



April 17th 2019

The financial sector must be at the heart of tackling climate change

Published by The Guardian April 17th 2019

An open letter from Governor Villeroy de Galhau (Banque de France), Governor Carney (Bank of England) and Frank Elderson (Chair of the Network for Greening the Financial System).

The catastrophic effects of climate change are already visible around the world. From blistering heatwaves in North America to typhoons in south-east Asia and droughts in Africa and Australia, no country or community is immune. These events damage infrastructure and private property, negatively affect health, decrease productivity and destroy wealth. And they are extremely costly: insured losses have risen five-fold in the past three decades. The enormous human and financial costs of climate change are having a devastating effect on our collective wellbeing.

The impact of climate change has compelled governments to act. Catalysed by the Paris agreement, governments around the world are putting policies in place to limit the global rise in temperatures to 2C, and preferably as close to 1.5C as possible. The actions undertaken by individual countries will deliver a collective transition to a low-carbon economy. But this transition brings its own risks. Carbon emissions have to decline by 45% from 2010 levels over the next decade in order to reach net zero by 2050. This requires a massive reallocation of capital. If some companies and industries fail to adjust to this new world, they will fail to exist.

The prime responsibility for climate policy will continue to sit with governments. And the private sector will determine the success of the adjustment. But as financial policymakers and prudential supervisors, we cannot ignore the obvious risks before our eyes.

That is why 34 central banks and supervisors – representing five continents, half of global greenhouse gas emissions and the supervision of two-thirds of the global systemically important banks and insurers – joined forces in 2017 to create a coalition of the willing: the Network for Greening the Financial System (NGFS).

On Wednesday, this coalition's first comprehensive report seeks to translate commitments to act on climate-related financial risks into concrete action. The four recommendations in the report provide all central banks, supervisors and the financial community with deliverable goals that will help to ensure a smooth transition to a low-carbon economy. We therefore call on policymakers and the financial sector to do the following.

First, integrate the monitoring of climate-related financial risks into day-to-day supervisory work, financial stability monitoring and board risk management. Supervisors are encouraged to set

expectations to ensure financial firms are adequately addressing the financial risks from climate change, including by conducting scenario analysis to assess their strategic resilience to climate change policy. Firms are encouraged to take a long-term, strategic approach to the consideration of these risks, and to embed them into their business-as-usual governance and risk-management frameworks.

Second, lead by example, specifically central banks are encouraged to integrate sustainability into their own portfolio management.

Third, collaborate to bridge the data gaps to enhance the assessment of climate-related risks. Public authorities should share and if possible make publicly available any climate-risk data.

Fourth, build in-house capacity and share knowledge with other stakeholders on management of climate-related financial risks. An important element to achieving effective consideration of climate risks across the financial system is to support internal and external collaboration.

The success of these recommendations relies on two important factors, which lead to two broader calls to action on disclosure and classification of climate-related financial risks. First, to support the market and regulators in adequately assessing the risks and opportunities from climate change, robust and internationally consistent disclosure is vital. The market and policymakers must continue to work together to determine the most decision-useful metrics for climate-related financial disclosures.

Second, the NGFS encourages regulators to develop an adequate classification system to identify which economic activities contribute to the transition to a green and low-carbon economy. This will be particularly valuable in supporting financial actors to make sustainable investment and lending decisions.

If the financial community acts on these recommendations we will be two big steps closer to ensuring an orderly transition to a low-carbon economy. We recognise that the challenges we face are unprecedented, urgent and analytically difficult. The stakes are undoubtedly high, but the commitment of all actors in the financial system to act on these recommendations will help avoid a climate-driven “Minsky moment” – the term we use to refer to a sudden collapse in asset prices.

As long as temperatures and sea levels continue to rise and with them climate-related financial risks, central banks, supervisors and financial institutions will continue to raise the bar to address these climate-related risks and to “green” the financial system. We need collective leadership and action across countries and we need to be ambitious. The NGFS is the core of the response of central banks and supervisors. But climate change is a global problem, which requires global solutions, in which the whole financial sector has a crucial role to play.