











## KEY TRENDS

# Recent trends in green finance

### The emergence of transition finance as a major theme

Many tools and methodologies are now in place or under construction for greening the financial sector. That this broad-based movement is not reflected in sufficient volume of financing is notably because it is impossible to move quickly from financing the existing economy, especially in the midst of a crisis such as the world is currently experiencing, to financing exclusively assets and activities adapted to a carbon-neutral world.

To date, the spotlight has been trained on assets at risk from transition, which initial investigations carried out in 2018 by a few European financial authorities have estimated at some 10% of banks' balance sheets. Emphasis has also been placed on green assets, which appear to constitute at best 20% of portfolios among even the most involved players. According to an EIOPA estimate,<sup>1</sup> they make up around 5% on average of European insurers' portfolios. However, not all assets between these two poles are neutral, and it is important that they too evolve.

To this end, the concept of transition finance has recently emerged.<sup>2</sup> This term was coined to describe financing for companies that are progressively reducing their carbon emissions. Criteria for debt instruments are currently being explored. The European taxonomy project also includes a category for businesses in transition. However, criteria capable of completely eliminating the risk of greenwashing have yet to be defined. To this end, release of the *'Framework for Financing a Whole-of-Economy Transition'*, promised for November by Mark Carney, now climate advisor to the UK Presidency of COP26, is a step awaited with great anticipation.

### The global health crisis highlights the need to make

#### Just Transition a reality

The concept of Just Transition, born several years ago, is finding its first operational response in impact debt tools such as sustainable bonds and loans along with their various permutations. The European taxonomy attempts to take this into account as well, with the introduction of minimum social criteria for an activity to be considered sustainable. The challenge today is to generalise this notion within the financial sector to ensure that the low-carbon transition can be socially acceptable. This process also reflects a desire on the part of those providing financing to achieve greater impact by linking social and environmental issues, as proposed in the structure of the Sustainable Development Goals.

1 <https://www.eiopa.europa.eu/content/eu-sustainable-finance-taxonomy-perspective-insurance-and-reinsurance-sector>

2 See for example: <https://www.climatebonds.net/transition-finance/fin-credible-transitions>

## **Deploying strategies in line with the Paris Agreement and achieving net-zero emissions by 2050**

For the past two years, this ambition has gained ground as the search for a suitable methodology continues. First made by public development banks, this commitment is being extended to the private financial sector. It is also taking root among companies, whether spontaneously or under pressure from investors, who are making it an increasingly explicit requirement. The publication of undisputed sector scenarios and national transition strategies worldwide would greatly facilitate these alignment strategies.

## **The need for accurate and relevant information**

Despite efforts to increase transparency on climate-related risks and opportunities, the financial community considers that companies still fail to provide them with the practical information needed to make informed financial decisions. Likewise, the climate, environmental and broader sustainability performance of financial products and services that claim such ambitions remains difficult to assess and compare. Any resolution of these issues will entail a generalisation and standardisation of mandatory disclosures, which is something regulators can impose. Europe is well on the way to achieving this already. The creation of open-access, verified databases would facilitate access to this information. Meanwhile, artificial intelligence tools are beginning to emerge to analyse this data and provide guidance for decision-making.

## **Orienting the public money earmarked for crisis recovery is a critical issue**

Lastly, a further issue arises from the coronavirus pandemic and the massive public funding deployed to revive the world's economies. This situation calls for environmental and social considerations to be taken into account in choosing priorities for funding and measuring their impact. While emergency measures to date appear more conservative than transformative, it is important that the recovery plans currently being designed and deployed not be a missed opportunity for building a more sustainable, low-carbon economy.



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