Investment Leaders Group Forum

17 May 2016

Royal Society
6-9 Carlton House Terrace
London SW1Y 5AG

Your Royal Highness,

Ladies and gentlemen,

I am honoured to speak in front of such a distinguished audience. Bruno Bézard, Head of the Trésor, would have been very happy to be here but unfortunately, he has pressing European matters to address and has asked me to replace him.

It is a pleasure meeting you, here in this wonderful city. And this place is close to another one, Carlton Gardens, where the Général De Gaulle and the Free French Forces had their headquarters from June 1940 to June 1944.

It is a place dear to all French people and a great symbol of the close links that unite France and the United Kingdom.

It is also a place that tells you something about how important it is to rise to challenges, not to fear to be lonely if you're certain to be doing the right thing. And a place that is a testimony of what could be achieved.

COP21 achievements

In terms of achievements, 2015 has been a great year.

Almost a month ago in New York, 175 of the 195 parties to the UNFCCC [UNF Triple C] signed the Paris Agreement. An agreement reached last December, concluding a round of discussions that started after the 2011 Durban summit.

The Paris Agreement has sent a strong signal to the world and to the global financial sector. Governments from around the globe have firmly committed to hold the increase in global temperatures well below 2°C, to increase the resilience of their economies and to make financial flows consistent with a 2° pathway.

Those objectives do not only concern governments. Non-State Actors have a critical role to play in this regard and that's why, the French presidency together with the Peruvian presidency launched the LPAA – Lima-Paris Action Agenda that especially mobilized the business world.

Among the business community, there was a number of remarkable financial institutions, including some of you. Financial institutions that demonstrated how finance could be part of the solution and made it clear that they were already rising to the climate change challenge and needed governments to act to be able to do even more.

Your mobilization played a key role to help deliver the Agreement. A role that leveraged and complemented the efforts of governments, but also of a number of other players. And let me here, in this academy, pay tribute to the efforts of climate scientists that provided the ground for raising this global discussion to a higher level.

Why finance matters for the transition toward climate resilient & low carbon economies?

Now that the Paris Agreement provided a strong policy signal, we need a climate-smart financial sector. This is what drove our COP presidency agenda regarding finance.

Achieving the low-carbon transition will require some dedicated investments. In this respect, some figures, running in the thousands of billions of dollars may obfuscate the understanding of the challenges.

Given the projected growth of population and the development of new cities, necessary investments in infrastructure, land and energy management amount to USD 89 trillion from 2015 to 2030 or USD 6 trillion/year. It is then estimated that a 5% net increase (representing USD 4.1 trillion, i.e. USD 300 billion/year would be enough to reach a decarbonized world.

So the transition requires the mobilization of capital toward green investments but it is primarily a capital reallocation issue. We need to deliver climate consistent infrastructures for energy, transportation, cities, etc. Just to pick up one example, the journal *Applied Energy* published an article earlier this year demonstrating that any new coal power plant build after 2017 will lock in carbon emissions that will make it very probable that the 2°C goal won't be achieved. This confirmed similar findings that the IEA published five years ago.

Achieving this climate-consistent capital allocation requires efficient climate policies. This is what governments committed to in Paris in their INDC, this is what needs to be delivered soon as time is pressing.

But the efficiency of these policies that somehow will be pricing the carbon externality at a global level could be greatly enhanced by a financial sector that is able to understand these issues and anticipate the impact of the policies both in terms of risks and opportunities.

Understanding that stringent climate policies are on their way – and, noticeably, regardless of the Paris Agreement just think of the EU 2030 climate and energy framework – will lead to the early recognition of the changing economics of fossil-fuel related activities and assets, avoiding a large scale stranding of assets. It will also lead to smarter investments in renewable, energy efficiency, etc.

Understanding that climate change will have consequences will help mitigating the various impacts of climate change and improve resiliency.

In the end, fostering a business oriented appropriation of climate related issues by the financial sector is a critical complement to efficient climate policies. It turns the financial sector from being a passive player to being the most important amplifier of the policy signal, both making it more effective and accelerating its impact, almost frontrunning it.

How the financial sector is responding?

There are three drivers in the business-oriented appropriation of climate-related issues: reputation, demand and economics.

As for most financial institutions, your reputation is a key asset underpinning your business. So much of finance has to do with trust that reputation may be as valuable as cleverness. As such, NGO and the wider civil society have played a key role in raising these issues.

However, having an excellent reputation does not necessarily entail you invest in a smart way that takes account of factors such as climate change nor does it ensure that you're actually contributing effectively to the transition. And while some institutions can consider themselves as being in the business to address bigger issues, not all institutional investors could act solely or primarily on the basis of its transition related impact.

Client demand has been the next driver for change. Some institutions have sought to design SRI solutions that both match client's preferences and deliver value. Some financial institutions may be more agnostic about climate change but will nevertheless try to accommodate the perceived demand for green assets. This has prompted very interesting innovations, most of which trying to address supply-side problems to bring green assets to the market: green bonds, infrastructure investments, yield cos, etc. – I won't have time to further discuss these innovations but they do matter a lot.

But here again, this driver has its limitations and drawbacks. Acting primarily to accommodate client demand may lead to greenwashing, especially if green assets are relatively scarce or difficult to bring to the market. And scarcity may lead to another problem: green bubbles which when they deflate may cause significant harm to the transition.

In the end, a better understanding of the economics of climate change may be the driver that moves actors farther and in a more sustainable manner. While reputation may only get you to address the most visible issues and clients' preference could vary, recognizing the challenges and opportunities ahead is key to contributing to a climate-consistent capital allocation. No matter how your regulation is designed, whether it is articulated around the notion of fiduciary duty or embedded in a prudential approach, the understanding of the changing economics of climate change and of the low carbon transition has to have an impact on your investment strategy and practices.

Reputation, demand and economics. This is what we should try to leverage on. And I think that your group is remarkable on these three dimensions and I'm confident that you will demonstrate a true leadership about how one's reputation, one's drive to satisfy client's demand and one's understanding of the economics of climate change both in terms of risks and opportunities could make a huge difference.

Developing policy

As I mentioned, the French COP21 presidency wanted to be ambitious and consistent, ensuring that all policy area had taken on board the climate urgency. Not as a conflicting objective but to ensure a proper alignment of policies.

As a financial regulator, I was asked to foster a global engagement with the financial sector – private and public financial institutions, regulators, supervisors, etc. This has been a journey worth taking.

Fortunately, we were able to build on previous work, most notably a white paper on financing the low carbon transition we prepared for more than two years and published in 2014.

Leveraging on these initial ideas and contacts, we tried to support, encourage and bring together leading institutions that demonstrate their willingness to "be serious about climate change". The early milestone of this engagement has been the Ban Ki Moon summit in September 2014, leading to the Climate Finance Day in May 2015 when some investors started to take action on a wider scale and culminated during the COP itself when some of you demonstrated that it was possible to “go mainstream” on a very wide scale. While many actors were considering how to address these issues or act on their intuitions, “de-siloing” the approaches and ensuring the wide disseminations of knowledge and ideas has been a constant objective.

As closing the knowledge gap was and still is a big issue, another challenge has been to mobilise some critical part of the financial ecosystem, such as research teams, rating agencies and academics.

Another dimension has been to ensure that global policy makers were seizing the moment.

Initial discussions among G20 members have been interesting but soon the FSB was asked to start looking at these issues. To be honest, we thought that there was a possibility that it could happen but weren’t sure that the probability was very high – yet, we thought it was the right thing to do and so did Mark Carney when we reached out. Barely a year after that discussion, the FSB mandated a task force on climate-related financial disclosures that has just published its interim report and a dedicated G20 study group is making significant progress towards a common agenda around these issues.

At EU level, we’ve raised these issues with our German and Swedish colleagues last fall. Here again, past the initial discussion, the momentum is growing fast and the UK, the Netherlands, Italy and others are very actively engaged.

Mindful of the need to ground this international outreach into real policies, ministers also asked us to move forward in implementing policies at domestic level.

The Energy Transition Act, discussed in Parliament in 2014-2015 and passed last summer, included a series of provisions related to that agenda.

First, on corporate disclosure. Because investors cannot act without data and information, some provisions require listed firms and large unlisted firms to disclose carbon emission beyond the usual scope 2 as well as the financial impact of climate-related developments. This is very much in line with the rationale of the FSB’s TCFD.

Then, on investor reporting. Building on a previous reporting requirement for asset managers, French asset managers and institutional investors are now required to report how they take into account ESG factors in their investment strategy and policy both in terms of analysis and action, with a strong focus on climate. The aim of this reporting is not to force institutions to do specific things but to ensure that they did ask themselves important questions and to accelerate the emergence of industry-wide best practices. The secondary legislation, adopted during the COP21, provides a reporting framework that could guide the reporting of any institutions wishing to explain how it is addressing climate-related issues.

Finally, on risk assessment. We are currently very actively working with the Banque de France which is also the banking and insurance supervisor on how to assess climate-related risks in the banking sector, preparing a report that is due to the Parliament before the end of this year. In doing so, we hope to close a number of knowledge gaps and to "de-silo" knowledge within the banking sector as well as with the insurance sector, MDBs and bilateral agencies, etc. In some sense, while the report was mandated well before the Bank of England published its insurance report, it could be understood as the sister report on banks.

It will be a lie to pretend that delivering these policies has been easy. We're faced at time with resistance or at least reluctance. And developing rather new policies requires a combination of innovation and humility. But the high-level objective was always clear to us: to prompt action and to raise the level-playing field. Through these policies, we do not pretend we know better but we seek to ensure that those whose job is to know are seriously considering these issues and acting on it.

In the end, I must say that on balance, the French financial ecosystem has been rather receptive. Maybe the fact that Paris is home to a large and vibrant ESG asset management community with 580 billion euros of assets under management being either managed with a SRI mandate or invested with an ESG integration dimension, the pioneering work of French issuers, underwriters and investors in the green bond market or the appropriation of these issues by leading insurance companies have made it easier. And I certainly hope that our policy leadership will contribute to maintaining a strong momentum, fostering the development of players that could contribute to the transition not only in France but more widely.

Let me conclude briefly. Like today, we must all remain mobilized to ensure the mainstreaming of climate issues into the inner workings of the global financial system. Private and public-sector led efforts must continue to amplify this momentum. In 2015, we have just gone through the first toll booth on the highway to a 2°C world. Many kilometers remain but I'm confident that, with everyone's efforts, we will manage to reach our final destination.