Climate Transition Conversation Guide

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Companies are setting net-zero and other climate commitments in growing numbers to demonstrate their readiness to take action in the face of climate change. However, meaningful details about how these commitments and even climate change itself will affect corporate strategy are scarce. Such clarity is particularly important for assets, companies and industries in transition. The lack of clarity is impeding market reactions to climate commitments.

Investors are looking for clearer insights on the impact of climate change on corporate capital allocation plans, opportunities for revenue generation, and changes to strategic goals and KPIs. Companies are looking to communicate how they are evolving their business model and approach for resilience in a transitioning world.

FCLTGlobal's *Climate Transition Conversation Guide* (based on Driving the Conversation: Long-Term Roadmaps for Long-Term Success) provides a framework that companies and investors can use to engage fruitfully on how climate change impacts corporate plans for long term value creation. And it provides examples of how companies have communicated their transition plans to investors.

Companies can use this tool to drive internal deliberations and decision making as they develop a robust climate transition plan that is integrally linked with their long-term strategy. Investors can use this tool to engage portfolio companies on the details of this integration.

QUESTIONS TO CONSIDER:

1. **Corporate Purpose:** How does climate change affect the way that the company intends to create value now and in the future?
2. **External Environment:** How does climate change influence the company's core drivers of growth, competitive environment, and management's view of the market?
3. **Strategy, Goals and KPIs:** How does climate change affect the company's strategic plan, and related goals and KPIs?
4. **Capital Allocation and Investments:** How does climate change affect the company's capital allocation plan?
5. **Risks:** How has climate change been reflected in the company's risk management framework?
6. **Accountability and Incentive Alignment:** How is the company structured to allow for the integration of climate change into the business strategy at all levels?

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1. Corporate Purpose: How does climate change affect the way that the company intends to create value now and in the future?	
a. Is the company's approach to value creation affected by climate change or its climate commitment? b. Does climate change threaten the accomplishment of the company's purpose? c. Could the company's purpose be enhanced by climate change? For instance, could the company contribute to climate change solutions?	BP statement of corporate purpose puts climate change at the center of who the company is and how it will create value. *"Our purpose is reimagining energy for people and our planet. We want to help the world reach net-zero and improve people's lives."*

2. External Environment: How does climate change impact the company's core drivers of growth, competitive environment, and management's view of the market?	
a. How do the physical and transition impacts of climate change affect the company and the industry across time horizons and recognized impact scenarios? Are these impacts material? b. Do climate change impacts affect the company's core drivers of growth? Are they enhanced, changed, or at greater risk? c. How could climate related policy or regulatory developments affect the company's business? d. Will the transition to a low-carbon future unlock business opportunities, technology, capital and markets? e. Does climate change affect the company's suppliers and customers? How is the company positioned to meet their evolving needs? f. Is the company well positioned to capitalize on climate change solutions? Is there an opportunity to develop a competitive advantage? g. What could the company learn from its competitors' approaches to climate change?	Total's strategic plan presentation provides a detailed analysis of external drivers based on its climate scenario analysis – including projections on massive electrification, deep decarbonization through the use of renewables, and potential plastics bans lowering use demand for oil. NextEra's strategic plan presentation identifies trends that are disrupting the energy sector today and projected changes over the coming decade. Edison International's strategic plan presentation includes a detailed analysis of California's greenhouse gas reduction goal and regulatory context as a driver for the company's strategic plan.

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3. Strategy, Goals and KPIs: How does climate change affect the company's strategic plan, and related goals and KPIs?	
a. What is the time horizon for the company's strategic plan? b. Has the company made a climate commitment? Has this commitment and climate impacts across relevant time horizons been factored into its strategic plan? c. To what extent will climate change be integrated into the company's strategic plan by 2030? What action steps will the company take immediately to operationalize this integration? d. What are the company's biggest challenges in integrating climate change into its strategic plan? e. Does climate change or the company's climate commitment impact existing, new, and planned products or business lines? f. Does climate change or the climate commitment positively or negatively affect sales, income and earnings projections and goals? g. Has the company adjusted its Research & Development portfolio to accommodate climate impacts or operationalize its climate commitment? h. Does climate change or relevant commitments impact existing KPIs (e.g., profitability, revenue growth, costs)? i. Should the company adopt new KPIs that would better reflect climate change impacts on the strategic plan (e.g., expected revenue growth from climate change opportunities)?	Enel's 3-year strategic plan lays out climate change as the center of the company's plan, noting how the climate change transition will transform the energy world in the coming decades and laying out an ambition to be a "renewables super major with the world as its geographic footprint". This strategy is underpinned by specific long-term Renewable Energy Storage capacity by 2030"). ASML's annual report includes a detailed discussion of the company's vision to improve its own energy efficiency and that of its value chain, and the strategic and technological challenges that the company faces to implement this vision. Danone's annual financial results presentation discloses its "carbon adjusted" Earnings Per Share (EPS) as well as its cost of carbon per share.

4. Capital Allocation and Investments: How does climate change affect the company's capital allocation plans?	
a. Will the company's existing capital assets be impacted by the physical or transition impacts of climate change or the implementation of its climate commitment? b. Are any capital assets at risk of being stranded on account of the climate transition? What is the strategy for at risk assets? c. Do the company's accounting assumptions (e.g., depreciation schedules, internal hurdle rates, weighted average cost of capital) need to be revised to take relevant climate commitments into account? d. How are climate change and decarbonization efforts be reflected in the company's planned capital allocations? Does the company factor in a price on carbon as a part of capital allocations? e. Are there opportunities to acquire assets to operationalize its climate commitment? f. How does the company's capital allocation strategy reflect assets in transition, including investments needed to decarbonize such assets? g. What is the company's strategy on investing resources (capital, talent, other) to explore opportunities to generate value in pursuit of its climate commitment? Which businesses and initiatives are best positioned in this regard?	BP's ESG investor pack declares: "*Each new material capex investment approved in 2020 was evaluated to be consistent with the Paris goals.*" The company also identifies the carbon price factored into investment appraisals, and growth in capital investments into its non-oil and gas business. Volkswagen's net zero announcement included details of the company's planned investments in decarbonization efforts. The company's strategic plan presentation includes additional details on how capital will be reallocated in support of these goals.

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5. Risks: How has climate change been reflected in the company's risk management framework?	
a. Does the scope of the company's climate change risk identification process cover its value chain? Is it adaptive to the evolving science of climate change impacts? b. Is climate change reflected in the company's risk inventory? How do climate change trends impact the existing risk inventory? c. How does the Enterprise Risk Management process allow the company to identify the new, emerging and changing impacts of climate change on the business? Does the company have a process to factor in the latest climate science into its climate risk assessment? d. What is the company's tolerance for the risks that have been identified? e. What are the company's plans to adapt to its climate risk exposures, for instance through insurance, contingency reserves and other mechanisms? Does the company have a plan to respond if the scope of risks exceeds this level? f. Does the company face the potential that climate change risks could precipitate losses that would threaten its purpose?	Unilever's annual report contextualizes the company's climate change efforts in a detailed financial analysis of the impacts of climate change on key agricultural commodities that the company depends on. Prosus' annual report includes a detailed matrix laying out the company's key risks and impacts on capital. The matrix identifies sources of risk, measures to respond to risk and changes to be monitored. Climate change is identified as a source of risk to financial and natural capital.

6. Accountability and Incentive Alignment: How is the company structured to allow for the integration of climate change into its strategic plan at all levels?	
a. How does the company's board oversee climate change risks? Is the climate commitment addressed in board discussions in strategy, risk, and compensation? How frequently does the board discuss climate change? b. Is the responsibility for overseeing climate change risks and implementing the climate commitment spread across corporate leadership, including the Named Executive Officers? c. How fluent is the board, senior management and the workforce on climate change impacts on the business? Do they have access to training or capacity building on climate change? d. Has the company put systems in place to engage employees across the organizational structure on the implementation of its integrated climate and business strategy? e. How are executives and employees at all levels effectively incentivized for performance on the integrated climate and business strategy? What is the nature of the linkage?	Verizon's TCFD report details how each of its board committees engages on climate change. This includes its Finance Committee, which oversees the company's capital allocation efforts, including its green finance program. The company also discloses how all top management are involved in the implementation of its climate change efforts. The board has linked the incentive award of all employees to climate change targets.

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HOW DOES THE CLIMATE TRANSITION CONVERSATION GUIDE OVERLAP WITH THE TCFD?

In 2015, the Taskforce on Climate Related Financial Disclosures (TCFD) released a set of climate disclosure recommendations that are now considered to be the gold standard in climate change reporting.

The Climate Transition Conversation Guide is not a disclosure framework. The goal of the tool is to support companies in having internal conversations and investor dialogue that drive the integration between climate change, capital allocation and long-term strategy. The resulting integrated strategy would then contribute to all business and ESG reporting, including TCFD based reports.

The table below maps how the Climate Transition Conversation Starter contributes to elements of TCFD reporting.

<table>
<tr><th>Climate Transition Conversation Starter</th><th>TCFD Recommendations</th></tr>
<tr><td>Corporate Purpose: How does climate change affect the way that the company intends to create value now and in the future?</td><td rowspan="4">Strategy: Disclose the actual and potential impacts of climate-related risks and opportunities on the organization’s businesses, strategy, and financial planning where such information is material.

Metrics and Targets: Disclose the metrics and targets used to assess and manage relevant climate-related risks and opportunities where such information is material.</td></tr>
<tr><td>External Environment: How does climate change influence the company’s core drivers of growth, competitive environment, and management’s view of the market?</td></tr>
<tr><td>Strategy, Goals and KPIs: How does climate change affect the company’s strategic plan, and related goals and KPIs?</td></tr>
<tr><td>Capital Allocation and Investments: How does climate change affect the company’s capital allocation plan?</td></tr>
<tr><td>Risks: How has climate change been reflected in the company’s risk management efforts?</td><td>Risk Management: Disclose how the organization identifies, assesses, and manages climate-related risks.</td></tr>
<tr><td>Accountability and Incentive Alignment: How is the company structured to allow for the integration of climate change into the business strategy at all levels?</td><td>Governance: Disclose the organization’s governance around climate related risks and opportunities.</td></tr>
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FCLTGlobal’s mission is to focus capital on the long term to support a sustainable economy. We are a non-profit organization whose members are leading companies and investors worldwide that develops actionable research and tools to drive long-term value creation for savers and communities. To learn more, visit www.fcltglobal.org.