A POLITICIAN'S VIEW

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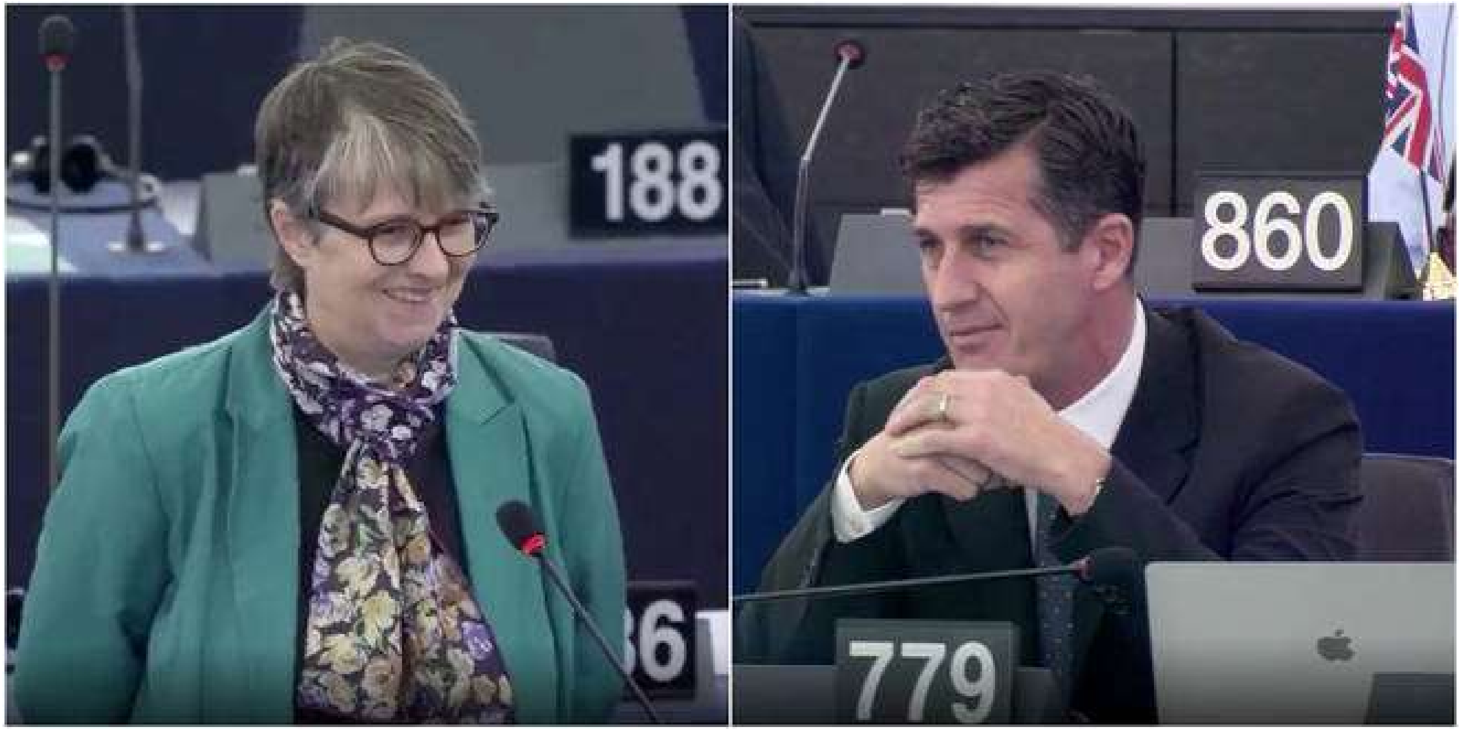
DUAL PERSPECTIVE

Served on ECON

But also a Professor of Economics!



WHERE ARE WE GOING?

- The Parliament’s initial position – my initiative report
- The complex tale of mandatory disclosure (SFDR)
- The Taxonomy – when science meets politics
- Climate benchmarks – a sign of hope?

MY INITIATIVE REPORT

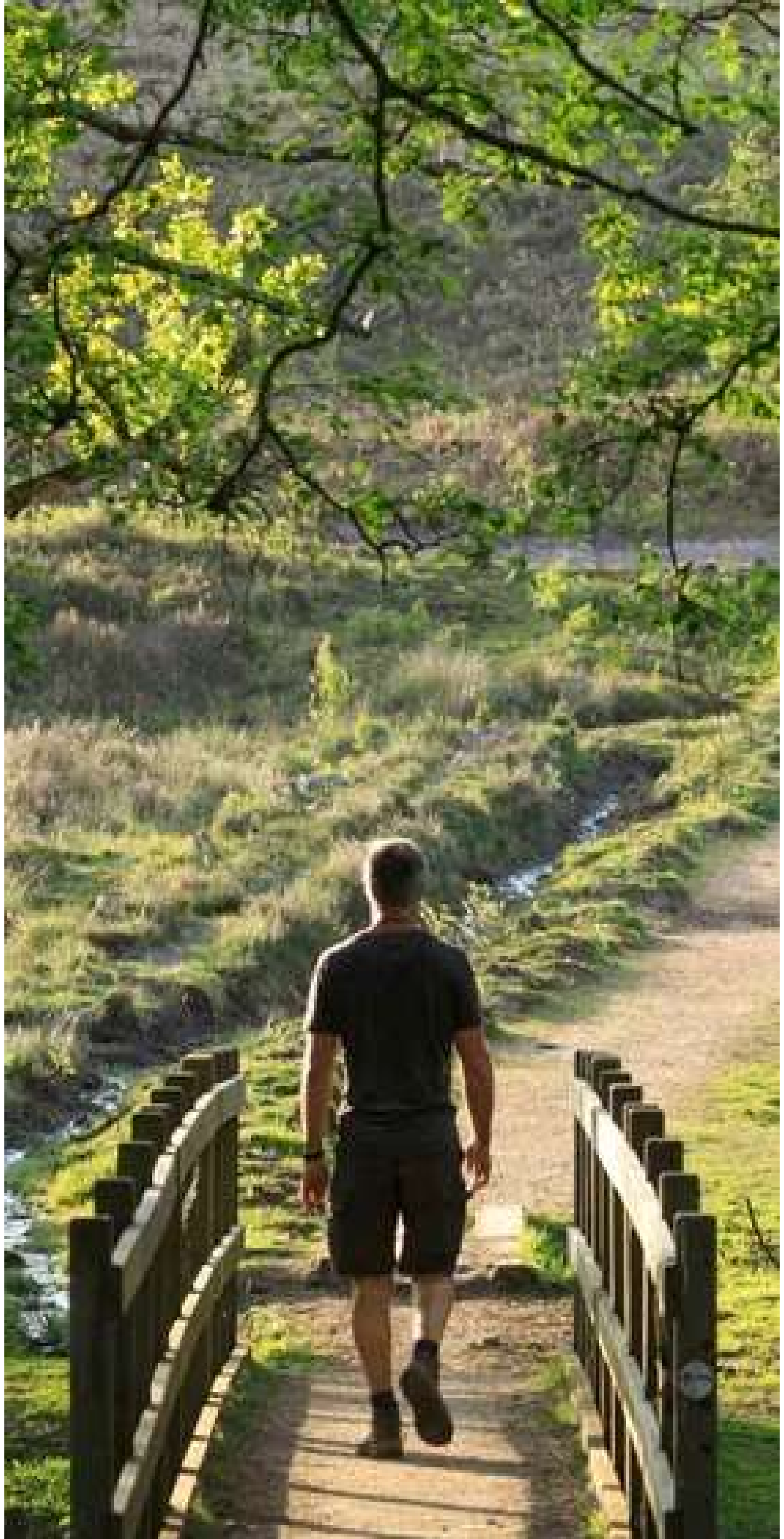
- We were clear about the sequencing
- The need for consistency
- Using existing metrics where possible
- And scientifically based data, not policy reports
- Not much of this was taken up in the proposals from the Commission!

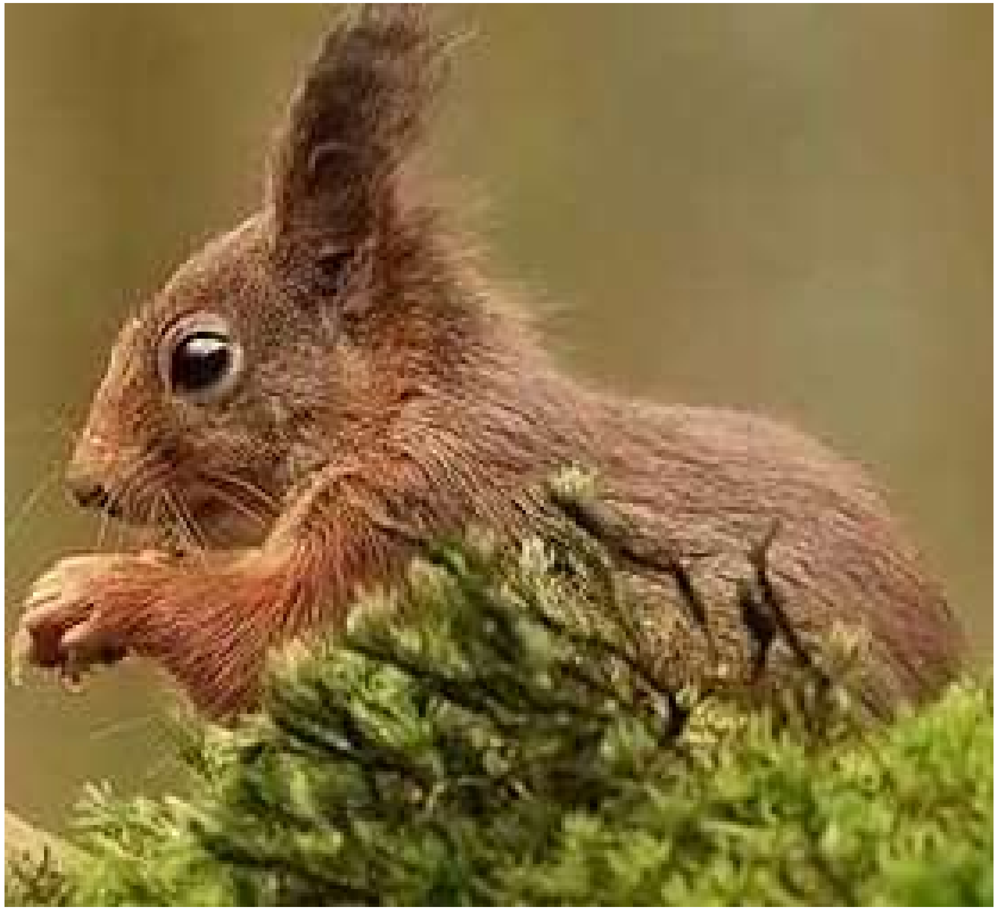
SFDR:A QUICK RECAP

- The first mandatory disclosure regime in the world
- Three articles became important:
  - Article 6: funds that do not integrate any kind of sustainability – could include tobacco companies or thermal coal producers
  - Article 8 applies “where a financial product promotes, among other characteristics, environmental or social characteristics”
  - Article 9, for bespoke sustainable investments “where a financial product has sustainable investment as its objective and an index has been designated as a reference benchmark.”

SFDR—WHAT WE INTENDED

- Mandatory disclosure—not definitions
- Our compromise was the comply-and-explain let-out
- Heavy-energy industries and member states dependent on fossil fuels were strong opponents
- When did the Art. 6, 8 and 9 definitions come into the picture and from whom?
- Industry has turned a requirement for reporting in a labelling regime





SFDR—WHAT WE GOT

- Transparency? Hard for fund managers to choose between categories
- Clarity for investors? Complexity of reporting has led to dependence on unreliable data vendors and reports rather than metrics
- Encouraging greenwashing? By 2022, Meager was reporting that around eight in ten funds labelled as sustainable (or 'light green') are invested in fossil fuel companies
- Streamlining: Failure of regulatory alignment?

WHAT IS REALLY SUSTAINABLE? EU TAXONOMY

Climate change mitigation

Climate change adaptation

The sustainable use and protection of water and marine resources

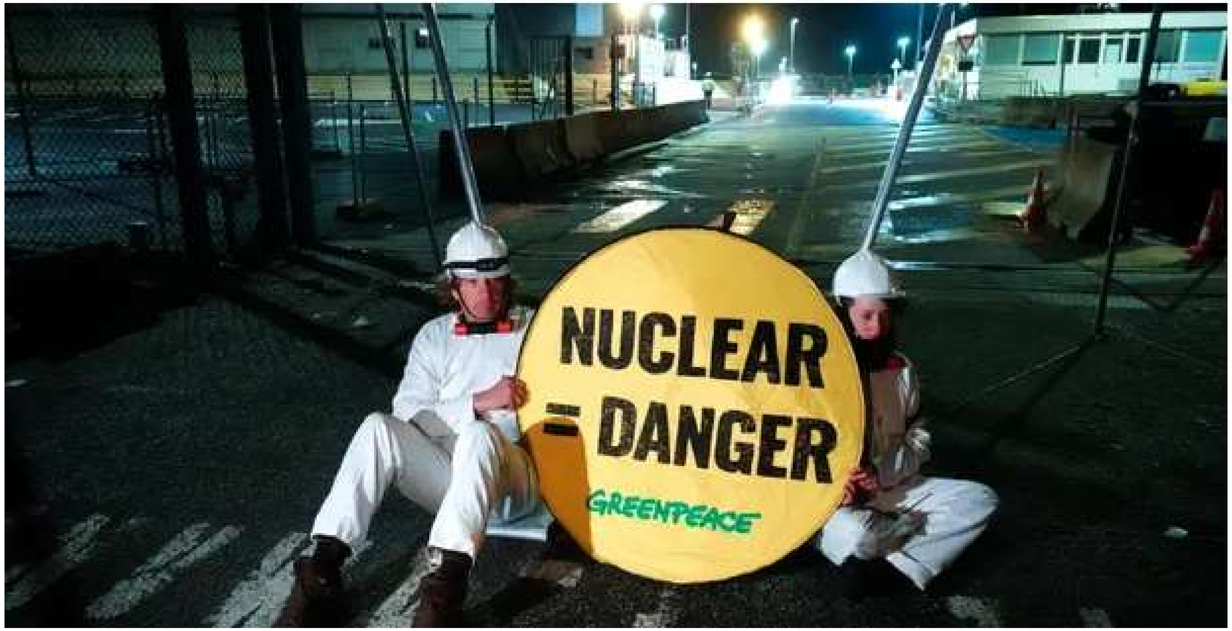
The transition to a circular economy

Pollution prevention and control

The protection and restoration of biodiversity and ecosystems

EU faces legal action after including gas and nuclear in 'green' investments guide

European Commission accused of acting unlawfully in two separate cases bought by environment groups



THE TAXONOMY GETS POLITICAL

- Essential first step—unless we know what is Green we cannot create financial incentives for investors
- To prevent greenwashing we need to have clear definitions of what is sustainable
- But this creates stasis whereas we need a rapid and dynamic transition
- Because of definitional weakness, politicians and lobbyists watered this down
- What is the future for the taxonomy now gas and nuclear are defined as sustainable?

EU SUSTAINABILITY BENCHMARKS

- Many investors rely on benchmarks in particular in portfolio allocation and to measure the performance of financial products
- Two new benchmark classifications—EU Climate Transition Benchmarks (EU CTB) and EU Paris-Aligned Benchmarks (EU PAB)
- Administrators of benchmarks that pursue ESG objectives must (i) publish an explanation of how key elements of the methodology reflect ESG factors; and (ii) explain in the benchmark statement how ESG factors are reflected for each

WHY THE BENCHMARKS WORK

Paris-Aligned benchmark is for companies and investments that already conform to the highest climate standards—scientifically measurable – clearly in the green niche

Climate transition benchmark states in its own name that it is for directing investment towards companies that are undergoing transition to achieve such niche status within a stated timeframe – scientifically verifiable and dynamic

A MORE ACADEMIC VIEW

Introducing sell-by dates for stranded assets: ensuring an orderly transition to a sustainable economy

Molly Scott Cato & Cory Fletcher

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RISK FACTORS ASSOCIATED WITH ASSET STRANDING

- Environmental challenges (e.g. climate change, water constraints)
- Changing resource landscapes (e.g. shale gas, phosphate)
- New government regulations (e.g. carbon pricing, air pollution regulation)
- Falling clean technology costs (e.g. solar PV, onshore wind)
- Evolving social norms (e.g. fossil fuel divestment campaign) and consumer behaviour (e.g. certification schemes)
- Litigation and changing statutory interpretations (e.g. changes in the application of existing laws and legislation)

A 'DEFINITIONAL TRICHOTOMY'?

- Niche, transitional, or short-life?
- It is activities that will be eliminated *not companies*
- Without this distinction, politicians and lobbyists defend dirty activities
- Sustainable finance legislation then incentivises greenwashing and become counter-productive
- Must have dynamic pressure for transition – and keep the niche pure and tightly defined

NECESSARY CONDITIONS FOR SUCCESS

- A reasonable list of data with some smart summary metrics
- Clear, water-tight definitions with scientific backup that are not subject to political negotiations
- Dynamic rather than static legislation with clear incentives
- A clear sense of the transition pathway for the European economy

PHILOSOPHICAL VIEW

- The most ambitious policy suite in the world
- We were hardly likely to get this right the first time
- We are blundering our way in the right direction
- The sustainable finance agenda may save life on Earth if anybody can so it's an ambitious target and worth fighting for even when it feels tough!