

## TRANSITION PLANNING IN THE FINANCIAL SECTOR



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### One (single, multipurpose, consistent) transition plan to rule them all

Forget about “net zero”, “transition plan” is the new catchword of the climate discussion. Only an intuition a couple of years ago, the idea of corporates and financial institutions devising and disclosing “transition plans” is fast becoming a regulatory reality with the adoption of CSRD, CSDDD, and CRR3. A very appealing feature of transition plans relates to its ability to provide a forward-looking perspective on issues that the usual backward looking disclosure fails to capture. Indeed, the NGFS started to develop its thinking on transition plans when realising that transition risks are only very poorly captured through the disclosure of past (scope 1, scope 2 or even scope 3) emissions or the implementation of a taxonomy (see “Capturing risk differentials...”, May 2022).

However, as for all popular ideas, careful design and skilful implementation are

required to avoid turning a sensible idea into an intractable and eventually pointless compliance exercise. As the practitioners are working on the first generation of transition plans, it might be useful to keep four potential pitfalls in sight to ensure the relevance of the exercise.

The first challenge relates to the nature of the exercise: before coming up with a transition plan, a firm should start by planning its transition, i.e. clarifying how it plans to navigate the transition to the end goal of a net zero economy. In that respect, transition planning comes first and is a combination of revisiting the strategy of the firm and thinking through the operational planning and delivery.

In the case of financial institutions, this both requires clarifying the positioning of the institution toward its clients and the economy as well as its vision of the transition and encompasses a wide range of topics from products to engagement with clients, sectorial policies, risk management, etc. This process might be broader and deeper than most strategic reviews and the supervisor would have an interest in the quality of the planning of the transition even before considering its outcome.

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The second difficulty arises from the high expectations that a large number of stakeholders have. The first take away of the NGFS report on transition plans (“Stocktake on Financial Institutions’ Transition Plans...”, May 2023) was that “transition plan” is a multifaceted concept. It needs to speak to a wide range of users with various use cases: analysts would want to understand how the firm approaches a changing business environment while supervisors need to be satisfied that the risks are identified, assessed and managed.

Rather than a piecemeal approach, this calls for a modular solution: the transition plan should be the outcome of a unified transition planning exercise with a core document being complemented by modules providing relevant additional

details. This solution is probably the only way to ensure that the various needs are satisfied in a consistent manner.

The third challenge speaks to the need for transition plans to connect with the reality of the economy. The transition of a financial institution is closely intertwined with the transition of its clients. This calls for developing a rather granular view of the transition: broad brush macro views of the transition are never sufficient in that respect and attention should be paid to both sectors and geographies.

While the development of sectorial transition pathways has started, little attention is paid to a significant issue: the transition toward a net zero global economy is very different across countries and regions:

- In Europe, while low carbon electricity is or is fast becoming a reality and we benefit from large interconnected electrical grids, the main challenge relates to the shift to electrification.
- In East Asia, where generating electricity still largely rely on fossil fuels and with a more limited potential for renewable (across the archipelagos), both the starting and the end points differ.
- In low and middle-income countries, especially in Africa, the transition is a development agenda where access to energy is enabled by natively low carbon energy systems.

Failing to recognise these differences and to account for the countries’ own strategies will make transition plans irrelevant.

Last but not least, the best plan does not matter if circumstances change or if it is poorly executed. In that respect, the fourth risk is to fail to update the plan and assess the delivery. While not yet a challenge at this stage, the disclosure associated with transition plans needs to provide meaningful information on adjustments and achievements. Otherwise, transition plans will only be aspirational gimmicks being rolled over to tomorrow.

Expected to serve very different purposes by providing a forward-looking understanding of how a firm strategically approaches its transition across its business lines and geographies and gets ready for a challenging execution, transition plans need to be carefully designed or risk being an irrelevant compliance exercise.



## JOSÉ MANUEL CAMPA

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### Transition plans: seizing the momentum for financial institutions

The width and breadth of the transformation required to shape our economies towards sustainability entails significant updates in the business models of companies and financial institutions. Along the way, organisations expose themselves to new transition - related drivers of financial risks.

Understanding the implications of such evolution requires familiarity with at least two concepts: “transition planning” and “transition plans”. Transition planning is commonly understood as the internal process undertaken by an organisation to deliver on its climate - related targets and/or to prepare a long - term response to manage the risks associated with that transition. Transition plans are the documents used to disclose to relevant audiences the results of the transition planning process.

In the EU, the Corporate Sustainability Reporting Directive (CSRD) and the Corporate Sustainability Due Diligence Directive (CSDDD) will require companies and banks to develop and implement specific plans to ensure that their business model and strategy are compatible with a sustainable economy in line with the Paris agreement and

the objective of climate neutrality by 2050. For EU banks, the revised Capital Requirements Directive (CRD6) requires them to develop and monitor specific transition plans as well, with the aim to monitor and address financial risks arising in the short, medium, and long term from the adjustment towards legal and regulatory sustainability objectives in the EU.

Of course, a forward - looking dimension is critical and transition plans should establish different time horizons, including specific milestones. Short-, medium- and long-term objectives are essential in that regard. For example, in the EU jurisdiction, an important milestone is the reference year 2030, which corresponds to the Union’s 55% reduction objective in GHG emissions. In short, institutions should carefully define and select scenarios and pathways underlying targets.

In that perspective, what are the main building blocks necessary for a financial institution to build robust transition plans?

The EBA has been mandated to issue Guidelines to specify requirements for the identification, measurement, management, and monitoring of ESG risks. Their goal is not to force institutions to exit from carbon intensive sectors but rather to stimulate their proactive reflection on technological, business, and behavioural changes, including risks and opportunities that will drive their business.

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#### Transition planning remains crucial to managing financial risks in sustainable economies.

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Consequently, a critically important building block will be the materiality assessment, which should be consistent with the institution’s business strategy. The plans must also demonstrate consistency with risk and funding strategies, including risk appetite, ICAAP and risk management frameworks. This implies setting clear targets with supporting metrics. Responsibilities tied to the governance of the plans should be clearly allocated. Along the way, engagement with counterparties is key, especially considering or reviewing their own transition plans. Such consideration is particularly relevant for transition finance, as robust and credible

counterparty plans can positively inform loan granting processes and investment due diligence.

As institutions build these transition plans trust needs to be preserved. Therefore, avoiding greenwashing that may ultimately result in weakening such trust is an important concern. To avoid such risks, it is of utmost importance to have a consistent oversight framework. Supervisors and other public authorities need to cooperate closely with clearly defined remits for transition plans. Prudential authorities should focus on risk - related aspects: how does an institution’s transition plan effectively allow to manage environmental financial risks considering its sustainability concerns? Other public authorities (e.g. agencies specialised in environmental affairs and market conduct or other relevant authorities) could focus on underlying scientific or public policy considerations and checking compliance with applicable (e.g. disclosures) requirements.

Finally, international cooperation is paramount. Various initiatives (e.g. ISSBB, GFANZ) have now published guidance and recommendations regarding the plans. In the field of banking supervision, I welcome the work conducted by the Network for Greening the Financial System, allowing to take stock of international practices and to explore further the link between financial institutions and corporate’ transition plans, as well as the work conducted by the Basel Committee to consider the role of transition planning in banks’ risk management processes and the potential role of prudential supervisors vis-à-vis transition planning. The momentum is being built. Let’s continue to seize it.



## ANTOINE VAN CAUWENBERGE

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### The case for credible disclosures of climate transition plans

Developing a clean energy economy requires prompt and suitable policy actions, along with both public and private investments. Private funding should include bank financing and, even more importantly, capital market funding. Securing private capital requires reliable and comparable disclosures to investors, which is where capital market regulators play a key role, ensuring investor protection, market integrity and stability. Under the umbrella of the International Organization of Securities Commissions (IOSCO), the global community of market regulators have led the efforts for a globally coordinated approach to promote sustainability-related disclosures by corporates. Several jurisdictions have begun the process of using the International Sustainability Standards Board's standards, which were endorsed by IOSCO in July 2023 as suitable for capital markets. Adhering to ISSB or ISSB-informed standards, especially when entities are independently audited, will mitigate the risk of greenwashing.

Moreover, in recent years, there has been a growing focus on the publication

of transition plans to support net-zero commitments, with regular reporting on progress. When assessing the transition risks associated with an investment, financial institutions and investors may factor in information from transition plans.

The ISSB sets requirements for an entity to disclose its plans to transition towards a lower carbon economy, without mandating such plans. In this respect, market regulators are monitoring the transition plan landscape to assess the risks of net-zero greenwashing. To date, based on the disclosures, plans have varied in quality and often lack details on the actions intended to meet net-zero goals.

The fact that the Glasgow Financial Alliance for Net Zero (GFANZ) has outlined a structure for transition planning and plans for both financial institutions and the real economy is to be welcomed. In the EU, the European Sustainability Reporting Standards impose granular disclosure on transition plans and climate commitments by relevant entities. In addition, the European Commission's recommendation of June 2023 on facilitating finance for the transition to a sustainable economy includes non-binding recommendations to entities on the use of transition plans. Going forward, the forthcoming Directive on Corporate Sustainability Due Diligence will mandate that companies falling within its scope adopt a transition plan, without prejudice to transition plan requirements from a prudential perspective for banks.

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In the UK, the Transition Plan Task Force combines a sector-neutral Disclosure Framework with additional sector-specific guidance, aimed at assisting entities in various sectors to interpret more accurately the disclosure framework for their specific industry needs.

In order to address risks of an alphabet soup of transition plan frameworks, IOSCO is monitoring any risks of fragmentation and inconsistency, focusing on investor protection and market integrity, and liaising with other international bodies such as the Financial

Stability Board. At COP28, IOSCO announced that it would examine how proper disclosure of existing transition plans by listed companies and asset managers with transition targets can work for the benefit of investors. IOSCO is also encouraging global standard setters to work towards globally agreed sustainability audit standards, since the use by auditors and assurers of a global framework of technical and ethical standards developed in the public interest will enhance the quality of the disclosures.

Additionally, the challenge of data availability should not be underestimated. Consequently, improving access to reliable and comparable climate transition data should be a key international focus. In this regard, the launch of the proof of concept for the Net-Zero Data Public Utility (NZDPU) as a free and centralised data repository could be a driving force in enhancing accessibility of company-level climate data. The repository may be used by financial institutions when assessing the emission levels of portfolio companies as part of an effort to develop transition plans. Entities may also use it when searching for comprehensive data on their value chains to measure and disclose their Scope 3 greenhouse gas emissions or benchmark their performance against their peers. To ensure cross-border comparability, jurisdictions might emulate early adopters by establishing connections between national and regional data portals and the NZDPU to populate the database.

In conclusion, it is important to acknowledge that developing reliable transition plans and disclosures can be resource-intensive and challenged by data availability, making it a gradual process. Nonetheless, it is in the best interest of entities to take this challenge seriously. A company's transition plan is essential for mitigating strategic and financial risks linked to the transition, while also providing clear insights into its business strategy that can draw in new investors.



## ERIC CAMPOS

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### An EU transition framework to promote climate transition and its financing

Human societies must solve an unprecedented equation whereby our 150-year-old economic and social model that has enabled the simultaneous growth of wealth production, greenhouse gas (GHG) emissions and nature loss must transition in just a few years if humanity is to continue to thrive. Science tells us that addressing the climate change consequences requires a drastic reduction in the GHG emissions and a parallel increase in residual emissions sequestration starting now in the hope to reach carbon neutrality by 2050 and limit global warming to 1.5°C by the end of the century.

At Crédit Agricole we believe the financial sector has a unique role to play to contribute to solving that equation: through our products & advice, client relationship & engagement, and credit analysis we can support the real economy transition. This is why our Group has joined the Net Zero Alliances and defined a “Net Zero by 2050” project to operationalize these commitments. This includes decarbonisation paths and action plans to reduce our GHG emissions across our financing, investment and insurance portfolios on 10 sectors based on the IEA scenario.

Our “Net Zero by 2050” project lays the groundwork for our transition plan, in line with new EU requirements<sup>1</sup> to implement transition plans towards the Green Deal 2050 carbon neutrality objective. Transition plans can usefully shed light on exposures to physical and transition risks and on our action plan to adapt to the net zero objective. However, the decarbonisation of our balance sheet can only be addressed through the decarbonisation of our clients’ activities based on credible transition plans.

To be comparable and rated in a credible way transition plans require a common transition framework at EU level, which could easily be structured on clear building blocks, based on existing initiatives<sup>2</sup>:

- Reference (science-based sectoral transition pathways), compatible with recognised international scenarios and with regional specificities where relevant to ensure certainty;
- Sectoral action plan structure (KPIs, milestones...) to guide companies as to how to get there;
- Means (Capex and Opex);
- Governance requirements to ensure transition is embedded in companies’ strategies and business models;
- Disclosure requirements (cf CSRD);
- Just transition considerations and impact;
- Significantly harmful activities considerations.

#### EU transition framework should also acknowledge and incentivise transition finance.

Such framework would help companies build their own transition plans and allow to identify and compare more effectively companies or activities whose transition is in line with the sectoral pathways and those that lag behind. Thus, transition plans can also very usefully support client engagement and advice.

That EU transition framework should also acknowledge and incentivise transition finance, thereby working as a lever to increase and mainstream transition finance. This is essential considering that in the EU alone transitioning will require

about EUR 700 bn annually in additional investments<sup>3</sup>. Currently the cornerstone of the EU sustainability framework is the taxonomy, usefully telling us where the landing zone is for an activity to be considered sustainable.

However, its transparency requirement, the green asset ratio (GAR), requires applying the taxonomy strictly, among others by forbidding the use of proxies and imposing compliance with all technical screening criteria on retail financing.

As a result, our GAR will be low despite tremendous efforts to produce it, while in parallel our work on transition finance is not acknowledged, regulatory speaking. For instance, over the last two years we have reduced our financed emissions in the oil & gas sector by 40%<sup>4</sup> but this cannot be reflected in the GAR. Considering that today’s efforts to support the transition will only materialise in the long run, a clear signal is needed now to promote transition finance efforts. For instance, the transition framework should provide that any financing which contributes to the client’s decarbonisation (within the EU transition framework) is considered transition finance. That would then allow voluntarily disclosing a “transition asset ratio” showing the extent to which financial institutions finance the transition and counterbalancing the GAR.

Finally, such a transition framework would be helpful to mitigate greenwashing risk. A science-based approach towards carbon neutrality, common definitions, actionable plans and transparency requirements would protect investors from greenwashing. At the same time, it would reduce reputational risk for both financial institutions and companies.

1. *under the CSRD, CRD6 and CSDDD*
2. *such as NZBA-Transition-Finance-Guide.pdf (unepfi.org), Oct. 2022*
3. *Annual amount needed to meet the Green Deal goals, RepowerEU and Net Zero Industry Act, European Commission Communication, June 2023, EUR-Lex - 52023DC0317 - EN - EUR-Lex (europa.eu)*
4. *Compared to 2020*



## ERIK LJUNGBERG

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### Transition planning – Reaching a net- zero society with energy efficiency funding

The financial sector has a crucial role to play in the transition to a net-zero society. Both as an awareness catalyst and capital allocator - driving behaviour and financial flows towards more sustainable activities. We have the opportunity, and responsibility, to break new ground. And perhaps, it is more important than ever. Looking back at 2023, the warmest year on record, the need and urgency to transition is undeniable. Yet, we are lagging - the global community is getting increasingly closer to failing to reach key international climate targets. In this, transition planning in the financial sector - and in turn society at large - has a key role to play in reaching a net-zero society.

A transition plan should be viewed as a strategic tool which is embedded across the company. It should reflect how the Executive Management and the Board are steering the company towards its sustainability commitments and transforming the business to respond to sustainability impact, risks and opportunities. The plan should be seen as

a dynamic document that continuously is adapted as regulations and strategy evolve. The plan can also be a useful tool to transparently inform stakeholders about a company's climate-related work. Internally, a clearly formulated plan does not only increase employee engagement but can furthermore support structuring climate-related work and identifying additional developments that could benefit the company.

Swedbank's vision is a financially sound and sustainable society. We are therefore determined to facilitate a just climate transition which not only aligns with the Paris Agreement and contributes to meeting the UN Sustainable Development Goals but also includes social aspects. Swedbank's plan is moreover closely aligned with our commitments to the Principles for Responsible Banking and the Net-Zero Banking Alliance. Going forward, the introduction of more detailed requirements of transition plans and disclosures in CSRD, CSDDD and CRR3 are welcomed aspects that can minimise the risk of greenwashing related to transition planning.

About 80 percent of our lending portfolio is related to real estate. Thus, our approach to transition focuses on incentivising the use of climate solutions and enhancing the energy efficiency of our customers' properties. Why? Because energy efficiency, small scale local production and storage of energy, have become some of society's most important tools to mitigate climate change.

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**Transition planning  
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The world needs to double progress on energy efficiency and triple renewable energy capacity by 2030 to reach net-zero emissions from the energy sector in 2050.<sup>1</sup> Also, the transformation of the global economy needed to achieve net-zero emissions by 2050 requires 9.2 trillion USD in annual average spending on physical assets, which is 3.5 trillion USD more than today.<sup>2</sup>

Our estimates show that in our four home markets there is an opportunity to release up to 90 terra watt hours by making buildings more energy efficient based on an investment of EUR 200 billion until 2040. By providing funding

to our customers for the installation of heat pumps, procurement of solar panels, insulation improvement, energy storage or other solutions, we will make our customers are better off and more resilient. Increased energy efficiency in the real estate sector would also benefit society as greenhouse gas emissions can be reduced. In addition, significant volumes of renewable energy might be released that can be used to electrify sectors such as heavy industry and transport in Europe.

The shift towards a more energy efficient Europe will require research, innovation and production at scale. A new industry is emerging that literally will fuel growth. This is an opportunity for Europe to strengthen its competitiveness by becoming more energy independent while promoting new businesses and generating job opportunities. With the revised European Performance of Buildings Directive now agreed, the EU Commission and national governments must consider how they can support the acceleration towards an even more energy efficient society. In this regard, it is important that corporate transition plans and national energy and climate plans are consistent. Finally, if we are to limit the global warming to 1.5 degrees and reach the goals in the Paris Agreement, public and private actors need to be bold, foster more collaboration and make sure Europe puts on the yellow jersey in the race to net zero.

1. <https://www.iea.org/commentaries/tripling-renewable-power-capacity-by-2030-is-vital-to-keep-the-150c-goal-within-reach>
2. <https://www.mckinsey.com/capabilities/sustainability/our-insights/the-net-zero-transition-what-it-would-cost-what-it-could-bring>



## SHINICHI TSUNODA

Operating Officer & General  
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### Accelerating the net zero transition in Japan and beyond

The last year has seen Mizuho issue an updated corporate identity and medium-term business plan, with sustainability featuring prominently in both. This is testament to our commitment to the successful and orderly decarbonisation of the global economy, including supporting the transition of Japanese industry, within our home market.

At this pivotal time, we acknowledge the importance of robust transition planning, both in relation to our own business and that of our clients. We are also acutely aware of regional context and variations in what constitutes viable transition pathways, as there is no one-size-fits-all approach to decarbonisation. In addition to engaging with our clients, we actively contribute to transition-oriented multilateral efforts that can benefit us all.

#### Importance of robust transition planning

Our stakeholders have high expectations of Mizuho, as one of the leading Japanese financial institutions. Among others, we

are expected to assume a leadership role in Japan's industrial growth strategy, similarly in GX (green transformation), and to contribute to the sustainability transition elsewhere in Asia. The north star that we are working towards is net zero by 2050, in support of a low-carbon sustainable society.

With these aims and expectations in mind, Mizuho recognises the importance of transition planning, both in relation to our own business and that of the companies we finance – indeed the two are interlinked. We formulated our Net Zero Transition Plan in 2022 and have revised this more recently, in order to promote an integrated response to climate-related issues across the Group. Our approach revolves around facilitating a real economy transition while capturing business opportunities and enhancing risk management practices.

Importantly, we understand that transition planning should not only be about responding to climate change, but doing so while taking into account social and governance considerations – in other words, a just transition. For example, this means promoting respect for human rights and good governance practices.

#### Regional context for transition: idiosyncratic opportunities

Through our deep experience of financing Japanese corporates on the one hand, and the breadth of our global presence on the other hand, we understand that the net zero transition will not be uniform across economies. Transition pathways vary by region, as each geography needs a decarbonisation strategy fit for its economic and social realities (for example, its current energy mix and demographics).

**The north star that we  
are working towards  
is net zero by 2050.**

In Japan, we have identified technological innovation and business structure reform as the key drivers of the country's industrial competitiveness, and we see sustainability efforts as linked to and even instrumental to success in these areas. Geographic attributes also play an important part in identifying what is realistic and viable. For instance, Japan's renewable energy production prospects are influenced by a shortage of land for solar power and onshore wind power generation. However, this is offset by ample opportunities for renewable energy production through

offshore wind power, thanks to Japan's long coastline and good offshore winds. Mizuho's business focus in renewable energy in Japan is, accordingly, on offshore wind, alongside carbon capture and utilisation (CCU), carbon recycling and hydrogen.

#### Multilateral efforts

Our reach is not limited to Japan and we serve clients and engage with a range of stakeholders all over the world. Multilateral cooperation is crucial for the success of the global net zero transition – between governments, regulators, industry and financial institutions. To date, regulatory fragmentation in the spheres of climate risk and sustainability has posed challenges for businesses such as ours that operate across borders. Thus, we welcome increased multilateral efforts aiming for more consistency and regulatory convergence in these areas. Clarity and certainty will help financial institutions such as ours support the real economy transition, delivering the finance that is needed for its success.

Mizuho plays its part in multilateral efforts, for example, through our recent participation at COP28 in Dubai as part of the Japanese delegation. The scale of the financing and investment needed to meet the challenges we face is unprecedented and can only be met through collaborative efforts – for us, this was one of the key takeaways from COP28. We continue our ongoing involvement with industry bodies and organisations developing sustainability- and climate-related standards and frameworks, as well as regulators across the jurisdictions where we operate.