Climate Action in Financial Institutions

PRINCIPLES FOR MAINSTREAMING CLIMATE ACTION

Credit Agricole CIB's Development of a Medium-Term Transition Risk Index

Institution	Principle	Related Work Stream(s)
	PRINCIPLE 2: MANAGE Climate Risks	CLIMATE RISKS: APPROACHES, TOOLS, METHODOLOGIES

Publication date: 2017

Date Policy/Tool Established	Additional Capacity Required (e.g., staff, resources, other)	How Established?
Development: 2016 Operational since: 2017	Fully integrated in existing CSR processes.	Development as part of the overarching CSR Program (FReD) under the supervision of CERES committee.

Monitoring, reporting tools	How Implemented?
Integrated in the existing CSR scoring monitoring and reporting tools.	Developed internally with the help of: - in-house engineers - external extra-financial agency and - previous work by academics (Chaire Finance et Développement Durable)

Key Lessons

- Connecting a customer-specific assessment to a macro sector and issue-based approach provides an easy readable transition risk index at the customer level
- Using existing processes helps mainstreaming new due diligences.

Introduction

Development of the Medium-term Transition Risk Index is part of the CACIB principal approach decided in 2009 for assessing and managing the climate-change impacts of the Bank and related risks.

As a first step, a methodology was developed with academics and used, since 2011, to map the carbon footprint of the finance provided by the Bank by sector and country using an innovative climate-focused issue-based approach named P9XCA.[1]

It was decided in 2015 to initiate an Action Plan (as part of the Group's overarching CSR program FReD) to assess the importance of the climate risks (physical, transition, legal) at different point in time (short term, medium term, long term) and develop a methodology for assessing these risks at client level - the risk identified as the most important.

The transition risks in the medium-term (2020 to 2030 period) was found to be the most important for CA CIB to take into consideration, based on two criteria: materiality; and the identification of actionable means of managing risks (please see Crédit Agricole's case study on the use of P9XCA methodology to assess materiality of climate risks)

Development and Design

Research indicates that the transition at a gradual pace may result in no negative impact on the economy globally (see the results of the survey "Investing in Climate, investing in Growth" OECD 2017[2]). However, a fundamental question is then to distinguish between those customers who could benefit from the transition and those who could lose. A key challenge for CACIB was to complement our sector and issue-based approach with a client-specific assessment.

The Medium-term Transition Risk Index was therefore defined for the Bank's corporate customer groups using a combination of three factors:

- The carbon intensity of finance provided to each corporate customer group (which indicates the extent to which the issues will affect financing in the sector), as calculated by the P9XCA methodology. This indicates the level of importance of the transition for a given sector
- The anticipated level of emission reductions by year and unit of GDP for a given country, derived from the Intended Nationally Determined Contributions (INDC). This indicates the importance a country places on the transition.
- The responsiveness of the customer when faced with climate challenges and its ability to adapt, as evaluated by a nonfinancial agency or estimated using a geographic average. A score is compared relative to the average of each sector; the index is thus positive when the counterparty demonstrates an above average preparedness - and is negative if it does not.

Implementation

The index was first calculated in the second semester 2016 and tested with a selection of customers in the oil and gas sector.

During the first semester of 2017, the index was fine-tuned and applied to the whole CIB customer base so that it can now be used as part of the annual CSR scoring process of clients.

It builds on the climate-related due diligence process that was introduced in 2015 for customers in selected sectors and countries.

Experience and Impact

The Medium-term Transition Risk Index is easy to use. The more the customer stands out from its peers, the more the sector is considered to be at risk, and the more the country has committed to a rapid energy transition - the higher the absolute value of the index is. For example, a player in the Energy or Transport sectors in a country committed to significantly lowering emissions will have more to gain or lose than a player in a sector less directly affected or in a country with lower greenhouse gas reduction ambitions. The extent to which this actor is affected will depend on its ability to adapt its strategy and economic model to the new situation.

An initial result of CA CIB's experience in using the index has been the decision to strengthen due diligence when the index indicates a low level of performance by customers.

1 Please see "Use of a sectoral and issue-based cartography of global financed emissions for developing CSR sector policies" in the 2015 Edition of the Emerging Practices Paper.

2 http://www.oecd.org/env/investing-in-climate-investing-in-growth-9789264273528-en.htm