Business as Usual: Bank Net Zero Commitments, Lending, and Engagement

**Executive summary**

Parinitha Sastry and co-authors conducted the first large-scale causal evaluation of the impact of banks’ net zero commitments on their lending and the climate impact of borrowing firms. Their results cast doubt on the efficacy of voluntary net zero commitments for reducing financed emissions, whether through divestment or engagement.

This Policy Brief is based on the webinar of the 25th of March 2024 with Parinitha Sastry and hosted by Alissa Kleinnijenhuis (Cornell University) entitled “Business as Usual: Bank Net Zero Commitments, Lending, and Engagement”.

**Policy Brief**

As the effects of climate change are beginning to be felt, there are increasing calls from policymakers and other stakeholders to transition the economy away from carbon-intensive production. The United States and Europe have set net zero targets for 2050; China has one for 2060, and India for 2070. The net-zero transition will require a massive mobilization of capital: McKinsey (2022) estimates it will require $9.2 trillion per year in investment for energy and land use systems between 2021 and 2050. This raises the important question: where will the financing for the global net zero transition come from? Banks play a central role in capital allocation, so they are key to financing the green transition. Banks have made ambitious public commitments to reduce financed emissions and increase financing for sustainable activities. Most prominently, more than 138 banks, representing over 40% of global banking assets, have made explicit net zero commitments through the Net Zero Banking Alliance (NZBA), one of the most stringent initiatives. These “net zero banks” have made a commitment to “align lending and investment portfolios with net-zero emissions by 2050” with “intermediate targets for 2030 or sooner.” These targets must be set within 18 months of joining the alliance, and they specify the sectors that each lender has targeted as high priority for decarbonization. In addition to announcing sectoral targets for reducing financed emissions, net zero banks also make outright pledges to scale up sustainable finance.
The announcement of bank net zero commitments has triggered contrasting reactions. Many laud the NZBA initiative as evidence that banks are beginning to seriously incorporate climate change concerns in their lending and investment decisions, suggesting that banks can help to bridge the large financing gap for the net-zero transition. In the United States, some even went further, taking lender divestment from fossil fuels as a given and holding net zero banks responsible for divesting. Others, however, have pointed out that these net zero commitments are voluntary and could simply reflect greenwashing behavior. In our recent research paper (Sastry et al., 2024), we conduct the first large-scale causal evaluation of the impact of banks’ net zero commitments on their lending and on the climate impact of borrowing firms. We use two administrative data sources from the European Central Bank that provide a comprehensive view of European banks’ lending portfolios. The first is a bank-firm credit registry with granular information on the near-universe of lending within the euro area. The second is banks’ global lending by sector and country. We organize our empirical analysis around three hypotheses for how banks can impact financed emissions. Net zero banks can decarbonize their portfolios in two ways: divestment and engagement. Banks can divest from polluting firms and reallocate capital to less emission-intensive firms. Alternatively, net-zero banks can continue to lend to polluting firms, but engage by pushing them to reduce their emissions. For example, banks can encourage polluting firms to set climate targets and invest in cleaner technologies. If net zero banks neither divest nor engage with polluting firms, then net-zero commitments have a limited impact on financed emissions and instead represent greenwashing by banks. We obtain the following findings.

- First, we reject the divestment hypothesis. Net zero banks do not divest from polluting sectors, nor do they scale up project financing for renewable power projects. Figure 1a plots lending to mining as a share of total worldwide lending to all sectors by banks with and without a net zero pledge, and Figure 1b presents a similar plot for total lending. The figures reveal that there is no evidence of a lending reduction to mining borrowers by net zero banks relative to non-net zero banks, either before or after the adoption of NZBA (denoted by the vertical line). In addition, Figure 2 shows that, within the context of project finance loans for power generation, banks do not reallocate their portfolio towards renewables projects.

- Second, we reject the engagement hypothesis. Borrowing firms dependent on net zero banks are not likelier to set their own climate targets (Figure 3), nor do they reduce their verified emissions.

We conclude that net zero commitments do not lead to meaningful changes in bank behavior. Overall, our results cast doubt on the efficacy of voluntary net zero commitments for reducing financed emissions, whether through divestment or engagement. This evidence would support recent efforts by governments to improve the credibility of net zero commitments. More broadly, it suggests that voluntary private-sector initiatives may have little impact on decarbonization.
Figure 1a: Lending Share to Mining

Notes: Source: Sastry et al. (2024)

Figure 1b: Total Lending to Mining

Notes: Source: Sastry et al. (2024)
Figure 2: Project Finance Loans to Power Generation

Notes: Source: Sastry et al. (2024)

Figure 3: Number of Borrowers with an SBTi Target by NZBA

Notes: Source: Sastry et al. (2024)
References


The E-axes Forum is an independent nonprofit, nonpartisan research organization on macroeconomic policies and sustainability. The Forum is dedicated to aggregating knowledge from around the globe with the aim to catalyze the engagement of economists and decision makers who are working on policies towards achieving a sustainable economy.

www.e-axes.org
228 Park Ave S., PMB 35845, New York, NY 10003