Trade off between harmonised versus country specific sustainable finance standards in the Global South

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Overview

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3. Harmonised sustainable finance standards as a solution?
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1. Introduction

Appropriate a global sustainable financial governance framework

⇒ essential for mobilising sufficient investments to achieve the SDGs

⇒ Standards for defining, implementing and monitoring sustainable finance instruments, important role for further developing the market for sustainable finance instruments

One core obstacle to mobilise sufficient financial resources

= fragmented architecture of standards for sustainable financial instruments

⇒ various standardisation measures including criteria regarding the definition, disclosure, impact reporting and external reviewers exist

⇒ reduces investors' confidence in the integrity of the sustainable financial market

⇒ global financial governance is key to support the transition to a sustainable economy

2. Benefits + challenges of sustainable finance standards for investors

Benefits for investors

- Reference values for financial market participants
- Reduction of transaction costs for investors
- Increased transparency
- Strengthening of trust between issuers and investors
- Enhancing market integrity

Challenges for investors

- Proliferation of sustainable finance standards/ Market fragmentation
- Increased complexity
- Intransparency
- High transaction costs
- High cost of certification and verification

3. Harmonised sustainable finance standards as a solution?

Challenges of harmonsied sustainable finance standards in all countries

Designing a global sustainable financial governance framework that works in all types of countries is challenging.

=> country-specific circumstances have to be taken into account.

- development of financial markets: Institutions, depth of the market including actors, human resources capacities etc.
- Economic / industrial structure

⇒ A ‘one size fits all’ approach will not work.

⇒ A flexible approach according to the principle of proportionality is needed that takes into considers the development of a country’s financial market, the quality of its institutions and its human resources capacity, industry structures …

⇒ How can a we ensure interoperability of different standards?

4. Example: Green finance taxonomy

Green finance taxonomy (GFT):

= set of criteria for assessing whether and to what extent a financial asset is green

= Important tool for attaining sustainability goals

Reason: sustainability goals aligned with high-level policy objectives such as carbon emission reduction according to Paris agreement

4. Example: Green finance taxonomy

Effectiveness of taxonomies in contributing to sustainability objectives

depends on: investors' interest in assets with taxonomy based labels.

=> taxonomies increase investor interest

=> raise market transparency

=> Taxonomies secure market integrity by assuring that those assets that cannot deliver the sustainability performance that is needed for the label are evident to investors.

=> Market integrity, in turn, contributes to maintaining investor interest in sustainable financial markets over the longer term

Design of Sustainability Taxonomies

Which sustainability goals are targeted?

- Focus on environmental goals
- Independency or interlinkage of objectives

Objective

Scope

Which economic sectors and activities are covered?

Industrial classification system
Eligibility of sectors and activities

How is the purpose translated into measurable targets?

- Unit of measurement
- Thresholds

Target

Outputs

What types of information are reported? Who reports?

- disclosure requirements
- Data availability
- Verification systems

4. Example: Green finance taxonomy

Benefits for investors

- Assess investment portfolios for taxonomic alignment
- Find new investments' taxonomic alignment
- Design investment and product policies and strategies
- Enlarge disclosure to enable taxonomic assessments

Challenges for investors

- Market fragmentation: No uniform taxonomies worldwide
- Increased complexity: detailed approach
- High transaction costs to compare GFTs

4. Example: Green finance taxonomy

Challenges of taxonomies for investors

- Market fragmentation: No uniform taxonomies worldwide

⇒Trade-off between harmonised and country specific taxonomies considering country specific circumstances

⇒Interoperability of taxonomies is crucial for investors

Design of Sustainability Taxonomies: Global South

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Policy alignment = challenge

- policy frameworks insufficiently designed
- governments lack of capacity.
- weak institutions
- limited market structures

=> Fewer objectives

Objective

Scope

Economic sectors and activities

- Different industry classification systems worldwide

⇒ Mapping of classification systems or

⇒ Agree on one classification system

Thresholds

- stronger focus on relative improvements than on universal static thresholds

Target

Outputs

Information

- disclosure requirements
- Data availability weak
- Verification systems less developed

=> Capacity building support

5. Conclusion

Trade off between harmonised versus fragmented sustainable finance standards in the Global South

Interoperability of taxonomies is crucial for investors, in particular if the primary objective is to attract foreign investments

=> A ‘one size fits all’ approach will not work

=>A flexible approach according to the principle of proportionality is needed that takes into account the development of a country’s financial market.

=> strike an appropriate balance between interoperability and local applicability

Possible solutions:

- General framework based on principles allowing country specific design?
- Common Ground Taxonomy (EC)?

Thank you!

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