

Greener Finance for Sustainable Future

30-31 October 2019



The main outcomes of Greener Finance for Sustainable Future -conference

Bank of Finland and the Finnish Ministry of Finance co-organized a conference titled "Greener Finance for Sustainable Future" on 30th-31st October. The Sessions of the conference were Setting the scene, EU taxonomy, Green Investing, ESG Information & Disclosure and Financial Stability & Risks.

The difference between 1.5°C warming and 2°C warming is significant, as the negative impacts of global warming are not linear. Everyone, each country, company, individual, and every financial market participant, needs to participate in the work against climate change. Otherwise the results will fall short of what is needed. The climate policies should be efficient, fair and they should address the free rider problem. In addition to climate challenges, the social aspect needs to be taken care of as the good social base will support the climate change mitigation.

The financial sector plays an important role in fighting the climate change, since financial sector directs the investment flows - either to environmentally sustainable or unsustainable businesses. Significant investments for emissions reductions are needed within the following sectors: energy, cities, food and land use, water, industry, innovation and transport. The climate policies implemented are not only a risk but also opportunities for economic prosperity if the transition is done correctly.

EU Taxonomy

EU taxonomy is a list of economic activities which enhance some environmental aspect without making any significant harm to any other. Investments to activities under taxonomy can be seen as responsible investments. Once finished, the Taxonomy can potentially be used outside of the EU

as well. The discussion on the EU taxonomy highlighted that there is a significant need for common language and for harmonization of the disclosure in that common language. In general the EU taxonomy seems to fulfil its intended purpose but it needs further development to make it more streamlined. It was mentioned many times that the needed money for mitigating climate change exists but at the moment it is in the wrong places - taxonomy could play a role in correcting this problem. A potential caveat in the EU taxonomy were the strictness and multi-objective evaluation, as only a few current economic activities fall within the scope of taxonomy, and the modest timetable of the legislation as compared to the urgency of needed climate actions.

Green Investing

Considerable investments are needed to support the transition into sustainable economy. The taxonomy for sustainable investments would be very beneficial for unlocking investment flows as at the moment the biggest obstacle in scaling green investments is the lack of supply of sustainable investment opportunities. Strangely, against the traditional supply-demand framework, the low supply and high demand for sustainable investments does not fully seem to be reflected in the price of sustainable finance. The lack of uniform ESG-ratings, proper disclosure, comparable data and harmonization of concepts are also complicating the green investing. While at the moment whether a company is green or not in itself has no impact on its revenues, but in long-run the non-green firm has the risk of losing revenues to green companies in its industry.

ESG Information & Disclosure

The problem with ESG-data is not necessarily the lack of it but rather the quality, the price and the comparability of the data. Therefore, it is quite reasonable that the ESG-ratings vary between different providers, especially considering that different ESG-ratings may have different weightings of E, S and G. It came up in the discussion that it is important to use the data and give feedback of it to the data providers in order to improve it. Also, there is a big demand for forward-looking data as traditional disclosure has focused on backward-looking items. Disclosure from the real economy companies is important in order to improve the ESG-data and its coverage. Companies should report more, and also SME companies should be encouraged to disclose - keeping in mind the burden of reporting for SMEs.

Financial Stability and Risks

Climate based financial risks can be divided to physical risks and transition risks. Analysing climate risks is difficult as these new risks cannot be properly identified from the past data. For financial companies it is necessary to do the risk analysis already now even though the best practises probably have not been found yet. At the moment, it is important to begin the work and invest in understanding the risks and building the analytical capacity, as this will take time. From risk management point of view, it is necessary to understand what the current situation and risk level is, what the right target is and how to achieve it. Scenario-analysis was seen as one of the most

prominent tools in building the understanding. Some existing risk analysis approaches are for example portfolio sensitivity analyses and ESG-analyses for individual companies. Including climate risks to stress tests was seen as a poor approach because there is not yet enough understanding of the complex dynamics between climate and financial risks. Incentivizing green investments through prudential rules, either with Green Supporting Factor or Brown Penalizing Factor, would be a poor idea as well.

The recording of the conference and the presentations can be found from [the conference webpage](#).