4. Sustainable Finance: Here to Stay

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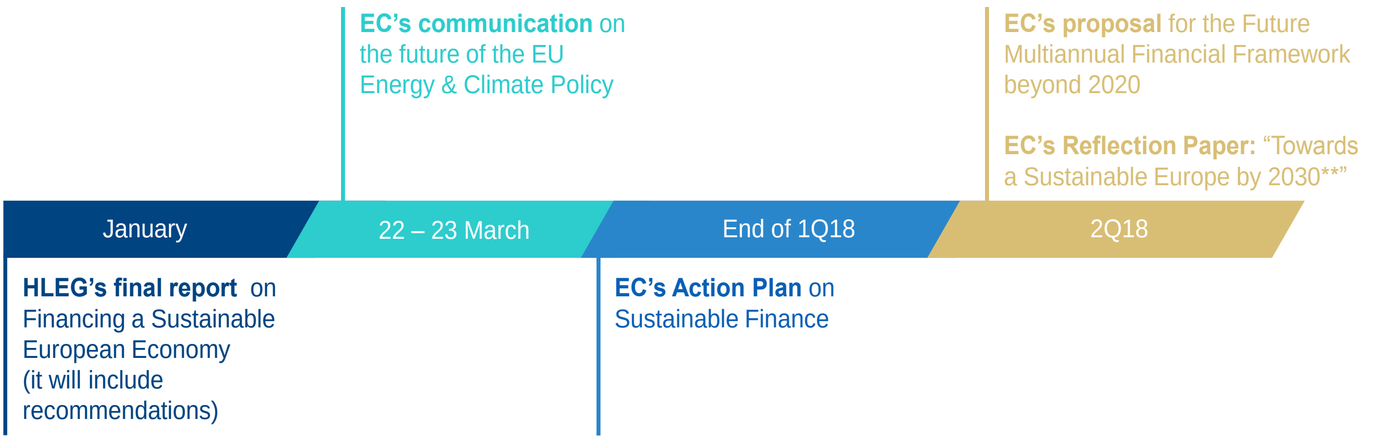
The One Planet Summit of last December has confirmed the irreversible, global and coordinated commitment towards embedding sustainability at the core of the whole financial system. Sustainable finance continues to evolve from the talk to the walk. However, there is still much work to be done to achieve a solid common framework that allows for long-term financial stability.

A financial regulation and supervision catch-up

There are at least three recent public documents that confirm the aforementioned engagement that are worth noting: **i)** It is the first time that eight Central Banks and Supervisors[1] have released a **Joint Statement** for Greening the Financial System to react to environmental and climate challenges at a global level. **ii)** The European Commission (EC) has launched **ten initiatives** for a modern and clean economy that involve all the players of the EU financial system. Last but not least, **iii)** the European Parliament has published two **Draft Reports**[2] that explicitly refer to sustainability issues - i.e.: climate-related risks to be integrated in the risk management of institutions and to be disclosed under Pillar II / the SREP[3]; even more, it is proposed to introduce green and social discount factors for the capital requirements associated with those asset classes/projects - analogously to the already existing support factors to SMEs and infrastructure loans.

Figure 5.1 The next most relevant landmarks at EU level in the short-term



Source: BBVA Research based on the EC's *EU Invests in the Planet: Ten Initiatives for a Modern and Clean Economy The Juncker Commission's contribution to the One Planet Summit*[4]

1: Banco de Mexico, the Bank of England, the Banque de France and Autorité de Contrôle Prudentiel et de Résolution (ACPR), De Nederlandsche Bank, the Deutsche Bundesbank, Finansinspektionen (The Swedish FSA), the Monetary and Authority of Singapore and the People's Bank of China.
2: **i)** On the proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) No 575/2013. **ii)** On the proposal for a directive of the European Parliament and of the Council amending Directive 2013/36/EU. Rapporteur: Peter Simon.
3: Pillar II: Risk management and supervision. SREP: the supervisory review and evaluation process.
4: Paris, 12 December 2017. * EU High-Level Expert Group on Sustainable Finance (Secretariat provided by the European Commission (EC) Commission. ** *Towards a Sustainable Europe by 2030, on the follow-up to the UN Sustainable Development Goals, including on the Paris Agreement on Climate Change".*

An overview of the markets' positioning

Markets have a role of the utmost importance towards filling the significant sustainable finance gap. Therefore, they need adequate information to correctly measure the risks and opportunities and to be able to compare. As such, there is an expanding demand for transparency and for disclosure. Globally, there are 237 companies with a market capitalization of over $6.3 trillion[5] already committed to following the Task Force on Climate-Related Financial Disclosures (TCFD) voluntary **recommendations** on climate-related financial disclosures. In addition to that, it has to be noted that some of the most prominent investment managers requested 60 of the largest banks to follow the TCFD recommendations last September[6].

A "solution of the market and for the market", as stated by Mark Carney recently.[7]

So what?

Two years after the Paris Agreement, there seems to be a clear consensus among all of the agents (regulators, supervisors, governments, companies and investors) on the fact that a sustainable financial system is needed for the improvement of the aggregated welfare function of the societies in which companies and markets perform our activities.

A sustainable financial system can have a direct positive impact on the real economy by promoting innovation, job creation and economic growth. For example, the EC estimates that "clean energy for all Europeans can create 900 thousand new jobs and unlock EUR 177 bn of investment every year"[7].

Two necessary short-term conditions for achieving that are: a commonly accepted taxonomy and framework, both aimed at promoting long-term financial stability, and allowing the measurement and comparison of risks and opportunities. In that vein, at an EU level, the High-Level Expert Group's final recommendations which will be released in a few days' time are expected to shed some valuable light on both of them.

This is a long-distance run. As such, it is important to advance with firm steps towards the finish line, being swift, ambitious and prudent at the same time. It is important to adequately dose the effort and the speed according to each point of the race. One false step at the beginning of the race could have non-negligible undesired consequences during the rest on the run.

5: Source: TCFD. Mike Bloomberg and FSB Chair Mark Carney Announce Growing Support for the TCFD on the Two-Year Anniversary of the Paris Agreement.
6: Source: Financial Times. *Big investors take aim at banks over climate change risk.*
7: EC's *EU Invests in the Planet*: *Ten Initiatives for a Modern and Clean Economy The Juncker Commission's contribution to the One Planet Summit.*

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