

We know that change is underway, but the targets leave us in no doubt that a mountain has yet to be climbed. Businesses and consumers across Ireland are at different stages in their transition journey towards low-carbon and sustainable activities.



Source: The Climate Action Plan, Figure 4.3

New research – consumers and businesses

New research carried out by Amárach for BPFI shows hugely encouraging progress when it comes to consumer behaviour around green initiatives. Two-thirds (64%) of respondents had at least one significant home improvement to improve energy efficiency with 42% of respondents planning to do at least one in the next three years.

However, much remains to be done. For example, only circa one in ten respondents said their home used solar power (13%) or heat pump systems (11%) with only 18% and 13% of respondents, respectively, planning to invest in these in the next three years. 42% of respondents said they had looked into solar power (33% for heat pumps) but were unlikely to make the investment in the next three years.

Consumer motivation for making such investments is also of huge interest. Customers are, at this time of high energy costs, more motivated by saving on costs (47%) than on the broader global goal of reducing temperatures and emissions (8%).

When we look to the behaviour of businesses, there is progress, but it is fair to say that much work remains to be done if Ireland is to reach its goals. Commission for Regulation of Utilities (CRU) research[1] on SMEs indicates the challenges that need to be addressed: some SMEs have made significant energy efficiency improvements in 2020 compared to 2019, however consideration of getting green power products in the future has declined across all different categories of green products, a worrying trend given the climate goals that need to be met.

Role of Banks

The role of the financial services sector in supporting a business, consumer, and societal transition to net zero is already at the heart of global policy frameworks and manifested in the EU Action Plan on Sustainable Finance, the EU Green Deal and the Irish government's Climate Action Plan.

The IMF estimates that the envisaged emission reduction target in Ireland will require investment close to €20 billion per annum over the next ten years of which about one third would be public capital spending, with the remainder coming from private finance. In Ireland without private sector finance, the targets set out within the Climate Action Plan cannot be achieved. The plan provides insight into likely opportunities for private finance, with mobilisation of €125 billion of capital investment in low-carbon technologies and infrastructure required up to 2030. Private finance in Ireland must be mobilized to support the transition by businesses and consumers in Ireland to achieve these targets.

Irish retail banks have a key role to play in supporting this cross-sectoral transition, especially for buildings, with residential mortgages and property-related lending equivalent to 78% of all private-sector lending to Irish residents at the end of 2021.

The government has targeted a reduction of 40% in emissions for residential buildings by 2030 and 45% reduction for commercial and public sector buildings. To achieve these targets, the government wants to see 0.5 million existing homes upgraded to B2 Building Energy Rating (BER) and 0.6 million heat pumps installed (of which 0.4 million would be installed in existing homes).

BPFI research highlights the critical role of financing in achieving our national targets. According to the Amárach research, 50% of consumers who have improved or plan to improve their home's energy efficiency rely on savings; between 43% and 54% of those planning to make home energy improvements in the next three years plan to use savings with between 26% and 38% planning to use government grants; credit union or bank loans or mortgage top-ups for the most part make up the rest of the financing.

The combination of savings, green finance and Government supports are key when it came to buying cars according to the research, highlighting the importance of public and private sector co-ordination when it comes to 'green transitioning' Ireland's car owners.

A total of 45% of those who bought any car type in the past year used savings with the use of other financing varying depending on whether the car was new or second-hand: about 21% of new car buyers are using hire purchase or personal contract plans, while 40% of second-hand car buyers used credit union or bank loans (33% of new). Buyers of new electric cars benefitted from government grants with 26,392 electric vehicle grants provided to consumers by the Sustainable Energy Authority of Ireland up to May 2022. The motivation for going green when it comes to cars was also extremely positive. It seems transport may be the first sector where going green for the sake of the environment is a key factor in customer decision making (25%).

Progress to date by banks

Irish retail banks have already made significant movements to deliver on the objectives of the Irish government's Climate Action Plan by providing much-needed finance at preferable green interest rates to thousands of customers to improve their energy efficiency:

- BPFI estimates that 65,000 new and second-hand green homes were bought with residential mortgages between 2017 and 2021, with more than 14,000 in 2021 alone;
- An estimated 3-4,000 personal loans and mortgage top-ups for electric or hybrid-electric cars;
- More than 54,000 home improvement loans, including loans for home retrofits, in the twelve months ending March 2022;
- Retail banks' green bond frameworks are used to fund their projects or assets that mitigate climate change by reducing emissions, protecting ecosystems, or having a positive environmental impact, specifically renewable energy, buildings and energy efficiency, clean transport. The sector has raised approximately €3 billion in outstanding green bonds. In addition, the Irish state has raised, through the National Treasury Management Agency's Irish Green Sovereign Bond Framework, around €6 billion since the first green bond issuance in 2018. The Irish Green Bond issuance is one of seven other euro area governments that issued green bonds in recent years.

Enhanced Public-Private coordination central to achieving future goals

The steps being taken towards increased sustainability, however, can be bolstered through continued, deeper partnerships between the retail banking sector, Government, and state bodies (Public-Private coordination).

Enhanced Public-Private coordination is essential for the successful decarbonisation of the economy in Ireland. BPFI's objective in its engagements to date has been to support Ireland's economy and society to make the climate transition in an equitable and positive fashion and to encourage sustainable economic activities. Further collaboration and coordination will assist in the scaling of green financing, identifying, and managing climate risk and supporting households, SMEs, and businesses to avail of energy efficient choices.

BPFI believe that a Public-Private coordinated approach will optimise the ability of state bodies and the private sector including retail banks to identify actions required to deliver on Ireland's climate targets. BPFI and its members are already engaging with and supporting the Irish Government to this end. In the context of a Public-Private coordinated approach, BPFI consider there are several key ingredients which could be pursued and worked upon together to effectively serve customers and businesses in their transition to net-zero:

1. Cross-sector Policy Certainty

Ireland's Climate Action Plan sets out the actions required to meet Ireland's EU 2030 targets and its net zero emissions goal by 2050, focusing on the key sectors of electricity, transport, residential, commercial, and public buildings, industry, and agriculture. The plan provides insight into government policy incentives to enable the transition and likely opportunities for private finance, with mobilisation of €125 billion of capital investment in low-carbon technologies and infrastructure required up to 2030. All sectors included in the Climate Action Plan require continued policy certainty for strategic and planning purposes. Indeed, the radical and long-term policy changes required to deliver on the government's 2050 net zero targets could potentially create considerable disruption if not implemented in a targeted and measured way. Continued policy certainty is essential for both the regulated financial services sector and, importantly, the sectors that are customers and clients of financial services firms. Continued provision of this certainty should be an absolute priority for the government.

2. Sectoral Transition Pathways

Government's provision of sectoral transition pathways is essential to foster, achievable and orderly transitions to net zero for each area of the economy. To translate climate ambition into climate action, banks must be able to understand transition pathways for each economic sector they support to enable the appropriate provision of advice and financing to each sector. In this regard, national legislation and policy guidance introduced in recent months is informing the context within which Irish retail banks engage with their clients including households, SMEs, and corporates as they support them to make the decarbonising transition of their economic activities.

The creation of sectoral pathways will also help the domestic business sector to develop realistic and detailed pipelines of sustainable projects into which finance can be provided. Private enterprises need to incorporate the true costs of unsustainability and the myriad opportunities for sustainable investments into their business models, in the process developing a pipeline of bankable sustainable projects. Retail banks, in turn, can mobilise the funding required to support their business customers through the issuance of green bonds and the provision of finance at rates linked to customer transition projects. This in turn will inform retail banks' strategic plans and prioritisation.

3. Requisite Skills

A recent BPFI survey of its membership indicated that nearly 20% of respondents believe availability of requisite skillsets is the biggest challenge to achieving the Government's ambition to become a green finance hub. According to Skillnet's Sustainable Finance Skills Gap Report 2021, traditional finance training is inadequate in its current form as it does not take into consideration broader ESG impacts and how this relates to financial impact. BPFI participates in the SF Skillnet Steering Group, to proactively promote and facilitate workforce learning in the area of Sustainable Finance within the Financial Services sector. We welcome the Government to endorse, support and incentivise the enhancements of skills in the financial services sector.
According to the state's training agency Solas, an additional 52,000 construction workers are required by 2030 to meet both new housing and retrofit targets.

Given the urgency of retrofitting targets, the Government must continue to facilitate and incentivise training in this space.

4. Influencing Consumer Behaviour

The critical role of the consumer and the public at large in the success of meeting climate goals is often overlooked. Through their purchasing habits and behaviours, however, they can directly and indirectly support the Climate Action Plan. For Ireland to reach the targets set by government, consumers and the public must play their part. As highlighted earlier, recent BPFI research (see also Section 3) has indicated that reducing energy/fuel costs is the main motive for customers to go green, which is not surprising in the current inflationary environment. However, it is to be noted that costs savings are a much more dominant motivation than supporting the transition to net zero. Whatever the primary motivation, what is positive is that consumers want to change. They are using hard earned saving to do so but can't transition on savings along. Affordable lending to supplement Government grants is required. It is vital that the transition process is made simple, and that Public-Private coordination ensures the momentum and the desire to change behaviour is made possible.

5. Incentives for SMEs

SMEs and business play a significant role in meeting Ireland's climate targets and Irish retail banks are supporting the transition with products and advisory services. However, Government might consider providing initiatives and incentives to SMEs like those offered to households under the National Retrofit Office. SMEs will require access to information and coordinated Public-Private effort to make the changes required to be more energy efficient.

Retail lenders have a role in supporting SMEs to make the transition; they are developing products and training relationship managers to help SMEs to both appreciate the opportunities and manage the transition of their business to more sustainable activities.

As also highlighted earlier, a recent survey carried out for the CRU in relation to electricity and gas markets in Ireland show that some SMEs have made significant energy efficiency improvements in 2020 compared to 2019 but consideration of getting green power products in the future has declined across all different categories of green products. To meet the Government targets on climate action and particularly to incentive consumers and businesses to prioritise actions to reduce greenhouse gas emissions, the Government might consider using incentives to stimulate behavioural change.

6. Reliable and consistent data

Given that almost 80% of lending by retail banks in Ireland is linked to property and with the integration of climate-related factors into the regulatory framework, it is crucial that banks begin to fully understand the existing risks on their balance sheet and how future lending decisions could alter their risk profile. To be effective in scaling up financing of energy efficiency and understanding balance sheet risks and opportunities, lenders need access to detailed, accurate information on energy performance. Having accurate and up-to-date data on exposures is critical. The results of the ECB's first climate-related stress test for the banking sector found that most banks which had gone through the stress test had an over-reliance on the use of proxy data when attempting to classify the energy performance of property. Specifically, the ECB noted that "65% of the banks [that went through the stress test] had to use [data] proxies, which in some cases are not adequately described or not sufficiently robust given the nature and number of assumptions banks need to make"[1] . One of its key recommendations to banks was to "become less dependent on the use of proxies, particularly in view of possible developments in climate risk disclosure regulations" and they need to make "progress in developing data infrastructures that allow for proper counterparty assessments"[2] .

The EU's current revision of the Energy Performance Buildings Directive (EPBD) is an opportunity to ensure access for financial service providers to the energy performance information of residential properties.

The EPBD revision will prompt enhanced energy efficiency by requiring further carbon emission reduction targets, leading to improved rates of renovation and the facilitation of more targeted financing to investments in the building sector, once appropriately calibrated. As discussed elsewhere in this report, Irish retail banks have developed innovative products to support customers buying energy efficient homes or financing renovations to improve energy efficiency.

The national database on energy performance certificates, known as BER in Ireland, is managed by the Sustainable Energy Authority of Ireland (SEAI). To facilitate lenders access to this database in a limited and supervised manner, BPFI has sought an amendment of the current regulation in Ireland but believes the current review of the EPBD represents an opportunity to secure changes needed, aligned with GDPR requirements, and ensuring a level-playing field across the EU. While the initial EC proposal sought to address this information asymmetry by providing financial institutions with access to energy performance databases under Art 19, BPFI believes the current drafting is too limited and should be revised to ensure that financial institutions can determine alignment with the building related elements of the EU taxonomy (to fulfil Taxonomy's technical screening criteria), while abiding by GDPR.

1 ECB 2022 climate risk stress test. https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.climate_stress_test_report.20220708~2e3cc0999f.en.pdf

2 Ibid.

1. Policy, Legislative and Regulatory Context Overview: Expectations for the Role of Retail Banks

"- …….. **if we do nothing to tackle the climate crisis, we risk knocking 10 percent off European GDP." Mairead McGuinness, Commissioner,** 4th ECB Forum on banking supervision, 16th November 2021

This section provides a brief overview of the legislative and regulatory frameworks globally and at EC and domestic levels seeking to influence the drive towards net zero. It provides important insight into the context in which retail banks in Ireland are operating strategically and from a risk management perspective.

Global Initiatives

The Paris Agreement[3] is the over-arching global commitment directing regulatory efforts towards mitigating climate change and supporting market-driven impact. It was the first ever universal, legally- binding global agreement on climate change. The Paris Agreement sits within the United Nations Framework Convention on Climate Change (UNFCCC) and was first adopted by 196 parties at the Conference of the Parties (COP) 21 in Paris on December 12, 2015. The Paris Agreement sets out a global framework to limit global warming to below 2°C and work towards limiting it to 1.5°C. It also aims to strengthen countries' ability to manage the impacts of climate change. It works on a five-year cycle of action points.

The Paris Agreement is unique as the first global agreement to specifically highlight the r**ole of finance and the private sector as key tools in the battle against climate change.** The Agreement places substantial emphasis on climate-related capacity-building, including the financing of projects (both from the public and private sectors) that enable countries to deal with the impact of climate change.

Alongside the Paris Agreement sits the UN's Agenda 2030, at the heart of which sits 17 **Sustainable Development Goals (SDGs)** laying out a path to end extreme poverty, fight inequality and injustice, and protect the planet. The Agenda 2030 was signed in New York in September 2015 by all Member States of the UN and is managed by the UN Global Compact.

On September 24th 2018, the UN Secretary-General released a four-year strategy for financing the 2030 Agenda for Sustainable Development, which underscores the UN's critical role in supporting and accelerating the mobilisation of sustainable financial markets. It focuses on three objectives:

1. Aligning global economic policies and financial systems with the 2030 Agenda;
2. Enhancing sustainable financing strategies and investments at regional and country levels; and
3. Seizing the potential of financial innovations, new technologies and digitalization to provide equitable access to finance.

3 https://ec.europa.eu/clima/policies/international/negotiations/paris_en

The strategy specifically urges a shift towards sustainable finance through the use of regulation and incentives, This has resulted in a clear global shift towards "greening" financial systems, with the SDGs at its heart. Financial sector policymakers, regulators and supervisors, and market participants are taking steps toward building a more sustainable financial system. The strategy calls for countries to strengthen enabling environments to reduce investment risks. These include:

- Predictable and rational policies and regulations;
- Stronger public institutions and the rule of law;
- Efforts to deepen still embryonic domestic financial systems; and
- A financial regulatory and supervisory regime that strengthens stability while avoiding the inadvertent deepening of the short-termism of private capital markets

European Commission Initiatives

The European Commission, which has led much of the regulatory drive across global financial markets, tends to refer to 'sustainability' and 'sustainability risk' rather than ESG, with a focus on the economic benefits of a climate-neutral economy. However, ESG considerations are at the heart of this drive, and constitute a globally accepted and understood framework of criteria. With new regulatory requirements come a whole new set of challenges:

- disparity and fragmentation of ESG reporting frameworks
- differences between regional regulatory approaches
- varying and complex data requirements needed to meet both demands

EU Action Plan on Sustainable Finance

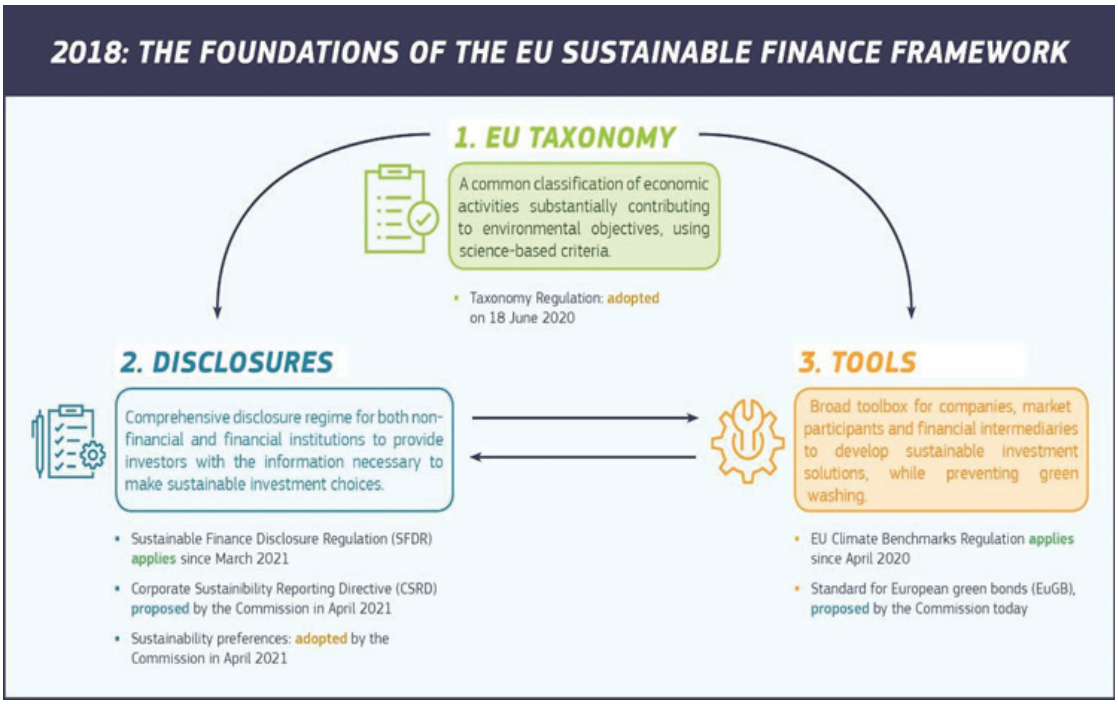
The recommendations of the High-level expert group on sustainable finance form the basis of the action plan on sustainable finance adopted by the European Commission in March 2018. The action plan set out a comprehensive strategy to further connect finance with sustainability. It included ten key actions that can be divided into three categories:

1. Reorienting capital flows towards a more sustainable economy

2. Mainstreaming sustainability into risk management

3. Fostering transparency and long-termism

Subsequent legislative and regulatory action by the EC since 2018, an outline of which is beyond the scope of this paper, has sought to deliver on these objectives. The financial services sector is core to the EU's objective of connecting finance to sustainability. This creates challenges but also opportunities for the sector.



EC Green Deal Framework

The European Green Deal is not a law, but it is the cornerstone of Europe's sustainable economic growth strategy, and the foundation on which almost all its subsequent ESG and sustainability legislation is based. Launched on December 11th, 2019, it is an integral part of the European Commission's strategy to implement the UN's 2030 Agenda and the SDGs. Its goal is to transform the EU into a modern, resource-efficient, and competitive economy, where:

- There are no net emissions of greenhouse gases by 2050;
- Economic growth is decoupled from resource use; and
- No person and no place is left behind

The Green Deal creates an action plan that outlines the investments needed and the financing tools available to achieve climate neutrality by 2050. Essentially, it aims to encourage the channeling of private investment towards the transition to a climate- neutral economy. It also provides financial support and technical assistance to help those that are most affected by the move towards the green economy, through the Just Transition Mechanism, which plans to mobilise at least €100 billion over the period 2021-2027 in the most affected regions.

The Green Deal includes an investment pillar as a key initiative, highlighting the importance of financial resources to meet its objectives. The European Green Deal Investment Plan, is also known as the Sustainable Europe Investment Plan. The Investment Plan is organised along three dimensions, which involve multiple stakeholders:

- **Funding.** Over the 2021-2030 period, the European Commission wants to mobilise at least €1 trillion of sustainable investment by increasing the resources devoted to climate action under the EU budget, and leveraging additional public and private financing. Part of the overall resources will be specifically designed to support the regions most exposed to the challenges of the transition.

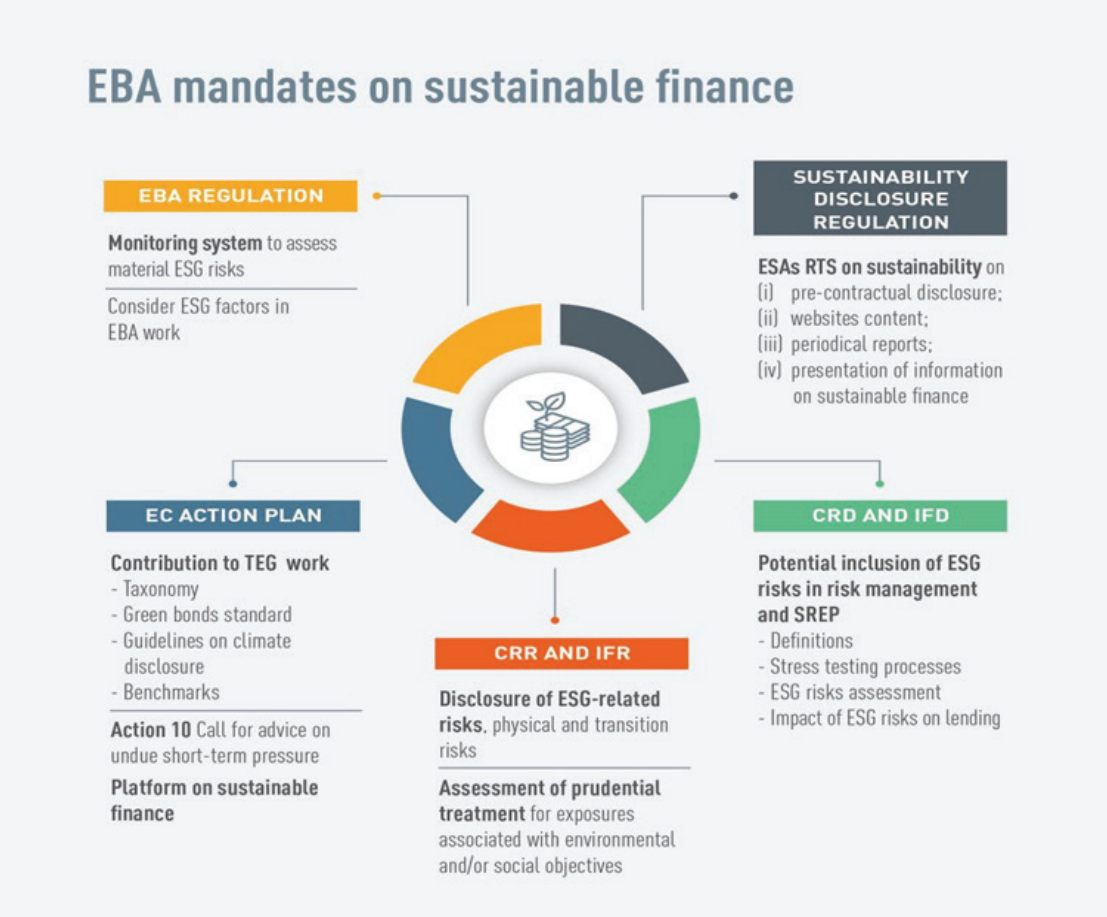
- **Enabling framework**. The Commission plans to use a mix of regulation and incentives to ensure that sustainability is duly considered in investment decisions across all sectors.
- **Support for implementation**. Advisory and technical support will be provided to public administrations and project promoters with a view to creating a pipeline of sustainable projects.

The Investment Plan aims to create an enabling framework to promote sustainability in investment decisions, through a mix of initiatives that include the EU Taxonomy, the EU Action Plan on Financing Sustainable Growth, and legislative proposals in the field of green public procurement and guidance on the application of the 'energy efficiency first principle' whenever this is relevant to investment decisions.

European Central Bank (ECB) / European Banking Authority (EBA)

Retail banks in Ireland are regulated by the ECB under the single supervisory mechanism. The EBA is entrusted with developing draft technical standards, guidelines, and recommendations in order to enhance convergence of supervisory practices and ensure consistency of supervisory outcomes within the European Union. The ECB carries out its tasks in compliance with the EBA's rules.

In December 2019, the EBA, published its Action Plan on Sustainable Finance. The objective of the action plan was to outline the EBA's plans on deliverables and activities related to environmental, social, and governance (ESG) factors and ESG risks. The action plan highlighted some key policy messages on the topic of sustainable finance to provide some clarity to relevant financial institutions on the EBA's high-level policy direction and expectations about ESG risks. It emphasises three areas where institutions are encouraged to consider taking steps before the EU legal framework is formally updated and the EBA regulatory mandates delivered: (i) strategy and risk management, (ii) disclosure, and (iii) scenario analysis.



Under its action plan, the EBA's first (of 3) mandates[4] was to prepare a report assessing the potential inclusion of ESG risks in the supervisory review and evaluation process (SREP) performed by regulatory competent authorities. The **EBA, Report on Environmental, Social and Governance (ESG) risks management and supervision was published in July 2021.**

The EBA's assessment addressed the following:

- development of a **uniform definition of ESG risks**, including physical risks and transition risks where the latter includes the risks related to the depreciation of assets due to regulatory changes;
- development of appropriate **qualitative and quantitative criteria** for the assessment of the impact of ESG risks on the financial stability of financial institutions in the short, medium and long term where criteria shall include stress testing processes and scenario analyses to assess the impact of ESG risks under scenarios of different severity;
- the **arrangements, processes, mechanisms and strategie**s to be implemented by financial institutions to **identify, assess and manage** ESG risks;

4 Analysis of the three mandates are beyond the scope of this paper. **On 24th January 2022**, the EBA issued Final draft implementing technical standards on prudential disclosures on ESG risks in accordance with Article 449a CRR (Second Mandate). The EBA's Third Mandate is to assess whether a dedicated prudential treatment of exposures related to assets or activities that are associated with environmental and/or social objectives would be justified.

- **the analysis, methods, and tools to assess the impact of ESG risks on lending and financial intermediation activities of financial institutions.**

The overarching recommendations to financial institutions from the EBA was to take proactive actions to ensure preparedness for ESG-related challenges and regulatory developments; in short to mainstream sustainability into governance, risk management and strategy processes and decision-making. This work is well underway within the Irish retail banks.

Ireland's Climate Initiatives

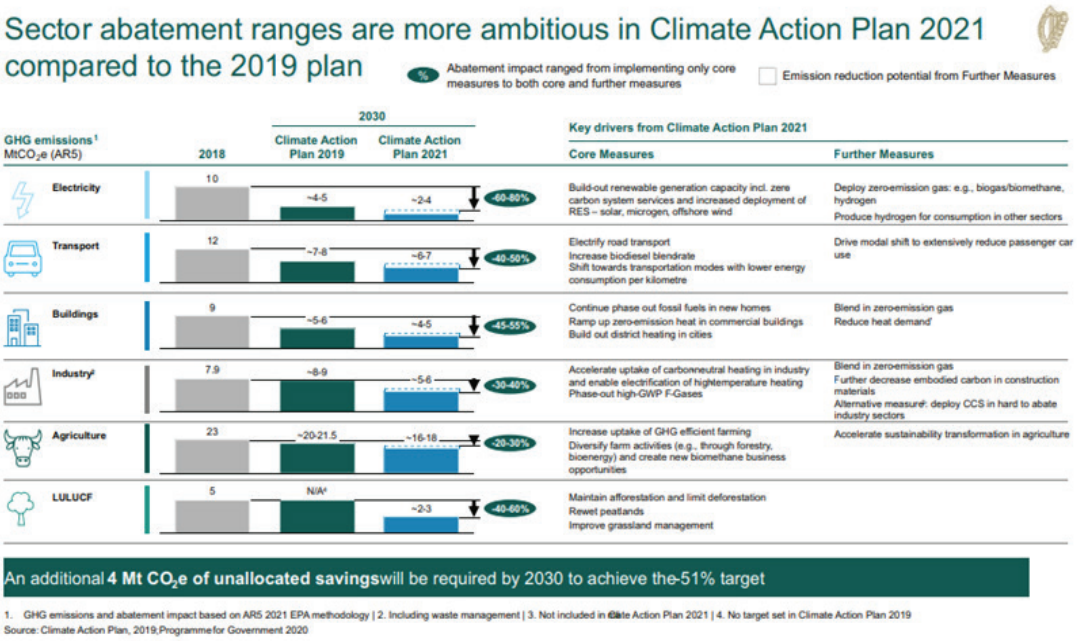
In Ireland, national legislation and policy guidance introduced to meet the objectives of the EC Green Deal are informing the context within which Irish retail banks engage with their clients including households, SMEs and corporates as they support them towards decarbonising their economic activities.

The **Programme for Government 2020** set out to agree a legally binding target of net-zero greenhouse gas emissions no later than 2050, and a reduction of 51% by 2030. National legislation and policy guidance introduced in recent months is informing the context within which Irish retail banks engage with their clients including households, SMEs, and corporates as they support them to make the decarbonising transition of their economic activities.

The **Climate Action Plan 2021** sets out the actions required to meet Ireland's EU 2030 targets and its net zero emissions goal by 2050, focusing on the key sectors of electricity, transport, residential, commercial, and public buildings, industry, and agriculture. The plan provides insight into government policy incentives to enable the transition and likely opportunities for private finance, with mobilisation of €125 billion of capital investment in low-carbon technologies and infrastructure required up to 2030.

Retail banks are core to supporting the transition, especially for buildings, with residential mortgages and property-related lending equivalent to 78% of all private-sector lending to Irish residents at the end of 2021. The government has targeted reduction of 40% in emissions for residential buildings by 2030 and 45% reduction for commercial and public sector buildings. To achieve these targets, the government wants to see 0.5 million existing homes upgraded to B2 Building Energy Rating (BER) and 0.6 million heat pumps installed (of which 0.4 million would be installed in existing homes)[5] .

5 50% of houses in Ireland have a BER rating of D or lower and require significant energy upgrades



Source: The Climate Action Plan, Figure 4.3

The **National Retrofitting Office**, established under the auspices of the Sustainable Energy Authority of Ireland (SEAI), aims to deliver on government's ambitious retrofit targets. The office will address barriers to retrofit, including driving demand and activity; financing and funding; supply chain, skills, and standards; and governance. There will also be state investment of €8 billion to 2030 to enable the supply chain to scale up and create thousands of high-quality jobs. Key ambitions include;

- 500,000 existing homes upgraded to a B2 BER rating
- 600,000 heat pump installations, with 400,000 to be installed in existing homes
- SEAI establishing One-stop shops to make process efficient for householder.

The establishment of this office, combined with new European Investment Bank/ Strategic Banking Corporation of Ireland grants, creates potential to scale up lender support for customers looking to finance their home upgrades.

The Strategic Banking Corporation of Ireland (SBCI) is developing initiatives to support lenders providing products to finance energy efficiency to households, SMEs, and farmers. It will provide wholesale finance through private-sector lenders to support consumers and small landlords who wish to invest in the energy efficiency of a residential property as well as helping eligible SMEs and farmers reduce their energy bills and their carbon emissions by investing in energy-saving measures. To help realise government's ambitious home retrofitting objectives, lenders successful in their bid to participate in the Strategic Banking Corporation of Ireland's national retrofitting programme, will offer more financing opportunities for retrofitting to consumers. SBCI will provide a first-loss guarantees of 80% to eligible lenders (part funded by the European Investment Bank) in order to deliver on government commitment to encourage financing of unsecured loan products for householders who wish to avail of the range of grants provided via the SEAI. SEAI is responsible for the National Retrofitting Office and will work with lenders and other stakeholders, including contractors to develop one-stop shops to facilitate ease of use for customers.

The **Sustainable Finance Roadmap**, which has been developed by Sustainable Finance Ireland and UN-convened FC4S, in collaboration with public and private stakeholders across Ireland including the Department of Finance, identifies key collaborative actions for Ireland to deliver on, including talent, access to data and corporate reporting.

These initiatives will help Irish Retail Banks to scale up efforts to support households, SMEs and corporates looking for finance to improve the energy performance of their homes and businesses.

2. Sustainable Finance: Work of BPFI

"Ireland's banks are at the core of the climate transition, supporting customers and clients to move away from a dependence on carbonising and polluting activities and to avail of the opportunities of greener economic pursuits".
(Brian Hayes, Chief Executive, BPFI)

BPFI Activity on Sustainable Finance in Ireland's Green Transition

BPFI is actively supporting its membership (which includes the Irish retail banks) on this important issue and represents the sector at the following fora in Ireland and Europe:

Forum	Objectives
Central Bank of Ireland Climate Risk and Sustainable Finance Forum	A consultative forum providing a space for cross-sectoral discussions among representative bodies, financial sector participants, climate change experts and the Central Bank. Its overall purpose is to build a shared approach to the understanding and management of the financial risks and opportunities posed by climate change.
Department of Finance Public Private Climate Group	This group was set up under the Sustainable Finance Roadmap Pillar 4: Enabling Environment. It aims to improve information flow between industry and the public service and is intended to cover: progression of the Department of Finance's climate-related financial commitments including with regard to the transition to a low carbon economy; the work of the Department on the international Climate Finance and Sustainable Development agenda; and identifying opportunities arising from the transition to a low carbon future for domestic and international finance firms.
Sustainable Finance Skillnet Committee	Sustainable Finance Skillnet is a national pubic-private network working to develop skills and leadership capacity to advance ESG best practice across Ireland's financial services sector. The Sustainable Finance Skillnet is supported by Skillnet Ireland (www.skillnetireland.ie) - the national agency responsible for the promotion and facilitation of workforce learning

BPFI welcomes opportunities to engage in public-private collaboration towards a shared goal of sustainability.

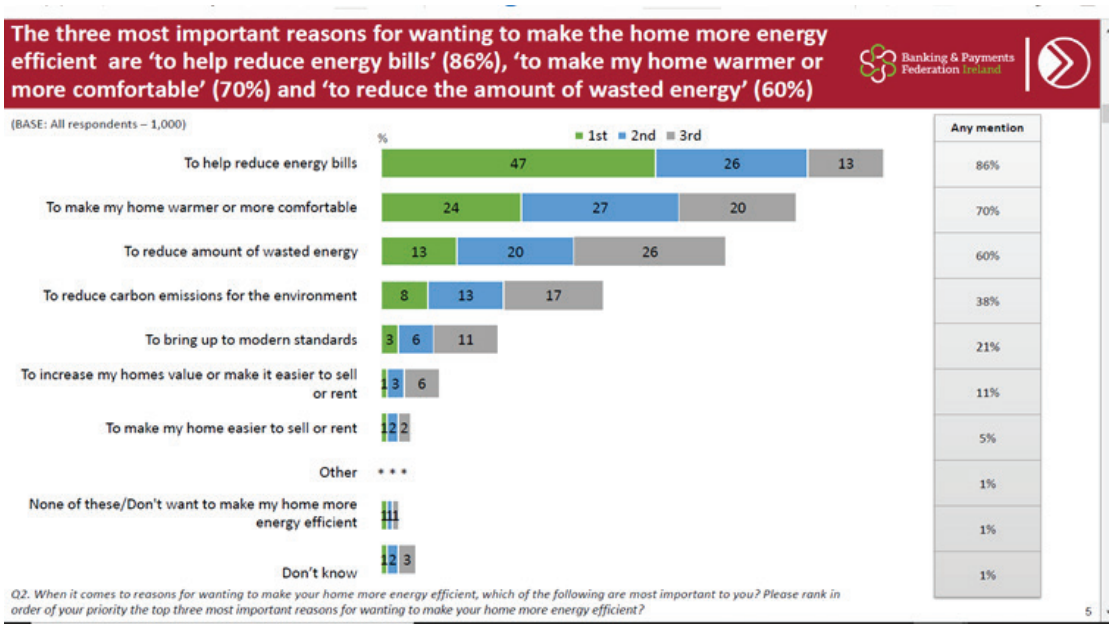
Consumer Research

In May 2022, Amárach Research conducted a customer survey exploring behaviours and attitudes to climate related transition on behalf of BPFI. The results of the survey indicate reducing energy/fuel costs is the main motive for customers to go green, rather than a strong motivation to support the transition to net zero. Output from this survey in relation to house energy efficiency and electric vehicles is presented below.

Home energy efficiency improvements

According to the Amárach Research survey:

- 47% of consumers cited reducing energy bills as the main reason to make their homes more energy efficient;
- other key drivers for home energy efficiency improvements are to make the home warmer or more comfortable (24% cited it as the main reason) and to reduce the amount of wasted energy (13%);
- 8% of respondents cited reducing carbon emissions as the main reason for home energy efficiency improvements;
- two-thirds (64%) of respondents had at least one significant home improvement to improve energy efficiency with 42% of respondents planning to do at least one in the next three years,
- more than half respondents (53%) had attic or wall insulation while about a quarter had upgraded heating controls (26%) or condensing boilers (24%);
- only circa one in ten respondents said their home used solar power (13%) or heat pump systems (11%) with only 18% and 13% of respondents respectively planning to invest in these in the next three years;
- 42% of respondents said they had looked into solar power (33% for heat pumps) but were unlikely to make the investment in the next three years;
- 50% of consumers who have improved or plan to improve their home's energy efficiency rely on savings; between 43% and 54% of those planning to make home energy improvements in the next three years plan to use savings with between 26% and 38% planning to use government grants; credit union or bank loans or mortgage top-ups for the most part make up the rest of the financing.

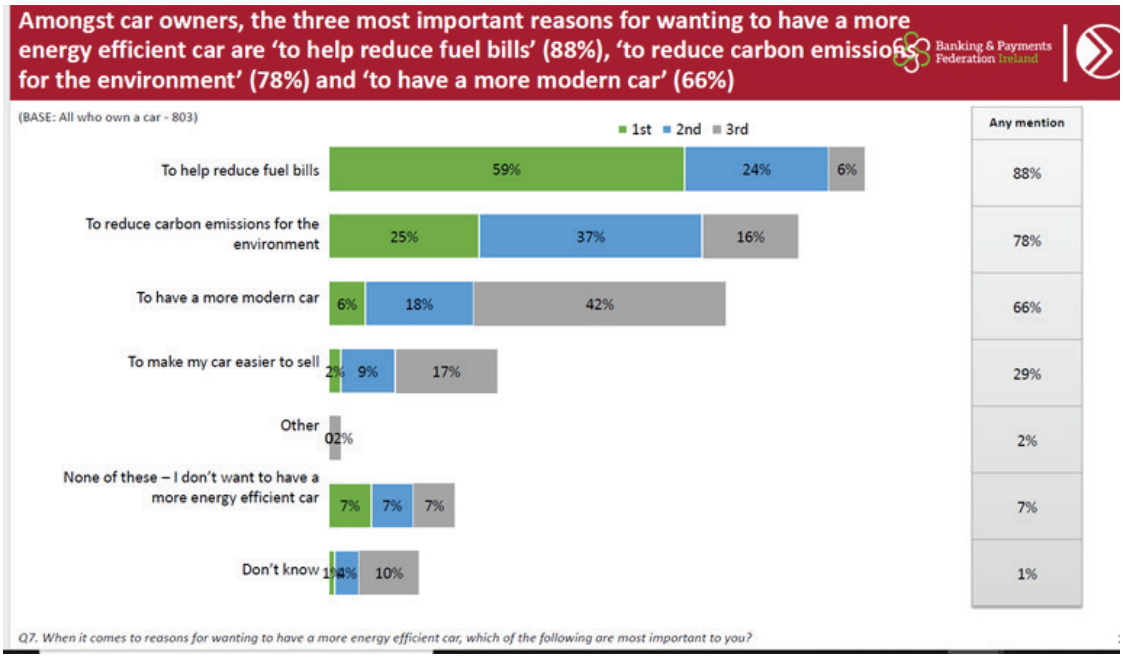


Car Financing and Electric Vehicles

Almost 41,000 new electric or electric-hybrid private cars[6] were registered for the first time in the twelve months ending March 2022, about 39% of all new cars in that period. According to the Amárach Research survey:

- 59% of car owners cited reducing fuel bills as the main reason for wanting a more energy efficient car;
- 25% of car owners said reducing carbon emissions was their main reason for wanting a more energy efficient car;
- 45% of those who bought a car in the past year used savings with the use of other financing varying depending on whether the car was new or second-hand: about 21% of new car buyers are using hire purchase or personal contract plans while 40% of second-hand car buyers used credit union or bank loans (33% of new);
- buyers of new electric cars benefitted from government grants with 26,392 electric vehicle grants provided to consumers by the Sustainable Energy Authority of Ireland up to May 2022.

6 Including electric, petrol and electric hybrid, diesel and electric hybrid and petrol or diesel plug-in hybrid electric cars



The main conclusions drawn from this survey are:

- Lenders can prompt customers seeking to finance renovations to opt for energy efficient options via discounted financing.
- Demand for solar panel and heat pump solutions appears weak even though awareness of such solutions appears to be strong
- Savings are also driving car financing, with 45% of those who bought a car in the past year using savings.
- Lenders are developing products to reward customers looking to finance electric vehicles. It seems transport may be the first sector where going green for the sake of the environment is a key factor in individual's decision making;
- There is on-going need for further and constant and coordinated consumer education. Consumers can often be confused as to why, where, and how to start their transition. BPFI's research has reflected consumers' need to supplement their savings with other sources of finance to make the necessary investments in their domestic properties towards net zero.

3. Irish Retail Banks: A green journey

The path of Retail Banks to support net zero is threefold:

1. Raising finance through the issuance of green bonds to be allocated to eligible loan portfolio of new and existing green loans;
2. Investing and underwriting "green" assets and businesses to support those households and companies whose lifestyles and/or activities support the government's plan to decarbonise the economy;
3. Playing their part in this economic transition by financing those more carbon intensive assets and companies that need to become "greener".

Actions taken by Irish Retail Banks

Irish Retail banks are changing to support this transition, including:

(i) successfully issuing green bonds and developing a strong global reputation in this space;

(ii) making significant internal changes to repurpose business models and risk management frameworks to mainstream sustainability into their strategic and risk management processes;

(iii) actively championing the engagement and empowerment of retail clients (SME and households), with innovative products supporting customers to make sustainable choices and amplify the impact of their financial products. For example:
- lower-interest rates on mortgage products when the property has an efficient energy performance,
- e-vehicle financing,
- financing of renewable energy projects,
- lower-interest rates on personal loans for the purpose of improving the energy efficiency of a house to a BER Rating of B2 or higher (aligned with government's retrofitting goals),
- provision of finance whereby reducing cost of servicing a business loan is linked to demonstrated reduced carbon emissions (known as sustainability-linked loans),

(iv) appointing specific teams charged with driving sustainability in their financial institutions;

(v) leading out on engagement with customers and stakeholders;

(vi) setting science-based targets for their portfolios and lending practices[7] that measure and reduce their entire carbon footprint in line with the Paris Agreement;

(vii) advising business on decarbonising economic activities;

(viii) advising the agri-sector to support transition towards sustainable farming;

7 To guide strategy Irish retail banks have set Net Zero lending targets.

(ix) advising and supporting households and businesses signposting grants available for retrofitting and in the case of businesses, highlighting regulatory requirements that might apply (e.g. new Corporate Sustainability Reporting);

(x) embarking on significant data identification and management to identify risk and to report on their progress in reducing their own greenhouse gas emissions and that of their suppliers and clients;

(xi) reporting in line with the recommendations of the Task Force on Climate-related Financial Disclosures[8] (TCFD) as well as embracing the United Nations Principles for Responsible Banking[9] . (These global principles require regular inspections and public disclosures to achieve the vision of having "a responsible banking industry that is an integral part of the society of the 21st century because it serves and contributes to a sustainable, equitable economic and social development, protecting our natural environment").

These initiatives are producing tangible results. Irish retail banks have already helped thousands of customers go and live green in recent years:

- BPFI estimates that 65,000 new and second-hand green homes were bought with residential mortgages between 2017 and 2021, with more than 14,000 in 2021 alone;
- An estimated 3-4,000 personal loans and mortgage top-ups for electric or hybrid-electric cars;
- More than 54,000 home improvement loans, including loans for home retrofits, in the twelve months ending March 2022;

Irish retail banks understand their role in building a sustainable economy in Ireland. The steps being taken towards increased sustainability, however, can be bolstered through stronger and deeper partnerships between the retail banking sector, Government, and state bodies (Public-Private Coordination).

8 www.fsb-tcfd.org/publications/

9 Principles for Responsible Banking – United Nations Environment – Finance Initiative (unepfi.org)

4. Towards optimizing the execution of EU Policy and Regulation by Retail Banks in Ireland

> **" We shall require a substantially new manner of thinking if mankind is to survive."**
> **(Albert Einstein, Theoretical Physicist)**

It is noteworthy that Irish retail banks are demonstrating agility in responding to policy calls for action against a backdrop of two significant players leaving the domestic market (and the related commercial and operational pressure this has created), intense regulatory scrutiny of how banks are integrating ESG factors into their governance and risk management frameworks, customers struggling in a high inflationary environment coupled with economic uncertainty, an absence of third party data to support disclosure expectations and an investor community that expects ESG integration yielding an acceptable return on tangible equity.

Consumer and Business Sentiment

The critical role of the consumer and the public at large in the success of stakeholder capitalism can be overlooked. Consumers and the public champion environmental change and the narrowing of the socio-economic divide that is so blatantly present in our world. For the Climate Action Plan to succeed, consumers and the public must play their part. Through their purchasing habits, behaviours and personal initiatives, consumers can directly and indirectly support the Climate Action Plan.

The cost of living crisis has focussed consumer and business minds on the need to reduce energy bills. As noted earlier, a recent Amárach Research survey commissioned by BPFI showed that 47% of consumers cited reducing energy bills as the main reason to make their homes more energy efficient while 59% of car owners cited reducing fuel bills as the main reason for wanting a more energy efficient car. Continued Government action is needed to influence consumer attitudes and behaviours.

While businesses are also keen to save money and reduce emissions, they will need incentives and initiatives like that offered to households under the National Retrofit Office. SMEs will need coordinating efforts and access to information to make the changes required to be more energy efficient. Similarly, the government will need to stimulate behavioural change.

Interest, understanding and acceptance among consumers and market participants of government environmental policy that will support engagement on retail bank products and services that reward sustainable behaviours is required.

Government Policy and Supporting Action

At a broader level, the radical and long-term policy changes required to deliver on the government's 2050 net zero targets could potentially create considerable disruption if not implemented in a targeted and measured way. Policy certainty is essential for the regulated financial services sector but also for the sectors that are customers and clients of financial services to ensure a minimal disruption and maximum impact, particularly given the role in supporting the real economy, via financing of households, SMEs, and corporates.

The government's provision of sectoral transition pathways is essential to foster credible, achievable, and orderly transitions to net zero for each area of the economy. To translate climate ambition into climate action, retail banks must understand transition pathways for each economic sector and support these pathways with financing. This will inform banks' strategies and ensure their financing and advice to customers supports Ireland's climate targets.

Going forward, skills will be an imperative ingredient of success. A recent BPFI survey of membership indicated that nearly 20% of respondents believe availability of skillsets required is the biggest challenge to achieving government's ambition to become a green finance hub. According to Skillnet Ireland's Sustainable Finance Skills Gap Report 2021, traditional finance training is inadequate in its current form as it does not take into consideration broader ESG impacts and how this relates to financial impact. Moreover, according to the State's training agency Solas, an additional 52,000 construction workers are required by 2030 to meet both new housing and retrofit targets. Given the urgency of retrofitting targets, we hope government can provide urgent training and incentives in this regard. Consumer education / business education.

Access to reliable and consistent data on climate-related activities is fundamental to sustainable business decision making and to lenders' risk management strategy and practices. The EU's current revision of the Energy Performance Buildings Directive is an opportunity to ensure access for financial service providers to the energy performance information of mortgaged properties.

Investor Sentiment

Access to capital is pivotal for any company and shareholder and investor sentiment towards a sector/company/jurisdiction is at the heart of this access. Retail banks have unique characteristics versus other companies, not least that they are subject to intensive prudential regulation pertaining to levels of capital and liquidity related to their asset portfolios/strategy. For years CSR/ESG issues were a secondary concern for investors. Today institutional investors and pension funds have grown too large to diversify away from systemic risks, so they must consider the environmental and social impact of their portfolio (Eccles and Klimenko, 2019[10]). Their underlying clients are demanding products with ESG related objectives. The level of capital flowing into funds that incorporate ESG criteria have grown considerably over the past 5 years so what was once an issue on the fringes of investment is becoming part of the material financial analysis of a company's value. Investors (arising also from legislation directed at the asset management sector) are ratcheting up pressure on companies to enhance their ESG framework. There is no avoiding the integration and dependencies of all stakeholders in this regard. Retail banks must manage investor expectations on ESG integration and in providing an acceptable return on tangible equity to ensure the long-term access to capital. The importance of government's provision of sectoral transition pathways was noted above. The creation of sectoral pathways will also enable the domestic private business sector to develop a pipeline of bankable sustainable projects at scale. This in turn will inform retail banks' strategic plans, prioritisation, and investor dialogue.

Ireland's retail banks are at the core of the climate transition, supporting customers and clients to move away from a dependence on carbonising and polluting activities and to avail of the opportunities of greener economic pursuits. The new sustainable finance legislative regime will impact on corporates and SMEs in addition to households as the banking sector looks to support the transition. Retail banks play a critical role in translating into the real economy the Green Deal ambitions of the EU and Climate Action Plans of the Irish government and sector-level collaboration on deliverables in the forthcoming revised Climate Action Plan is essential. All stakeholders, including the Irish Government, have a role to play in supporting business to make the transition to sustainable economic activities. BPFI stands ready to support these stakeholders in this regard. Working with all sectors of the economy and society, we can start to transform our environment and leave a cleaner, more sustainable planet for future generations.

10 Eccles and Klimenko, 2019, Sustainability: The Investor Revolution, Investors are getting serious about sustainability