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Sustainability

New York Climate Week: It's all about acting faster and together

Increased severe weather events have alerted us to act faster against climate change. We think New York Climate Week adds value by emphasising value chain partnerships, infrastructure building and quality reporting. And there needs to be more alignment between corporate sustainability teams and the C-suite to future-proof decarbonisation efforts



With 2023 being the hottest summer on record, last week's New York City Climate week further emphasised the need to act

This year has shown us that it is more imperative than ever to accelerate efforts against climate change. The summer of 2023 was the hottest since the National Aeronautics and Space Administration (NASA) started recording in 1880, which has largely increased the chances of average temperature of 2023 exceeding the 1.5-degree-Celsius threshold of global warming. Primarily driven by human activities, the record temperatures have resulted in heatwaves in Europe, the US, Japan, and South America. What is more, wildfires in Quebec more than doubled this year compared to the past decade, leading to severe air pollution in Canada and the northeast US. Meanwhile, severe flooding happened in California, Brazil, Malaysia, Libya, South Korea, China, and more. Extreme weather events are becoming more frequent, more diverse, and more impactful.

These are going to increasingly affect our lives and businesses around the world. To name a few, heat and flooding will likely undermine labour productivity in apparel hubs in Asian countries. Extreme weather can affect operations in the agriculture sector. Hurricanes and sea level rises will pose greater risks to the real estate sector. All these will put higher pressure on the insurance sector. It is estimated that global economic losses from extreme weather events mounted to \$125bn in the first half of 2023, up 41% from the previous ten-year average, and only half of the loss was insured.

Therefore, not only do we need to act, but we need to act faster to keep the door to limiting 1.5 degrees Celsius of global warming open. More challengingly, we need to execute climate ambitions in an environment where uncertain economic conditions are keeping interest rates elevated, and policy inconsistencies are adding complexity to corporate decision-making.

The urgency to act is emphasised at New York Climate Week. We are glad to see businesses, investors, policymakers, NGOs, and consultancies go beyond celebrating achievements to identify areas of improvement to decarbonise the global economy, mobilise capital to facilitate changes, and deploy policy to speed up a just energy transition. Below we have summarised what we think are the most important takeaways from Climate Week.

Decarbonise the value chain not siloed sectors

A very popular phrase used at the New York Climate Week is 'value chain'. Scope 3 emissions make up the ballpark of most sectors' total emissions, and companies have realised that decarbonisation needs collective efforts from themselves as well as their suppliers and consumers.

0% 20% 40% 60% 100% 80% Agricultural commodities Capital goods Cement Chemicals Coal Construction Scope 1 Electric utilities Scope 2 Financial services Food, beverage & tobacco Scope 3 Metals & mining Oil & aas Paper & forestry Real estate Steel Transport OEMs* Transport services

Scope 1, 2, and 3 emissions by sector

Source: CDP

Note: OEMs refer to original equipment manufacturers

For instance, in the <u>steel</u> industry, automotive companies are large end-use consumers. Globally, 12% of the steel produced goes to car manufacturing. To decarbonise, car manufacturer Volvo is collaborating with steelmaker SSAB to expand the production and use of green steel produced from hydrogen. Steel company ArcelorMittal has been partnering with automotive suppliers such as Gestamp and Snop to produce low-carbon steel car parts.

More industries are doing the same. In <u>food and agriculture</u>, Walmart launched 'Project Gigaton' aiming to reach a gigaton of avoided emissions through providing resources to support suppliers'

decarbonisation efforts. In petrochemicals, demand for low-carbon plastics from consumer goods and food & beverage companies is driving product innovation.

One commonly mentioned challenge of these initiatives comes from the consumer side, as many companies find it relatively hard to convince consumers to pay a higher price – even slightly – for a product that is 'done right'. To tackle that, there needs to be more customer communication about a company's sustainability stance and belief, which can then help enhance brand trust and loyalty. Governments also have a crucial role here to incentivise lower-carbon production and/or customers that purchase those products.

Get prepared for the climate disclosure wave

We have long been arguing that quality sustainability data reporting is a crucial step in helping businesses and investors compare ESG efforts, benchmark achievements against targets, and create a more robust environment for ESG investing and sustainable finance issuance.

At New York Climate Week, California Governor Gavin Newsom announced that he would sign into law two first-of-a-kind state bills – the Climate Corporate Data Accountability Act (SB 253) and the Climate-Related Financial Risk Act (SB 261) – that passed the California Legislature. SB 253 would require public and private companies conducting business in California and have a revenue of \$1bn or more to disclose Scope 1-2 emissions data starting 2026 and Scope 3 emissions data beginning 2027. SB 261 would require public and private businesses with revenues of at least \$500 million to release reports on climate-related financial risks.

California's passed climate bills

	SB 253: Climate disclosure	SB 261: Climate-related financial risks
Content	Scope 1, 2, 3 emissions	Publication each 2 years of a climate- related financial report
Required entities	Public and private companies with revenues of \$1bn or more	Public and private companies with revenues of \$500mn or more
Likely number of companies impacted	1 5,400+	10,000+

Source: ING Research based on publicly available information

The two bills would have a significant impact as California is the world's fifth-largest economy as well as a pioneer in climate legislation. It is estimated that SB 253 would affect more than 5,000 companies, while SB 261 would influence some 10,000 companies. Voluntary reporting of sustainability data is already happening, but with the new bills, companies will need to manage their supply chain emissions more actively and deploy more resources toward monitoring and data aggregation. It will not be easy – nor cheap – to do it, but quality climate disclosure is itself a positive long-term investment.

California could trigger more states to introduce similar laws, as evidenced by a flurry of state mandates to phase out internal combustion engine car sales in roughly a decade following California's announcement in 2020. It could also improve the outlook of the Securities and Exchange Commission (SEC) releasing the final <u>proposed rules on climate-related disclosure</u>, although the SEC's rules will likely have a less comprehensive scope (e.g. excluding Scope 3

emissions reporting) and run a higher risk of being challenged in court.

As the US prepares mandate sustainability reporting, we expect an eventual <u>convergence</u> of disclosure mandates around the world. It is because rules such as the EU's Corporate Sustainability Reporting Directive (CSRD) would require eligible companies worldwide to comply if they conduct business in the jurisdiction. It is also because of the increasing need for substantially comparable data across regions. Thus, no matter where a business is, it needs to start thinking now about becoming on par with these standards.

Infrastructure, infrastructure, infrastructure

Infrastructure is crucial to make sure that clean energy can be delivered to customers, and that clean technology products such as EVs can be properly charged. But now, infrastructure is far from sufficient. This is the case in the transport, electricity, and hydrogen sectors.

In the transport sector, there are 3mn EVs on the road today in the US but only 144,000 public and private charging ports – that is about 20 EVs per charging port. The National Renewable Energy Laboratory forecasts there will be 33mn EVs in the US in 2030 in the mid-adoption scenario, which will require 28mn charging ports (26.8mn private and 1.2mn public). In the power sector, transmission lines need to be expanded by 60% by 2030 and triple by 2050 to meet the growing demand for renewable energy. On top of that, as of last year, more than 2,000 GW of renewable generation and storage capacity – higher than the existing capacity in the US – need permitting debottlenecking to be connected to transmission lines. In the hydrogen sector, a combination of constructing dedicated pipelines, repurposing natural gas pipelines, and developing shipping and trucking alternatives to transport the element.

Such infrastructure expansion needs strong policy support. Various government incentives and initiatives can help de-risk investment, as some investors might be realistically unwilling to finance new technology infrastructure unless there is an outlook for higher profitability or economies of scale. Regulation modernisation is also needed to streamline the permitting process. This year, the Biden administration has rolled out phased reforms to the National Environmental Policy Act (NEPA), the building block that shapes energy project permitting processes. These reforms would entail, among others, capping the time for a project's environmental reviews, limiting the scope of reviews, and simplifying the reviewing procedure. This will not solve the infrastructure problems overnight but is expected to have a positive impact in the long term.

Bring hard-to-abate sectors to the solution

The world cannot achieve net zero without slashing emissions from hard-to-abate sectors. In 2022, emissions from the industry, which includes <u>iron & steel</u>, cement, and <u>chemicals</u>, accounted for 26% of global emissions. But since hydrocarbons are an essential component of these industrial materials, reducing emissions from these sectors is not easy. As participants at New York Climate Week have been advocating, we fully agree that hard-to-abate sectors need to be included in the energy transition ecosystem, where massive investment is needed to nurture low-carbon business models.



Global CO2 emissions contribution by sector (2022)

Several common decarbonisation pathways are available for exploration. The first is raw material recycling. In the steel industry, companies have been making efforts to scrap and recycle steel, though the challenge lies in both an insufficient recycling rate and a lower quality of recycled steel. In the chemicals industry, companies have been developing a more advanced process where chemical molecules can be broken down again to feedstock levels to close the entire plastics supply chain loop.

Second, cement, steel, and chemicals companies can benefit from carbon capture and storage (CCS) technologies. However, CCS is not yet scaled up enough to be cost-competitive with fossil fuel options. What can help with the situation are increased government incentives (such as Section 45Q tax credits under the <u>Inflation Reduction Act</u> in the US), wider adoption of corporate internal prices of carbon, and the development of CCS hubs so that companies can take advantage of shared infrastructure and resources.

Third, hydrogen is becoming a promising technology. In steel production, hydrogen can be used to replace coal or natural gas when iron ore is processed into pure iron. For chemicals, hydrogen can be used as a combustion fuel during steam cracking or as a feedstock for synthetic products. The crucial point here is that the hydrogen needs to be green (produced using electrolyzers and renewable electricity) to have meaningful emissions reduction. Indeed, the emissions intensity of steel produced using electrolysed hydrogen, but coal-fired electricity, can be even higher than that of the traditional process.

Finally, companies can reduce emissions by using renewable electricity to heat furnaces in steel and chemical production. It is worth noting, nevertheless, that these processes can add tremendous electricity demand. This can then add pressure to land usage for renewables deployment, as well as the transmission lines needed to deliver electricity.

Decarbonising hard-to-abate sectors are difficult, but not impossible. And it certainly cannot be ignored, because these sectors provide us with materials key to modern society, including cars, airplanes, bridges, and buildings. A positive trend is that coalitions have been formed in these sectors to accelerate sustainability efforts, and industry-wide standards are being developed and refined to provide a better guidebook for companies.

What does it mean for sustainable finance issuers?

• Enhance communication and connection between corporate treasurers and sustainability teams

The continuing commitment to enhance a company's ESG performance and the use of sustainable finance to realise this commitment need buy-in from the C-suite, as well as the corporate treasurer. But sometimes there are information gaps between these roles and the company's sustainability team. It is therefore essential to have two-way conversations between these teams on sustainability principles, areas of outperformance and improvement, and align these with the company's business priorities and long-term strategies.

• Strengthen impact reporting

Issuers need to more rigorously report how their sustainability efforts have made an impact. Of course, for the impact reports to be valuable, a company should have already set up long and short-term science-based climate targets, as well as a sustainable finance framework with credible third-party verification. Reporting impact is becoming more important because it can paint a clearly defined picture of success and largely reduce greenwashing risks. Organizations such as the International Capital Market Association (ICMA) provide issuers with metrics of impact reporting; we would encourage companies to not only follow those but also go more granular about their data. For instance, many companies report renewable energy generation, but there are not always breakdowns by product, operation, project, or geography. There should also be sufficient historical data, as well as a good combination of absolute data (e.g. water usage amount) and ratios (e.g. water usage energy intensity). Lastly, there needs to be greater disclosure on the methodologies companies use to monitor, collect, and report sustainability data. This would add an additional layer of clarity to investors.

• Attract and upskill talent

Companies are already starting to feel the rising competition to attract talent for the clean energy transition. A survey by the US Interstate Renewable Energy Council shows that roughly 90% of US solar companies have experienced difficulties finding the right labour for capacity expansion, largely due to insufficient skills. In the future, the need for labour in the clean energy industry is going to exponentially grow.

Big swings in 2023, but global sustainable finance remains in rude health

Level of difficulty finding qualified solar workers in the US



Source: US Interstate Renewable Energy Council

Top reasons for difficulty hiring solar workers in the US



Source: US Interstate Renewable Energy Council

Sustainability talent is needed not just in the energy sector, but in any other sector as well. Companies will need skilled employees to set sustainability agendas, manage supply chains, report quality ESG data, and enhance ESG strategy implementation. To stand out among peers, companies need to provide upskilling programmes to prepare workers for the energy transition, offer competitive benefits, and more importantly, foster a diverse and inclusive work culture to retain talent.

In the future, companies might also want to pay more attention to climate adaptation. Today, while listed as one of the objectives under the Green Bond Principles, climate adaptation accounts for 2% of the total use-of-proceeds sustainable debt issuance considerations. There could be more adaption-themed sustainable finance products in the long-run when climate change damages do become disastrous enough for more capital to come in to finance efforts against floods, wildfires, heatwaves, and rising sea horizons.

Conclusion

We need to think of fighting climate change as reducing risks – to lower the impact of extreme weather conditions or the rising cost of doing business. We need to think of it as harnessing opportunitie – to develop and future-proof clean technologies that can support our economic

activities sustainably. We also need to think of it as preserving humanity – to ensure future generations can continue to thrive on planet Earth. The cost of doing it will be high, but the cost of delaying efforts will be tremendously higher.

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