PRI RESPONSE

INVEST 2035: THE UK'S MODERN INDUSTRIAL STRATEGY

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PRI Association

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ABOUT THE PRI

The Principles for Responsible Investment (PRI) works with its international network of signatories to put the six Principles for Responsible Investment into practice. Its goals are to understand the investment implications of environmental, social and governance (ESG) issues and to support signatories in integrating these issues into investment and ownership decisions. The PRI acts in the long-term interests of its signatories, of the financial markets and economies in which they operate and ultimately of the environment and society as a whole.

The six Principles for Responsible Investment are a voluntary and aspirational set of investment principles that offer a range of possible actions for incorporating ESG issues into investment practice. The Principles were developed by investors, for investors. In implementing them, signatories contribute to developing a more sustainable global financial system.

The PRI develops policy analysis and recommendations based on signatory views and evidence-based policy research. The PRI welcomes the opportunity to respond to the UK Government's call for feedback on the UK's Modern Industrial Strategy.

ABOUT THIS CONSULTATION

The UK government has released a consultation on the UK's Modern Industrial Strategy, setting out their vision for a credible, 10-year plan to deliver the certainty and stability businesses need to invest in high growth sectors. In the proposed Industrial Strategy, the government recognises the need to prioritise and target policy interventions carefully, in areas that will deliver the largest growth benefits, institutional capabilities to set the foundations for long-term and agile policy implementation.

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KEY RECOMMENDATIONS

The PRI welcomes the government's consultation on the UK's Modern Industrial Strategy, central to driving the wider Growth Mission and embedding a long-term, clear and stable direction of travel into policymaking.

The UK's Nationally Determined Contributions (NDCs) set strong targets for an 81% reduction in GHG emissions from 1990 to 2035, whilst the Climate Change Committee (CCC)'s annual progress reports offer a pathway to achieve the net zero transition. The focus should now be on the Industrial Strategy to bring targeted policy interventions together and set a clear direction on long-term measures to deliver on net zero, regional growth, and economic security.

The PRI's key recommendations are:

- taking a **whole-of-government approach** to the transition, backed by sectoral roadmaps with clear pathways to decarbonisation and an investment strategy with time-bound commitments and incentives to crowd-in private finance;
- create an enabling policy environment by implementing **wider sustainable finance policies and standards,** such as mandatory transition plan disclosure requirements and a robust, evidence-based sustainable taxonomy, in a coordinated manner with clear timelines for delivery;
- set out details on the **governance of the Industrial Strategy Council**, to best support the delivery and monitoring of the Industrial Strategy; and
- remain **flexible to tailor the Industrial Strategy to specific geographic and economic characteristics** where required, considering socioeconomic implications of the transition.

DETAILED RESPONSE

The PRI's response will be split between Section 1 and Section 2. Section 1 will consider the business environment of the Industrial Strategy – providing recommendations on an enabling environment, the role of regulation, barriers to overcome, and data. Section 2 will consider the framework for the Industrial Strategy – offering analysis on the social transition, international best practice, and institutions.

SECTION 1: BUSINESS ENVIRONMENT

AN ENABLING ENVIRONMENT

This section will respond to Questions 6, 19, 20 and 23.

To make the UK an attractive destination for green investment, investors need certainty on a broad direction of travel with policy and regulation, an ability to deliver on returns, and availability of investable business models.

The government can play a role by creating an enabling environment and de-risking transition finance, to further unlock investment in the transition. To this end, the PRI sets out a framework for a whole-of-government approach to create this enabling environment and guide the financial sector. We also provide recommendations on scaling up blended finance solutions to create a strong set of incentives, clarity, and help de-risk investments in low-carbon technology.

A whole-of-government approach

Investors' net zero commitments and transition plans are contingent on a **clear and enabling policy framework.** An effective policy approach to address multiple goals, spanning climate to the cost of living, needs to be the responsibility of governments as a whole, and needs to be executed as such.

To support this, the PRI has developed a conceptual framework for a whole-of-government approach, summarised below.

- **The economic transition must be a central goal of public policy.** This must be backed up by governance structures, notably through allocating cabinet or ministerial responsibility for the economic transition and making the transition an integral part of the statutory mandates of regulatory and oversight bodies and agencies.
- **Governments must adopt national transition plans** that are informed by science and international norms. They should include short-, medium- and long-term sustainability targets and define resource allocation. The specific details of each plan and its implementation will depend on a series of factors, including economic context, economic structure, political and institutional capacity and expertise, the sources and types of finance available to the country, domestic economic, social and environmental priorities, and the nature of the relationships between the various actors involved in the policy development and implementation processes.

- **The economic transition requires all major areas of government policy to be aligned.** Specifically, the economic transition necessitates coordinated and integrated action across three levers: addressing economic externalities, incentivising markets for solutions, and enabling finance to support the transition. This is elaborated further in our response.
- **Public and private finance to enable the transition**: This will require policy makers to provide policy certainty over the short, medium and long term, remove barriers to private finance, remove perverse incentives, set up green development banks, and support the private sector with concessional finance, grants, guarantees and other risk-sharing instruments, long-term credit lines and investment guidelines. In acknowledging the importance of private finance, it is also necessary to be realistic about the role that private finance can play. There are likely to be areas where there is no business case for action, where costs significantly outweigh benefits, or where the benefits accrue to actors other than those making the investment.
- **International collaboration to complement national transition policy reform**. While domestic legislation is the critical determinant of the level of capital flows into the economic transition, rules-based international regimes supported by governments are critically important to global capital markets. There are various reasons for this: international regimes are seen as important signals of intent and as providing a higher level of certainty that government commitments will be delivered; they can enable governments to work together, helping to address the reluctance of individual governments to act in a way that may undermine national competitiveness; and they can create the rules and markets necessary to incentivise private sector investment. In addition, collaboration across markets on transition policy will be essential to avoid fragmentation and costly competition between governments.
- **Monitoring and review processes.** There is much that we do not know about the economic transition. Priorities may change. Technologies that do not exist today may be developed. The relative economics (the cost curves) of technologies and solutions will change over time. In addition, our understanding of policy interventions – what is needed, what works, what doesn't work, what the costs are – will further develop. Robust and regular monitoring is critical to ensure that the policy interventions adopted are meeting their goals, and to ensure that the spillover and knock-on effects – whether social, environmental or economic, relating to processes and institutions or to outcomes and impacts – are identified and addressed by policy review processes. These processes should not only consider performance against defined short-, medium- and long-term goals, but should also consider the effectiveness of actions taken, the factors that have shaped or influenced performance, and changes in the political, economic, social and environmental context of the country (which may shape the types of policy interventions that can be adopted). An important corollary to this point is that policy makers need to retain the flexibility to change course if policy is not as effective as it needs to be or if the social, environmental or economic impacts are not acceptable. This need for flexibility may, at times, conflict with the demand from investors for policy certainty.

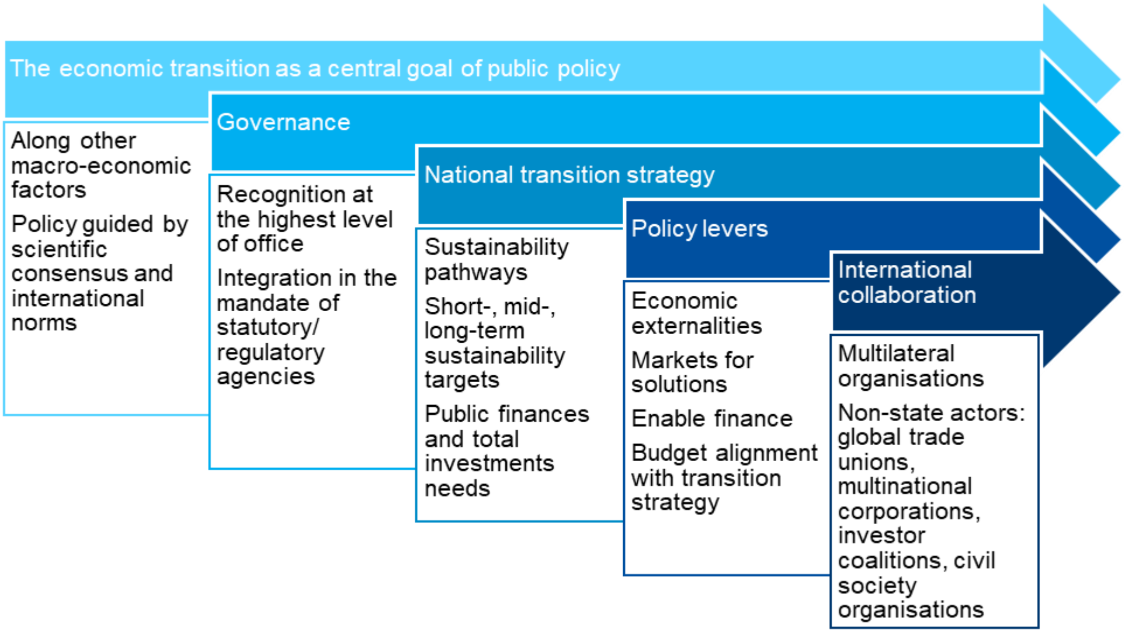

Figure 1: A high-level policy framework for a whole-of-government approach to the economic transition

The PRI recommends that the UK government take forward these elements of a whole-of-government approach within their Industrial Strategy.

Levers for a whole-of-government approach to the transition

Ensuring that HM Treasury's Budget is aligned with the UK's net zero transition is a **cross-cutting measure**, which enables a role for fiscal policy to mitigate effects in the short-term through spending, taxation, managing borrowing, and in the long-term, shape investment and industrial patterns.

The economic transition necessitates coordinated and integrated action across three levers: addressing economic externalities, incentivising markets for solutions, and enabling finance to support the transition. The PRI offers a non-exhaustive list of policy tools that governments can put in place to activate these independent levers.

Addressing economic externalities

- Pricing instruments (e.g., carbon pricing and emission trading schemes)
- Adopting performance standards (e.g., for vehicles, buildings and household appliances)
- Setting phase-out dates for polluting sectors (e.g., unabated fossil fuel power plants) and demand-side measures for hard-to-abate sectors
- Subsidy reform (e.g., phasing out harmful subsidies)
- Requiring minimum social safeguards from economic actors (e.g., decent work) and highlighting good-job externalities (e.g., increased social cohesion)

- Regulation relative to public goods (e.g. affordability standards in the housing market, data protection regulation)

Incentivising markets for solutions

- Setting sustainability targets (e.g., for renewable energy, energy savings and nature restoration)
- Issuing credible and predictable sector-specific policies, targets, and transition plans
- Providing tax exemptions and/or subsidies for clean technologies and sectors
- Supporting measures for early-stage innovation and R&D
- Adopting and implementing public procurement policies
- Up-skilling and re-skilling of the work force

Enabling finance to support the transition

- Embedding sustainability outcomes in financial regulation – as per the PRI and World Bank policy toolkit and the Legal Framework for Impact
- Providing public finance in support of sustainable finance (e.g., green development banks, concessional finance, grants, guarantees and other risk-sharing instruments, long-term credit lines and investment guidelines)

THE ROLE OF REGULATION

Public policy critically affects the ability of institutional investors to **generate sustainable returns and create value**. It also affects the sustainability and stability of financial markets, as well as social, environmental and economic systems. Policy engagement by institutional investors is therefore a natural and necessary extension of an investor's responsibilities and fiduciary duties to the interests of beneficiaries.

There is a **clear and global trend of growing sustainable finance policies and standards**. This reflects a welcome focus from governments in ensuring that financial entities play an active role in the transition, as well as creating the right policy environment to ensure a shift towards net zero financial centres. However, discrepancies in approaches across jurisdictions, asset classes or a lack of coordination with the private sector can sometimes create issues in implementation of these regulations and create unintended, adverse consequences.

To support the credibility and integrity of the transition, it is crucial that **wider sustainable finance policies and standards**, such as transition plan requirements, taxonomies, and disclosure requirements are developed in a coordinated manner. This is key to ensuring that investors have the **information and tools** needed to transition, rather than just guidance, which will ultimately enable the transition to accelerate more comprehensively across the wider economy.[1]

[1] PRI response to the FCA's anti-greenwashing guidance consultation (2024)

The Institute for Public Policy Research (IPPR) analysed that regulation must be better resourced and aligned more closely to the real economy.[2] Targeted regulation to unlock capital for the transition can offer the UK a competitive advantage amongst global competition for green growth. A supportive regulatory environment would set a strong foundation for a transition planning ecosystem. To this end, PRI offers recommendations on regulatory alignment with:

- a UK Green Taxonomy;
- credible transition plans;
- broader frameworks; and
- the National Wealth Fund with wider government policy decisions.

Alignment with a UK Green Taxonomy

The PRI has called for the development of a **robust, evidence-based sustainable taxonomy** to support the acceleration of the transition. A UK Green Taxonomy will offer greater transparency on the alignment of economic activities with the UK's climate objectives.[3]

As the PRI and World Bank's Policy Toolkit on Taxonomies of Sustainable Economic Activities highlights, a well-designed, effectively implemented sustainable finance taxonomy can help investors plan and report on a transition towards sustainability by setting the **objectives and direction of travel** for different economic activities. For example, the ASEAN Taxonomy for Sustainable Finance is used as a tool for transition for high emission sectors and a tool for providing access to funding for sustainable projects, assets, and activities.[4]

The GTAG paper Applying the UK Green Taxonomy to wider policies explores how various policy tools can be used to boost transition finance flows. As per GTAG's advice, current and planned taxonomy-alignment and eligibility should be a key component in the developing transition plans framework.[5]

In developing an approach to implement the UK Green Taxonomy, the UK government should consider whether an **extended taxonomy,** encompassing activities that can be classed as transition activities, should be implemented, either immediately or in a second phase. This could increase transparency over transitioning economic activities, allowing a more detailed breakdown of how companies are implementing their transition plans by allocating capital to transitioning their economic activities. By increasing transparency over what counts as a transitional activity, an extended taxonomy could increase the **robustness of transition finance products**, addressing concerns that transition finance will simply enable business as usual investment.[6]

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[2] IPPR, Making markets: The City's role in industrial strategy (2024)

[3] PRI's response to the FCA's Sustainability Disclosure Requirements (SDR) and investment labels consultation (2022)

[4] PRI and World Bank, Policy Toolkit on Taxonomies of Sustainable Economic Activities (2022)

[5] GTAG, Applying the UK Green Taxonomy to wider policies: the value case and options (2023).

[6] GTAG, Developing a UK taxonomy adapted to the UK's needs in the short and medium term (2023)

The Monetary Authority of Singapore (MAS) has launched a multi-sector transition taxonomy, which sets out detailed thresholds and criteria for defining green and transition activities and recognises the role that certain economic activities have in the energy transition, without having to label them as inherently sustainable or green activities.[7] Defining credible transition thresholds is particularly important for hard-to-abate sectors that have a more challenging pathway to meet a 1.5°C aligned outcome.

Whilst a taxonomy is a useful tool, it cannot enable the transition to a sustainable economy on its own and should be developed in parallel to other instruments (i.e. sectoral roadmaps and corporate transition plans) to ensure a coordinated and effective approach, as well as interact with other policy instruments such as stewardship and broader disclosure requirements.[8]

Alignment with credible transition plans

Direct recognition of a 1.5°C-aligned net-zero transition in the UK's Industrial Strategy and a clear delivery roadmap would send certainty to the wider economy and show decisive international leadership.

Good quality transition plans, aligned with the Transition Plan Taskforce's (TPT) disclosure framework, will play an important part in the UK's Growth Mission. 65% of UK businesses believe that achieving the goals in their transition plans will make them more competitive.[9] With investment appetite growing globally for the transition, these plans can help companies attract capital from global investors who, more and more, value good-quality disclosures from their investee companies when allocating capital. Furthermore, the recent Transition Finance Market Review made clear that **widespread transition planning**, both at the national and corporate level, will play a key role in the development of the UK as a leading global hub of transition financial and professional services

Transition plans should not be a standalone output, they should build upon existing reporting frameworks. They should be used as both a strategic tool and a practical action plan, setting a precedent for accountability and the necessary steps in the journey towards a net zero economy. The UK government can play a role in driving forward the TPT's outputs, ensuring that they are fully operationalised in the UK's financial ecosystem. With this framework in place, investors will be able to understand the climate risks and opportunities that companies are exposed to and make investment decisions based on this information.

Ultimately, investors' role in the transition is contingent on a **clear and enabling policy framework** that guide and signal the financial sector to not only reduce their financed emissions, but also finance greater emission reductions in the transition. Net zero transition plans should not be seen as a substitute for effective sectoral policies, nor should the responsibility and accountability of creating

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[7] Monetary Authority of Singapore (MAS) Press Release: MAS Launches World's First Multi-Sector Transition Taxonomy (2023). PRI response Singapore Green Finance Industry Taskforce consultation on a Green and Transition Taxonomy (2023)

[8] PRI's response to the Australian Treasury's consultation on Australia's Sustainable Finance Strategy (2023)

[9] Lloyds Banking Group. Credible Transition Plans: Reporting vs Reality

such an enabling policy environment be entirely delegated to the private sector. Concerted efforts are needed from both public and private sectors for an orderly and equitable transition.

Alignment with broader frameworks[10]

In a global economy, alignment across jurisdictions is an operational imperative. To ensure the UK remains an attractive place for investment, alignment with broader frameworks should be sought, to promote internationally coherent solutions, share best practices, and avoid market fragmentation.

To scale up transition finance, **clarity and harmonisation** should be sought by implementing consistent frameworks across the economy, building on the work of the TPT, the Green Technical Advisory Group's (GTAG) guidance on implementing a green taxonomy, and International Sustainability Standards Board (ISSB).

Relevant government departments and regulators should swiftly roll out a comprehensive and credible transition plan disclosure regime under the FCA's Sustainability Disclosure Requirements and investment labels regime (SDR) which incorporates and builds on the TPT disclosure framework requirements.[11] As highlighted in PRI and IIGCC's briefing on sustainable finance policy priorities, transition plan disclosures should move from operating on a "comply or explain" to a **mandatory basis** at the earliest possible opportunity, with adequate signposting of timelines provided. This should include the anticipated consultation on transition plans for the UK's largest companies.

More broadly, aligning UK reporting requirements to international standards offers the transparency investors need to manage climate and sustainability-related risks and opportunities. Adoption of the ISSB standards in the UK is crucial to achieve **interoperability of corporate sustainability disclosure requirements** – promoting comparable data across investment portfolios – and to build on existing progress in reporting on sustainability-related risks and opportunities.[12]

The PRI has called for **economy-wide implementation of the ISSB Standards** across jurisdictions by 2025 at the latest.[13] We support an **endorsement mechanism** for current and future ISSB standards to become part of UK law, and continued engagement with the ISSB Jurisdictional Working Group to promote interoperability.

In the EU, the Platform on Sustainable Finance's (PSF) report on A Compendium of Market Practices looks at how the EU's sustainable finance framework can be used to support and inform the transition efforts of economic actors beyond mere regulatory compliance. This work highlights that a sustainable finance framework needs to address the challenge of **financing meaningful and credible interim**

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[10] GFANZ identifies four strategies necessary for financing a whole economy transition to net zero, defined as financing or enabling: the development and scaling of climate solutions; assets or companies already aligned to a 1.5 pathway; assets of companies committed to transitioning in line with 1.5 aligned pathways; and the accelerated managed phaseout of high-emitting physical assets. This framework offers broad structure and clarity around the areas of financing and enabling, considering specific climate solutions as well as the complexities of transitioning hard-to-abate sectors, at a global level.

[11] IIGCC's response to the TPT's consultation on sector-neutral transition plan disclosures (2023)

[12] PRI's response to the FRC's call for evidence on ISSB standards (2023)

[13] PRI's response to the FRC's call for evidence on ISSB standards (2023)

steps towards the transition. Providing tools and policies that enable market actors across the economy to finance their transition plans and reach their sustainability targets is required.

Adequately measuring companies' and investors' role, performance, and impact on sustainability matters is a crucial foundation for successfully redirecting capital to support the transition, which relies on ensuring consistent and comparable data. Through the development of transition plans, taxonomies, and wider disclosure requirements, a strong foundation of transparency can be created, serving as a framework to drive capital towards the transition.

Aligning the National Wealth Fund with government priorities

Regulation alone is unlikely to drive the £50 billion of low carbon investment each year required to meet the UK's climate commitments.[14] The Industrial Strategy should draw on a broad range of tools to mobilise the required private capital.

Scaling up blended finance could establish clear pathways and standards. By taking onboard some of the financial, policy, or political risk at the early stages of development, the UK government would send a signal that these projects are **compatible with institutional investors' risk appetite and fiduciary duties**. This offers a strong incentive for further sources of capital to be deployed.[15]

In the National Wealth Fund: Mobilising Private Investment, the UK government set out a long-term vision to increase the impact of public investment, with the NWF as the UK's impact investor. The clarity on how the NWF plans to go further than the UK Infrastructure Bank on more catalytic capital, impact, a renewed focus, proactive approach, and greater regional focus is welcomed.

Aligning the NWF's climate finance to a net-zero carbon budget that is consistent with the goals of the Paris Agreement is crucial. To ensure this investment strategy delivers on economic growth, the government should reduce the risk of conflicting signals by aligning wider government actions and policy developments with the Fund's activities. Instead, the foundation for a successful NWF should be strategic coordination, better integration and stronger governance structures than the previous UK Infrastructure Bank.

The NWF should go beyond a project-by-project basis. Instead, it should create a platform to enable concessional capital providers, private investors, policy makers and investee companies or projects to negotiate a package of concessional funding for coordinated project portfolios based on the condition that the government will conduct necessary policy reform to drive the transition.

The NWF should:

- Identify the need for blended finance and assess the amount of concessional funding needed by working collaboratively across financial and real economy policymakers, investors and businesses
- Coordinate projects to mitigate unintended consequences

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[14] Climate Change Committee (CCC), The Sixth Carbon Budget: The UK's Path to Net Zero (2020)

[15] House of Commons Environmental Audit Committee (EAC) The financial sector and the UK's net zero transition (2023)

- Aggregate transition projects to an investment size more manageable for large-scale institutional investors and to diversify idiosyncratic project risks.
- Link projects with policy reform needed to reduce risks and capital costs.
- Support the development of a pipeline of viable projects across the value chain by taking a project life cycle approach and facilitating the deployment and exit of different forms of private capital.

A recent report from the LSE Grantham Institute set out a comprehensive, non-exhaustive list of public instruments and policy tools that can be used to catalyse private investment in blended finance models.[16]

BARRIERS

This section will respond to Questions 7 and 22.

In the Industrial Strategy consultation, the government recognise that the UK has faced significant shocks, alongside a longer-term slowdown in productivity growth, persistently low levels of investment and slowing market dynamism.

In both recognising the need for and setting out an industrial strategy, the government has overcome an important barrier – a lack of overarching direction from the top. The previous lack of industrial strategy led to fragmented implementation and stop-start approaches to policy that undermined a stable and orderly transition. Rollbacks on crucial climate policies diluted investor confidence in the UK as an attractive investment destination for long-term investments.

A lack of a supportive policy environment to facilitate the flow of capital towards the transition is one of the main barriers to achieving net zero, regional growth, and energy security. To this end, the PRI recommends addressing the following barriers in the UK to create a supportive policy framework:

- the interpretation of fiduciary duty;
- inconsistent signals from government; and
- a whole of economy approach to climate objectives and sectoral roadmaps.

Interpretations of fiduciary duty

There are inconsistencies in the interpretation of fiduciary duty due to a lack of clarity around how fiduciary duty interacts with sustainability and climate change considerations. The 2021 report A Legal Framework for Impact, which includes extensive analysis of the UK legal framework, shows that investors are generally permitted to consider pursuing sustainability impact goals where this would

[16] LSE Grantham Institute, Investing in our future: practical solutions for the UK government to mobilise private investment for economic, environmental and social policy priorities (2023)

contribute to their financial objectives.[17] Following on from A Legal Framework for Impact our UK specific report, UK: integrating sustainability goals across the investment industry, explores how policymakers can support investors' abilities to invest for sustainability impact. The report finds that because the UK legal framework relies on broad interpretation of regulation, which evolve through practice and precedent, the concept of financial interest is routinely narrowly construed and subject to confusion. Many UK investors remain hesitant to change their established practices and pursue sustainability impact goals, even when this is required to achieve financial objectives.[18] This can lead to shorter-term factors being prioritised, whilst sustainability issues, including the transition, considered as less relevant for investment decisions.[19]

In February 2024, the Financial Markets Law Committee published Pension Fund Trustees and Fiduciary Duties: Decision making in the context of Sustainability and the subject of climate change, which examines the legal uncertainties surrounding the inclusion of sustainability and climate change when taking decisions as pension fund trustees. The paper **clarifies the interpretation of the law**, underscoring that sustainability issues should first be considered as a financial factor by pension fund trustees and then assessed for materiality.[20] It is also highlighted that "*it may be necessary to consider whether a strategy should reject shorter term gains because they create identifiable risks to the longer-term sustainability of investment returns in the fund*."[21]

By updating standards and guidance, policymakers can provide clarity on when investors' legal duties enable or require them to consider pursuing sustainability impact goals such as invest in the net zero transition.[22]

The FMLC paper helps to clarify uncertainties around fiduciary duty, which in turn can help to shift trustees' practices to systematically consider relevant sustainability risks and objectives, as owed to beneficiaries. To facilitate this shift across the wider investor community, policymakers should integrate the findings of the FMLC paper into relevant guidance and make clear that **the requirement to consider sustainability risks encompasses an obligation to consider taking active steps to pursue sustainability impact goals** when this would help achieve financial risk/return objectives.

Guidance is required not just to understand fiduciary duties but also their application: this should address **how investors can assess sustainability risks and impacts and how to set and pursue sustainability impact goals**. Lastly to ensure that the relevant time horizons for sustainability risks and impacts are being considered, policymakers should clarify that investors **should take into**

[17] Freshfields Bruckhaus Deringer, PRI, United Nations Environment Programme Finance Initiative (UNEP FI), Generation Foundation A Legal Framework for Impact: Sustainability impact in investor decision-making (2021)

[18] PRI, UNEP FI, Generation Foundation A Legal Framework for Impact UK: Integrating sustainability goals across the investment industry (2022)

[19] Persad, Xu, Greening, Institutional investor behaviour and the energy transition: A complexity framework for accelerating sustainable finance from UK investors, *Energy Economics* (2024).

[20] Financial Markets and Law Committee (FMLC) Paper-Pension-Fund-Trustees-and-Fiduciary-Duties-Decision-making-in-the-context-of-Sustainability-and-the-subject-of-Climate-Change-6-February-2024.pdf (fmlc.org) (2024).

[21] Financial Markets and Law Committee (FMLC) Paper-Pension-Fund-Trustees-and-Fiduciary-Duties-Decision-making-in-the-context-of-Sustainability-and-the-subject-of-Climate-Change-6-February-2024.pdf (fmlc.org) (2024).

[22] Freshfields Bruckhaus Deringer, PRI, United Nations Environment Programme Finance Initiative (UNEP FI), Generation Foundation A Legal Framework for Impact: Sustainability impact in investor decision-making (2021)

account not only long-term sustainability impacts but also short- and medium-term sustainability impacts, since these may affect financial risk and returns over a range of timescales.[23]

Consistent policy signals

Whilst incentives, tools, and frameworks are useful for the UK's transition, there is no substitute for **long-term, stable government signals**. The government needs to ensure that the policy signals it sends provide investors with confidence and certainty to invest in the growth of sectors in the long-term that will drive the UK's transition.

Delays fail to deliver the necessary framework and policy signals to investors. The prerequisite of a leading green financial centre is a regulatory environment that encourages and enables alignment towards net zero and sustainable economic development. This should be supported by an equally ambitious, whole-of-government approach on the economic transition.

In the absence of strong policy incentives and consistent, clear, and continuous signals, the capacity for industry to invest in the net zero transition will be at risk. As the PRI, IIGCC, and UKSIF wrote in our letter to Prime Minister Keir Starmer, the government should establish a long-term ambitious whole-of-government approach to the delivery of the UK's net zero strategy, underpinned by credible and comprehensive decarbonisation pathways and targeted incentives. This includes fulfilling commitments in Financing Growth Plan.

The PRI commends the government for setting out a comprehensive, mission-driven industrial strategy for consultation. Furthermore, announcing 2035 Nationally Determined Contributions (NDCs) with ambition to reduce GHG emissions by at least 81%, in line with limiting global temperature rise to 1.5°C sends a **clear signal on UK climate leadership**. Announcing NDCs ahead of the February 2025 deadline and at COP29 instead would encourage other countries to set ambitious NDCs too.

Whole of economy approach to climate objectives and sectoral roadmaps

The previous government set out a number of climate targets, however the 2023 Independent Review of Net Zero demonstrated that the previous government's Net Zero Strategy **did not provide "adequate certainty to business and investors"**. The Environmental Audit Committee highlighted the lack of consensus within government on the speed of transition away from fossil fuels despite endeavours to reach net zero by 2050.[24] A misalignment between these strategies and wider policy government decisions impacted the credibility of the previous government's plans to reach net zero.

There is a need for **further granularity from the new government**, including a **mapping of the investment required across sectors and regions** to ensure that solutions are targeted towards investment gaps that need to be filled. The UK government should develop **specific sectoral transition plans with clear roadmaps to decarbonisation** to this effect.

[23] Freshfields Bruckhaus Deringer, PRI, United Nations Environment Programme Finance Initiative (UNEP FI), Generation Foundation A Legal Framework for Impact: Sustainability impact in investor decision-making (2021)

[24] House of Commons Environmental Audit Committee (EAC) The financial sector and the UK's net zero transition (2023)

Aviva Investors' white paper on making financial flows consistent with the Paris Agreement highlights that transition planning across the global economy can provide a series of **self-reinforcing actions and information flows.** Signals from national strategies can inform workplans for financial regulators and supervisors and help to shape actions from the private sector. As the best available scientific evidence shows, some sectors (such as hard-to-abate industries or sectors critical for electrifying the economy) must decarbonise faster than others, requiring credible detailed decarbonisation pathways.[25]

The Net-Zero Banking Alliance offer additional guidance on a sectoral approach, setting sector-level targets for hard to abate industries, including agriculture; aluminium; cement; coal; commercial and residential real estate; iron and steel; oil and gas; power generation; and transport.

Sector-specific work is underway in the real-estate sector, with the cross-industry Net Zero Carbon Buildings Standard which brings together Net-Zero Carbon requirements for all major building types, based on a 1.5°C trajectory.[26]

In developing PRI's Investing for the economic transition: The case for whole-of-government policy reform, we interviewed leading policymakers and investors on the transition. Stakeholders stressed that **investors need confidence** that governments will pursue a coherent approach to the economic transition, and that national strategies will not be jeopardised by changes in government or by wider social, political, economic, or environmental challenges.

As the London School of Economics (LSE) highlights, there are numerous market failures and path dependencies that necessitate a green industrial strategy, underpinned by a clear and consistent long-term direction of travel. For example, GHG emissions are currently not accurately priced in, which provides a justification for government ? to pursue crucial environmental policies and remove barriers to green investment. Policies, incentives, public investment, and investment subsidies should be coordinated as part of an overarching and lasting strategy that provides a clear sense of direction for the private sector.[27]

Sectoral roadmaps need to set out more detail on the decarbonisation trajectories across key sectors of the economy, as well as the investment roadmaps required to unlock private investment, and associated tax, spending and regulatory/policy commitments to incentivise demand.

The European Commission and the EU's Industrial Forum have developed a blueprint for sectoral roadmaps, based on stakeholder feedback. This blueprint highlights that sectoral roadmaps should detail a shared vision and understanding of what the decarbonisation of economic sectors looks like; how and within what timelines different sectors, industries and specific technologies are expected to progress; and what role public and private finance and companies should play in enabling and accelerating this net-zero transition.[28]

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[25] Deloitte, Decarbonization of hard-to-abate industries. GFANZ, Guidance on use of sector pathways for financial institutions (2022). PRI response, Transition Plan Taskforce: A sector-neutral framework for private sector transition plans. (2022)

[26] Net Zero Carbon Building Standard.

[27] Valero and Van Reenen, Embedding green industrial policy in a growth strategy for the UK (2023)

[28] For example, the UN Race to Zero and the Glasgow Financial Alliance for Net Zero (GFANZ) have developed 17 investment roadmaps. PRI 2030 EU Policy Roadmap (2024)

DATA

This section will respond to Question 13.

Despite improvements in sustainability reporting, many investors still struggle to access decision-useful data, given limitations around digitisation (e.g. annual reporting in pdfs) and gaps in the metadata for each datapoint. The UK government can partially mitigate this issue by creating a data platform, similar to the Net-Zero Data Public Utility (NZDPU) or the forthcoming European Single Access Point (ESAP), to inform decision making. This would not lead to new requirements, but rather enhance the accessibility of data produced to meet existing (or planned) requirements for companies and investors.

SECTION 2: FRAMEWORK FOR THE INDUSTRIAL STRATEGY

SOCIAL TRANSITION

This section will respond to Questions 8, 28 and 29.

Governments will only be able to successfully facilitate, enable, and deliver national economic and sustainability objectives if they effectively anticipate, prevent and manage negative social impacts of the economic transition and ensure broad societal support for transition measures.

PRI's discussion paper on the socioeconomic implications of the transition explores how social issues could inform a whole-of-government policy approach to the economic transition.

Key findings of the paper include:

- The economic transition's success depends on achieving **buy-in across diverse societal groups and sectors.** Policy makers need a complete understanding of the transition's stakeholders, including their needs, societal constraints, and the drivers of their resistance to the transition.
- Policies should target the **root causes of social discontent and economic disparities** to foster inclusive development and social cohesion, committing to the respect of fundamental rights as a baseline for any policy intervention.
- To effectively address the transition's socioeconomic implications, policy makers should adopt **a whole-of-government approach,** involving all stakeholders on whom different policy areas of the transition depend, and all available policy levers (addressing externalities, incentivising markets, and enabling finance to support the transition).
- Investors play an important role by engaging with policy makers to support the development of socially conscious transition policies.

A whole-of-government approach to the transition within the UK Industrial Strategy can help to mitigate negative social impacts by ensuring that all relevant perspectives are considered and integrated into policy planning and implementation. An industrial strategy, through cross-departmental coordination, can enable policy makers to identify synergies and avoid policies that conflict one another, making the transition smoother and more efficient.[29]

The framework's components for integrating social issues into the transition are:

- Identification of relevant stakeholder groups that might benefit or incur risks;
- Decipher relevant policy areas; and
- Enable policy levers.

[29] Kennedy et al. A Primer on Implementing Whole of Government Approaches. (2015)

As relevant for the UK's Industrial Strategy, PRI offers analysis on labour rights and regulations, as well as fiscal policy and economic restructuring.

On labour rights and regulations, this policy area focuses on protecting worker rights, especially for workers who transition out of old and into new jobs and supporting current and future workers to build new skills and shift to new careers. Current statistics show continuing skills gaps and employment mismatch between those working in the highest emitting sectors, or brown sectors, and transition-aligned green sectors.[30] This policy area is essential to ensure that current and future labour forces are well equipped and motivated to participate in the necessary sectors to bring about a sustainable economy. This calls for re-skilling programmes and – more broadly – advancements in the education sector to align supply and demand in labour markets.[31]

Other areas of priority can include ensuring that jobs lost due to the transition are offset with green jobs that at the same or higher level, and in the same geographic areas.[32] For example, the UK has ended its reliance on coal power, which is a positive step for emissions, yet could result in direct job losses. The government's Office for Clean Energy Jobs commits to championing clean energy projects across the UK to support highly skilled green jobs of the future. The Office for Clean Energy Jobs should take a regional approach, to engage more effectively with the needs of affected stakeholders. Existing regional approaches should be further supported, such as Celtic Freeport, an initiative to accelerate Wales' Green Economy through job creation and attracting inward investment.

Fiscal policy and economic restructuring will play a central role in the transition, including subsidy and tax reforms designed to ensure that the transition's benefits are equitably distributed across society. Redistributive tax measures are essential to achieve an equitable transition. Implementing a progressive tax and incentive system can mitigate systemic inequalities and generate revenues to support vulnerable populations affected by the transition, while rewarding early adopters and leaders in sustainable practices. Targeted subsidy reform plays a pivotal role in facilitating both short-term adaptation and the sustained advancement of the transition. Governments can redirect funds towards transition-aligned initiatives by reducing harmful subsidies, such as those supporting environmentally damaging activities. This area also underscores the importance of a nuanced fiscal policy approach featuring balance and coordination between incentives and regulatory measures.

By embedding a socioeconomic approach to the transition into the UK's industrial strategy, the government will send appropriate signals on long-term planning, resilience, and building out the future needs for the next generation. It is important to note that PRI's analysis focuses mainly on the climate transition, however other transition, such as the technological and demographic transitions can also affect the socioeconomic conditions of different societal stakeholders, as well as their fundamental rights.[33] This should be accounted for in the UK's Industrial Strategy.

[30] EBRD, Transition Report 2023-24. (2023).

[31] Borde et al. Education as a strategy for climate action and mitigation. (2022).

[32] ILO World Employment and Social Outlook 2018 – Greening with jobs [Summary]. (2018).

[33] PRI How investors can advance decent work. (2022).

INTERNATIONAL BEST PRACTICE

This section will respond to Questions 17 and 24

International partnerships

The UK government should **leverage the role of export credit** in supporting companies transition to net zero and shift financial flows through **UK Export Finance**. Greater access to financing for companies across the globe also provides a key supply chain opportunity for the UK.

The **Clean Energy Transition Partnership (CETP)** has effectively reduced international public finance for fossil fuels by £10-15 billion, marking a two-thirds reduction from pre-CETP levels in 2021.[34] However, data from the International Institute for Sustainable Development shows that CETP members have the potential to shift $28 billion from fossil fuels into clean energy annually.[35] There is opportunity to raise the ambition and demonstrate international support for CETPs through government commitments to the Clean Energy Action Plan announced at COP29.

International examples of best practice

There are numerous examples of best practice in providing the right ecosystem for transition finance that can be drawn from. The PRI has drawn from three examples – the US, Europe, and Japan – which touch on **incentive structures, industrial strategy, longevity and policy certainty**, as well as alignment with the real economy.

US

The US has put in place landmark legislation that provides permanent incentives for investment in key sectors for the economic transition.

Since 2020, the US has passed three large-scale industrial and real-economy policies with transition implications. These policies are primarily incentive-based, covering specific economic sectors, including renewable energy, climate resilience, electrical grid improvements and electric vehicle adoption. The Inflation Reduction Act created permanent incentives to attract capital investment in renewable energy through 12 clean energy tax provisions, including Investment and Production Tax Credits. Over a period of 10 years, the Inflation Reduction Act is estimated to raise revenue of around $73 billion, primarily through tax credits and tax deductions as the main instruments.[36] The Inflation Reduction Act offers long-term certainty for green energy investments.

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[34] Clean Energy Transition Partnership, Clean Energy Transition Partnership set out 'Action Plan' to scale up finance for clean energy at COP29, (2024)

[35] International Institute for Sustainable Development, Putting Promises into Practice: Clean Energy Transition Partnership signatories' progress on implementing clean energy commitments,.(2023)

[36] European Parliament EU's response to the US Inflation Reduction Act (IRA) (2023)

The EU was also reactive to the US' Inflation Reduction Act, producing its own Net Zero Industry Plan. Both offer strong subsidies and tax breaks, as well as clear policy signals on green industrial ambitions.

Other policies in the US cover infrastructure and industrial priorities, such as the Bipartisan Infrastructure Law, which allocates US$550bn for areas including electric vehicle infrastructure and climate resilience, and the CHIPS Act, which provides funding to encourage research into and development and manufacturing of net zero technologies. Further to this, the Biden administration has, through Executive Order 14057, established an official "whole-of-government-approach" to achieving net zero by 2050, with an interim economy-wide target of reducing net greenhouse gas emissions to 50-52% below 2005 levels by 2030.

European Union

The EU has adopted ambitious legislation on sustainable finance, climate change and nature under the banner of its EU Green Deal (EGD). The framework has put an increasing emphasis on transition, and steps have been taken to better integrate sustainability objectives into public finance instruments.

The EGD provides an overarching framework to help transition the EU economy towards a sustainable model. While the overall goal is to address climate change by reaching climate neutrality by 2050, the EGD addresses a range of interrelated economic, societal and environmental objectives. These include reducing emissions, creating jobs and growth, addressing energy poverty, reducing external energy dependency, and improving citizens' health and wellbeing.

Since the adoption of the EGD, the EU has adopted a set of strategies and real-economy policies with important transition features. These include: (i) the adoption of the EU Climate Law, which sets stringent climate goals for 2030 and 2050; (ii) the Fit for 55 package, which aims to accelerate the decarbonisation of key sectors of the economy; (iii) the Green Deal Industrial plan, to scale up EU's manufacturing capacity for net zero technologies; (iv) the 2030 Biodiversity Strategy that aims, among other things, to protect a minimum of 30% of the EU's land and sea area; and (v) a strategy for financing the transition, which seeks to reorient financial flows toward sustainable activities. To support the EGD's objectives, 30% of the EU's 2021-27 budget is to be spent on climate action.

Japan

Japan has taken important steps in integrating the economic transition at the highest levels of government, as well as putting in place policy tools that aim to enable the transition of the high-emitting sectors that make the greatest contribution to the country's emissions.

Japan's GX Basic Policy is a 10-year roadmap that positions the economic transition as a central policy goal: its main objectives are to develop markets in the areas of energy supply and decarbonisation, while strengthening Japan's industrial competitiveness and economic growth. The roadmap also encourages a just transition by simultaneously promoting the acquisition of new skills and the smooth movement of labour to growth sectors, including the green sector.

Furthermore, the economic transition is recognised at a high level in terms of governance: the GX Basis Policy was developed by the GX Implementation Council, which was chaired by the prime minister, and consequently adopted through a Cabinet decision.

INSTITUTIONS

This section will respond to Questions 30 and 32

Industrial Strategy Council

Following the consultation period, the government should set out details on the **governance** of the Industrial Strategy Council, to best support the delivery and monitoring of the Industrial Strategy. To this end, the PRI offers recommendations below.

As highlighted in the PRI's whole-of-government framework for the transition, a **monitoring and review process** should be factored into government interventions. Robust and regular monitoring is critical to ensure that the policy interventions adopted are meeting their goals, and to ensure that the spillover and knock-on effects – whether social, environmental or economic, relating to processes and institutions or to outcomes and impacts – are identified and addressed by policy review processes. This should enable the Industrial Strategy Council to be **agile and responsive to technological change.**

A statutory, permanent, and independent Industrial Strategy Council is a sensible approach to provide a foundation of stability and ensure longevity. The UK government's proposed approach sets out that the Industrial Strategy Council will feed into wider developments. The government should reduce the risk of conflicting signals by aligning wider government actions and policy developments with the Industrial Strategy. The Industrial Strategy Council should be the mechanisms for this synergy.

The UK has a strong background of cross-sector collaboration, bringing together industry experts and government officials to drive innovative solutions to accelerate the transition. The TPT, GTAG, and Transition Finance Market Review are good examples of working groups bringing together industry experts, academia and regulators, with clear mandates, governance, direction, and goals set by government.

Co-designing solutions offers a pivotal feedback loop to ensure policies are effective.[37] Ongoing dialogue between practitioners and policymakers should continue to serve as a model for best practice on cross-sector collaboration. The Industrial Strategy Council should continue this, with a view to taking forward recommendations from these groups.

The Industrial Strategy Council could also track that **financial regulation is broadly aligned with the Industrial Strategy's objectives**. Regulators and policymakers should play a direct and coordinated role in supporting the Industrial Strategy to achieve its objectives. If financial regulation and real economy policies are misaligned, these risks creating an unsupportive, conflicting policy environment for the Industrial Strategy. Instead, government bodies should be resourced and mobilised to support the government's Industrial Strategy mission with the Industrial Strategy Council playing a coordinating role.

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[37] IPPR, Making markets: The City's role in industrial strategy (2024)

Regional specificities

An effective industrial strategy will have both national and regional elements.[38] A high-level industrial strategy, set out by the UK government, is crucial for setting a coherent direction of travel. It is equally important to tailor this strategy to specific geographic and economic characteristics, such as the skills base or potential for renewable energy.[39]

The government's **targeted approach** recognises the need for government intervention should where catalytic support to scale up industries is needed, where there is insufficient market coordination, or where economic activities or sectors produce positive or negative spillovers. This should enable **strategic flexibility for regional considerations to be taken into account under the national Industrial Strategy**.

A core component of PRI's [framework on integrating social issues into the transition] is consultation with affected stakeholders. In the Industrial Strategy Council's monitor and review process, ongoing dialogue with affected stakeholders should continue. This should be embedded in its governance structure.

As the Green Alliance highlight, locally targeted actions allow regions to prioritise the most impactful and cost-effective policies and technologies, develop skills where these are needed, and enable projects to scale to the right size for infrastructure investors.[40] Local governments also have a role in communicating their responsibilities in the success of the Industrial Strategy, and co-benefits of the transition. For example, [Scotland's Green Industrial Strategy] sets out what a supportive policy environment entails at a national level, then goes into further granularity on opportunity areas for Scotland specifically.

Scotland's Strategy highlights that success requires a strategic approach to ensure prioritisation of resources and investment, coordinating policy, and partnerships. This demands that regional specificities be taken into account, and the Industrial Strategy should be flexible to areas regions may want to prioritise to achieve objectives on net zero, regional growth, and economic security.

Devolved nations

A clear indicator of regional specificities being taken into account is consideration on how devolved nations take up national government priorities.

Cooperation and coordination across national government, devolved nations, and local government is a crucial foundation to ensure that the transition is not only accelerated, but that local communities reap the co-benefits. **Empowering local governments to shape industrial policies tailored to local needs should be explored**. For example, Scottish social housing standards, and continuing

[38] Valero and Van Reenen, Embedding green industrial policy in a growth strategy for the UK (2023)

[39] Green Alliance, The cluster effect: Why the UK needs a place-based green industrial strategy (2023)

[40] Green Alliance, The cluster effect: Why the UK needs a place-based green industrial strategy (2023)

public funding for area-based energy efficiency programmes, have resulted in more consistent progress on energy efficiency than in England.[41]

Explicit, long-term policy support for devolved nations on taking up the priorities set out in the UK's Industrial Strategy would be beneficial to securing the benefits and building the capacity for devolved nations to transition. As the Industrial Strategy sets out, greater institutional capabilities would enable agile policy implementation. Here, the Industrial Strategy's objectives on net zero, regional growth, and economic security are strongly aligned.

The PRI has experience of contributing to public policy on sustainable finance and responsible investment across multiple markets and stands ready to support the work of the UK government further to the modern industrial strategy in the UK.

Please send any questions or comments to policy@unpri.org.

More information on www.unpri.org

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[41] Tingey and Webb, Net zero localities: ambition and value in UK local authority investment (2020)