Climate-related risks and opportunities

The appetite in the Netherlands

November 2017
Climate changes business

Key findings of TCFD survey

KPMG has conducted research based on a survey under Dutch listed companies in the financial and non-financial sectors. Thirty-four senior managers responded to the questionnaire. The results confirm that climate-related risks and opportunities deserve further attention, primarily with regard to the understanding of the financial implications of climate change.

- Already being affected: 3%
- Affected in the short to medium term (1-5 years): 6%
- Yes, but only on the long term (>5 years): 27%
- No, will not be affected: 35%

Almost all respondents expect business bottom line to be impacted by climate-related risks, but companies have different views on the term. More than one third say they already experience financial impacts from climate change.

However

Only 1 out of 10 companies do not have a clear picture of the potential associated financial exposure.

Half

44% of the companies have assessed their exposure to long-term financial risks

70%

Of the companies have discussed climate-related risks at the Board level

Main reasons

for companies to start implementing the recommendations of the TCFD:

1. Climate-related financial risks may have a material financial impact
2. Reporting is expected to become mandatory, want to be prepared
3. Increasing demand from investors for this type of information

62% of the respondents say their company is already adapting their strategy to respond on climate-related risks and opportunities.
The final recommendations of the Task force on Climate-related Financial Disclosures

Many of the world’s largest companies are under ever-increasing pressure to cut their carbon emissions, as the global economy shifts towards a low-carbon model. The Paris Agreement has further fueled this pressure. At the same time, climate change has already shown substantial impact on businesses, is expected to continue and could even end up being more impactful than suspected today. At the global scale, predictions indicate that it could also impact the financial stability of individual economies. The Task force on Climate-related Financial Disclosures (TCFD) was established to improve transparency of the financial sector and businesses on the risks and opportunities of climate change.

Contrary to existing reporting frameworks, the TCFD explicitly focuses on the impact of climate change on a company – not the other way around. The final recommendations have been published in July 2017, the essence of their final framework is shown below. The recommendations focus on four financial sectors (Banks, Insurance companies, Asset managers, Asset owners) and four non-financial groups (Energy, Transportation, Materials & buildings, Agriculture, food & forest). For each the TCFD has provided further guidance.

Further information is to be found at www.fsb-tcfd.org.
The final recommendations include a number of specific aspects that preparers should take notice of:

- The disclosures are expected to be included in mainstream financial filings;
- Companies are requested to report on the governance and risk management recommendations regardless of materiality considerations. By disclosing this, it will be clear whether the fundamentals have been paid attention to by preparers;
- For the other recommendations, financial materiality considerations apply as they do for other financial reporting. Such considerations should be subject to the applicable legal requirements;
- The focus of the recommendations is on future-oriented information for the risks and opportunities and should cover short-, medium- and long-term information that enables financial sector parties in taking investment and financing decisions.
- Companies are expected to report on future scenarios; including a 2-degree scenario in accordance with the Paris Agreement, that inform the users about the resilience of the company’s strategy under various future climate scenarios;
- Whereas scenarios should be expressed in financial or quantitative terms eventually, the Task force expects that companies will start the journey with qualitative disclosures.

Key conclusions from our survey on climate risks and opportunities

In this phase most companies are exploring the implications of the TCFD recommendations for their reporting and their business. In order to assess the current state of play, KPMG has conducted research based on a survey under Dutch listed companies in the financial and non-financial sectors, to which 34 senior representatives responded. The results confirm that climate-related risks and opportunities deserve further attention, primarily with regard to the understanding of the financial implications of climate change.

Climate risk is a recognized issue, whilst views on horizon of impact differ
Climate change is widely recognized as an issue that impacts the bottom line of companies: 90+% of the respondents confirmed this. They differ though when it comes to the time horizon of the impact: a third says their financial performance is being affected already, whereas another third expects such impact in the next 5 years to come. The final third expects no financial impact in the short- to medium-term.

KPMG view: climate change is a long-term issue that requires a long-term view on the company’s business and portfolio. Even when you expect longer-term impact only, you would still need to consider what such impact could imply for your investments, your products and your markets.

Board is engaged, but financial exposure unknown
It is only a minority of 30% of the companies for which climate-related risks and opportunities have not been discussed at Board Level. Board’s involvement has resulted in more than 50% of the companies having assessed their exposure to financial risks. Surprisingly though, 90% of these companies do not have a clear picture of the potential associated financial exposure. With that in mind, it is also noteworthy that the majority (60%) has adapted their strategies to adapt to these risks and opportunities – without exactly knowing what the financial exposure to risks is.

KPMG view: the assessment of the potential financial impact of climate-related risks is fundamental to understand the issue – or in other words: get the risks or opportunities to life. Without it, companies may stick to the traditional risks only, such as carbon emissions and miss transition risks such as shifting consumer preferences.
Embedding in systems and processes in early days
Clearly, identifying, assessing and monitoring climate-related risks and opportunities requires related systems and processes to ensure proper embedding in performance management. A vast majority (90%) of companies have embedded climate-related risks in their risk management systems, of which about a third has done so for all climate-related risks. Six out of ten though have not identified and/or implemented any metrics to measure and manage climate-related risks and opportunities and only one out of six have set metrics that are part of their global management and control processes.

*KPMG view:* many risks and opportunities are not defined by financial but rather by non-financial (or better: pre-financial) metrics. Mapping existing non-financial metrics to the risks and opportunities identified and critically reviewing the cause-effect relationship between these are fundamental to embed proper monitoring.

Scenario analysis will grow in the coming years
The TCFD has introduced scenario analysis as a way to test the resilience of a company’s strategy to the impacts of climate change. Only one third of respondents said that they already apply scenario analysis and 40% of the respondents are planning to start with it, mostly on the short term.

*KPMG view:* as clear guidance for consistent approaches is still lacking and scenario analysis is new, companies should not overcomplicate. Our advice would be to start with identifying climate-related risks and exploring how climate-related risks may impact its business, strategies and financial performance in qualitative terms.

TCFD framework is not well known
The survey shows that close to half of the respondents are not aware of the TCFD recommendations. Whereas the recommendations were only issued recently (July 2017), this indicates that Dutch investors, the Central Bank as well as other parties have still work to do to further raise awareness of (the relevance of) the recommendations.

**Recommendations will be implemented, with delay**
The TCFD has indicated that the implementation of the recommendations needs to be approached as a journey, where companies continuously learn and improve their understanding of climate-related risks and disclose on them. It is encouraging to learn that the majority of companies intends to implement the recommendations. Timing differs though: a third suggests it will implement the framework in its next annual report, a half will do so in future years. In terms of the scope of implementation, a quarter of companies intends to implement all the TCFD recommendations right away once they start, whereas about 40% will go on a journey towards full implementation.

*KPMG view:* the recommendations regard real business issues and implications. In light of that and given the complexity, even if companies do not start on the disclosure journey, they should consider the business implications and start preparing themselves for managing the risks – if these appear to be material.

Companies recognize business impact and face lack of expertise
The main reasons for adopting the recommendations as provided by the respondents are the perceived material financial impact on the company and the increased interests arising from investors. Some companies also expect the recommendations to become mandatory in the future and want to be prepared. Finally, from an implementation perspective, most of the companies expect or face difficulties that include the lack of experience and expertise, lack of accurate information and the lack of resources and funding.

*KPMG view:* the risks and opportunities from climate change are complex to assess and manage, as they are new to companies in terms of the financial lens taken by the Task force, they are long-term and therefore uncertain by nature and because they can be non-linear and therefore different from the more traditional business risks. To address the risks and opportunities effectively, many disciplines should be involved: sustainability, risk management, control, strategy – but most importantly: finance.
Where to start?

Whereas the TCFD recommendations relate to disclosures, they effectively trigger business-related questions. We have learnt that after an initial maturity assessment the journey towards implementation starts more often with the identification of risks and opportunities than anything else. In our view the pathway towards implementation will vary amongst others with the level of understanding, the business, the ambitions of the company and the actions taken to date with respect to climate change.

So where to start? We have outlined below typical questions that we have identified in client conversations and related implications. At KPMG we have developed various tools to support you in steps to be taken and these are also outlined below for your reference.

<table>
<thead>
<tr>
<th>Fragen wir hören:</th>
<th>Was bedeutet das für sie?</th>
<th>Wie können wir Ihnen bei Ihrer Frage helfen?</th>
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</thead>
</table>
| - Ist mein Unternehmen bereit, die TCFD-Ratschläge umzusetzen und zu berichten?  
- Inwieweit entsprechen meine Darstellungen den TCFD-Ratschlägen? | - Verstehen Sie die TCFD-Ratschläge und ihre Auswirkungen in Bezug auf die vier Aspekte | Unsere Climate Maturity Assessments decken die vier Schlüsselbereiche der TCFD-Ratschläge ab und helfen Organisationen, den Niveau der Maturität zu bewerten. Der TCFD Gap Analysis hilft Ihnen dabei, das Niveau der Bereitschaft für Ihre aktuelle Berichterstattung oder interne Prozesse für die TCFD-Ratschläge zu bewerten. |
| - Welche klimarelevanten Risiken und Chancen können bei meinem Unternehmen auftreten und welche finanziellen Auswirkungen hat das?  
- Wie bedeutet das und wie können sie beurteilt werden?  
- Wo in dem Wertschöpfungsprozess und in welchen Ländern ist mein Unternehmen am stärksten ausgesetzt an klimarelevanten Risiken?  
- Wo ist der Unterschied zwischen klimarelevanten Risiken und anderen Risiken (z.B. operational, finanziell, strategisch)? | - Identifizieren Sie relevante klimarelevante Risiken und beurteilen Sie, wo sie in Ihrem Business qualitativ liegen  
- Priorisieren Sie die klimarelevanten Risiken, basierend auf:  
  • Externe Trends (z.B. die Übergangsphase zu einer niedrig kohlenstoffintensiven / erneuerbaren Technologie)  
  • Geschäftsgrundlagen (z.B. Ratschläge von Regulatoren, die klimarelevante Risiken offenlegen)  
  • Der potenzielle finanzielle Impakt der Risiken auf Ihre Geschäft, zuerst qualitativ abzuschätzen. | Unsere Prioritization and Visualization Model ermöglicht Ihnen die Identifizierung und Visualisierung der Risiken und Chancen in einem interaktiven Dashboard. Als klimarelevante physikalische Risiken sind diese meistens auf Landesebene identifiziert, unser Country Risk Index deckt Ihre Risiken auf der Basis Ihrer Unternehmensleistungsdaten, Produktionsvolumen, Wasser, Energieverbrauch und anderen Länderdaten ab, um zu ermitteln, in welchen Ländern Ihre Betriebe und Wertschöpfungskette am stärksten ausgesetzt sind klimarelevanten Risiken. Unser Risk Landscape Tool gibt Ihnen Einblick in, wie Klimaänderungen Ihre Organisationen betreffen können. |

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<th>Questions we hear:</th>
<th>What does this mean for you?</th>
<th>How we can help you address your questions?</th>
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<tbody>
<tr>
<td>- What are relevant scenarios for my company to consider?</td>
<td>- Define a set of 2 or 3 scenarios based on your geography and industry, including a scenario assuming global warming of 2°C</td>
<td>Climate Scenarios Analysis gives you insight in how your organization’s strategy and financial plans may be affected by climate-related risks and opportunities in short, medium and long term. Our Resilience Radar is able to link company-specific prioritized risks to measure the resilience of your business model in different future scenarios.</td>
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<tr>
<td>- How will my strategy perform under different climate scenarios, including a 2°C?</td>
<td>- Start with a qualitative assessment of how your organization’s strategy and financial plans may be affected under the scenarios</td>
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<td>- Is my strategy resilient to climate-related risks and opportunities?</td>
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<td>- How can my company develop models that respond to the implications of each scenario?</td>
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<tr>
<td>TEST RESILIENCE OF STRATEGY</td>
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<td>- How to select and implement material indicators for effective monitoring of climate-related risks?</td>
<td>- Identify and assess existing climate-related risk indicators to select key material indicators – or identify gaps</td>
<td>Our Targets and Metrics Assessment could support you with defining own metrics and targets that address key disclosure areas. By disclosing on a selection of strategic and sector-consistent metrics and targets, your company is able to meet the emerging financial disclosure expectations of key stakeholders.</td>
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<td>- How robust are my processes including metrics measuring to manage &amp; monitor relevant climate-related risks and opportunities?</td>
<td>- Assess the current state of your processes for identifying and reporting climate-related risk</td>
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<td>- Adapt existing ERM/risk management processes to be effective in identifying and managing climate-related financial risk</td>
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<td>- Implement new reporting systems &amp; controls</td>
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<td>MEASURE USING METRICS AND TARGETS</td>
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Contacts

Wim Bartels
Partner
E: bartels.wim@kpmg.nl
T: 020-6567783

Arjan de Draaijer
Partner
E: deDraaijer.Arjan@kpmg.nl
T: 020-6567943

Anne-Cecile Moreno
Manager
E: Moreno.Anne-Cecile@kpmg.nl
T: 020-6564610

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