OPINION

ALIGNING THE FINANCIAL SYSTEM WITH SUSTAINABLE DEVELOPMENT

Simon Zadek

The UN Environment Inquiry into Design Options for a Sustainable Financial System was launched in 2014 with a mandate to improve the financial system's effectiveness in mobilising capital towards a green and inclusive economy.

Our starting hypothesis was that many of the solutions to mobilise the trillions for sustainable development lay in the workings of the global financial system itself, and so could not be resolved at the necessary scale through action downstream in specific mobilisation initiatives. The focus was therefore on the 'rules of the game' and the task was to stimulate practices in advancing such rule change.

Over the first phase, the Inquiry reviewed innovative actions across dozens of countries, exploring the practice of advancing aspects of sustainable development in financial market development. Key was extensive and intensive engagement with financial policy-makers, regulators and standard-setters, as well as market-based rule setters such as stock exchanges and rating agencies, and of course financial market stakeholders themselves.

Quiet Revolution

From the beginning, there was a focus on the practices of developing countries, not least because of their lead in advancing innovative approaches to financial inclusion. There was a particular focus on two countries, China and the UK, in seeking to learn from and harness their respective leadership in (very different) aspects of sustainable finance. What the Inquiry found was that many parts of the world were not organised according to such convention. Particularly in developing countries from South Africa to Indonesia and Bangladesh, and from the China to Peru, we found a 'quiet revolution' in progress in shaping financial market according to diverse policy priorities, from financial inclusion, to air pollution, to black economic empowerment, and to climate.

Birth of a New Narrative

On 8 October 2015, the Inquiry launched its first global report, "The Financial System We Need: Aligning the Financial System with Sustainable Development", at the International Monetary Fund/World Bank Group Annual Meetings in Lima, Peru. It was the first time that the UN, let alone the UN agency responsible for environmental issues, had chaired a panel of central bank governors to talk not about the environment, but the future of the financial system. It was evident that we had crossed an invisible threshold. A new, or perhaps revived, narrative was being established making the matter of environment, climate and sustainable development the business of financial policy-makers and regulators. Reinforcing this was the announcement by China during this pivotal discussion that it would not only take the topic of green finance into the G20 finance track during its Presidency in 2016, co-chaired with the Bank of England, but that it was asking UN Environment to manage this work stream on its behalf.

A Noisier Revolution

Today, it would be hard for any central bank governor to dismiss the relevance of sustainable development to his or her work. Such a shift in such a short time period is remarkable in itself, and a testimony to the work of many and the early impacts of the universal embrace of the 2030 Agenda and the Paris Agreement on climate. Although there is much to be done in translating this movement into tangible, ambitious action, we also see a growing proportion of bankers, investors, stock exchanges and insurance firms making commitments to align their operations with climate change and broader sustainable development objectives.

Considering market practice, for example, there has been a fourteen-fold increase in labelled green bond annual issuance from just USD 11 billion in issuance in 2013 to USD 155 billion in 2017, including emblematic cases such as Nigeria's issuance of the world's first, fully-certified, sovereign green bond. Yet, such progress needs to be set against the scale of the global bond market of around USD 100 trillion. Similarly, there has been an increase in divestments in carbon-intensive assets to an estimated USD 5 trillion in 2016, although this equally needs to be set this against investments in coal, oil and gas over the same period of around USD 710 billion.

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FIGURE 1 **INQUIRY'S FOUR GLOBAL REPORTS**

National action is critical, and there are a growing number of examples of ambitious roadmaps in development and implementation, many of which the Inquiry has supported. Notable examples include:

China: Agreed by China's State Council in August 2016, the "Guidelines for Establishing a Green Financial System" are the world's most comprehensive set of national commitments, covering a range of priorities from banking to capital markets and insurance. This built on the work of the China Green Finance Task Force co-convened by the People's Bank of China and the Inquiry on behalf of the UN Environment.

European Union: Building on developments across a number of member states the European Union set up the High-Level Expert Group on Sustainable Finance (HLEG) in 2016 to map out options for community-wide action. This has laid the foundations for a comprehensive action plan on sustainable finance proposed by the European Commission released in early 2018.The Inquiry has tracked the global number and range of policy measures to advance aspects of sustainable finance. At the end of 2013, 139 subnational, national-level and international policy and regulatory measures were in place across 44 jurisdictions. Most of these were first-generation efforts to improve disclosure in securities markets and by pension funds. Four years on, the number of measures has not only doubled – to 300 in 54 jurisdictions – but the pattern of activity has changed fundamentally, with a substantial rise in system-level initiatives, which now account for a quarter of the total (see Figure 2). These initiatives include the growth in national level roadmaps for green and sustainable finance in countries, across such diverse cases as Indonesia, Italy, Morocco and Singapore. Specialised sustainable finance regulations and guidelines have also been developed. Bangladesh, China, Vietnam and Pakistan have developed guidance for banks to include environmental and social factors into risk management.

Momentum to Transformation

Despite the impressive momentum achieved, progress remains insufficient to deliver the financing required for the 2030 Agenda or the Paris Agreement. Indeed, the vital signs of sustainable development give strong reasons to be highly concerned, whether in terms of ecosystem decline, widening social fractures due to high carbon-trapped economic development and unrealised economic potential. Finance is not the only factor at work, but is a keystone in shaping tomorrow's economy and its impacts.

Progress to date should not discourage more transformative ambition to reshape finance, given the challenges we face and the opportunities that this finance could realise. There is certainly a need for more of both to get to where we need to be. While the job is clearly not done, many stakeholders can and will take the agenda of sustainable finance forward, within national governments, civil society, international organisations, financial institutions and across the UN system.

Aligning the financial system with the 2030 Agenda is not just a matter of more of the same, but of harnessing major change opportunities, given the complexity and dynamism of this system. For example:

- Financial crises offer major opportunities to reshape aspects of the financial system, as has the recent one, albeit with mixed results.
- International political agreements offer opportunities to shape systemic outcomes, such as the Paris Agreement which has helped to system-level initiatives to advance climate considerations across the financial system.
- Digitalisation will transform the financial system and its relationship with the real economy, creating many new opportunities for advancing financing for sustainable development.
- Major investment programs such as China's Belt and Road initiative, provide opportunities to influence the alignment of major investment flows.

The opportunity lies in harnessing such transformational waves. The Inquiry, although having completed its 50-month journey, has spawned and supported the emergence of many on-going initiatives, including:

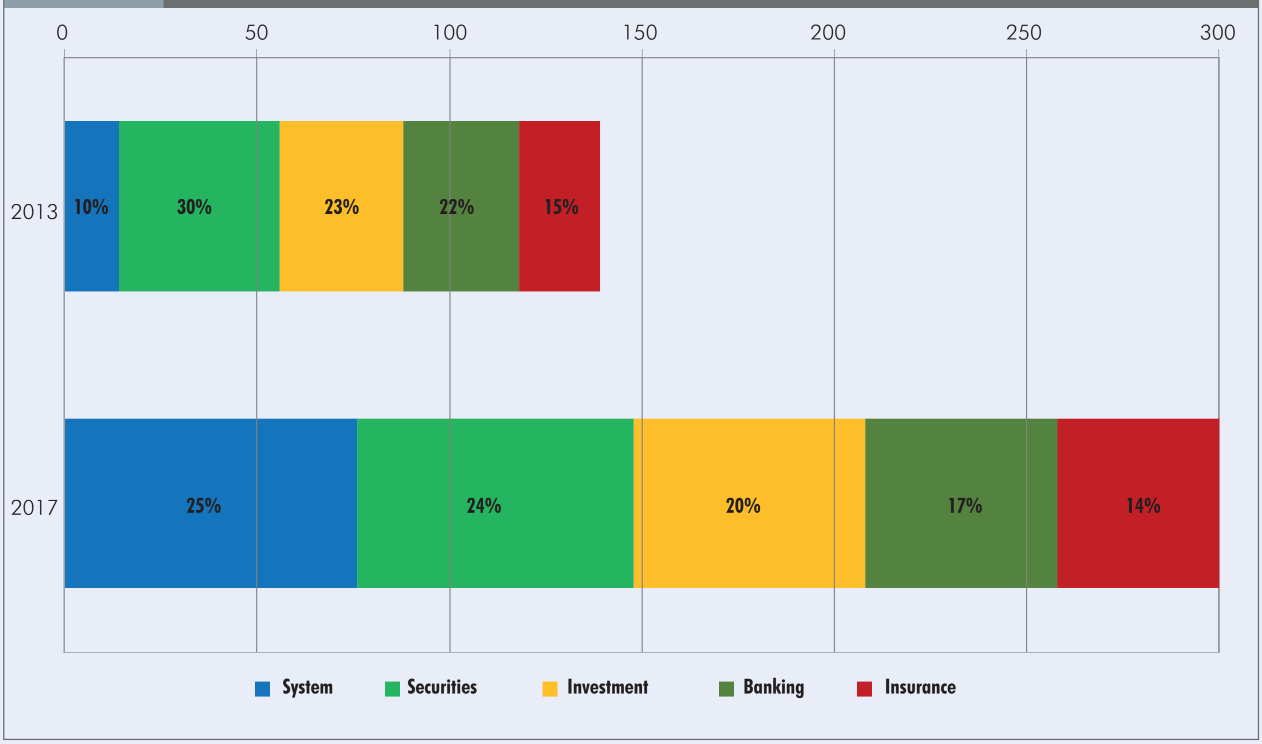
- Sustainable Finance at the G20: UN Environment will continue to advance sustainable finance under the Argentinian G20 Presidency, notably the Sustainable Finance Study Group.
- Coalitions for Action: Three coalitions have been established, each involving UN Environment, to advance aspects of our work:

Network of Financial Centres for Sustainability: Launched in Casablanca in September 2017, the network gathers financial centres committed to harness their financial expertise to drive action on climate change and sustainable development (http://unepinquiry.org/publication/accelerating-financial-centre-action-on-sustainable-development/).

Sustainable Digital Finance Alliance: Co-founded by UN Environment and Ant Financial Services, and established as a Swiss-based, non-profit, public-private partnership, its goal is to catalyse the more effective harnessing of the digitalisation of finance to meet the needs of sustainable development (https://www.sustainabledigitalfinance.org/).

Sustainable Insurance Forum: A network of leading insurance supervisors and regulators seeking to strengthen their understanding of, and responses to, sustainability issues for the business of insurance. It is a global platform for knowledge-sharing, research and collective action (http://unepinquiry.org/sif/).

FIGURE 2 THE DOUBLING IN POLICY AND REGULATORY MEASURES FOR SUSTAINABLE FINANCE, 2013-2017



Roadmaps for Sustainable Finance: a growing number of organisations are now stepping in to support countries and regions in developing roadmaps, such as the IFC's Sustainable Banking Network. Further development work is, however, still required, in the development of tools, ways to link these roadmaps to other planning processes such as green economy planning and climate-related National Development Contributions.

UN Environment's Inquiry as Catalyst

The Inquiry's added value, beyond being in the right place at the right time, was to uncover the many relevant innovative initiatives created by extraordinary champions from around the world, connect these initiatives through the exchange of experience across its partners, and to shape an overarching narrative that validates the ambition to align global finance with sustainable development.

- The Inquiry has been a catalyst for change, not an underlying driver. Its work leveraged three, historic drivers:
- The aftermath of the financial crisis, which created an opening for fresh thinking about the role of the financial system, and strengthened the resolve for policy action on finance.
- The growing importance of developing countries with new ideas about how finance and development should work together.
- The global negotiation and agreement of the Sustainable Development Goals (SDGs) and the Paris Agreement on climate change.

In addition, especially in its latter phase, the Inquiry has increasingly emphasised the potential to harness the digitalisation of finance in realising the 2030 Agenda and the Paris Agreement goals. This is work-in-progress, and currently includes active engagement on the topic through Argentina's G20 Presidency, and the decision by the UN Secretary General to champion a Task Force on Digital Finance and the SDGs.

Note

The Inquiry's complete knowledge base of over 120 reports can be downloaded at: http://unepinquiry.org/.