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Economy and Fair Work Committee

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Session 6

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ECONOMY AND FAIR WORK COMMITTEE
9th Meeting 2023, Session 6

CONVENER

*Claire Baker (Mid Scotland and Fife) (Lab)

DEPUTY CONVENER

*Colin Beattie (Midlothian North and Musselburgh) (SNP)

COMMITTEE MEMBERS

*Maggie Chapman (North East Scotland) (Green)
*Jamie Halcro Johnston (Highlands and Islands) (Con)
*Fiona Hyslop (Linlithgow) (SNP)
*Gordon MacDonald (Edinburgh Pentlands) (SNP)
*Graham Simpson (Central Scotland) (Con)
*Colin Smyth (South Scotland) (Lab)
*Michelle Thomson (Falkirk East) (SNP)

*attended

THE FOLLOWING ALSO PARTICIPATED:

Heather Buchanan (Bankers for Net Zero)
James Close (NatWest Group)
Ben Howarth (Association of British Insurers)

CLERK TO THE COMMITTEE

Anne Peat

LOCATION

The James Clerk Maxwell Room (CR4)

Scottish Parliament

Economy and Fair Work Committee

Wednesday 22 March 2023

[The Convener opened the meeting at 09:30]

Decision on Taking Business in Private

The Convener (Claire Baker): Good morning and welcome to the ninth meeting in 2023 of the Economy and Fair Work Committee. Under item 1, I ask members to agree to take consideration of the evidence received for our work on the disability employment gap and next steps in private at future meetings.

Members *indicated agreement.*

The Convener: Thank you.

Just Transition (Grangemouth Area)

The Convener: Our next item of business is the fifth evidence session for our inquiry into a just transition for the Grangemouth area. Today's session will focus on how public policy and funding can be used to unlock private capital to finance a just transition. I welcome Heather Buchanan, co-founder of Bankers for Net Zero, James Close, head of climate change at NatWest Group, and Ben Howarth, sustainability officer at the Association of British Insurers. As always, it would be helpful if members and witnesses could keep their questions and answers as concise as possible.

I will start. You are all here to talk about the importance of green finance. I ask you to set out your views on the appetite for that in Scotland, in terms of both supply from investors and demand from individuals and businesses.

I come to Heather Buchanan first. Bankers for Net Zero, I think, published a report on mainstreaming net zero that said that there was a lack of a comprehensive strategy to support small and medium-sized enterprises to make the transition in significant numbers. It was a United Kingdom report, but did you find that the picture in Scotland is similar? Could you say a little about whether there is an appetite for green finance in Scotland?

Heather Buchanan (Bankers for Net Zero): We still have not really cracked how to support small and medium-sized enterprises. We do not have a standardised method of measuring what that looks like, or an agreed methodology for it. If we cannot measure it to start with, that is a problem. With a lot of the stuff that we are doing, it seems as if we are moving things around the edges but not getting to the heart of what a good transition looks like for an SME and what a good transition plan is. A lot of work is going on in that area, but it is still a very crowded space and there is a general lack of understanding of where to go and what needs to be done. I think that, for the most part, most people get it, but most SMEs are clearly worried about the day-to-day bills and meeting the payroll rather than making some of the major investments that the transition may require.

There is a lot of competing information out there, so, to a certain extent, the transition almost goes into the "too difficult to do" box.

The Convener: In advance of the 26th United Nations climate change conference of the parties in Glasgow, we took evidence from a panel of SMEs, and that is what we heard. It does not seem as if much has changed. There have been additional pressures, such as the cost of living crisis and problems with supply chains following the war in Ukraine. The SMEs said that it was difficult to know where to go for information and support.

Heather Buchanan: Absolutely, and which sources are considered credible is another key question. As you say, there is a desire to do this work, particularly now as energy costs and so on are going up, which is critical for people. However, as with consumers, there is a question about the level of investment that is required, particularly in your own infrastructure, as well as a certain amount of people waiting to see whether the technology is the right technology. People do not think that they have strong market signals to really lean into things, unlike what happened with electric vehicles. There was a very clear policy—internal combustion engines are to be phased out—so everybody can now lean into EVs. We do not really have that clarity for businesses. Certainly, with rising energy costs, now is the perfect time and the perfect opportunity to lean into things, but we are finding that the incentives are not there.

The Convener: The inquiry is into a just transition for the Grangemouth area, which is a recognition that the major petrochemical site in Grangemouth has a big impact on our climate targets and our emissions. Is Bankers for Net Zero involved in that area? Is it more focused on SMEs, or is it looking at the bigger challenges that we have with industry?

Heather Buchanan: We are involved across the board. One of the big things is making sure that, as we transition to net zero, particularly in areas such as Grangemouth, the policy drivers are such that we create a glide path rather than cliff edges. There are many competing interests that the key thing that we need is a collaboration point. Over the past few years, it has been very interesting to see that willingness to collaborate—whether that involves the banks or other parts of industry for example—so that there can be open discussions about the challenges that we face. That collaboration has been an absolute game changer in terms of helping to develop policy, but we still have a long way to go.

The Convener: I have a similar question for James Close on the appetite for green finance in Scotland. Do you see demand for your services from businesses? Do you have any insights into businesses in Scotland and in the Grangemouth area in particular that are looking to ensure that we have a just transition?

James Close (NatWest Group): Thank you for inviting us today. We are happy to be here to discuss the very important issue of a just transition.

We have done a lot of work with our SME customers in particular. Many of them want to be involved in the transition, but, as Heather said, they do not necessarily have the know-how and the tools to enable them to get involved, although I think that they recognise the opportunity.

We published our first "A Springboard to Sustainable Recovery" report ahead of COP26, and the second ahead of COP27. The second suggested that there is a pretty big revenue opportunity in sustainable transition in the UK for SMEs that is worth £175 billion in the United Kingdom and £22 billion in Scotland. We have an opportunity to unlock that through policy signals that will get the large-scale enterprises focusing on the transition, and then pushing that through the supply chain to SMEs.

Grangemouth is not an area within my specific remit; I cover the UK as a whole. However, there is an opportunity for Scotland to build on the comparative advantage that it has shown in offshore wind and renewables, particularly now, when we see aspirations starting to emerge around carbon capture, utilisation and storage. Many of the assets and capabilities in Grangemouth lend themselves to being part of that transition.

Alongside that, however, there has to be the finance that enables that to happen. As a UK bank that predominantly provides senior debt, we need to see the capital structure into which we are lending. That is where we need good, strong policy signals, so that the equity investors know what they are letting themselves in for.

Also, we are looking at derisking some of the novel technologies through Government intervention or through the support of the UK Infrastructure Bank or its Scottish equivalent, so that there are some first-loss or credit guarantees that sit around the provision of senior debt. Of course, the more senior debt you can get into these businesses—because it is cheaper than other forms of capital—the cheaper the cost of the capital, which means that the business case for doing just transition-related activities becomes much stronger.

The Convener: Is it fair to say that we are not yet at the stage where the scenario that you have just described is happening. Are we on the precipice of that happening? What are the barriers? What is stopping this from getting under way?

James Close: Those of us who work in this space live with the tension between frustration and optimism around what could happen. However, I feel that there are some important unlocking activities going on. The Inflation Reduction Act in the US is a massive provider of capital to stimulate new sustainable technologies, and green new deal investment plan—the equivalent in the European Union—will do similar things for the EU.

In the UK, we need to figure out how to match those measures. We are probably not going to have the financial firepower to do so on the same scale, but we can use our ingenuity and the first-mover advantage that we have, given that we have been committing to these targets for a very long time. Scotland has a very advanced set of commitments and expectations around what can happen relating to the transition.

What gets me most excited at the moment is the mission zero work that Chris Skidmore has been doing, in which he has set out a whole economy transformation, the opportunities that sit around that and how players can come together to take advantage of those opportunities. That work was done specifically through the lens of opportunity, which I think is very helpful.

The Convener: I invite Ben Howarth to respond to the question. I will then bring in Michelle Thomson, who has an interest in some of the issues that have been raised, followed by Colin Beattie.

Ben, my initial question was around the appetite for green finance in Scotland. How do you see the picture developing in Scotland?

Ben Howarth (Association of British Insurers): Thank you for the invitation to speak to the committee today and for allowing me to give evidence remotely. It is much appreciated.

Overall, the appetite of ABI members to be part of green finance, particularly in Scotland, is very strong. ABI members have made a number of net zero commitments, as my fellow witnesses have done. Particularly on the pension side of our membership, the market share that has actively made a public commitment to the race to zero campaign is very high at around 80 per cent of the market. Members that have made those commitments are now looking at investment opportunities to live up to them.

I think that that is where the challenge is, and I echo much of what previous witnesses have said. When our members have spoken, I think that, to be frank, they have said that a lot of those commitments were made in the build-up to COP26 and that, by this point, they expected to see more opportunities to make direct investments. We want to see the pipeline of investment opportunities grow. To answer your question, there is definitely an appetite for and a very strong interest in green finance. As I said, those members have made public commitments, so they want to live up to it.

To look at it from the other side, what is the demand from customers? It is fair to say that the picture is nuanced. For example, one of our members, Scottish Widows, did some research on green pensions last year that shows that there is a growing appetite among end customers—pension savers or some employers who are choosing pension schemes—to be offered a broader range of green pensions and other green finance options. It seems to be a particular priority for people who are changing jobs. They look for their employer to offer a pension that is demonstrably sustainable.

That appetite is growing. I would not characterise the majority of customers as having it, but the cohort is growing, so there is an increasingly strong business case to provide those options. Obviously, what our members need are the investment opportunities so that those funds and pension products are resilient and strong and give a good financial return.

At the other end, it is also fair to say that there will be some customers whose number 1 priority is always going to be financial returns rather than any moral or ethical considerations. Even then, they want to see strong and resilient returns and, to be frank, if you look at the long-term picture for the UK economy, you will see that it is clear that net zero is a tremendous growth opportunity. James Close mentioned the Chris Skidmore review, which is the latest in a long line of research that demonstrates that the best and most sustainable growth in the UK is found in net zero. I think that there will be a strong demand from customers for these products.

I can come on to what we can do about some of the issues but, to answer the core question, demand is strong and there is definitely an appetite. There is more to do, which is about having a pipeline of investment opportunities. That is what we need to see. There are things that our members can do to help with that as well, which I am happy to come on to. However, that is probably enough for the first question.

The Convener: Following COP26, there were lots of investment opportunities and lots of talk about what we would do next, but those things have not been realised as much as you would like. What has been worst: what is happening in Ukraine, other external factors, a lack of commitment or a lack of leadership? What would you say are the barriers where we are not seeing things happen at the pace that we would like to see?

09:45

Ben Howarth: Having looked at the situation, I do not think that there is one single factor. Clearly, the Ukraine war has caused a lot of challenges. As far as I can see, it seems that there are some technologies that are close to deployment—hydrogen is an example that gets a lot of attention. However, those technologies have not reached the point of commercial deployment or, for ABI members who are investing pension savings, they are not ready for venture capital early-stage investment. They will be coming in at a later date.

What ABI members want to see are projects where there is a clear business case and strong evidence that there will be a good return. Across a number of areas, there are projects where you can clearly see the direction of travel and enough indications that Governments in Scotland and across the UK are prioritising those technologies, but we are not seeing the actual investable opportunity being put forward. Perhaps the technologies are just not quite mature enough or—to go back to what previous witnesses have said—perhaps there have not been strong enough policy signals.

Equally, there are some areas where the approach is beginning to work. Electric vehicles are an example of where there is a strong policy signal, which then links into other investment opportunities, such as investing in charge points as well as in the vehicles. It is definitely not a completely bleak picture, but there are areas where we are looking for more signals and, to take it back to the committee's specific inquiry, a more concentrated look at Grangemouth and other areas that we know have a very high carbon footprint but also a lot of potential to be part of net zero. Those are the kinds of opportunities that we want to be involved in. We want to be part of those discussions so that we understand exactly what the role of our members' investment capacity can be and can start to unlock those investments.

Finally—this is more at the UK level—the solvency II reforms that the Government has announced are very welcome. We are confident that they will make things easier and we hope that, once they come into effect, there will be a real opportunity for our members to make investments in these technologies.

Michelle Thomson (Falkirk East) (SNP): I declare an interest as an ambassador for the all-party parliamentary group on fair business banking, with which I think Heather Buchanan now has a peripheral involvement.

Heather, you used a term that intrigued me when you talked about devising a glide path rather than a cliff edge. To me, that speaks to the current mismatch between the demand side and the supply side. I am interested in understanding the golden threads and the building blocks that are needed to be able to cut through. I know that Bankers for Net Zero has sent out a paper about something called Perseus, and you mentioned methodologies up front that are presumably meant and devised to be scalable. Equally, I think that NatWest and the ABI will be looking for those things, because they are the enabling structures.

Will you give us a little more flavour of what should ideally be in place to ensure that we have a glide path and not a cliff edge? Following on from that, what roles can the UK Government and particularly the Scottish Government play?

Heather Buchanan: Of the point about a glide path, it is not just about the supply and demand; it is also about the policy signals. I have an example that illustrates that perfectly. Yesterday, I was at a round table at the Bank of England where we talked about the capital requirements for lending to SMEs, which are due to increase in the near future. On the one hand, we have financial institutions being told that they have to hold more capital for loans against SMEs. On the other hand, we have Government saying that SMEs need more finance in order to fund the transition. In such situations, we have two different branches of Government and the financial system working at odds with each other. SMEs—the businesses—are caught in the middle with, in general, more expensive capital.

Imagine that you are a food supplier that supplies four supermarkets and has two bank accounts. You will potentially be asked for six different sets of information, because nobody has agreed on what is required. To a certain extent, it is as if we had the big four going out and competing with one other on how they present a balance sheet. Nobody does that. Everybody knows what a profit and loss statement looks like and what a balance sheet looks like. However, we have not really got to that stage for SMEs.

With project Perseus, we are not looking to replace any of the carbon calculators that are out there; we are very much looking at how we can use the principles that we see in open banking. We have partnered with a not-for-profit called Icebreaker One, which rolled out open banking in the UK. How can we get to a point where we can automate the recording of greenhouse gas emissions and intensities and, at a very basic level, make that scalable?

Another workstream is speaking to international boards such as the international sustainability standards board, the United Nations Environment Programme Finance Initiative, the UN race to zero campaign and the CDP—all the acronyms under the sun—about how we can reach an agreement whereby we all decide what is proportionate reporting for SMEs. That will enable it to become a much more seamless thing. We need to get to that stage. Right now, data at that level, and particularly assurable data, is so disparate that it is very difficult to forecast. It is based on assumptions, averages and values rather than on the granularity that we really need as the bedrock to make investment decisions and move forward.

What can the Government do in policy? Anything that helps to reduce the capital burden on businesses, particularly at the SME end, will be helpful. The finance sector is looking into heating being a service so that, rather than people having to invest in a boiler or heat pumps, they will get them on a lease basis. There are quite a few levers of that type, but we need to get the measurement right. We need to go back to basics before we can build out again, because it is too confusing at present.

Michelle Thomson: James, is the concept of scalable building blocks and underpinning measures something that you are looking at as well?

James Close: Very much so. The work that we have done in our climate transition plan, which we published along with our annual results, shows what needs to happen to reduce the carbon intensity of the emissions that we finance in order for us to hit our 2030 target of halving the climate impact of our financing. What we look at there is the gap between what will happen through existing policies and what is required to change to drive new policies.

As we project back from 2030 and what the economy will look like then, as we hit our targets as a nation, we can start to work out where the gaps in the financing are going to be. For example, at the moment, battery technology is perceived to be part of advanced manufacturing, but it is going to be pretty much everywhere—in mobility systems, housing and heat systems in buildings—and I think that a different way of thinking is going to be required in order for us to scale up.

We recognise that it is also going to be important to experiment, but all the experimentation should be done with a view to scaling up. Part of that is on the energy efficiency side, which is a major area of opportunity. Our chief executive, Dame Alison Rose, has been appointed as co-chair of the UK energy efficiency task force with Lord Callanan, the housing minister. I think that that is an opportunity to translate policy into practical implementation across the members of that task force.

Michelle Thomson: Ben, given your representatives' wish for long-term patient capital, will you add your view on the concept of scalable commoditisation, if you like, of the market? Having heard what the two other panellists have said, how confident are you that we can really pull the golden threads together in the time in which we need to act, given the scale of the challenge?

Ben Howarth: I agree with a lot of what the other panellists have said. I will give an example. Electric vehicle charging points are a good example of a technology that is already being deployed but which needs to scale up rapidly. Our members will be looking for a bit more consistency. Many projects are being delivered by individual local councils. There are some examples of good practice that we can build on but, to reach the target across the whole of the UK—I apologise that I do not know the figures for Scotland—a tenfold increase will be required. We have about 35,000 points now, but we need to increase that to 300,000 in the next 10 years. That is a lot. It is potentially a very exciting opportunity for our members, because it provides exactly the kind of returns that they want. There are fairly predictable use patterns and fairly predictable returns. However, a lot of work needs to go into putting the things in the ground.

The investment models that we have are probably not too bad, but we need to scale them up rapidly and perhaps get to a point where, rather than individual councils managing contracts and investments, we partner the schemes up and bundle them together to get a bigger scale of investment.

The other panellists gave some interesting examples to do with SMEs. ABI members tend to operate at the institutional investor level, so they will not be investing in individual SMEs, but they can invest in the underpinning, connecting infrastructure that will help SMEs to change. I would put my example to do with charging points and the example of energy efficiency in the same bracket, because they are essentially about trying to do the same thing in lots of different areas. The more that we can build that and have consistency, the greater the likelihood is that we will get that scale capital. That is where our members can really kick in and, I hope, provide that support.

How confident am I that it is going to happen? I do not think that anyone is under any illusion that it is not a massive challenge. However, there are signs. I return to the point about consumer demand, because there are real opportunities for different parts of the financial services sector and other industries to work together. Given the insurance side of our membership, we have a really important role to play in supporting some of that. Innovative insurance products are coming out that can perhaps help to derisk this work. They are not the solution to the problem on their own, but they can definitely play a part.

We are seeing consumer demand. Electric vehicles is a good example of an area where strong signals are being given. In my first role at the ABI, I worked full time on motor insurance, and at that point—it was only just over five years ago—

I never spoke about electric vehicles. The subject did not come up. It is now probably the hottest topic for the person who has taken over that role. That is an example of something that has changed radically.

We are really supportive of the fact that there is a task force on energy efficiency, which NatWest is involved in, and we are really keen to participate in it.

As long as we keep building the momentum and do not let it slip, we will have a real opportunity. Going back to the subject of the committee's inquiry, I note that making it work in concentrated areas where there is clearly a particular demand and a particular drive, then taking the best practice and scaling it out everywhere else is the way to go. It is very encouraging that we are looking in detail at Grangemouth. I would not undersell any of the complexities, but I am certainly optimistic that we can make this happen.

Michelle Thomson: I will ask just one more question, because a lot of information has been brought out and I know that my colleagues will want to pick up on it.

The focus of our inquiry is a just transmission for Grangemouth, and we have talked about some of the significant structural issues. To add to that, I ask each of you to give a view on how we can overcome another structural issue around financing, which concerns the role of women-led businesses, and incorporate up front the measures that Heather Buchanan outlined. The just transition is a massive area. To what extent are your representative organisations aware of the importance of women and women-led businesses being at the heart of it?

Heather Buchanan: I think that James Close will have more to say about that, given the work that Dame Alison Rose has done. The subject is a discussion point but, to be honest, it is probably not as prominent as it could be. We tend to look more at the data and the details around things. I would say that it is not a regular conversation point, which is—

Michelle Thomson: So it is good that I asked the question.

Heather Buchanan: Absolutely.

James Close: This is something that we are very committed to. The Rose review stimulated a lot of interest in the subject, and there is also the Stewart review to promote female entrepreneurship in Scotland.

This week, we did a female entrepreneurship bond on international women's day, which involved us going into the capital markets to raise money for us to then lend to female entrepreneurs. The really interesting thing about that, as well as the demand to be part of such bond structures, is that we see the impact that comes from our lending in the activities to which it is deployed. Scaling up the finance for female entrepreneurship is a very important part of stimulating it and making it grow and work in an appropriate way.

10:00

Ben Howarth: I agree 100 per cent that the subject is incredibly important. I do not think that it is talked about enough in the context of climate change and the net zero transition.

In our industry, we are well aware that the insurance and long-term savings sector is not as diverse as it should be. We published a blueprint last year and we set ourselves the ambition to become the most diverse and inclusive sector in the UK, which refers to the way that we operate as well as the people who work in the sector.

If we consider the composition of company boards, there is strong and compelling evidence that diverse boards have better outcomes in relation to sustainability and are more likely to be aligned to net zero.

There are some practical steps that we can look at. I note that your inquiry has focused a lot on skills. I suggest that, as we start to develop the new skills that are required, we make the area as diverse and inclusive as possible, using many different routes. We could look in more detail, although not necessarily in this session, at secondments, work placements and partnerships between businesses in order to build wider skills. Some of the professions will be chartered or will require particular qualifications or skills, but a lot of it is about extending experiences and coming at things from fresh perspectives.

If businesses that are collaborating on the just transition also collaborate in that practical sense, using opportunities such as secondments, work experience and flexible working and building those things in as much as they can, it will both encourage a more diverse workforce and get more people in with the skills and experiences that the businesses need. That is not a direct answer to the question about women, but I hope that it will help if we have an approach whereby we really think about increasing diversity and inclusion, bringing more people in, increasing skills, having more social mobility and having businesses work together to address the challenge.

Colin Beattie (Midlothian North and Musselburgh) (SNP): My question, like everybody else's, is about money. Money is the key to everything in this. In previous sessions, this committee has heard that there are substantial amounts and increasing volumes of private capital available to invest in the transition. In last week's evidence, however, we heard that the overall cost of financing the transition was a major barrier, which seems a little bit out of step. What are the barriers to matching the supposed supply of private capital with the demand in the market?

On a slightly separate matter, what can policy makers do to support that? I ask Heather Buchanan to comment first.

Heather Buchanan: If you look even on a consumer level at the demand side, green finance is a bit boutique still and we need to make it more Ikea for people to get more involved. On retrofits, for example, something that has been suggested, which the Scottish Government could do, is that businesses and individuals could be required to have building passports. Energy performance certificates are a bit of a blunt tool and are now quite outdated. If we could have more accurate asset-level data along with building passports through which people could, slowly but surely, see progress towards decarbonising their own building stock, you could start linking that to incentives, which could be a reduction in business rates or council tax. Such things, which you can slowly work towards, would unlock a lot.

It is such a crowded space and there is a general understanding that we need to do something, but everybody knows what a Malm wardrobe, chest of drawers or dresser looks like, whereas we really do not have that kind of understanding in this area. Thinking about how we can make that much more standardised and understandable is the first step towards unlocking that.

Colin Beattie: What about policy makers? Is there anything that they could or should be doing to facilitate this?

Heather Buchanan: Reforming EPC standards would be a start. Building passports is another thing. If you rolled them out across the country—that is something that sits within the devolved Administration's powers—and incentivised them with the taxation structure and very clear targets, that is probably what would cut through most. Other things, that are probably more reserved matters such as VAT reduction, will need to be looked at, but within the competency of devolved nations, that kind of direct engagement with the housing stock is critically important and could unlock things.

James Close: It is a very interesting question. One of the reasons why I work for a bank is because of the power of finance and money. Money is pretty rational. It goes to where it gets the best risk-adjusted returns.

The problem is that the perception of risk in some of these areas is greater than the reality. We encourage our credit officers to think not just about what they have financed in the past, where the asset security has come from and the historical financial performance, but whether those investments are going to be viable for the future. That starts to reframe the risk-and-reward equation in a way that becomes more amenable to enabling the finance to flow.

However, there are a few barriers to that. The first is information and data, which Heather Buchanan talked about. You need to be able to put the information around current and future carbon intensity into the hands of the people who are making the decisions. For us, that links to our target of halving the climate impact of our financing. We are no longer just thinking about purely allocating capital. In effect, we are thinking about allocating capital within a carbon budget. That should incentivise us to do more of the kind of sustainable finance that is required.

Another important thing is looking for means to price the externalities. How can you put in place a shadow carbon price or a carbon price that is broader than the one that is already in the economy to enable us to price our capital more effectively? That is one of the things we are doing as part of the implementation of our climate transition plan.

A third thing is policy: policy is a major driver of risk perception. We have a good strong level of ambition around net zero commitments in the UK, and in Scotland in particular, and now we need to get underneath the skin of that and into the specific policy drivers that will enable the transition to take place. That will set the context for the choices and trade-offs that people allocating capital will make. If they see clearer policy signals and less risk, they will be more inclined to allocate capital to transition-related activities.

Colin Beattie: Is it correct to take as read what has been said in previous sessions—that there is a substantial sum of money available and that it is increasing all the time? You have covered some of the issues around that, but there must be a way of tapping into the willingness to invest.

James Close: I think that that is true. There are lots of things that organisations can do to make that money more visible. For example, we have our target of £100 billion of climate-sustainable financing funding by 2025. Last year, we allocated £24 billion to those kinds of activities, which I think builds confidence that that money can flow effectively. Providers of capital want to put their capital to work. They do not want to just sit with the capital on the sidelines—they want to make it work.

Another important point is about getting the alignment right between asset owners—people such as Ben Howarth's members, who can take long-term financial positions—and the fund managers who are allocating funds on behalf of investors, and the banks who are the conduit of finance to the real economy. When we make our commitments, we think that asset owners and fund managers will see the benefits of our building a resilient balance sheet that is focused on the transition, which again gives us more incentive to lend for transition-related activities.

Colin Beattie: You have touched on a few bits around this, but is the volume of private capital the type of capital that is willing to invest in the long term? Is it maybe even patient capital? Some of the up-and-coming industries that will support us in the future are still developing and are still years away from reaching a point where they are going to be making the contribution we hope for. Is it the wrong kind of capital that is sitting there waiting?

James Close: Early-stage businesses generally require venture capital, which has higher return expectations because there are generally higher defaults associated with it. However, when you get to the point where you have greater confidence that those technologies will be viable, the perceived risk comes down and the price of capital reduces, which makes it better for that long-term, patient capital that is looking not for volatile returns but for standardised returns.

Another thing to consider is recognition of the difference between equity financing and debt financing. As a bank, we are primarily providing debt financing. We invest in a capital structure that already has equity and long-term patient capital alongside it, if that is the structure that has been designed. The more robust that capital structure is, the easier it is for us to lend into it, and that has the benefit of bringing the cost of capital down.

Although there is a big issue around the supply of capital, I would say that the issue is also about the price of capital. That goes back to where I started, which is that capital is priced on a pretty rational basis, and that rational basis is based on perceived risk.

That is what we are trying to solve. The sorts of things that we have been talking about here that can help are long-term commitments and ambition, good policy signals, consistency between political parties, so that there is a multi-partisan approach to long-term policy, and the introduction of derisking instruments that will support that capital allocation. Then comes the rapid scaling up from proof-of-concept venture-capital style structures to ones that have associated scale-up and can be invested in at scale.

Colin Beattie: Ben Howarth, can I bring you in here?

Ben Howarth: Is my microphone on?

Colin Beattie: Yes, Ben.

Ben Howarth: Brilliant. The light did not come on.

James Close's points are very powerful. Your question was about what practical things policy makers can do, and James touched on one of them. It is important to have a clear view that investment is not a single thing or a blob, and that there are lots of different types of investors who will come in at different stages. Policy makers need to focus on that early stage of technologies that we see as strategically significant for the whole of the UK and get them to the point where they are ready for scale, which is when the big capital that ABI members represent can come in. Doing that is not easy.

James talked about transition plans, which is an area where policy makers could focus and do a couple of things. One is to make sure that where firms are working on their transition plans, there are similar transition plans from the Government, that there is information that they can build on, and that there is a process for reviewing those transition plans and making sure that everyone is joined up. The practical step is to not see the transition plans that the Government is working on as just a report requirement for businesses but as a rich and important source of information that should be used to set policy making.

If you have identified technology as being strategically significant, the next thing is to get all the potential investors—or at least their representatives who can provide expertise—into the conversation as early as possible. Start thinking about projects as being multi-stage projects. Whereas the key focus now might be getting the venture capital in and getting the proof of concept to the point where it is proven and we can scale it, the investors who might be coming in at the scaling-up phase can lend their expertise and start saying, "This is what we will be looking for." Then you can start thinking about the point at which you know that capital will be needed and put that into your transition plans.

Thinking practically, people might continue to invest in some of those carbon-intensive sectors that have a longer-term pathway to net zero. However, if they can see a clear point where they should shift some of that investment, and they can plan for it and have some productive conversations with the people driving the technology, they can build into their transition plans that, let us say, 2028 is the year when they start to focus on the new technology and scaling it up. That we, they can build transition plans that will work. If we can utilise transition plan requirements to structure some of those conversations, it will be particularly helpful.

10:15

Another thing that I would do is think about other parts of the financial services sector. ABI represents insurers. Some of the early-stage ventures might not be at the point where there are looking for commercial insurance—they are just going to cover their risks—but at the point that they are, it is good to know that insurers tend to price on historic claims data. Some of the new ventures will not have that, but it can help if they have been able to bring insurers into the conversation and perhaps even have had their business management teams come in and look at the project at an early stage. I mentioned secondments earlier, in a different context, but some ABI members are already out sending people on secondments to carbon capture storage plants.

Insurance is one of the ways that you can de-risk such projects. Take offshore wind, for example. A lot of the time, you will find that there is an insurance policy that is paying out if you have a particularly unwindy month and the energy generation is lower than expected. You can start to bring insurance into that conversation at an earlier stage.

I suppose that if there was just one message for policy makers, it would be that they should recognise that the traditional model—of an entrepreneur taking an idea forward, demonstrating that it is viable, and going to the market at that point—has changed. We aim to get that process a bit shorter, but we recognise that it might be appropriate to have structured conversations—which, for reasons such as competition law, public policy makers and Government should perhaps facilitate directly—to bring different people in at an earlier stage, so that planning can take place. I think that that will help.

That will not solve all the problems. Going back to the evidence the Bankers for Net Zero gave, there is a lot of consumer demand and practical challenges for individual households that need to be overcome separately, but bringing the process together can help. That is why I would still encourage policy makers to bring everyone into the room as early as possible, but also recognise where there may be competition sensitivities or other commercial sensitivities. That is why policy makers could structure those conversations.

Equally, I know that you have heard evidence from development banks. They can provide finance that gets projects to that second phase and gives a degree of derisking. With that, people offering scaled investment can come in slightly earlier in the journey, because they know that they are not accepting intolerable levels of risk. That is a very practical thing. It is great to see those kinds of development banks taking an interest.

James Close: We have blueprints for doing that. The amount of capital that has been deployed into offshore wind has been extraordinary, and that has been done in a very cost-effective way. That is partly because that approach has been supported by the structure, which has included contracts for difference and the use of insurance mechanisms to enable some of the technical risks to be managed more effectively. A lot of learning can be taken from the offshore wind sector and applied to nascent areas such as hydrogen and carbon capture and storage.

Jamie Halcro Johnston (Highlands and Islands) (Con): A lot of the questions that I was going to ask have been covered, so I will ask a follow-up question of James Close and Heather Buchanan. You have talked about the technology, the associated risk and the various stages of investment, and Colin Beattie talked about developing technologies and mentioned hydrogen. From your perspectives, are you seeing those technologies developing as quickly as you expected or would want them to? Where are they against expectations?

James Close: In many ways, that is the impossible question. As they say, things happen slowly until they happen quickly, and that is a good analogy for offshore wind. Five years ago, you would not have believed that we would be deploying capital at the pace and scale that is happening at Dogger Bank, for example, for SSE, which we have been involved with.

We know the technologies that are out there, ranging from straightforward ones such as insulation—although a lot of homes still do not have even very basic insulation, let alone the high-quality external wall insulation that we need. We are starting to get to the point of seeing heat pumps coming forward at scale, and the price starting to reduce quite rapidly. It will be interesting to see what happens with the hydrogen economy in the United States and Europe. The UK and Scotland do not need to lead everything. There are ways of being a fast follower. I think that the same is true of battery technology: battery technology exists; the Chinese are producing vast numbers of batteries. How do we replicate that for our UK supply chain in a way that is going to be cost effective?

We can see a pathway, but you just need to read the report of the Intergovernmental Panel on Climate Change that came out earlier this week to know that we are at the last-chance saloon in terms of doing the right things to enable change to happen, and it almost feels that we ought to be declaring a state of national emergency to accelerate some of those things.

I go back to the Skidmore report. Everything is in there. It is a brilliant piece of analysis and makes recommendations ranging from the things that we have talked about today to other important parts of the decarbonisation agenda, such as farming and land use where we can change the way we do things to sequester carbon and reduce pressure on the carbon budget.

Jamie Halcro Johnston: I am from Orkney, where a lot of work is being done on hydrogen. It is extremely interesting and exciting, but from speaking to many people about their confidence about how hydrogen is going to fit into the grand scheme of things, I know that that is the million-dollar question—I will call it that, rather than the impossible question. The finance side is interesting. If you want to know what is going to happen with regard to an event, you ask a bookie; to find out what is going to be successful, you ask the banking sector, because they are looking to what will work. With large-scale innovations such as hydrogen, what confidence can you have that it is going to play a major role? Where do progress on that?

James Close: One of my colleagues says that hydrogen is a bit like Heineken—it refreshes the parts that others cannot reach, and I think that is true. We run the risk of thinking that hydrogen is the panacea but I am not sure that we are going to be putting hydrogen into our gas grids and boiler as a substitute for natural gas, partly because we are not going to be able to manufacture enough green or blue hydrogen to allow that to happen. However, I think that it has an important role to play in decarbonising the big industrial sectors where heat is quite often produced by highly polluting technologies such as coal. Scotland has a leading position in green steel and I think that hydrogen and arc furnace technologies are going to be part of the solution.

Technologists know more about that than I do. We, as banks, try to take all the evidence that comes from the think tanks and research arms and translate it into something that we can use to price the capital. With hydrogen in particular, we will see ways of pricing capital into that sector differentiating quite substantially depending on whether we think that it is going to be viable in the long term or less so, and also taking account of the environmental integrity that is associated with it. There is a bit of sequencing to be done here. We are going to be decarbonising the grid at a rapid rate. Do we want to use all of that to produce green hydrogen or do we want to use it to produce the electricity that is going to run electric vehicles and be used for heat pumps?

Jamie Halcro Johnston: Heather Buchanan, I ask you the same question. I represent a region—the Highlands and Islands. How do we make sure there is a regional approach to this, and regional support?

Heather Buchanan: The regional bit of it is incredibly important. Something that we can do locally is have a much more joined-up approach. To go back to retrofitting, I note that doing large-scale social housing projects is a very good way to kick start the market, upskill an area in general and bring the price curve down for the supply of things. Think back to when we put the gas grid in many years ago. That was not done household by household; it was done as a piece of large-scale national infrastructure. That first move and getting that confidence is important. Do we go street by street or community by community? Our core recommendations around the building stock include going into social housing where you can take preferably post-1950s buildings that are a bit easier to retrofit and do those at scale. That would naturally bring down the costs.

Jamie Halcro Johnston: Ben Howarth, do you have anything to add?

Ben Howarth: I think that my fellow panel members have covered it. On the house-by-house point, I see the point at which someone makes an insurance claim being a potential opportunity. For someone who may not have been considering having major work done on their home or getting a new vehicle but has had an unexpected event, the point at which they make an insurance claim is when they could make that change—banks or others will often be providing the finance and could partner with the insurer, building partnerships between different sectors. There are already some examples of that happening, but I think that we could accelerate it by not just prioritising people based on pre-existing things but recognising the potential opportunity when something unexpected happens. That could be helpful, particularly with retrofitting houses and switching to electric vehicles.

The Convener: I am going to allow Graham Simpson a short supplementary question before I come to Colin Smyth.

Graham Simpson (Central Scotland) (Con): James Close has mentioned the Skidmore report a couple of times. It is detailed and around 300 pages long, I think, with lots of good recommendations. It mentions that we should be taking a place-based approach, which of course is what we are looking at here. Interestingly, it says that Governments often get in the way of progress. Given that Chris Skidmore and his committee have done all this work, do you know what is happening with that report? Is it going anywhere? Will it lead to anything?

James Close: It has been broken down into net-zero missions in specific areas. There have been requests to support them, which we are planning to do, and the Government is also expected to respond to the report and to the High Court judgment on the delivery of the net-zero ambition. The report provides a good platform for continued dialogue and translation into action.

Having been involved in several events that Chris Skidmore has organised, what I like about the way that he is going about this is the diversity of actors who are starting to come together in these conversations. Convening people in local areas to have those discussions is extremely powerful and that is not just through the Skidmore report, although that can provide an excellent frame around all of this. There are also plans in Teesside to organise some significant engagement activities.

The regional approach is important and having a net-zero badge can be a source of regional pride and can that build on comparative advantage. That is the case, for example in the Humber, around offshore wind and carbon capture and storage; in Grangemouth and the opportunities there; and Teesside and the north-west of England, which has the potential for a hydrogen cluster. All of that is also a great way of getting out of the London-centric nature of the UK economy, focusing on regional comparative advantage and stimulating growth in local areas. I think that that is the essence of a just transition.

10:30

Colin Smyth (South Scotland) (Lab): You will be pleased to know that you have already answered just about every question that I had. I am going to turn the discussion around a bit.

The message so far is that we have these ambitious targets for net zero but the UK Climate Change Committee has been pretty scathing of the UK and Scottish Governments for not having a plan in place yet to meet those targets. You have all said that the good news—notwithstanding the risk associated with new technologies—is that there is substantial funding available, although the Governments are not using the policy levers to make sure that that funding comes forward.

We are not the Government; we are a parliamentary committee. What do you think are the barriers preventing the Governments from enabling you to bring forward that finance? Why are the Governments it not putting forward those policy changes and what do we need to do as a committee to change that? Other than getting on with the job, what would you like to see the Governments change? What do they need to change to enable that funding to come forward? Do not worry: you can be as frank and as critical as you wish. It is okay—we will not tell them what you say.

Heather Buchanan: First and foremost, we need to be much more joined up. Everything is quite disjointed and you will have different Government departments going with different strategies, without an overarching co-ordination mechanism. As I said earlier, you get to the point where there are competing messages going out and policies working against each other. That is one element.

I will go back to the measurement issue. I know that I have said this before, but I am aware of consultancies that get multiple requests from various Government departments to do the same things, which means that you could have a position where each of the big four consultancies creates a different framework to report on to four different Government departments. Basic stuff like that can happen; the infrastructure still does not exist.

The collaboration point is important to make with regard to banks. Rather than Government just making a policy that potentially does not work, it is important to collaborate on policies. That can derisk things for politicians, too. Obviously, politicians have a risk framework—it might sometimes be less rational than a financial one, but it exists, nonetheless. How do we get to a point where we can give politicians the confidence to know that, if they make those bigger policy decisions, the capital will flow? We know that, often, things are rolled out in such a disjointed way that everybody gets burned by it and then become even more risk averse.

Colin Smyth: You very diplomatically did not say what the Governments need to do, but you make fairly valid points.

James Close: On prioritising the financing, we have seen some indication that money is going to be there for certain technologies over time. There is a long history of that money not being delivered. I remember being involved in carbon capture and storage many years ago, when £1 billion of Treasury funding was ring fenced but never came forward. There is probably some work to do to highlight that this is the growth opportunity for the UK. If we can get that on to the Treasury's agenda and into its mindset, it will be viewed as an investment in productivity.

Certainly, I cannot see any better investment in productivity than energy efficiency, particularly as energy prices are extremely high and, even when they come down, they are going to be volatile. Energy efficiency must be the answer to UK productivity. When you start to frame it that way, you start to get the money ring fenced and allocated to do quite sensible and powerful things alongside the private sector. It does not have to be just the public sector, but the public sector must play a role in that financing.

It is important to ensure that some of the forces that are slowing down progress that have significant vested interests, very deep pockets and very strong links across Whitehall are more marginalised. There is a disproportionate amount of what we might call high-carbon-intensity businesses lobbying for the status quo, and that gets in the way.

Colin Smyth: The idea of presenting net zero as the path to growth, not the barrier to it is interesting.

Ben Howarth, you have said that the ABI has done research that showed that you can contribute up to £1 trillion towards some of these long term projects. Why is the Government not biting your hand off to get that to happen?

Ben Howarth: To be fair to the Government, I think that it is interested in that and is keen to unlock that investment, and certainly the two reforms that it announced earlier this year are something that we strongly welcome. I definitely am not in the camp of saying that the Government is doing nothing and that it is not trying to unlock this investment and it probably would say to us in turn, “Why is it not coming quicker?”, so I think we need to bring those things together. I would not be fully critical of the Government.

To answer your question about what is not happening, my sense that people are trying to do so much at once that that becomes very challenging. It is important to prioritise what is being done and keep the momentum going so that we do not see the bumps and ups and downs along the road. If someone working in a sustainability team in an ABI member sees those bumps, they will go back to their board and say, “We need to keep this as a priority” but the board might have a sense that the issue might not be as much of a Government focus as it was two years ago, which might mean that it thinks that it need not spend time and effort on that agenda. One of the things that Governments in Scotland and in the UK can keep doing is emphasise the point that this is the strategic priority for the UK.

I agree with James Close that it is important for Governments to continue say unambiguously that this is the direction of travel for the UK economy, this is where the growth opportunities are and that current business models will not be viable in the next 10 or 20 years. Governments must not let this agenda slip and must keep giving businesses an unambiguous direction to continue to focus their investment, time and effort into this.

It is challenging, so there is no getting away from the fact that it is difficult, but also, increasingly, because of the volume of different things that people are trying to do at once, the place-based approach, which involves focusing on particular areas where we can create momentum, is a good way of doing that. If you take it issue by issue—if you just look at electric vehicles and then you just look at hydrogen—some of the issues are easier to deal with because there is already a clear decision-making structure within Government and there is a single department that leads on that issue and can take decisions, pass bills and get things done. However, in relation to other issues, four or five different departments are involved and there are two or three years between the policy intent being set out and any legislation happening, during which time momentum has slowed quite a lot. If we can focus on regional activities and draw various people together, we will have workable case studies that we can scale up and put into practice in other places, which means that we do not have to reinvent the wheel each time. The solution to the volume of effort that is required is a more focused and regional approach that looks at everything and draws all the strands together.

The other thing that Government can do is focus on the end customers and individual households to help build the case that this is something that is worth their time and effort and that there is a good reason to spend a bit of extra money on energy efficiency, as it will pay off in the long term and be of value to society. There is always going to be a bit of reluctance if people are asked to pay more for something, but the more that we can do to build that customer confidence and customer demand the better, and that is something that Government can assist with.

I recognise that the Governments have been doing some good stuff, but there is a need to focus a bit more on the regional approach and on the case for why individual households and individual small businesses need to do invest in energy efficiency and what the long term benefits of doing so are.

I will not underplay the issue: this is very difficult. Although I am sure that most ABI members would ask why things are not happening quicker on the part of Government, we also recognise that we are dealing with one of the most complex, if not the most complex, public policy challenges that anyone has ever worked with. It was never going to be easy, but the main point is to just keep the momentum going.

Maggie Chapman (North East Scotland) (Green): Good morning. I thank the witnesses for their contributions so far. I am interested in exploring what needs to happen and what needs to change for SMEs. James Close mentioned the “A Springboard to Sustainable Recovery” research, the revenue opportunities and the job creation and SME creation that are required. I am particularly interested in the 40,000 SMEs that will be required to deliver the 2030 goals. The year 2030 is approaching fast, and the IPCC report that was published this week gives the stark message that we are not on track to meet the 2045 goals, never mind anything sooner.

Can you unpack what we need to be thinking about in relation to SMEs? What needs to be in place to support their creation? Given the comments that we have heard about a place-based approach, with our focus being on Grangemouth, what is your analysis of the spread of sectors that central Scotland communities, workers and entrepreneurs should focus on?

James Close: On the first part of your question, six things are needed. First, we need access to funding. How do we provide access to funding that reflects the societal benefit of climate action? Our challenge is in prioritising lending to SMEs. Heather Buchanan said that she met people from the Bank of England to look at that. We do not want to constrain our lending to SMEs; we want to encourage more of it. That is a socially useful way to allocate capital.

Secondly, we need to build awareness among the SME community of the opportunities that exist. For example, many of the businesses in Scotland that have been supplying the offshore oil and gas industry can pivot quite quickly to supporting the renewables sector and green businesses.

The third element is knowledge. We are rolling out our carbon planner, which relates to carbon footprinting capability. That is available not just to our customers but to any SME, and it is a useful framework to build knowledge.

A big area relates to skills and capabilities. A lot of work needs to be done in that regard. Some foundational pieces exist, but SMEs need to get trained and competent people to do, for example, insulation installation or heat pump installation.

Market access is important so that SMEs can work out where they can play a part in the supply chain and how they can link up with the big organisations that often create demand for SMEs, rather than directly with consumers.

There is a lot of support out there, but it is quite difficult to navigate towards the right support for the right activity. Support with that navigation can be quite helpful, and that, again, lends itself to place-based approaches. When we looked at schemes in the north-east of England, for example, we found that there were dozens of them, so streamlining could be quite beneficial.

Could you remind me what the second part of your question was?

Maggie Chapman: What opportunities and sectors should central Scotland communities focus on?

James Close: The biggest one relates to energy efficiency, particularly around building an industry capability to retrofit the UK’s homes. I do not want to diminish how challenging that will be in a tight labour market, but our report shows that, in SMEs, there is a difference in pay between standard jobs, which pay about £22,000, and green jobs, which pay about £29,000. There will be a benefit for people’s earnings if we can get them into those supply chains. That might mean that we have to make other parts of the economy more productive. How can we get people to move from less productive areas that can be automated to areas that are much harder to automate, such as energy insulation?

Another opportunity relates to renewables, particularly around solar installation on homes and other buildings as the cost of solar comes down. There is huge potential with onshore wind. That has been a very difficult policy area, which, again, lends itself to SME supply chains and place-based solutions.

A lot of big businesses are looking to decarbonise, and some interesting activities are feeding into that in relation to, for example, the circular economy. I was on a panel with Business in the Community to promote the circular economy and to encourage SMEs to build the business models of the future, which will involve a sharing economy, a reuse economy and a recycling economy.

Those are a few of the big things. The report details some of them quite well—the analysis is quite good—so it is worth having a look and mining that information.

10:45

Maggie Chapman: Heather Buchanan spoke along similar lines about the need for things to be joined up and for a clear landscape without competing policies or messaging. We have heard about the potential for new SMEs and emerging businesses. What do we need to do for existing SMEs to ensure that they are part of the picture? There will obviously be some churn, but how do we support existing SMEs?

Heather Buchanan: First and foremost, we need to simplify things. We are working quite closely with Sage in relation to what SMEs are engaged with all the time. Everybody says that SMEs do not have anything in common, but that is not quite true. They all do their taxes and must file tax returns, and they all have bank accounts. They all have an energy supply, if not necessarily a direct relationship with their energy supplier. Using the two common factors that we know about, we have been looking at how we reach and engage with SMEs.

The retail banking sector has an opportunity in that regard—this relates to James Close's point about the tools that are used—because everybody logs on to their bank account, generally several times a week. What opportunities are there for potential signposting? We know that SMEs are much more likely to go to their accountant or bookkeeper for advice on such matters—they are very much trusted advisers—so how do we ensure that there is consistent messaging from accountants? We work very closely with the Institute of Chartered Accountants in England and Wales and are speaking with the Institute of Chartered Accountants of Scotland in relation to getting out similar messaging.

How do we bake something really simple into the process? Do we just need an extra line in profit and loss statements on the intensity of energy consumption? Does that need to become part of everyday accounting so that, rather than being a burden, it becomes baked into processes? SMEs do not have the time to go out and learn about these things. Anybody who comes into this world will know that it is acronym soup—it is like a foreign language even for people who work in the industry—so there should not be that much expectation on consumers and SMEs to have to learn those things. Right now, a lot of the signposting involves getting sent lists of acronyms and links to various sites. We should make things really simple and provide something that is clear. If that is worked into reporting and if there are links to business rates and taxation, the processes for all these things—getting a building passport for a premises, for example—will, all of a sudden, become very simple. Nice and easy.

Maggie Chapman: Ben Howarth mentioned in an earlier response the potential growth for end customers in things such as green investments and green pensions. What levers should we be looking at? Are they levers that we in Scotland can use, given that a lot of the area is reserved? Are there things that we can do to support businesses to make those kind of choices or to widen the options for their workers?

Ben Howarth: Yes, there definitely are.

Just quickly, on the previous point that Heather Buchanan made, I would add insurers to the list of businesses that SMEs engage with regularly. We publish good practice guidance for our members, where a small business is in their supply chain for claims—for things such as vehicle or home repairs—to try to begin to solve the problem of SMEs being flooded with information. That is important.

I would also add—this is less of a focus for the ABI but it is something that we are looking at—that thinking creatively about apprenticeships is important in dealing with the skills challenge. Perhaps we need to think about incentivising SMEs to think of apprenticeships a bit more broadly and not just as an entry point to employment but as continuous professional development. Those are areas that we could look at where we can make a difference. We could think about some of the stuff on flexible working that is coming in as a way of allowing people to take on training in a more measured way during their career, even if they are on a lower income.

On the pensions point, as I mentioned earlier, we are seeing a steady growth in consumer demand for green pensions. That applies to other financial services products, but it applies particularly to pensions. It is not the majority of customers at the moment, but the demand is definitely growing and it is growing quickly enough for the pensions sector to look at the issue as a growth opportunity and as consumer demand that it must facilitate.

The biggest challenge now is that the evidence base for what is and is not green is not always clear enough. It is challenging to present someone with a green pension that can be credibly backed up and that can be said objectively to be green. The terminology that people use is very varied, so it is challenging to compare products on a like-for-like basis.

The good news is that, across the UK, the Financial Conduct Authority is looking at the issue with its sustainable disclosure requirements and investment labelling regime. That only kicks in originally for investment funds, so not all products that ABI members will put into the pensions market will be part of that in the first phase. However, we have indicated that we would support extending that approach further and we definitely want to work with the FCA to broaden that out to as much of the pensions sector as possible.

That will help, because customers will then have a single way of assessing what they are getting, which will avoid confusion. There could be a transition investment that still invests in high-carbon assets, although they have a pathway to net zero, versus an impact investment in a wind farm that is demonstrably low carbon, or an investment in low-carbon assets that are perhaps not really driving the transition. The FCA is starting to solve that with its investment labelling, so it should be clearer to customers what they are getting.

At the end point—going back to the discussions about what the people developing projects could do—if they start to think of that as their framework and evidence base for what they put out to the market, that will allow investors to say, "Okay, I can see how this will fit into my fund. It is being marketed at particular customers who have a particular preference." I appreciate that there is a lot more complexity in reality if you look at the climate science, but we are trying to communicate with customers. If we start to see that FCA framework with those three labels as a glue that pulls a lot of this together so that we can take investment in a project over here all the way through to an end customer who wants a green pension, and they can understand what they are getting, that will be really important.

The other aspect is employers, who will often be the ones who choose which pensions people get. Therefore, it is about engaging them in the process and making them understand what the offerings are. Over time, I would expect more employers to say, "This is a benefit—we will offer you a pension that is sustainable and that aligns with your values." That is another market driver—it is about the individual saying to employers which pension they would choose.

For someone who is entering the workforce now at 22 or 23, and is starting to save into an auto-enrolment pension for the first time, their pension will not mature until after 2050, so they will be thinking about the world that they have to retire into, which is a strong incentive to put that consideration first. Older customers might be primarily focused on how much they are going to be funded at retirement—we think about those different customer cohorts a bit differently.

I would not want to oversell this and say that we have a perfect solution where every customer who wants one can get a completely green pension at the moment, but we have good building blocks with the FCA regime. We know that customer demand is growing and, if we get some of the other things right that we have discussed in this evidence session, that will allow pension providers to offer a greater range of choice in terms of green and sustainable funds.

To go back to James Close's point that this is a growth opportunity, this is a growing market and a growing forward investment opportunity. I am optimistic that it could work, but we recognise that there is a lot more to do. I hope that the ABI, with our climate road map and some of the other things that we are working on, can help to drive that in the sector.

Maggie Chapman: Thank you.

Gordon MacDonald (Edinburgh Pentlands) (SNP): We have touched a lot on the areas that I want to ask about, but you will be happy to know that I have one question with three parts.

Retrofitting of housing stock is a great opportunity. There are 2.6 million homes in Scotland, and we need to retrofit 113,000 homes per year. In Scotland, 99 per cent of businesses are SMEs. You have talked about capital investment and equity investment but, for many of those companies, it is cash flow that kills them.

My first question is: what more can the finance and banking industry do to support SMEs to take up those opportunities, in particular in relation to the cash flow problem?

Secondly, 75 per cent of homes are either owner-occupied or private lets. In my constituency, we are currently two years into a refurbishment of 181 blocks of flats in the Wester Hailes area, and many of the home owners there are being asked for a £40,000 contribution towards the external cladding, new roofs and insulation. Many of them cannot afford it. What can mortgages or buy-to-let mortgages do to support that funding?

Lastly, how do we encourage local job creation from investments from the finance and banking sector? Those are three easy questions.

James Close: They are very good questions. On the first point, on access to finance, particularly on the supply chain side, lending to SMEs comes down to creditworthiness, obviously, but there are supply chain products that we can offer to customers that support short-term liquidity. I wonder whether there is scope for the British Business Bank and the Scottish equivalent to co-lend to deal with some of the supply chain challenges and cash flow issues that SMEs have. It would help to unlock our financing if those sorts of institutions can take some first-loss financing.

The second point was about the fact that 75 per cent of houses are owner-occupied and whether individuals can borrow. Through the concept of a retrofit portal, we are looking at getting additional borrowing facilities to customers, so that they can borrow on the back of their mortgage. Quite a lot of work has been done in the past on the green new deal and the way that money can be securitised. There are also proposals on stamp duty that would facilitate some of those things. We need to get serious about that and figure out ways to provide additional borrowing facilities in a way that makes it secured debt at a low cost. Again, a bit of regulatory support could probably be provided to get that capital recognised in the appropriate way.

I am not a mortgage expert by any stretch of the imagination, but I wonder whether the problem that we have in the broker market in the mortgage industry means that we are effectively commoditising mortgage lending and not thinking about the long-term requirements of an individual customer. We have to work on building relationships with our customers so that they see us as almost giving a John Lewis guarantee of never being knowingly undersold and providing access to the best possible pricing for finance over a long period.

Your third point was on encouraging local job creation. We must prove that these jobs are good jobs, that they pay well and are fulfilling, that they build individual skills and that there is potential for career paths to come as a result. That will then attract people into that particular industry. It probably needs to be supported by training and apprenticeship schemes that can be rolled out locally.

11:00

It is in part about making the jobs ones that people really want to do. It is not that there is anything wrong with being a barista in a coffee shop, but this job has more purpose to it, in terms of helping people to reduce their energy bills and live in a warm home. Let us frame the argument in terms of improving people's quality of lives, because they can live in affordable and warm homes, which is the most fundamental part of Maslow's hierarchy of needs.

Gordon MacDonald: Heather, your report "Tooling up the Green Homes Industry", sets out three of the economic barriers as being the cost of heat pumps, the high-quality survey costs and payback periods for retrofits.

Heather Buchanan: We can also think a bit more laterally. The United States has the PACE—property assessed clean energy—programme. For a young couple who have just moved into their first home and who know that they are probably going to be there for only three or four years before they move on, the last thing that they want to do is to spend an absolute fortune on something that has a 25-year payback period. Instead of attaching that debt and cost to the first movers, who then move on, we could attach it to the property so that, when the next people move in, there will be costs associated. In the States, that is retrieved via the taxation system. I guess that the equivalent would be something where the work is done but then the occupants pay that back over a much longer period through the council tax system. Something like that, where the up-front cost is not borne by the first movers, is important.

Likewise, there is leasing. Does heat just become a service? We all used to spend loads buying servers and getting all the software packages, and we then had to upgrade them and they would break down and somebody would have to come in and fiddle around with them. Now, we all just basically sign up, subscribe and have our software service. Does heat become more of a service, with that infrastructure cost being borne elsewhere? Maybe people will be paying out the same amount, but they will be paying off the capital by leasing.

We have to think about doing things differently at the cash flow point to move that forward. We will have an issue until that comes about, or until prices come down significantly. With heat pumps, given that our housing stock is not the most modern in the world, we acknowledge that it is not just a matter of swapping one boiler for the next, and that there is a massive infrastructure and disruption issue there.

Everybody is probably sick of hearing about my house, but I have looked at all this stuff in depth, and I still live in a draughty and leaky house that I could not possibly afford to retrofit properly. That is a barrier. Coming from a point of relatively high knowledge about this stuff, I will still go back and put on quite a few jumpers at home, rather than do the work, because it is too disruptive and expensive.

Ben Howarth: The previous panellists have covered a lot of the issue, particularly the point about the cost, but I have two points. One is that you should think not just about retrofitting but about adaptation and resilience to the impacts of climate change, on which there is a lot of work to do. Try to think about where there are opportunities for change and where you need to get the skills base more broadly than just retrofitting in order to include all the things that we can do to make our homes more resilient to extreme weather. To go back to James Close's point, if we can build all that in together, it becomes an increasingly attractive proposition for people who are thinking about their careers.

The other point is that you should focus on on-going maintenance for some of this stuff and the skills that will be required for that, rather than just seeing it as an installation challenge. I would hope that that would make it more attractive as an on-going long-term career option, rather than just a one-off installation job after which we move on. That again might make the option more attractive to people who are considering investing in the skills. Ultimately, it will be beneficial to the insurance sector, as we would ultimately pick up the cost of anything that goes wrong, so we see that as important. The on-going maintenance and adaptation and resilience work are important.

I echo my previous point about apprenticeships. If we can do more to make those more attractive to individual employees, perhaps by supporting them not just with the cost but with entitlement to flexible working so that they can do the training, that will make it a more attractive proposition. The insurance industry's role in the up-front costing that you mentioned, particularly for SMEs, would probably be more limited, although it would not be none.

To link back to a point that I made earlier, one point where someone might, in their hurry, make a decision that they otherwise would not have done is when they have had a major claim that they were not expecting. If they have had a fire, flooding or a significant leak, they might be more willing to get major work done than they would otherwise. To use the example of my home, I am not particularly attracted at this point by the prospect of having builders in for months but, if I had a major incident, I would probably think, “Actually, I can add this other stuff on as well.” We should not lose sight of that opportunity when we are prioritising people.

Fiona Hyslop (Linlithgow) (SNP): This has been fascinating and informative, so I very much appreciate your joining us.

I will start at the macro level. I am interested in what you are saying about decisions that Governments can make that can make things happen. We are expecting the UK Government response to the Skidmore report, there is that point about the delivery plan, and we are hoping in Scotland for a decision on the Acorn project for track 2, because that shifts the dial considerably for Grangemouth, which is the focus of this inquiry.

What are the types of policy decisions that are needed to unlock things? Even in relation to heating buildings, which we have been discussing, the UK Government’s decision on gas boilers is not due until 2026—that is a decision that could be brought forward. I am interested in the types of decisions that would help us to move.

It is about investment in advance of need. I am also deputy convener of the Net Zero, Energy and Transport Committee and we are currently looking at the electricity infrastructure and whether it is an enabler or an inhibitor. The Office of Gas and Electricity Markets does not have a net zero policy focus. If it did, it might help some of that investment, and some of that investment in the grid helps us shift on hydrogen, and hydrogen is a big focus for what we are looking at for Grangemouth. It would help us if you illustrated the types of Government decisions that you are talking about that can help move things. Clearly, some of them are in reserved areas, but some are devolved. We are about to get a circular economy bill, so that might help. It would be helpful if you could illustrate the types of decisions that you mean.

Heather Buchanan: Baking a net zero objective into everyday decision making across all departments and branches, and having a department that ensures that those are all joined up and everybody is working to the same frameworks, is a starter. Again, it is back to basics. What are we measuring here?

One of the things that we are looking at, which is more to do with company law, is whether we need clear direction on what “fiduciary duty” means in the boardroom. We have often seen fiduciary duty used as almost a fig leaf for decisions that we would not consider to be fantastic or the most beneficial, with companies saying that they have to look after their shareholders. We know that within the law the duty is to other stakeholders. Do we need to focus those board-level decisions of businesses on what their duty means and is that a wider duty? There are some interesting very targeted things that you can do to unlock.

The policy signal on EVs is time and again cited as a very good thing. It was a simple and clear policy that sat within one department, which always helps, but it has moved the dial on things. Keeping things very targeted and having the framework to understand the progress is important. Right now, it is falling into the too-difficult box for a lot of people.

James Close: It is worth reflecting on what has gone well and not so well. In 2015, there was an agreement that houses would all be up to a certain standard heading towards net zero, which means that for the past eight years we have been building houses that are not. Resiling on policy in that way sends weak signals. It is important to build confidence and apply consistency.

It is also important to get industry in its broader sense on board. In the banking sector, I chair the UK finance sustainability committee and we have a good dialogue on some of the important issues that we want to present to Government, so that it understands where the banking sector and the finance sector in the UK are coming from.

The other point is that not everybody can do everything, but everybody needs to do something. The policy makers who sit at the top of the tree can work out how to piece that together in a way that is co-ordinated and consistent with existing ambitions in law. We have this in law, so let us execute to deliver the law that already exists.

Ben Howarth: There are a few things that I would cite. I have mentioned transition plans, and they are a UK Government initiative, but it would be a significant signal if parts of the public sector said, “We will use a similar framework and publish our own transition plans at the same point.”

Another signal that Governments could send is a strong desire to review what is happening with those transition plans and use the evidence. Businesses that are investing time and effort in writing them see them not just as a tool for potential investors to use to assess their progress, or for campaigners to look at to see how they are doing, but as something that allows them to flag up a concern or an area of uncertainty and have it addressed. I am hopeful that the transition plans will surface some of those tensions and areas where there is a pinch point and a decision needs to be made. A clear signal about how transition plans are going to be reviewed and used in policy making would help give businesses confidence. Hopefully some of that will flow out of points the previous panellists have made about setting out clearly what the dates are and when you want decisions to be made, so that everyone can bake that into their transition plan and say, "Okay, we know that this decision is coming in 2026. Here is what we need to do to prepare for that decision and our role in it, and here are the implications if you go in a different direction and do not take that decision." The transition plan is important.

The other part that is less to do with long-term Government planning is that there will be a lot of businesses and boardrooms that are looking at their net zero targets and thinking that they set targets and made commitments in good faith in the build-up to COP26. They invested a lot of time and effort internally in verifying them, but they were working on the assumption that they would have alternative things to invest in to meet those targets. If Governments could focus—I know that this goes slightly against the idea of an overarching objective—on bringing some things forward and saying, "Let us have some investable opportunities. Let us pick some areas that are relatively advanced and give them that extra nudge that they need so that they are ready to go to market as quickly as possible," that will keep the momentum going. The business community will then have the confidence to say, "Okay, we have made these net zero targets and now we are able to point at things that we have done and investments that we have made that are going to help us meet these targets." Keep that sense of momentum going.

Obviously, we want an overall strategy, but it would be good to start to look and critique and ask where are the things that are quite close that just need an extra nudge to get them over the line and get them ready to be investable. Giving people those opportunities will help build the momentum and stop people feeling that it is just something that happened up to COP26 when everyone was interested because it was here in the UK, but now momentum has been lost and boardrooms should focus elsewhere. If we can keep telling people that this is a moving agenda, that would help.

We mentioned a few other things that Governments can do, but those are two things that the Scottish Government can do with its stakeholders as much as the UK Government can do.

The third area is some of the investments that pensions funds will be making, which will clearly ultimately need regulatory approval from the Prudential Regulation Authority, which is absolutely correct, because they are managing pension savers' money. It would not be appropriate for the PRA to start making decisions that are not based on genuine assessments of the risk, but we could be very proactive in saying, "These are the investment opportunities that we prioritise. This is where we are likely to go to market in two or three years' time," and looking for pension funds to invest. Working closely with the Bank of England so that it has all the information that it needs to make those decisions quickly will be good, particularly if it is looking at potentially approving a new asset class. The more pre-work you can do in advance so that those decisions happen quickly, the better.

Ultimately, the PRA is going to make the right assessment of whether something is an appropriate risk for pension assets to be invested in, but the more proactive you can be in getting asset classes approved and having those conversations with the PRA, the better. That links broadly—and it is in the Chris Skidmore review—to getting all the regulators around the table in a more regular and perhaps co-ordinated fashion. It feels to me that—I will give the transition plans taskforce as an example of this—the financial services regulators are engaged, but it does not feel to me that some of the utility regulators or other real-economy regulators are quite as engaged. Ultimately, the regulators producing transition plans is just as important as banks and insurers producing them, so I think that we really need to see that, where these big initiatives are being driven, it is the whole of the economy and not just subsectors—not just finance and not just initiatives that are driven at the energy companies but something that everyone is working to. The more we can see that all the different regulators are working together, the better.

11:15

Fiona Hyslop: That is a very good overview of the bigger aspects that need to be dealt with. I am very taken by your agreement that place-based approaches can really work. How we translate that into the just transition plan for Grangemouth is going to be very interesting. It is convening power, and it is interesting that the ABI is a convener because everybody needs house insurance. Everyone needs a mortgage, but does a mortgage stay with a person or the building?

Grangemouth is a fascinating place to be a first mover when it comes to how you do everything, as in heat and transport. It has the biggest industrial site in Scotland. Most of the people who work at the site live within 10 miles, we have been told. There is something very geographical about that, and most of the housing—I defer to the constituency MSP on this—is post-1950s. How do you convene that and do it on a place base and entrust the private sector to do it—not just social housing, which would be easier to do?

Is doing things geographically as a package in that way investable? Alexander Dennis, the bus company that does hydrogen, is there so an interesting aspect is using industry as an anchor, as there is a major anchor industrial site. It may not be beyond the realms of possibility that we will get blue hydrogen and then green hydrogen. Hydrogen may not be for housing everywhere, but it might be in district heating in that area because of Acorn and so on. How ambitious is that? Is it realistic to look to use the convening power of local government or whoever to do something on that, or is that too small? Is Grangemouth too small? It has a major industrial site. Could that work together?

Heather Buchanan: I certainly do not think that it is too ambitious. There is a lot of money out there looking for specific projects where investors can see that there will not only be a financial return; that often means coming in and doing something in conjunction with the Government, which can help reduce some of that risk. Being able to demonstrate that it has a positive social and environmental impact is very important. I think that something on that scale is quite exciting and you would probably have people biting your hand off to partner up in a very joined-up way as well. We do not want utilities coming around digging up the road, filling it back in and then another one coming round and digging up the road and filling it back in, so getting a joined-up approach would be a massive opportunity. Certainly, from our members' perspective, a lot of them are talking about opportunities like that and looking at how they partner up with city councils and so on.

James Close: The key point is designing with the future in mind. If I am thinking of taking something like that to my risk committees, I know that they will ask me why I think that that option will be viable in the long term. Working back from 2030 in terms of what that particular part of the economy will look like, and giving people confidence that that will be viable for the long term and an important part of the next 30 years of industrial development is a very powerful way of starting to derisk it. Getting some Government money and turning that into an investment zone are the sorts of things that will help in that regard.

I cannot help but think about what might have happened in economic history. Consider the industries of the industrial revolution, such as the milling industry in the north-west. I am not sure that we would want to replicate all that, but that is how those clusters form. Similarly, consider the chocolate industry in York. The power of Rowntree's and Cadbury, and the work that they did to create not just businesses but communities is quite interesting.

Fiona Hyslop: It is back to the future, potentially, in a place-based way—

James Close: In a different way, yes—

Fiona Hyslop: —but it is about economic growth and productivity.

James Close: —but I am not sure that I would want that phrase to be quoted in there. [*Laughter*.]

Fiona Hyslop: Is there anything that you want to say on that, Ben? Does that sound attractive?

Ben Howarth: Yes. I definitely agree with the place-based approach. I consider that in terms of how individual businesses might be thinking about some of the net zero opportunities. A lot of them will say that it is one thing to sit down with carbon accounting and loads of spreadsheets to come up with a target and a pathway that says that that is how they will get to net zero, but it becomes exciting for them when they are bringing all their different functions and thinking, "This is what our business model looks like in the net zero economy, this is how we bring all of you into that, and this is how your roles could impact that and these decisions."

The model that you were describing almost does that at a scale of a place. That really allows you to start thinking about what Grangemouth will look like in a net zero economy and what business opportunities there will be. Everyone can then come in and say, "I can see my role in that. I can see where my business can help. I can see products that we can build and develop that would support that solution."

It is very important to have that vision of what things will look like in the future and the model that you are working towards rather than just taking things step by step. That can get more people to buy in and get more creativity. You might find businesses that we have not even considered in the context of this inquiry coming forwards and saying that they have a very important role to play.

I turn to the more practical side of how you get invfestment in such a model. One of the key things is that there might be challenges for individual bits of that project, so there will need to be a demonstration of creditworthiness to get debt financing or whatever. A financier that is involved in that project could use something like municipal bonds as a practical step and one of the ways in which to say, "That is how we get the kind of scale of investment that is perhaps not linked to the individual project but is linked to this as a concept and as a place-based solution.” If we can develop those kinds of models—municipal bonds and other ways for investors to come in at scale that are perhaps less linked to each part of the picture succeeding—that helps you with managing the risk.

There are various papers on how you develop green and municipal bonds. Doing that is not easy, but it is definitely doable. That is the model to use and that is where you would, I hope, see a lot more ABI members in the institutional investment side coming in and saying, “Yes, we would want to be involved in that.”

Fiona Hyslop: My degree is in economic history. It would be wonderful if Grangemouth is one of the first places to move to such a model. It is only miles from the birthplace of the industrial revolution at the Carron iron works in Falkirk, and only 10 miles from where shale oil was first discovered in Winchburgh. It would be quite something to imagine that re-engineered future in a place-based approach.

James Close: To be bit more explicit, I am thinking of the paternalistic relationship between businesses, their employees and their communities. Not everything was right there, but some really good work was done.

Fiona Hyslop: I was thinking of that as well. The mills at New Lanark is a good model. How do you improve things? You take everybody with you. The question that we are wrestling with is: what is a just transition? It is not just about the business but about the communities around it.

Heather Buchanan: Having that consistent framework and understanding of the transition plans is the magic sauce within all this to get the level of buy-in that we need, and to manage the risk and understand the fluctuations that will inevitably happen in the process.

Fiona Hyslop: I am conscious of time, but I think that Ben Howarth wants to come in.

The Convener: First, I will raise an issue that is linked to your line of questioning. The Government is due to publish the draft just transition plan for Grangemouth—we expect that that will probably be in late spring. Part of our reason for doing the inquiry is to feed into that proposal. What are expectations for the draft plan? Are there things in it that you particularly want to see at this stage?

I will come to Ben Howarth first, because that follows on from Fiona’s questions around placemaking.

Ben Howarth: First, that is entirely the right thing to be doing, and we as a sector welcome it. Secondly, one of the key things to emphasise is some of the timeline. I would ask that the plan is developed as much as it can be to have a similar format and structure to the transition plans that businesses are developing or that, at the very least, businesses be provided with the information that they would need to inform their decision making. That would make it more usable—they would practically be able to build it into their own plans. Therefore, using a similar structure would be helpful.

A sense of where there are those collective things, like municipal bonds, and where there are those opportunities, is really important. Also, the point that I was about to make previously is relevant: there needs to be a structure for citizen and local community engagement. Clearly, that needs to be done democratically; it is not for businesses to co-opt their needs. One of the things that businesses always need is rich information on what their customers and their potential customers really want. We need to have a structure in which the local community can strongly set out their preferences, and understanding what they want and what their needs would be can also help businesses to be creative. There is an opportunity to reflect and to build on that.

The other key thing that you need from a just transition plan is the opportunity to write it again, so you would publish it, reflect on it, take more input, see whether it is working and come back to it. Therefore, a structure for on-going decision making is very important, rather than seeing the plan, once it has been published, as being done and that it is now about implementation. I think that you must see it as a live process for continuing to bring people into the conversation.

The Convener: It is a draft plan so there will be a consultation phase following the publication of the plan. Heather Buchanan, what statements would you like to see in the draft plan?

Heather Buchanan: I agree with Ben Howarth—it is about the structure of the plan to a certain extent.

I would highly encourage you to engage with the transition plan task force that is working out of the Department for Energy Security and Net Zero. A lot of work is going on to make sure that there is an element of consistency between plans. The last thing that we want to be doing is reinventing things. Let us consider the corporates, where the money will be coming from and a lot of the people doing the work. They are all working towards having a comparable structure. More than just the details of it, that is about ensuring that there is consistency and read-across because, in so much of what we are doing in this area, nobody is comparing apples with apples. There is a kind of tropical fruit salad of different things going on and we need to get it down to a consistency that is understandable.

The Convener: I have a similar question around the draft plan for James Close. We have heard about the Grangemouth future industry board during our inquiry. That largely comprises public bodies that have been brought together to co-ordinate things. Last week, Scottish Enterprise, when we asked how GFIB ensures collaboration with the private sector as well as the public sector, said that that former aspect could be reviewed.

What are your views on the draft plan? What would you like to see in it? Have you, or any of the other witnesses, had any engagement with the Grangemouth future industry board?

James Close: I will check with colleagues, but I certainly have not had contact with the board.

The most important thing is to be clear around the vision: what is it that we want Grangemouth to be? That vision will then set the parameters for the plan. There will be multiple ways to get to that vision, but there must be clarity around the vision—and the mission, too. I am really taken by Skidmore's work in his report "Mission Zero. Independent Review of Net Zero", as well as by Mariana Mazzucato's great work on work between the public sector and the private sector on mission-related activities. The strategy will then follow.

The Convener: Thank you very much for your evidence this morning. It is much appreciated.

11:29

Meeting continued in private until 11:42.

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