

London, 28 February 2020

Mark Carney  
Governor  
Bank of England  
Threadneedle Street  
London EC2R 8AH

Dear Governor Carney,

**UK banks should be made to publicly disclose their coal loan exposures and significantly increase the applied risk-weighting of these coal loans**

The climate emergency threatens the prosperity and security of all of us. Central banks and financial supervisors must take immediate action to address climate change and particularly the growing financial, human and environmental damage being caused by coal.

We write as trustees of the Children's Investment Fund Foundation (CIFF), one of the largest funders of climate change-related grants in the world with current assets of \$6bn.

We note that in 2021, the Bank of England plans to test the resilience of the largest UK banks and insurers to physical and transition risks under different possible climate scenarios, and the financial system's exposure more broadly to climate-related risk. In addition, the biennial stress test for UK insurers already includes assumptions of a 40% to 65% cut in the value of coal-exposed equity investments due to their contribution to climate transition risks.

Financial institutions are key means of policy transmission, not only monetary. We therefore agree that climate risk assessment is an important part of setting an appropriate regulatory capital framework for UK banks. This is particularly the case for coal power financing, given **coal is the single largest source of greenhouse gas emissions globally and these risks are not adequately reflected in the risk analysis and designated risk-weightings of banks and central banks.**

Carbon Tracker estimates that over 40% of global coal power is already uneconomic<sup>1</sup>. In this context, UK banks' global coal power financing is highly likely to become non-performing and the assets stranded due to low plant utilisation, as zero-marginal cost renewables grow rapidly, as well as tightening regulations on air pollution and carbon emissions globally. Please see attached a presentation on why coal loans are highly likely to become, and should therefore be, accounted for as high-risk loans which are equity risk in nature.

Over the last three years alone, global financial institutions have channelled \$745bn in lending and underwriting to companies developing coal plants<sup>2</sup>, and UK banks remain counterparties for financing of their existing and new projects. BankTrack estimates that the big four UK banks (Barclays, HSBC, RBS and Standard Chartered) have provided over \$26bn of finance to international coal plant developers since 2017<sup>3</sup>. These numbers likely understate the scale of the problem: the stock of coal loans built up by UK banks over time is likely to dwarf the annual flow of new lending. Yet UK banks are failing to disclose their exposure to coal, leaving regulators and investors in the dark.

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<sup>1</sup> See <https://www.carbontracker.org/42-of-global-coal-power-plants-run-at-a-loss-finds-world-first-study/>

<sup>2</sup> See [https://coalexit.org/sites/default/files/download\\_public/COP25\\_PR3.pdf](https://coalexit.org/sites/default/files/download_public/COP25_PR3.pdf)

<sup>3</sup> See [https://www.banktrack.org/download/the\\_uk\\_dirty\\_coal\\_secret/the\\_uk\\_dirty\\_coal\\_secret\\_report.pdf](https://www.banktrack.org/download/the_uk_dirty_coal_secret/the_uk_dirty_coal_secret_report.pdf)

A new report by the New Economics Foundation – Banking on Coal <sup>4</sup> highlights that central banks and financial supervisors have a critical role to play in addressing these coal-related financial risks, in particular by:

- Excluding coal-exposed assets from central bank collateral frameworks and asset purchases;
- Accounting for coal risks in setting microprudential capital requirements;
- Introducing macroprudential capital buffers for coal exposures; and
- Ensuring that the risks of coal asset stranding are properly reflected in stringent stress tests.

We agree with these recommendations. In our view, the risks associated with coal financing are very high, and the broader exposure to the coal financing issuer is also increased. In addition, banks' forward-looking models introduced with IFRS 9 must properly account for the high and increasing probability of coal loan default.

**We therefore call upon the Bank of England to:**

- 1. Review and publicly disclose the appropriate risk-weighting of coal financing to recognise the high risk for UK banks and their stakeholders inherent in funding coal power globally;**
- 2. Require UK banks to publicly disclose their exposures to coal assets and financing, and the risk-weightings associated with these exposures, so that the market is able to properly assess risk and compliance with the communicated ESG policy.**
- 3. Exclude banks which have coal lending from asset purchases and collateral frameworks, because of their elevated risk.**

The Basel Committee approach to standardised risk weights relating to claims on corporates tend to range from 20% (AAA-AA rated loans) to 150% for assets below BB-, and 250% for equity and non-performing loans.

In our view, regulators should require UK banks to:

1. Provision against existing coal-related exposures and recognise a **risk-weighting of 250%** of their net book value, given the high risk of default of the underlying business. Coal loans are highly likely to become non-performing and hence should be treated as high risk and equity in nature in their risk assessment and the capital weightings assigned by banks and central bank regulators.
2. Increase the risk-weighting on the other borrowing and exposures of the parent company promoting coal power projects, to factor in the climate-related risk caused by their business.

The implication of using a 250% risk-weighting is to make new and existing coal loans uneconomic for a bank. These provisions and increased risk-weightings are necessary notwithstanding whether a bank currently designates such financing as performing assets. Central banks cannot allow banks to hide these loans and the totally unrealistic risk-weightings (likely closer to 50%) being used.

Disclosing the amount and percentage of carbon-related assets relative to total assets is also one of the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). Such disclosures should be mandatory.

Rating agencies have a key role to play but they cannot properly rate bank debt without loan book disclosure, and while this disclosure is only made to rating agencies privately, it severely limits the ability of investors to assess the risks themselves.

Central banks and financial supervisors are a critical catalyst in directing capital flows and safeguarding the resilience of the financial system. All stakeholders need to understand bank exposures to assets and financing linked to companies with high climate-related risk, particularly coal risk. **We urge UK bank regulators to require**

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<sup>4</sup> See <https://neweconomics.org/2020/02/banking-on-coal>

**UK banks to publicly disclose such exposures, as a matter of urgency.** It will be important for such action to be coordinated with other central banks, financial supervisors and rating agencies. In the event no action is taken, we would expect a public explanation as to why this is the case, given the increased risk to the banking sector.

Yours faithfully,



Graeme Sweeney  
Chairman CIFF



Chris Hohn  
CIFF Trustee

Copies to: Chancellor of the Exchequer, Rishi Sunak; Andrew Bailey, CEO Financial Conduct Authority; Alok Sharma, Secretary of State & President COP 26; Christine Lagarde, President European Central Bank; Paul Taylor, CEO Fitch Ratings; Doug Peterson, CEO S&P Global; Ray McDaniel, CEO Moody's Corp; Nigel Higgins, Chairman Barclays; José Viñals, Chairman, Standard Chartered; Mark Tucker, Chairman HSBC; Howard Davies, Chairman RBS; Frank Elderson, Chair Network for Greening the Financial System.