Central banks take on climate change

'Coalition of the willing' hopes to lead by example

by Danae Kyriakopoulou in Davos

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For the third year in a row, climate-related threats topped the worry list of global leaders surveyed by World Economic Forum. Following a year of unprecedented occurrence of natural disasters, from wildfires in California and Greece to floods in India, Japan, Korea and Nigeria, and earthquakes in Indonesia and Papua New Guinea, it is perhaps unsurprising that leaders are concerned.

The survey set the scene for a heavily climate-focused agenda at the WEF annual meeting in Davos. Starting with an award to British natural historian David Attenborough, the week continued with sessions on 'climate leadership', 'safeguarding our planet' and 'building sustainable markets'. It ended in spectacular fashion, as an estimated 70,000 students around the world went on 'climate strike'. They were inspired by 16-year-old Swedish climate activist Greta Thunberg's 'School strike 4 climate action' campaign.

Addressing a packed audience of world Leaders at Davos, she said, 'Some people say the climate crisis is something that we have all created, but that is not true, because if everyone is guilty then no one is to blame. And someone is to blame. Some people, some companies, some decision-makers in particular, know exactly what priceless values they have been sacrificing to continue making unimaginable amounts of money.' Thunberg has been invited to be the opening plenary speaker at next year's WEF.

In a separate panel, International Monetary Fund Managing Director Christine Lagarde termed climate change as one of the most pressing issues for the global economy. Even central banks, banks and insurance industries would need to take it into account in their decisions, she said. And they are. As 1,500 private jets flew into Davos to discuss climate change, the Central Banks' and Supervisors' Network for Greening the Financial System was holding its latest steering committee meeting in Mexico City.

The NGFS was set up by the Banque de France in December 2017. The network believes climate change is not only a threat to the environment and ecosystems; it also jeopardises the world's economy and financial system. Natural disasters and extreme weather conditions – triggered by climate change – pose a physical risk to financial assets. A transition risk arises from the costs the economy will have to bear in responding to the threat of climate change.

Self-described as a 'coalition of the willing', in only a year the NGFS has grown from eight founding members to 24. These include central banks from Africa, Asia Pacific, Europe and Central America. Last month, the group welcomed four new members, bringing the total number to 28. They are united in their belief that – in the words of Frank Elderson, board member of De Nederlandsche Bank and chair of the network – 'central banks have to lead by example'. But there is still plenty of variety within the broad umbrella of the coalition. The People's Bank of China is the only central bank with a dedicated policy to promote green finance through monetary policy. In contrast, Germany's Bundesbank 'takes green finance in monetary policy with a pinch of salt', according to Henner Asche, its deputy director general for markets.

Given the Bundesbank's conservative approach, it is surprising that it was chosen to chair the NGFS's workstream on 'scaling up green finance'. This will explore what central banks can do to support the transition to a more sustainable economy. Items on the workstream's agenda range from consumer protection against greenwashing to how central banks can adopt a dedicated green policy to manage their foreign exchange reserves. The network has two other workstreams. The first, chaired by the PBoC, focuses on how to supervise the financial sector while ensuring climate risks are taken into account in their decision-making. The second, led by the Bank of England, is on developing an analytical framework for assessing climate-related risks to the macroeconomy. In other words, putting a price on Thunberg's 'priceless values' (or rather on the risk of their absence) and mandating the financial sector to internalise the externalities of climate change in their decisions.

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