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CFOs are pivotal to the low-carbon transition

Research shows that chief financial officers have a critical role to play in companies' low-carbon transition, but they must have the necessary expertise to navigate a growing range of risks, says the Climate Bonds Initiative's Fabrizio Palmucci.

by **Fabrizio Palmucci** | OCTOBER 19

Image: Getty Images

Corporate chief financial officers (CFOs) can play a vital part in driving the low-carbon transition by leveraging their expertise and role in capital allocation and fundraising. This insight has emerged from a comprehensive study involving more than 30 CFOs, representing companies with a combined market capitalisation of $930bn.

The research, published in a report entitled 'The role of the CFO in driving low-carbon transition', was a collaborative effort between the non-profit Climate Bonds Initiative and the CFO coalition of the UN Global Compact, with interviews conducted in the first half of 2023.

The adoption of a low-carbon strategy goes beyond environmental responsibility: it is an imperative for CFOs wishing to fortify their company's business model. Recognising the financial significance of climate-related factors, CFOs must ensure their business models evolve to align with shifting economic conditions that are influenced by consumer preferences, shareholder demands, technological advancements, and regulatory changes.

In this context, active leadership within a company becomes paramount. In fact, the research underscores that in 30% of cases the development of a low-carbon strategy was initiated by the CFO, emphasising their central role in steering their organisations towards a sustainable and climate-resilient future.

It is crucial that CFOs move beyond the traditional financial aspects of their role. One very tangible reason is that non-financial metrics and environmental, social and governance ratings have the power to move the pricing of bonds and equities.

Hence CFOs and their teams need to upskill. In the survey, some respondents said their finance teams have been recruiting new talent to fill the required skills, or that their chief sustainability officer reports directly to the CFO.

Given that CFOs serve as the stewards of capital, their ability to present investors with a compelling and coherent narrative is paramount when seeking capital infusion. As non-financial disclosures gain increasing prominence, it becomes vital to ensure coherence between financial and non-financial information, reinforcing the CFO's pivotal role in shaping an organisation's holistic and credible story.

In-built risk

The low-carbon transition has the potential to disrupt traditional business models, as seen, for example, in the cases of fossil fuel electricity generation or internal combustion engine cars. CFOs must remain alert to the inherent risks posed by this transformation.

A CFO with long-term vision would go further and turn this challenge on its head to make it a source of competitive advantage (commercial, technological or regulatory). For example, more stable revenues, improved margins, more attractive products for consumers, or better access to private finance as well as subsidies. However, creating a transition plan and getting internal acceptance requires planning and the development of a business case. While in some instances the business case is obvious, in others it could hinge on assumptions that go beyond the status quo and thus requires a stronger vision.

Take the prime example of the transformation seen in the utility sector. Fifteen years ago, pivoting to renewables was considered highly risky due to unproven technologies and the potential for cost overruns. Fast-forward to today, and those utilities that did so and diversified early on now have a substantial competitive edge.

Numerous sectors are currently at an inflection point, particularly capital-intensive industries such as cement and steel. In their efforts to decarbonise they are grappling with multifaceted challenges that span costs, technology adoption and regulatory frameworks. How CFOs in these industries craft compelling business cases to drive decarbonisation initiatives is a complex issue that will shape their companies' future. Sustainable finance products are a key component to drive home such efforts.

The Climate Bonds Initiative's interviews have highlighted how instruments such as green bonds and loans or sustainability-linked bonds and loans can act as a catalyst to a company-wide low-carbon strategy. These financial instruments come with strings attached (for example, decarbonisation targets), so the CFO will need to ensure the company is positioned to deliver on both the financial and non-financial targets.

Creating a spark

Respondents also highlighted examples where the implementation of these financial instruments kick-started the development of fully-fledged transition plans. While not all these instruments suit every company, leading CFOs use them to galvanise the internal transformation, to broaden the investor base, to facilitate deeper dialogue with investors, and to enhance reputation and visibility.

CFOs need to upskill and develop climate know-how (and knowledge about other non-financial aspects) with the potential to not only accelerate the decarbonisation of their organisation, but also support it in developing a strategic advantage and driving bottom-line improvements.

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Navigating the terrain of climate transition and physical risks is a task riddled with uncertainties. CFOs must perform a delicate balancing act: evaluating the uncertainty and the affordability of the transition alongside competing shorter-term priorities. This challenge is particularly pronounced for smaller companies that are constrained by limited budgets.

It is, however, a challenge that presents both a new frontier and an extraordinary opportunity for CFOs to show leadership and steer their company towards a more sustainable future.

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This article first appeared in Sustainable Views, an intelligence service about ESG policy and regulation by the Financial Times Group.

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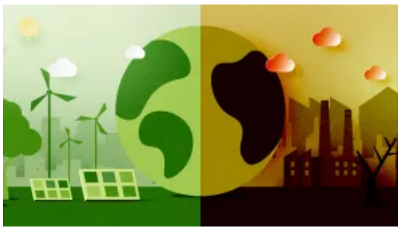

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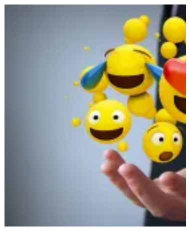

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