



# Institutions and Governance: Example of the Financial Sector



Bianka KRETSCHMER (Climate Analytics)

# Finance in the Paris Agreement

**Article 2:** The Agreement « aims to strengthen the global response to the threat of climate change [...], including by:

(a) Mitigation: «well below 2 °C and to pursue efforts to limit to 1.5 °C»

(b) Adaptation: Increasing the ability to adapt and foster climate resilience

**(c) Finance: »Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate- resilient development «**

→Signal to the finance sector to align investments with well below 2°C/ 1.5°C pathways

**Article 9, 10 and 11:** Provision and mobilisation of finance, technology transfer and capacity-building support (MoI) to developing countries

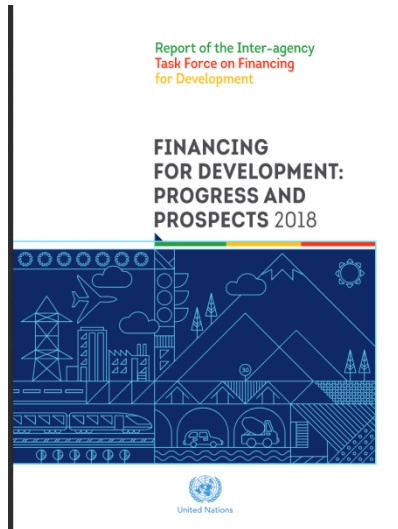


# The dual role of finance in a sectoral governance framework

- **Cross-cutting** as part of governance functions: guidance and signal, setting rules, transparency and accountability, **means of implementation** and knowledge and learning
- **Sectoral financial system – dual role (implications of Article 2.1c):**
  - 1. Sector to be decarbonised:** aligning financial flows and portfolios with Paris goals through mainstreaming climate into investment decision-making
  - 2. Finance as a lever for the low-carbon transition** in other sectors in the real economy through financial system reform



# Reforming the system: Aligning the global financial system with sustainable development



## Monitoring Financing for Development – Identified Key Challenge

- Incentives of actors in public and private financial institutions need to be aligned with long-term sustainable development.
- Without a long-term investment horizon, certain risks, such as those from climate change, will not be incorporated into decision-making.



## UNEP Inquiry: Design of a Sustainable Financial System

Some momentum across the financial system – transformation requires policy and regulatory innovation; and, over time, changes in governance, standards and norms.



# Complex sectoral system- high governance demand

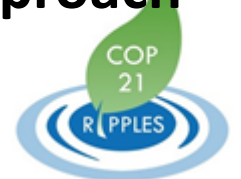
Governance functions	Governance demands	
<b>Guidance and Signal</b>	Consistent, credible and long-term climate policies for investors and financial actors to align their decision making with long-term climate objectives e.g. price signal (carbon pricing) or other signals	<b>High</b>
<b>Setting Rules</b>	<ul style="list-style-type: none"> <li>- Developing and agreeing on international standards, benchmarks and metrics for 1.5 degree-compatible investments</li> <li>- Setting carbon prices and eliminate negative carbon pricing</li> </ul>	<b>High</b>
<b>Transparency and Accountability</b>	<ul style="list-style-type: none"> <li>- Address issues of free-riding, double-counting, additionality of flows, and green-washing of continued high-carbon investment practices</li> <li>- Implementation of commitments</li> <li>- Issue of accountability and liability for adverse climate impacts</li> </ul>	<b>High</b>
<b>Means of Implementation</b>	- translating low-carbon and climate-resilient development strategies into climate investment plans ready for implementation	<b>High</b>
<b>Knowledge and Learning</b>	- Learning on how to mainstream climate across financial institutions and portfolios and knowledge sharing among investors on climate risk management etc.	<b>High</b>



# Governance complex: growing momentum

- **UNFCCC/ Paris Agreement** as framework with 2.1c and possible orchestration role (e.g. Global Stocktake, SCF looking at metrics for tracking 2.1c)
- **Specialised climate funds** (GCF, GEF, CIFs): incentive to partner organisations incl. MDBs etc.
- **Development finance institutions** (MDB and IDFC mainstreaming commitments, WB announcement etc.)
- **Investor initiatives** (Montreal Carbon Pledge, Portfolio Decarbonisation Pledge, UN Principles for Responsible Investment)
- **G20 initiatives** (Green Finance Study Group, FSB Task force on climate-related financial disclosure)
- **Divestment movements**
- **Carbon pricing initiatives** (Carbon Pricing Leadership Coalition, Friends of FFS Reform)
- **Sustainable finance research initiatives**

→ momentum for all governance functions - but no coherent, systemic approach



# Gaps to be addressed – how to move forward?

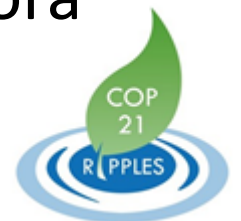
- Growing yet mostly indirect or partial guidance and signal, especially through some emerging (yet voluntary) collective action on transparency and mainstreaming commitments
- MoI provision has been increasing, however amounts remain insufficient compared to global investment needs
- High number of institutions provide knowledge and learning on sustainable and green finance, but remains niche. More focus needed on the brown side of equation.
- Untapped governance potential to achieve a sector-wide signal to move away from high carbon investment patterns and common rules for systemic integration of climate risks to guide the reallocation of capital
- Some movement on transparency, big question remains on accountability



# Commission action plan on financing sustainable growth (based on recommendations by HLEG)

**The action plan on sustainable finance** adopted by the European Commission in March 2018 has 3 main objectives:

- reorient capital flows towards sustainable investment, in order to achieve sustainable and inclusive growth
- manage financial risks stemming from climate change, environmental degradation and social issues
- foster transparency and long-termism in financial and economic activity
- --> will serve as blueprint for EU engagement in international fora





# Ideas for task on finance and transformation

- A lot of focus on “Paris compliant” (or the “do-no-harm” finance, not necessarily green)
- Need more focus on the “brown side of the equation”, hence not only a “push” to boost green technologies and finance, without talking much about the “pull-back” of brown/carbon-intensive activities and financing.
- Hence 4.3 could explore what is needed in terms of financial innovation, regulation and governance in order to achieve the transition - combine economic and governance incentives.

