

Submission to the Natural Resources Committee Inquiry into Environmental, Social and Governance

Australian Sustainable Finance Institute | 14 May 2024

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Introduction

The Australian Sustainable Finance Institute (ASFI) welcomes the opportunity to provide input and feedback to the Parliament of South Australia Natural Resources Committee's Inquiry on Environmental, Social & Governance.

Australia has ambitions of becoming an inclusive, net zero and nature positive economy. These ambitions require transformative action across the economy, including participation from policymakers, regulators, primary producers, and financial institutions. This submission sets out our views on the key challenges and opportunities in relation to ESG, with a particular emphasis in finance sector perspectives.

About ASFI

ASFI is a not-for-profit organisation working to align the Australian financial system with a sustainable, resilient, and inclusive Australia. Our members are 44 of Australia's leading financial institutions – including major banks, superannuation funds, insurers, asset managers, and financial services firms. ASFI members collectively hold over AU\$22 trillion in assets under management and are committed to allocating capital in a way that creates positive social and environmental outcomes.

The importance of ESG to capital markets

There is global recognition of the need to address climate change, halt potentially catastrophic nature loss and reduce growing inequality (which is exacerbated by both climate change and

nature loss) to secure a safe and prosperous future for current and future generations. This is reflected in global commitments and initiatives including the Paris Agreement on Climate Change, the Kunming-Montreal Global Biodiversity Framework (GBF) and the UN Sustainable Development Goals (SDGs).

Challenges in relation to climate, nature and inequality have implications for macroeconomic stability and long-term prosperity and are therefore attracting considerable attention from global capital markets. As a result, momentum for ESG¹ action is starting to reshape the direction of global capital flows. Key markets including Australia are increasingly introducing policies and regulation to drive sustainability across the finance sector, including through mandatory disclosure regimes, green finance incentives, and sustainable finance taxonomies. There has also been considerable growth in capital allocated towards sustainability objectives, as key finance players seek to respond to stakeholder expectations (including from customers and investors²), manage ESG-related risk and capitalise on ESG-related opportunities.

Overview of sustainable finance in Australia

The Australian Sustainable Finance Institute was established in 2021, following a finance-sector led collaboration to reshape Australia's financial system to support a thriving Australian society, a healthy environment and a strong and prosperous economy. The collaboration produced the [Australian Sustainable Finance Roadmap](#), which ASFI is responsible for driving, together with financial institutions, regulators and governments. Critical to achieving the aims of the Roadmap is policy and regulation that enables the incorporation of ESG considerations into financial decision making, and in particular to support accurate pricing of ESG-related risks and opportunities.

Alongside this, implementation of the Australian Government's [Sustainable Finance Strategy](#) is well underway. The Strategy, released in November 2023, sets out a pathway for creating an Australian sustainable finance policy architecture that addresses climate and sustainability related risk and opportunities, and channels capital consistent with Australia's net zero and broader sustainability objectives. Notable progress has been made on climate-related financial disclosures and an Australian sustainable finance taxonomy.

Rapid implementation of this Strategy will help bring Australia into alignment with global developments, supporting access to international capital. While the Government's initial focus is on climate, the Strategy commits to expanding focus over time to include other sustainability-related issues, in particular nature and biodiversity, and First Nations perspectives and outcomes.

ESG-related risks and opportunities for Australian primary producers

Australia is highly impacted by the physical risks of climate change and nature decline. For example, in 2021 the Australian Bureau of Agricultural and Resource Economics (ABARES), estimated that changes in seasonal conditions over the period 2001 to 2020 (relative to 1950 to 2000) had reduced annual average farm profits by 23%, or approximately \$29,200 per farm³.

¹ See [here](#) a summary by UN Principles for Responsible Investment of the issues typically captured by the term 'ESG'.

² For example, sustainability linked loans in Australia totalled \$30 billion in 2022, up from \$19 billion in 2021, while 'responsible' investment assets under management totalled \$1.29 trillion (RIAA, 2023, [Benchmark Report - Responsible Investment Association Australasia \(RIAA\)](#))

³ ABARES, Analysis of climate change impacts and adaptation on Australian farms:

<https://www.agriculture.gov.au/abares/products/insights/climate-change-impacts-and-adaptation>

These impacts were most pronounced in south-western and south-eastern Australia, with northern Australia and the coastal higher rainfall zones tending to be less affected.

Additionally, as a net importer of foreign direct investment (FDI), Australia faces significant transitional and economic risks in relation to the global shift to net zero. This is particularly important given Australia is already one of the most carbon intensive countries in the OECD, and its biodiversity is poor and worsening⁴. Australian producers that demonstrate strong ESG-related management and performance will be better positioned to attract capital, as global investors and purchasers look to improve the social and environmental footprint of their value chains and protect the value of their portfolios. Issues of particular focus include deforestation, greenhouse gas emissions, and modern slavery.

At the same time, increased interest in ESG attributes presents opportunities for Australia – a resource rich country - to lead in the production of sustainable agriculture, mining and other commodities. Capitalising on these opportunities will require strong policy responses that enable markets to price ESG-related risk, recognise and drive capital towards ESG-related opportunities, and generate robust, comparable, and transparent information to ensure efficient operation of markets.

Operationalising sustainable finance in Australia: key developments

ESG (sustainability) reporting

To accurately price-in ESG-related risks and opportunities, financial institutions require robust, consistent, quality, transparent and verifiable information and data about their clients and assets. Such information enables financial institutions to adjust their capital allocation away from high-risk activities to new opportunities.

In recent years there has been considerable momentum globally to increase the coverage and harmonisation of ESG (sustainability) reporting by corporates and financial institutions. This is demonstrated most notably in work by the International Sustainability Standards Board (ISSB) to develop a high-quality, comprehensive global baseline of sustainability disclosures focused on the needs of investors and the financial markets. In 2023 the ISSB issued its inaugural standards – IFRS S1 and IFRS S2 – which provide disclosure requirements to communicate sustainability-related risks and opportunities, and climate-related risks and opportunities respectively. These standards are fast emerging as global best practice.

Countries around the world have started to mandate adoption of the new IFRS standards. This includes the Australian Federal Government, which has recently introduced a [Bill](#) into Parliament to legislate requirements for mandatory climate-related financial disclosures (based on an adapted version of the IFRS standards that has been developed for an Australian context by the Australian Accounting Standards Board⁵) as part of annual reporting by corporates and financial institutions. The Bill is expected to be passed in mid-2024, with reporting period to begin from 1 January 2025 for the largest entities, and requirements for other large entities phased in progressively.

⁴ OECD Environmental Performance Reviews: Australia 2019: https://www.oecd-ilibrary.org/environment/oecd-environmental-performance-reviews-australia-2019_9789264310452-en#:~:text=Australia%20is%20among%20the%20top,and%20carbon%2Dintensive%20OECD%20economies.

⁵ We note the AASB standards are expected to be finalised following passage of the Government's legislation.

The introduction of mandatory climate reporting in Australia – supported by major Australian financial institutions and business groups⁶ - is a welcome development and key pillar of an emerging sustainable finance architecture that helps to ensure Australia's competitiveness, resilience, and ability to attract global capital.

Sustainable finance taxonomy

Directing capital to activities and assets that are aligned with sustainability/ ESG targets and commitments necessitates a set of definitions of sustainable activities. Sustainable finance taxonomies are a set of common definitions for sustainable economic activities that help financial institutions identify sustainable investments credibly and transparently and guide capital to support the achievement of global climate, environmental and social objectives. They also provide investors with confidence and assurance of sustainability claims, enabling comparability between investment products and portfolios and reducing transaction costs.

The [Australian sustainable finance taxonomy](#), currently in development by ASFI in partnership with the Commonwealth Treasury, is as a key enabler for Australia's climate and nature agenda. It is expected that the taxonomy will foster integrity and standardisation of sustainable finance efforts and that it will be a tool that can help prevent and combat greenwashing. The initial development phase covers climate mitigation criteria for priority sectors and associated technical work on data requirements, methodology for incorporating transitional activities, Minimum Social Safeguards and a 'Do No Significant Harm' framework.

The six priority sectors align with the sector decarbonisation plans currently being developed by the Australian Government:

- Electricity generation and supply (Energy)*;
- Minerals, mining and metals*;
- Construction and the built environment*
- Manufacturing/ industry;
- Transport; and
- Agriculture.

(* indicates the first sectors to be developed). The first three sectors will be released for public consultation in late May 2024.

Valuing Natural Capital, an ASFI and Farming for the Future partnership

In 2023, ASFI launched its partnership with Macdoch Foundation's Farming for the Future (FftF): ['Valuing Natural Capital'](#). The partnership brings together Australian agricultural producers and financial institutions to integrate natural capital considerations into financial and business decision-making of financial institutions.

FftF is creating a national-scale evidence base that connects on-farm natural capital management and farm productivity. This will inform the establishment of natural capital indicators and metrics related to farm business productivity, profitability, and resilience. It will be designed to help farmers integrate natural capital metrics in their business performance and set goals and targets to drive improvements in nature. This will in turn enable banks and agri-investors to work with farmers to invest in natural capital for the benefit of their businesses and for society more broadly.

⁶ See, e.g. [joint statement](#) by 15 peak industry groups supporting passage of the disclosures legislation.

Information and data needs and requirements from primary producers

As noted above, sustainable finance efforts need to be informed by robust and quality information and data from financial institutions' clients and assets, including those from primary producers, related to their ESG characteristics and performance. The most significant ESG-related data needs from primary producers include greenhouse gas (GHG) emissions and nature-related issues data and information, however, these needs differ depending on each financial institution's ambitions and requirements, and may differ according to the objectives of specific financial products. Other areas where ESG related information and data may be required include human rights, First Nations engagement, leadership and ethical business practices.

At present, financial institutions face multiple difficulties obtaining fit-for purpose information and data related to primary production. Some of these difficulties include:

- Lack of robustness, quality, consistency, transparency, and availability of information, particularly in the agriculture and land sectors.
- Misalignment between local and federal data sets and systems (integrated and consistent data sets are desirable for decision making).
- Cost, time, security and confidentiality concerns. Obtaining fit-for-purpose information and data is likely to impose time and cost burdens on primary producers. There is a strong awareness amongst financial institutions that these costs and efforts should be fairly spread out across value chain players in order to increase uptake of sustainable management practices and the collection of related data.

Thank you for the opportunity to provide this feedback. We would be happy to discuss any of our comments in more detail with you. Please contact Angelica Del Hierro at angelica.delhierro@asfi.org.au if you have any questions.