

IIF Briefing Note – November 2021

COP26: Outcomes and Implications for the Global Financial Sector

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Quick Read

- **Progress, but not enough to avert dangerous climate change:** The Glasgow Climate Pact acknowledges the urgency of emissions reductions to ‘keep 1.5c alive’, with accelerated timelines for updates to 2030 targets within countries’ Nationally Determined Contributions (NDCs). Landmark agreements were reached on reducing methane emissions, and abating deforestation. However, current policies still orient the world towards dangerous levels of warming, and the new agreement fell short of explicitly calling to end coal use.
- **Climate finance promises reaffirmed, but flows still lacking:** Developed countries have not delivered on the ‘\$100 billion’ of climate finance for developing countries, and a post-2025 financing mechanisms remains in the balance for future COPs. While new pledges to scale up finance for adaptation were a positive outcome, outstanding questions on other financing – such as funding to address “loss and damage” – will remain on the negotiating table.
- **A pathway forward for global carbon markets:** Negotiations on Article 6 of the Paris Agreement proved a success at COP26, with an agreement reached on implementing a new global carbon market for international transfer of mitigation outcomes.
- **Private finance is committed – yet mobilization remains complex:** The financial services industry played a key role at COP26, with new announcements from the private sector and regulators—and the launch of a new global sustainability standards board. However, while the private sector has a major role to play in decarbonizing the economy, many noted that their actions must be complemented by public policy to have a real impact on global emissions
- **Emissions reductions need to be fast and furious:** The final scorecard for COP26 is an improvement over previous COPs, but well short of outright victory. The IEA has estimated that if all COP26 commitments are met, global warming will be limited to 1.8c by 2100. But this is still too high, particularly given that current commitments for 2030 would leave global warming at 2.4c in 2100. The strength and speed of emissions reductions will need to ramp up rapidly in the coming decade to stabilize the global climate.

1. UNPACKING THE GLASGOW CLIMATE PACT

The Glasgow Climate Pact (GCP)—the formal agreement of negotiating parties at COP26—delivered more than expected. However, there is still much work to be done to “bend” the global emissions curve down to a 1.5c pathway. Key developments in three areas (mitigation and adaptation, finance, and implementation) will shape the future of the global climate agenda. This section summarizes some of the most consequential decisions (or lack thereof), and the key themes that are likely to shape negotiations in 2022 and beyond.

1.1 Mitigation and Adaptation

“Keeping 1.5 Alive” – near-term emissions reductions are critical for achieving Net Zero: The GCP has reaffirmed the importance of meeting the Paris Agreement Temperature Goals,¹ and specifically recognizes that carbon budgets available to limit global warming to 1.5c are being rapidly depleted, reflecting the latest views from the world’s climate scientists (IPCC AR6 WG1) released in the lead-up to the conference. While the GCP (§22) formally recognizes that achieving 1.5c will require emissions reductions of “45 percent by 2030 relative to the 2010 level,” the timeline for achievement of net zero globally was left open ended, at “around mid-century.”

Big win at Glasgow: bringing forward the timeline for more ambitious country climate commitments, focusing on 2030: Despite the fact that aggregate Nationally Determined Contributions (NDCs) made by countries ahead into the conference were oriented towards 2.7c of warming, one key achievement of Glasgow has been the acceleration of timelines for near-term emissions reductions milestones leading to Net Zero. The GCP (§29) formally **“requests Parties to revisit and strengthen the 2030 targets” in NDCs by end 2022.** Before, countries were not expected to submit revised NDCs until 2025.

Explicit recognition of need to reduce fossil fuels: In the context of the transition to ‘low-emissions energy systems,’ the GCP (§36) calls upon parties to accelerate “efforts towards the **phase-down of unabated coal power**² and **inefficient fossil fuel subsidies**, recognizing the need for support towards a just transition.” This marks the first time that fossil fuels have been mentioned in a COP decision – however, last-minute push-back from India and China to water down language from ‘phase-out’ to ‘phase-down’ has limited the impact of this statement to the aspirational level.

Broadening the solution set—reducing other greenhouse gases (GHGs), supporting conservation: The specific mention of the need to reduce **methane** (§37), reflecting the progress made on the [Global Methane Pledge](#), marks an important development from a close focus on energy sector CO2 emissions to consider sources from other sectors, such as agriculture. Similarly, specific recognition of the “importance of protecting, conserving and restoring nature,” including both terrestrial and marine ecosystems (§38), reflects a resurgent global agenda on biodiversity conversation, and new COP-linked coalitions such as the [Glasgow Leaders' Declaration on Forests and Land Use](#).

Comparatively less focus on adaptation: The formal agenda on adaptation within the UNFCCC requires countries to submit adaptation communications alongside NDCs, and is strongly linked

¹ Limiting global warming “to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels.”

² “Unabated” coal power refers to coal-fired electricity generation that does not employ carbon capture and storage (CCS) technology.

to commitments on finance, including for management of climate impacts that are now unavoidable (see notes on **Loss and Damage**).

IIF View: The 'Race to Zero' continues one leg at a time, with new rules and renewed energy

In the wake of COP26, it is heartening to see Net Zero affirmed as a unifying goal by all negotiating parties. While a clear timeline for achieving Net Zero was not reached at the global level,³ the framing of a 'Race to Zero' has helped inject sorely-needed energy into climate multilateralism, which had been waning. Thanks to a more constructive foreign policy approach from major countries including the U.S., new coalitions on thematic climate action areas (such as methane) and bilateral deals have emerged. However, agreement to leverage the most critical climate mitigation tools—stopping the burning of fossil fuels in energy and transport systems—remains intractable for key developing countries like India and China. As the costs of adaptation to climate change continue mount, the increasingly destructive physical impact of climate change may steer political will towards supporting decarbonization as a resilience strategy.

As past COPs illustrate, high-level agreements cannot drive emissions reductions without effective implementation. With near-term progress critically important, **a defining issue going into COP27 will be the strength of 2030 targets and mechanisms for emissions reductions** (reflecting the current debate on interim target-setting protocols within the financial sector Net Zero agenda). A key outstanding question is how often targets will need to be revised and updated over the course of the decade—and how monitoring of GHG emissions at country level⁴ will feed back into the process. Looking forward, it appears that the UNFCCC will be having a 'major COP' every year through 2025, shifting away from the five-year cadence that made Glasgow such a milestone.

1.2 Finance

"Deep regret" over the \$100 Billion – yet scant progress on a post-2025 plan: Developed countries have failed to deliver on the 2009 pledge to deliver \$100 billion in climate financing for developing countries by 2020,⁵ and several sections of the GCP (§44-46) pertain to the full delivery of these resources in coming years (leading to a cumulative amount of \$500 billion by 2025). A new framework for climate finance from 2025 onwards, which was on the agenda for COP26, may be addressed next year.

Adaptation finance doubled—but a 50:50 split vis-à-vis mitigation looks unlikely: The GCP (§18) urges developed countries to "at least double their collective provision of climate finance for adaptation to developing country Parties from 2019 levels by 2025." Adaptation finance accounts for [roughly 25% of climate finance](#), yet developing countries have pushed for a collective commitment to achieve a 50:50 balance, considering that adaptation projects are more difficult to fund, and that climate investment needs for some developing countries—including in Africa—are much higher for adaptation than mitigation. Moreover, as adaptation finance levels are quite low for some countries, compared to funds allocated for mitigation, a 'doubling' at country level might mean only a small increase—far short of the goal of a 50:50 split. Analysts have suggested

³ Countries' NZ targets range in date, with China and India aiming for 2060 and 2070 respectively

⁴ There are significant divergences in how countries monitor and report GHG emissions within their jurisdiction, leading to concern that [NDC pledges are built on inaccurate data](#).

⁵ Recent figures from the OECD suggest that climate finance flows reached [\\$80 billion in 2019](#), comprising an array of sources of funds of different structures.

that the [U.S. commitment of a six-fold increase in adaptation finance](#) at COP26 would lead to a total share of 25% for adaptation finance.

Loss and Damage – seeking compensation for developing economies: A contentious issue across several recent COPs has been whether and how developed countries should compensate developing countries to account for their historic contributions to ‘loss and damage,’ meaning the unavoidable impacts of climate change that will occur even if emissions reductions goals are met, that are beyond the scope of adaptation. The GCP (§66-70) makes specific reference to ‘further operationalization of the [Santiago Network](#),’ a technical assistance facility established in 2019 to support highly vulnerable countries address loss and damage issues. However, calls for establishment of a new financial program for loss and damage from developing countries received pushback from the U.S. and EU, resulting in a proposal for a new ‘Glasgow Dialogue’ (§73) engaging multiple stakeholder groups.

IIF View: Questions of justice and equity will continue to drive the debate on climate finance for developing countries

Developed countries’ failure to deliver the promised \$100bn in climate finance has been a key schism within the COP process, and a serious barrier to trust between developing and developed negotiating blocs. Many developing countries, which have much [lower historical emissions contributions to global climate change](#), have indicated that increasing their climate pledges will be contingent on the delivery of financial resources from developed countries.

Given that new climate finance pledges from developed countries at COP26 were limited, and that key elements of the financing framework remain in development, the question of official-sector flows of climate finance will remain central to the success of future COPs. The thorny nature of achieving ‘justice’ in climate finance—including by addressing the issue of historical responsibility for driving climate change—may become thornier still as the distributional impacts of climate change on societies mount. Governments in both developed and developing countries will thus need to contend with the challenge of achieving a ‘just transition’ away from high-carbon industries.

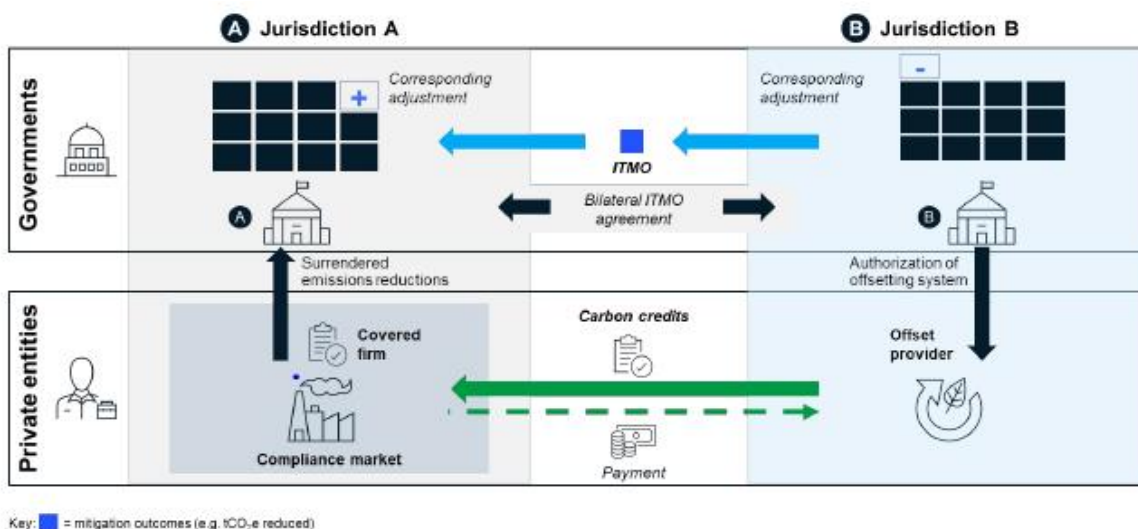
1.3 Implementation

Finalizing the Paris Rulebook –Timeframes, Reporting: COP26 saw the conclusions of several multi-year negotiation processes pertaining to the implementation of the Paris Agreement, including common time frames for NDCs (Article 4), and the use of public registries for GHG emissions reporting (Articles 4 and 7). These are important steps forward that will enable negotiators to use valuable time at future COPs to work through the complexities of reporting on progress, an agenda which is likely to define the future of the global climate agenda this decade.

Success on Article 6 offers a pathway for global carbon markets: One of the most significant breakthroughs in the COP26 negotiations was the agreement of a set of rules for implementing Article 6 of the Paris Agreement, which governs the establishment of a new global carbon market, including the framework for cross-border compliance markets to develop (termed ‘internationally-transferred mitigation outcomes,’ or ITMOs). Some of the most challenging issues in the negotiations related to [paragraphs 2](#) and [paragraphs 4](#) of the Article 6 text, covering bilateral transfers between countries, the new crediting mechanism which will serve as a replacement for the Kyoto Protocol’s Clean Development Mechanism (CDM), and the consideration of credits issued under the old mechanisms. Developments in four areas were key to a successful outcome:

- **Corresponding Adjustments (Article 6.2, Section III):** A central issue under Article 6 is how to ensure that there is no 'double-counting' of credits sold as ITMOs. In Glasgow, negotiators agreed to require "corresponding adjustments" under Article 6.4, breaking a lengthy deadlock that had plagued previous negotiations. Corresponding adjustments require seller countries to adjust their own greenhouse gas inventory to reflect the sale of ITMOs, as such the sold ITMO does not count towards the seller country's climate targets (see Figure 1). Importantly, the final text clarifies the process through which countries would decide and notify the UN system about decisions to count reductions towards their own NDC or sell the reductions as ITMOs. The decision has been welcomed by carbon market authorities such as [IETA](#).

Figure 1: Corresponding Adjustments under Article 6



Source: IIF, Vivid Economics

- **Treatment of 'legacy' CDM credits (Article 6.4, section XI):** Countries agreed to limit the 'carryover' of CDM-era credits into the market overseen by the new Article 6 mechanism, which could potentially have risked a significant oversupply leading to artificial suppression of credit values. Only CDM credits registered after the cut-off date of January 1, 2013 may be used under the new mechanism, under the first cycle of national commitments, amounting to approximately [120 million tonnes](#).
- **Allocation of Financial Proceeds (Article 6.4, section VII):** The question of how proceeds from the sale of ITMOs should be managed drove a significant amount of discussion at COP26, with developing countries arguing that a fee should be levied on ITMO transactions in order to fund adaptation projects in developing countries. Negotiations agreed that this tariff should cover 5% of all emissions reductions created under Article 6.4 of the Paris Agreement, levied on issuers. However, it is important to note that this fee only covers the sale of voluntary emissions credits under article 6, not on ITMOs.
- **Delivery of 'Overall Mitigation' (Article 6.4, section VIII):** In order to ensure that transfers of ITMOs contribute to an overall mitigation of global GHGs, negotiators agreed to implement a clause whereby 2% of the credits generated under Article 6 are in effect cancelled and cannot be sold.

IIF View: Progress on Article 6 will benefit both regulated and voluntary carbon markets.

Success on Article 6 should be considered a key victory of Glasgow. However, the many outstanding questions—such as the treatment of corresponding adjustments post-2030, and whether ITMOs should be limited to credits linked to carbon removals only—will have significant implications for the future of voluntary carbon markets, as compliance markets grow. In our recent report, [Getting to Net Zero: The vital role of carbon markets](#), the IIF explores how key factors – including demand, integrity, market infrastructure, and accounting frameworks – will shape how voluntary and compliance markets will interact over the next decade, with special focus on the impacts of Article 6. Building on this report, we see three key implications arising from a growing global compliance carbon market under Article 6 in coming years:

- **Tighter supply in voluntary markets, as firms seek to deliver the Net alongside Zero:** The expansion of the voluntary carbon market in recent years has been demand driven, as companies aligning to Net Zero have sought to secure high-quality carbon credits. An expanded market for transfers of ITMOs could potentially constrain expansion of pure-play voluntary market projects, as countries seek to secure future pipelines of credits. All else being equal, this could lead to higher prices in voluntary markets.
- **Greater stringency and higher integrity across the board:** While the new system of transfers under Article 6 may involve significant bureaucratic red tape, an increasing focus by supplier countries on projects in their jurisdictions is likely to lead to heightened official-sector scrutiny of projects, and potential expansions of regulatory frameworks to capture these projects. In a positive scenario, this would lead to a crack-down on some of the persistent quality issues that affected credit integrity in the past. However, checks and balances would need to go both ways—including assessment of adherence to key market frameworks for credit quality like the *Core Carbon Principles* (developed by the [Taskforce on Scaling Voluntary Carbon Markets](#)) to ensure that governments themselves are playing by the new rules.
- **Greater momentum towards global carbon pricing:** Ultimately, a global compliance carbon market can help set a common baseline for carbon pricing across jurisdictions, as countries familiarize themselves with emissions trading, and develop national level frameworks aligned with Article 6 rules.

The IIF is continuing its central role in support of robust voluntary carbon markets through the new Integrity Council for Voluntary Carbon Markets (**IC-VCM**), which will curate and oversee the Core Carbon Principles, focusing on the need to scale high-quality carbon credits in support of Net Zero goals.

2. BEYOND THE NEGOTIATING TABLE: ALIGNING FINANCE AND CORPORATE SECTORS WITH NET ZERO

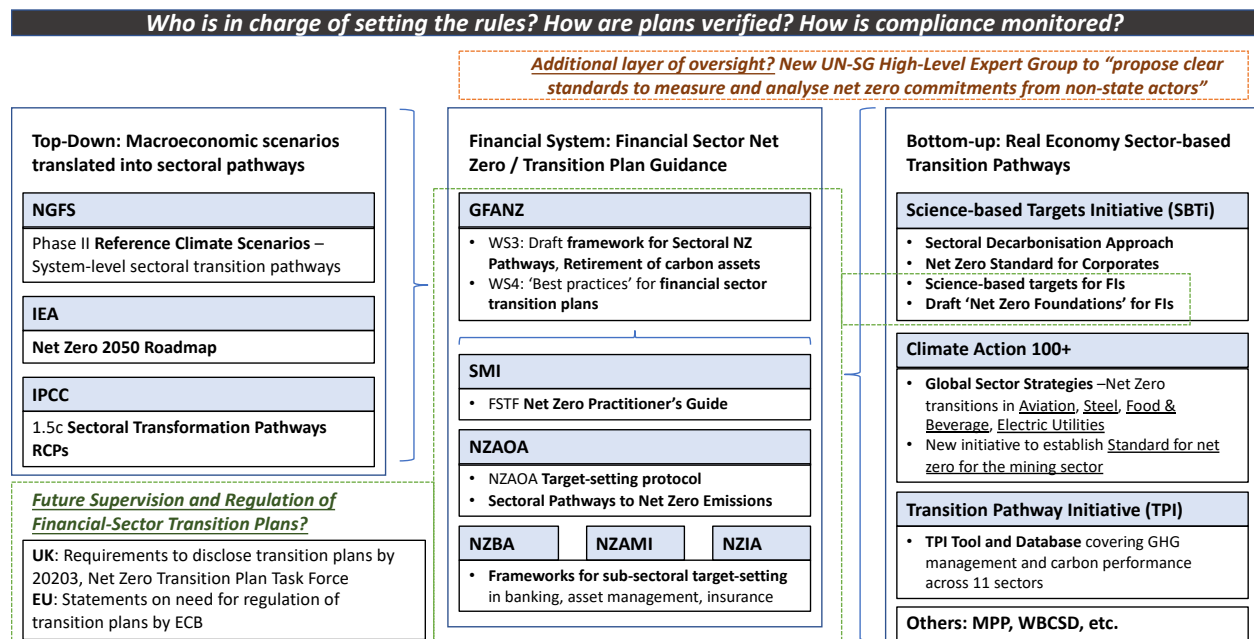
In addition to the decisions encapsulated in the Glasgow Climate Pact, COP26 saw many notable new announcements and initiatives engaging governments, international authorities, regulators, corporates, and financial institutions aimed at limiting global warming – with an unprecedented focus on the role of the financial sector.

2.1 Private Finance

Net Zero alignment – big promises to live up to: Alignment of financial institutions’ portfolios and business models with the goals of a Net Zero economy by 2050 (hereafter “Net Zero Alignment”) has emerged as a core agenda topic for sustainable finance, currently driven primarily by market-led initiatives. One of the key headlines emerging from Finance Day at COP26 was the announcement that the [Glasgow Financial Alliance for Net Zero \(GFANZ\)](#) has now expanded to comprise \$130 trillion of private capital “committed to transforming the economy for Net Zero.” While Mark Carney’s words at the conference hinted at great ambitions, other stakeholders – including NGOs – were quick to point out that [only a small share of these assets](#) have so far been formally aligned with a Net Zero pathway.

Going forward, GFANZ – and its sectoral alliances of asset owners and managers, banks, investment consultants, insurers, and others – will face major hurdles to ensure that promises are kept, with clear reporting on progress. One challenge will be developing industry-supported frameworks and common approaches for the **development and disclosure of transition plans**, which encapsulate a firm’s strategy for alignment, and the metrics that will be used to monitor progress towards achievement of Net Zero goals. Our analysis highlights the wide variety of initiatives seeking to develop guidance on financial sector transition plans, including those beyond the GFANZ umbrella (see Figure 1). Over all of this, questions of governance are now emerging. Also in Glasgow, the UN **Secretary General** announced the establishment of a [new High-Level Expert Group](#) to propose clear standards to measure and analyze Net Zero commitments from non-state actors (including private sector financial firms), which will submit recommendations on standards for commitment frameworks in 2022.

Figure 1: Financial Sector Transition Plans – State of Play



Source: IIF

2.2 Official sector financial initiatives

Steps towards global standards – new ISSB established: The launch of the IFRS-backed [International Sustainability Standards Board \(ISSB\)](#) is an extremely important step towards a harmonized

global framework for ESG disclosures—now widely acknowledged as an urgent priority. One key element of the new ISSB is that it will ‘consolidate’ key voluntary reporting frameworks by June 2022 – including the [Climate Disclosure Standards Board \(CDSB\)](#)—an initiative of CDP) and the [Value Reporting Foundation \(VRF\)](#)—which houses the Integrated Reporting Framework and the SASB Standards). The ISSB will do this in practice by acquiring the entities and their intellectual property. Alongside the announcement, the IFRS released ‘**prototype’ climate and general disclosure requirements** developed by the Technical Readiness Working Group (TRWG), which will form the basis of a forthcoming public consultation expected in Q1 2022. While positive, a range of transitional implementation and coordination issues are likely to emerge in coming years as jurisdictions align their own frameworks with the new ISSB baseline standards. A particular concern will be cases where one jurisdiction’s disclosure requirements go above and beyond the global standard, which could have extraterritorial consequences.

Stronger coalitions, new agendas: At COP26, the Central Banks and Supervisors Network for Greening the Financial System (NGFS) announced that it had reached 100 members, and released a ‘[Glasgow Declaration](#)’ indicating future work across a range of areas, including further development of Reference Scenarios, assessment of climate considerations in the context of **monetary policy**, further work on **data gaps**, TCFD reporting by central banks, and **capacity building** with a focus on emerging and developing economies. In addition, the NGFS indicated that it will take forward further exploratory work on topics such as **biodiversity loss** and risks associated with **climate litigation**.

Hints at greater supervisory and regulatory intervention on Net Zero alignment: Already, some central banks and supervisors have indicated that they intend to incorporate aspects of Net Zero Alignment into supervisory oversight—including commitments made under voluntary frameworks such as GFANZ). For example, at COP26, the UK announced a new policy package for a [Net-Zero Aligned Financial Centre](#), which will **require financial institutions and other major companies to publish science-based transition plans from 2023**. The ECB’s Frank Elderson has also recently called for ‘[legally-binding’ Paris-aligned transition plans](#) to be required for banks, which authorities including prudential supervisors could enforce.

2.3 Action by Corporates

Expanding Net Zero ambitions across sectors: COP26 saw an array of new thematic and sectoral coalitions focused on delivering Net Zero-aligned business practices, including in high-emission sectors such as steel, transport, and agriculture. Table 1 below provides a summary of key initiatives, their constituent entities, and core objectives.

Table 1: New initiatives and coalitions to accelerate climate action

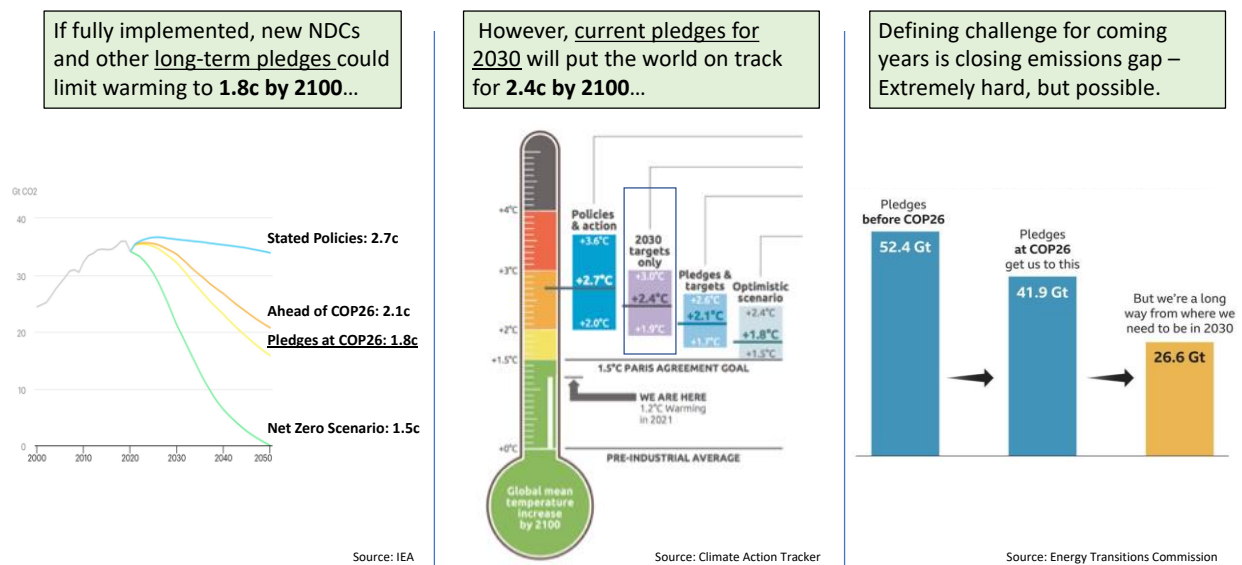
Sector	Participants	Date	Initiative
Financing	UK COP26 Presidency, Germany, Canada	Oct. 25	Published a Climate Finance Delivery Plan to outline when and how developed countries will meet their goal of providing \$100 billion in climate financing.
Energy	U.S., EU, 100+ countries	Nov. 2	Global Methane Pledge signatories committed to reducing methane emissions by 30% by 2030.
Energy	40+ countries	Nov. 2	Breakthrough Agenda signatories committed to accelerate the development and deployment of clean energy technologies in a number of sectors by 2030.
Energy	80+ countries	Nov. 2	Launched One Sun One World Grid with the goal of creating a more connected global grid and investing in renewable energy generation and transmission lines.
Financing	6 countries	Nov. 2	Several countries pledged \$8.5 billion to aid South Africa’s energy transition.

Biodiversity	100+ countries and 30 FIs	Nov. 2	Glasgow Leaders' Declaration On Forests and Land Use signatories agreed to halt deforestation by 2030; FIs agreed to divest from deforestation by 2025.
Biodiversity	12 countries	Nov. 2	As part of the Global Forest Finance Pledge , countries committed to providing \$12 billion for forest-related climate finance by 2025.
Energy	Asian Development Bank	Nov. 3	Launched Energy Transition Mechanism to accelerate retiring coal and moving to clean energy. Will raise \$2.5-3.5 billion to retire coal plans in SE Asia.
Energy	165 countries, cities, regions, businesses	Nov. 3	A number of new countries and companies joined the Powering Past Coal Alliance , pledging to phase out coal domestically and accelerate the clean energy transition.
Financing	IFC and Amundi	Nov. 3	Announced a \$2 billion fund to mobilize private investment into sustainable/green bonds in EMs.
Financing	UK, Fiji	Nov. 3	UK announced £100 million to respond to recommendations from the Taskforce on Access to Climate Finance and aid climate-vulnerable countries.
Financing	Climate Investment Funds	Nov. 3	Launched Capital Market Mechanism initiative to raise funds for clean energy and sustainable infrastructure projects in EMs.
Financing	International Finance Corporation, HKMA, Allianz	Nov. 3	Launched a global platform, MCPPI One Planet , for Paris-Aligned climate investments; will provide \$3 billion in EMs
Finance	IFRS	Nov. 3	The IFRS Foundation announced the formation of the International Sustainability Standards Board (ISSB) which will develop global baseline sustainability reporting standards.
Energy	44 countries, 32 companies and regions	Nov. 4	Countries pledged in the Global Coal to Clean Power Transition Statement to phase out the use of coal and stop building new coal plants.
Energy	12 countries	Nov. 4	Committed to a goal of doubling the efficiency of lighting, cooling, motors, and refrigeration by 2030.
Energy	Non-profits, government organizations, MDBs	Nov. 4	The Global Energy Alliance for People and Planet has committed \$10 billion to increase clean energy in Africa, Asia, and Latin America in the 2020s.
Energy	Governments, international organizations, private sector	Nov. 4	The Global Offshore Wind Alliance will work to scale up offshore wind energy capacity.
Agriculture	160 organizations	Nov. 6	The Global Action Agenda on Transforming Agricultural Innovation was launched with the goal of increasing investment in research to create more low-emission agriculture technology, and more.
Agriculture	WBCSD and 12 partners	Nov. 6	The Regen10 coalition was launched, which aims to scale regenerative food production systems worldwide by 2030.
Agriculture	WBCSD, UNEP FI, PCAF, EDF, Rabobank, Santander, Barclays, Wells Fargo Foundation	Nov. 8	The World Business Council for Sustainable Development announced the Banking for Impact on Climate in Agriculture initiative which will bring together banks to align their food/agriculture/land use portfolios with Paris Agreement/net zero goals.
Energy	22 countries	Nov. 9	Mission Innovation announced a goal to accelerate green technology innovation in four new priority areas – urban transitions, industry emissions, CO2 removal, and renewable fuel/chemicals/materials.
Industry	15 concrete customers	Nov. 9	ConcreteZero intends to set a commitment framework for the use of net-zero concrete and building industry consensus.
Energy	12 governments, multiple organizations	Nov. 10	The Beyond Oil and Gas Alliance launched with the goal of facilitating the phase-out of oil and gas production.
Multiple	U.S., China	Nov. 10	Issued U.S.-China Joint Glasgow Declaration on Enhancing Climate Action in the 2020 pledging to work together to cut emissions in the coming years.
Transport	100+ national and local governments, businesses	Nov. 10	Signed the Glasgow Declaration on Zero-Emission Cars and Vans which aims to end the sale of internal combustion engines by 2035/2040.
Transport	20+ countries	Nov. 10	The International Aviation Climate Ambition Coalition was launched with the goal of reducing carbon emissions from aviation and promoting innovation.
Health	52 countries	Nov. 12	Committed to building health systems which are low-carbon and resilient to climate change.

Adding it all up: Where does COP26 leave us in terms of emissions pathways?

Looking across all of these commitments and initiatives, COP26 suggests a range of potential future climate outcomes, depending on the timeframes being considered and the likelihood of pledges being met (see Figure 2). Looking out longer term to 2100, under a scenario where all new pledges at COP26 are fully delivered, the [IEA](#) estimates that global warming could be limited to 1.8c. While this is a notable decrease from the 2.7c which pre-COP policies would have led to, uncertainty beyond the long-term delivery of pledges – including the strength and speed of emissions reductions *this decade* – cast doubt on whether a 2c warming outcome really can be achieved. For example, estimates by [Climate Action Tracker](#) suggest that current pledges for 2030 will not deliver the emissions reductions needed to drive long-term warming down, and would instead result in warming of 2.4c in the absence of further revisions. Taking a sectoral view, the [Energy Transitions Commission](#) has mapped out key actions needed to drive emissions downward in the 2020s in line with a 1.5c pathway. [A comparison of multiple assessments](#) indicates a shared perspective: that while commitments made in Glasgow will certainly help, the heavy lifting is still to come.

Figure 2: Where does COP26 leave us in terms of emissions pathways?



3. KEY IMPLICATIONS FOR THE FINANCIAL SECTOR

Too much focus on the role of the private sector? Looking across assessments of COP26, two key questions stand out: **have private sector climate commitments been perceived as more ambitious than those of governments, and if so, might this be putting too much emphasis on the role of market actors?** The significant emphasis on private-sector commitments at COP26 calls into question the appropriate balance of private sector leadership and policy action to tackle climate change, with a potential risk of overemphasis on the former. While a wide range of private sector financial firms signalled readiness for action in Glasgow, many also reiterated the need for stronger climate policy measures, such as carbon pricing. Clearly, finance has an important role to play in terms of climate risk management and reporting, capital allocation, advisory and structuring practices, and engagement with corporate and public clients – **but this role will be limited if climate policy frameworks are not in place to shape the transition, especially as**

the risk of [arbitrage between aligned and non-aligned firms and sectors](#) increases⁶. This highlights another important question for the financial sector:

How far can financial firms go to deliver real progress on Net Zero ahead of government policy, beyond simply decarbonizing their balance sheets? The coming years will be defined by complex technical work in both public and private sectors to work out the ‘plumbing’ of delivering Net Zero. Sustainable finance policy and regulation provide the framework for much of this technical work to happen, in terms of disclosure requirements, classification regimes such as taxonomies, and guidance on approaches for forward-looking risk analysis. However, it may be beneficial aspects of the agenda – such as the formulation of a set of industry standards and codes of conduct for the ESG ratings and data products marketplace – are left to the market.

Ultimately, overemphasis on the role of the financial sector to address climate change risks could result in a **‘second-best’ environment developing**, whereby **central banks regulate the financial sector to drive Net Zero transitions in the real economy to meet national GHG targets, in the absence of economy-wide tools (e.g., carbon pricing)**. More broadly, as jurisdictional approaches develop in parallel with global standards (and in some cases with industry-led efforts as well), this raises fundamental questions about the relative roles of regulatory and market-led standards in sustainable finance. These questions are critical, given the economy-wide and broader societal imperatives of addressing sustainability goals. A future IIF paper will explore these questions in detail.

While a focus on longer-term real economy transition and alignment remains critical, financial institutions also need to address the ‘here and now’ of climate change – and prepare for the worst, as physical impacts continue to manifest with greater frequency and severity. A critical aspect of this will be ongoing engagement with climate scientists to ensure that efforts to assess future climate risks are appropriately calibrated with the latest data and predictions for worst-case outcomes within the climate system, which are still not well understood. Annex 1 of this document contains a summary of ten key insights from recent climate science that builds on the work of the IPCC.

We believe it is vital for financial firms to work collaboratively on industry approaches to Net Zero. This will be critical for credibility in engagement with official sector stakeholders as policy and regulatory action on alignment ramps up. Financial institutions should work quickly to develop common approaches for design and implementation of near-term climate action strategies (including transition plans), and collectively strive for greater coherence between overlapping frameworks and initiatives. In support of this, the IIF has established a set of new **Expert Groups on Sustainable Finance**, focusing on **policy, risk and alignment**, and **disclosure, data, and taxonomies**, to serve as a platform for collaboration and dialogue on critical aspects of the Net Zero and climate risk agendas.

⁶ For instance, if a share of financial sector which is not bound to net zero commitments continues to finance, and profit, from investments in high-carbon sectors, such as fossil fuel extraction.

Annex 1

Source: [10 New Insights in Climate Science](#) (Future Earth, The Earth League, WCRP)

<i>Stabilizing at 1.5°C warming is still possible, but immediate and drastic global action is required</i>	<ul style="list-style-type: none">• Estimates indicate that yearly reductions of 2 gigatonnes of CO₂ (equivalent to 5% of 2020 emissions) are needed to keep 1.5°C in sight.• A number of deep and rapid changes are needed, such as greater renewable energy usage and retirement of carbon-intensive infrastructure.
<i>Rapid growth in methane and nitrous oxide emissions put us on track for 2.7°C warming</i>	<ul style="list-style-type: none">• Methane and nitrous oxide are more powerful than CO₂ and emissions must be contained. Methane, for instance, is responsible for about 20% of global warming. The agriculture sector is the major emitter of these GHGs.• However, the use of readily available measures could make a 45% reduction in methane emission possible by 2030.• These options include reducing fossil fuel leaks, improving waste treatment technology, increasing efficiency of nitrogen usage, improved feedstock usage, and reduction of food waste.
<i>Megafires — Climate change forces fire extremes to reach new dimensions with extreme impacts</i>	<ul style="list-style-type: none">• Anthropogenic climate change is worsening fire events; researchers can show the connection and the IPCC predicts increases. Fires release GHGs which further contribute to the conditions for fires to occur.• Fires have significant impacts on human health. It's estimate that they cause over 677,000 deaths per year.• Megafires increased methane emissions by 0.5-7.0 megatonnes in 2019 and 2020.
<i>Climate tipping elements incur high-impact risks</i>	<ul style="list-style-type: none">• The IPCC AR6 warned that human-caused changes can lead to tipping points, which will cause massive environmental changes and cannot be reversed.• One such tipping point risk is melting of ice sheets, which could cause 2 meters of sea level rise by 2100 and 5 meters by 2150. Other tipping points could affect weather patterns, monsoon systems, and permanent damage to the Amazon as a carbon sink.
<i>Global climate action must be just</i>	<ul style="list-style-type: none">• Efforts to combat climate change must also consider global inequality. A just carbon budget redistribution would require the richest 1% to cut their emissions by 30 so that the poorest 50% of the population could increase their per capita emissions by three fold.• Both the impact of climate change and efforts to combat it disproportionately affect lower income communities.
<i>Supporting household behavior changes is a crucial but often overlooked opportunity for climate action</i>	<ul style="list-style-type: none">• Individual lifestyle changes are needed as a complement to public policy.• The food, housing, and mobility sectors need special attention and the public and private sectors should invest in low carbon solutions so households can cut their emissions.• 2.5 tonnes of carbon per capita (half of 2020 levels) can be emitted per household globally by 2030 to be on track.
<i>Political challenges impede effectiveness of carbon pricing</i>	<ul style="list-style-type: none">• Carbon pricing needs to increase quickly to be effective. 22% of global emissions are priced, but only 3.76% are priced according to recommendations in line with the Paris Goals (40-80 USD per tonne).

	<ul style="list-style-type: none"> • Carbon prices have been set low to increase political and consumer acceptability, but they are not high enough to have an impact. Some have suggested implementing a global carbon price. • 61 countries have carbon pricing in place along with over 800 companies.
<p><i>Nature-based Solutions are critical for the pathway to Paris – but look at the fine print</i></p>	<ul style="list-style-type: none"> • Nature-based solutions have an important role to play in climate adaptation and mitigation by improving ecosystem management and can play a role in reducing biodiversity loss and inequality – in conjunction with CO2 removal.
<p><i>Building resilience of marine ecosystems is achievable by climate-adapted conservation and management, and global stewardship</i></p>	<ul style="list-style-type: none"> • Oceans must be protected given the role they play in regulating climate and as carbon sinks and coordinated ecosystem protection is essential. • Policymakers should set clear goal and targets; one such recommendation is expanding the marine Protected Area from 7.7% to 30%.
<p><i>Costs of climate change mitigation can be justified by the multiple immediate benefits to the health of humans and nature</i></p>	<ul style="list-style-type: none"> • Mitigation efforts, though costly, will save lives and communities. Immediate emissions reductions are needed to protect vulnerable populations. • Nearly 7 million people are killed annually by air pollution. • Governments must act swiftly to stop supporting activities that harm human health and implement mitigation and adaptation strategies.