THE FINANCIAL SYSTEM WE NEED

ALIGNING THE FINANCE SYSTEM FOR SUSTAINABLE DEVELOPMENT

WASHINGTON DC, JANUARY 2016

SIMON ZADEK, CO-DIRECTOR, INQUIRY
Mark Carney, Governor, Bank of England

“Green finance cannot be a niche”

Atiur Rahman, Governor, Bangladesh Bank

“Developing economy central banks have been trying to address the risks of instabilities and imbalances at sources, by promoting sustainable financing”

Yi Gang, Deputy Governor, People’s Bank of China

“China will advance green finance during its presidency of the G20 in 2016”
FINANCING CHALLENGE & INQUIRY MANDATE

FINANCING CHALLENGE

<table>
<thead>
<tr>
<th>Amount</th>
<th>Description</th>
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<tr>
<td>US$16 trillion</td>
<td>Annual global investment. All needs to be green and resilient.</td>
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<tr>
<td>US$5-7 trillion</td>
<td>Annual investment needed for sustainable development goals.</td>
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<td>US$7 trillion</td>
<td>Annual environmental externalities.</td>
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REASONS WHY MISALIGNED WITH SUSTAINABILITY?

- Weak real economy regulation & pricing
- Inadequate/inefficient public spending

RATIONALES FOR ACTION IN FINANCIAL SYSTEM

- Managing risk:
  - Market failures in the financial system can aggravate externalities: short-termism, misaligned incentives.
- Promoting innovation:
  - Upgrading the standards and regulations required to catalyze investment, for example, in bond markets.
- Strengthening resilience:
  - Environmental factors can pose risks to assets and system stability.
- Ensuring policy coherence:
  - Ensuring coherence between financial regulation and wider goals, such as long-term investment, access to finance, environmental security.

Mandate

advance options to improve the financial system’s alignment with sustainable development.
### `A QUIET REVOLUTION`  

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<th>Diverse starting points</th>
<th>Measures in practice</th>
<th>Levers for action</th>
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<td>Financial inclusion, greening industry</td>
<td>Integration in prudential banking regulation</td>
<td>Enhancing market practice</td>
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<td>Air pollution</td>
<td>New investor reporting requirements on climate</td>
<td>Harnessing the public balance sheet</td>
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<td>Infrastructure investment</td>
<td>Coordinated roadmap led by regulator</td>
<td>Directing finance through policy</td>
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<td>Post-crisis rebuilding of trust in finance</td>
<td>Financial sector compact</td>
<td>Transforming culture</td>
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<td>Climate change</td>
<td>Incentives for clean energy bonds</td>
<td>Upgrading governance</td>
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FRANCE: Improving financial transparency

Corporations: disclose exposure to financial risks linked to climate change, contribution to climate change and strategic actions

Banks: incorporate climate factors into stress tests - end of 2016

Investors: disclose how they manage sustainability factors, carbon footprint and contribution to the energy transition

"It is essential that the financial system as a whole takes climate risk into account, anticipates ambitious targets and integrates this into investment decisions."

Laurent Fabius, Foreign Minister, France
CHINA: Greening the financial system

Green investment needs: US$400bn p.a to finance green investment; only 15% from public sources.

Green financial system: The People’s Bank of China co-authored a set of proposals with the Inquiry on closing the gap: green bonds, green ratings, lender liability, environmental insurance, stock market disclosure

International cooperation: Promoting green finance as part of its presidency of the G20 in 2016 (Green Finance Study Group)

“Greening a country’s financial system is not an “additional” performance requirement but concerns the efficiency and effectiveness of the whole system”

Development Research Council of the State Council, China
THE UK: *Prudence, stability and green finance*

**Fiduciary Duty:** Law Commission review clarified that material sustainability factors part of prudent investing.

**Prudential Regulation:** The PRA has examined the impact of climate on safety and soundness of insurance companies: physical, transition and litigation risks.

**Market Creation:** The Green Investment Bank instrumental in creating a new class of ‘renewable investment trusts’

**Greening the City:** City of London Corporation to launch Green Finance Initiative, sponsored by government – as part of “2016 Year of Green Finance”

“The central bank time horizon is relatively short. But the real challenges to prosperity and economic resilience from climate change will manifest well beyond this. We face a ‘tragedy of horizons’.” **Mark Carney, Governor, Bank of England**
“The sustainable finance programme is not only intended to increase financing but also to improve the resilience and competitiveness of financial institutions”

Muliaman D. Hadad, Chairman, Indonesia Financial Services Authority (OJK) Board
COMPETITIVENESS OF FINANCIAL CENTRES

CURRENT ASSESSMENT DOES NOT TAKE SUSTAINABILITY FACTORS INTO ACCOUNT

THE FUTURE? RACE TO DEVELOP AS LEADING GREEN FINANCE HUB

Global Financial Centre Index is based on business environment, financial sector development, infrastructure, human capital and reputation.

[Source: Y/IZEN GFCI 18]

GREEN FINANCE AS COMPETITIVE ADVANTAGE
Corporation of London forms Green Finance Study Group
AN AGENDA FOR ACTION
GROWING AND HARMONIZING

- **Reallocating capital**, for example, through a focus on capital market development (green bonds, green infrastructure trusts)

- **Improving market efficiency**, for example, through the FSB task force on climate-related disclosure

- **Deepening resilience**, for example, through a global forum of insurance regulators on sustainability

- **Strengthening the policy architecture**, for example, work on green finance during China’s G20 in 2016

- **Tracking performance**, for example, through the development of shared performance metrics
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Simon Zadek, Co-Director
Mahenau Agha, Head of Outreach

simon.zadek@unep.org
mahenau.agha@unep.org