



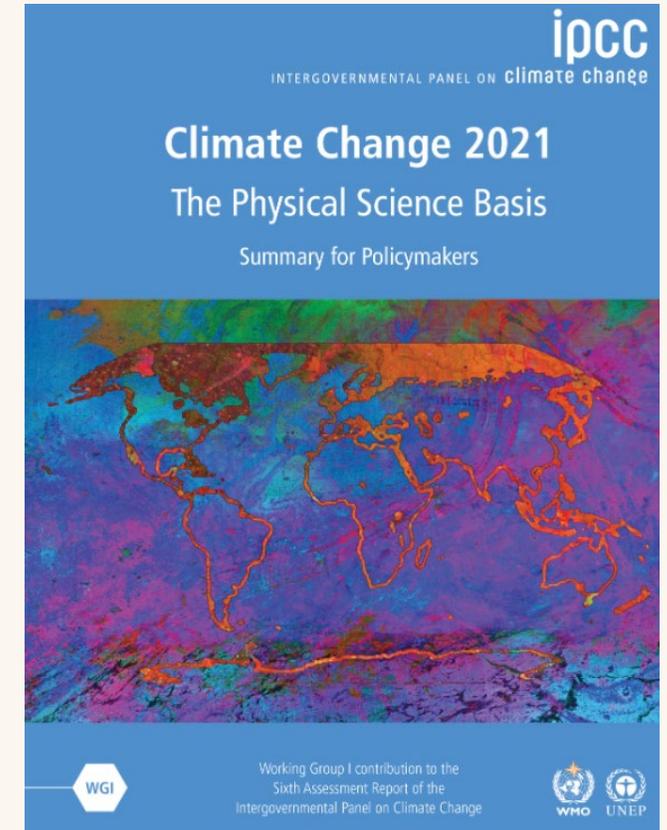
# Monetary Policy Approach to Green Growth

Green Growth Forum on 14 September 2021, Lahti and online

# Climate change as a long-term challenge

The 6<sup>th</sup> IPCC report paints a gloomy picture:

- More precise estimates compared to the 2013 report
- Global temperature has risen 1,1 degrees since pre-industrial times; mainly caused by human activities
- +1,5 degree will be reached by the early 2030s
- CO<sub>2</sub> concentration increases, sea levels rise, glaciers partially melt, more extreme weather events



# Central Bank's role in addressing the climate change

## Differing views:

- *“Climate issues are not the responsibility of the central bank, who should focus solely on price stability”*
- *“The central bank should be involved in climate issues (only) to the extent that they have impact on the objective of price stability and financial market stability”*
- *“Central banks must play an active role in combating climate change”*

FEDERAL RESERVE

## Powell says climate change is not a main factor in the Fed's policy decisions

PUBLISHED FRI, JUN 4 2021-8:07 AM EDT | UPDATED FRI, JUN 4



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The New York Times

## Why the Fed, Long Reticent, Has Started to Talk About Climate Change

## THE WALL STREET JOURNAL.

MARKETS

## Central Banks Jump Into Climate-Change Policy Fray

Some say regulators are going beyond their remits with focus on risks to financial systems and economies



U.S. MARKETS | NOVEMBER 20, 2020 / 3:12 PM / UPDATED 9 MONTHS AGO

## ECB has no mandate for direct role in climate change fight: Weidmann

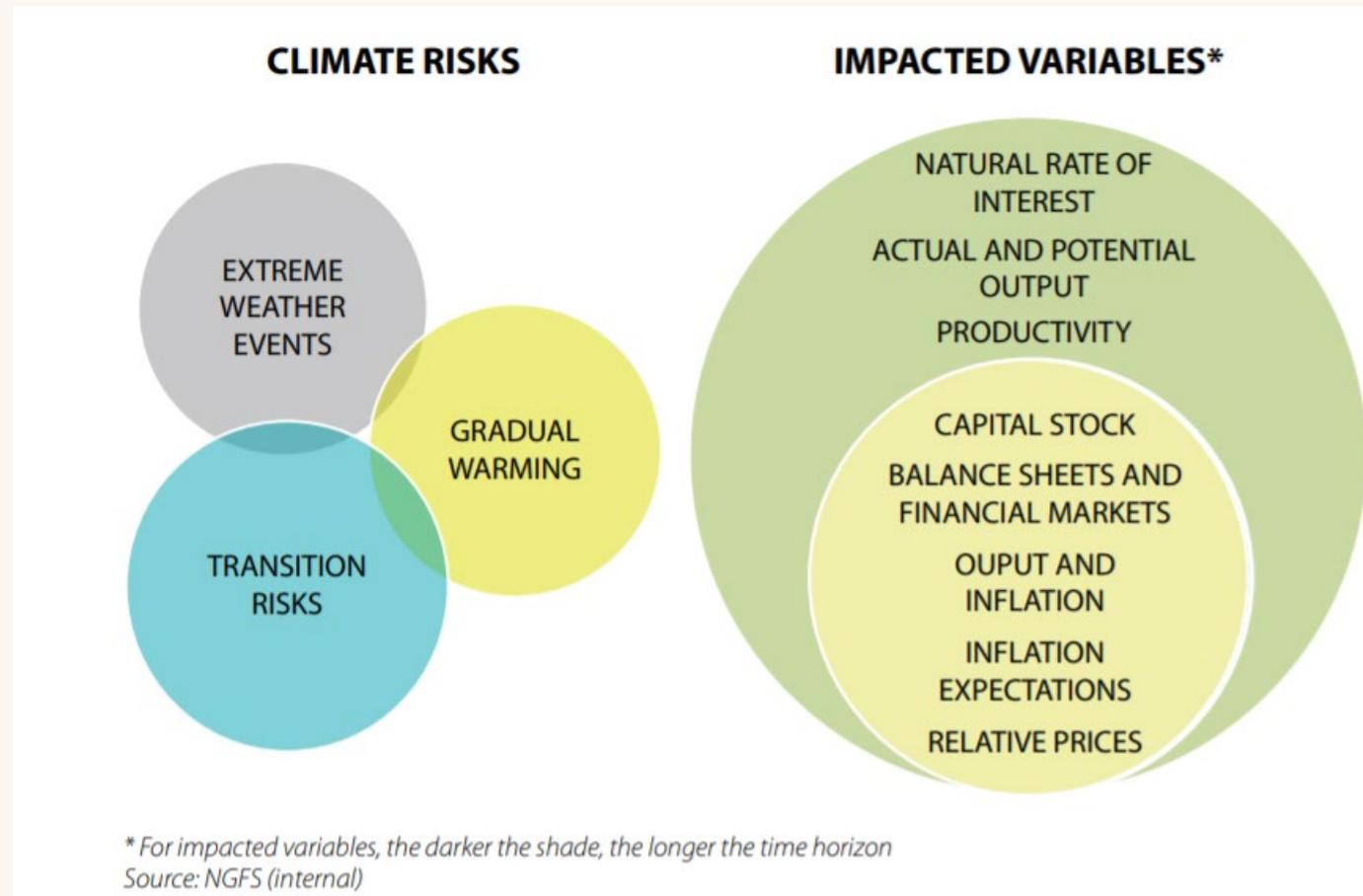


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## Bundesbank chief u-turns on climate-tilting ECB bond purchases

President Jens Weidmann also joins call for mandatory climate change disclosure

# Why central banks are concerned about climate change



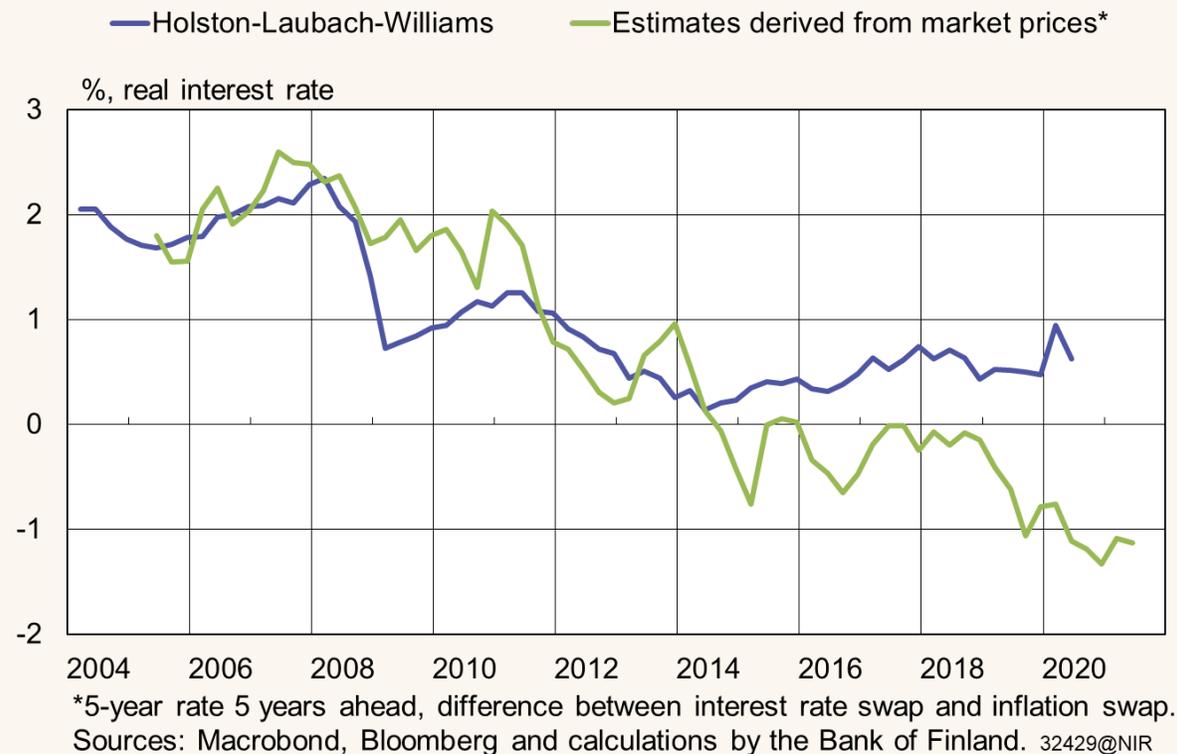
Modified from <https://www.ngfs.net/en/climate-change-and-monetary-policy-initial-takeaways>

# ECB's primary objective: maintaining price stability

- Climate warming, increase in extreme weather events, uncertainty and climate policy implications affect price stability
  - Both direct and indirect price effects through multiple channels
  - Both short-term and long-term price effects
  - Increases in inflation volatility
- The transition to a low-carbon economy entails changes in relative prices
  - Prices for carbon-intensive products and inputs should rise relative to low carbon ones.
  - It should happen steadily and gradually without accelerating inflation
- There can be differences in climate policy instruments in terms of price effects (e.g. carbon taxes vs. emissions trading)

# Climate change affects productivity and equilibrium real rate, and hence the room for manoeuvre for monetary policy

## Estimates of the equilibrium real rate of interest in the euro area



# Central Banks supporting green growth

- Massive investment needs
- Price stability helps maintain interest rates that support investment
- Contributing to financial stability and efficient functioning of financial markets
- Involvement in green funding through asset purchases
  - The Eurosystem already buying almost a quarter of eligible outstanding green bonds.
  - For example, the Bank of Finland's thematic assets alone exceed 500 million dollars.
- Research analysis and statistical data

# Monetary policy strategy review: July 2021

- Climate change consideration was part of the ECB monetary policy strategy evaluation this summer.
- The evaluation examined also e.g.
  - the definition of price stability (a symmetric 2% inflation target);
  - monetary policy instruments and their effectiveness;
  - economic and monetary analysis;
  - the ECB's communication policies.

# ECB Climate Action Plan

## Climate change considerations to be incorporated:

1. Developing new macroeconomic models and analysis
2. Developing new indicators for risk analysis
3. Climate related disclosure considered as a criterion for collateral and asset purchase
4. Emphasizing risk assessment capabilities such as climate stress tests and internal ratings to incorporate climate change risks
5. Incorporating climate change risks into the collateral framework
6. Taking climate change risks into account in corporate sector asset purchases

To be implemented by 2024 at the latest.

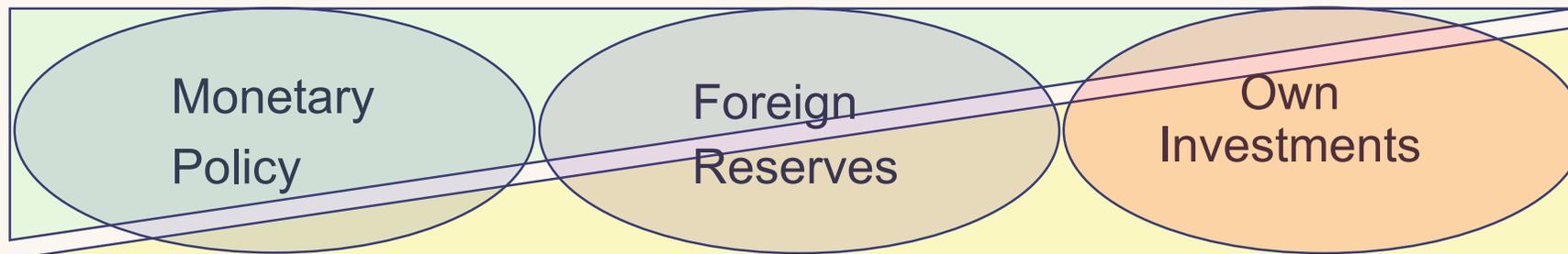
# The ECB roadmap of climate change related actions in 2021-2024

- **First milestone: Reliable data**
  - Gathering data needed for climate change risk analysis
  - Adapting models and make them fit for climate change
- **Second milestone: Knowledge**
  - Checking own exposure to climate risks
  - Checking firms' and banks' exposure to climate risks
  - Making disclosure of climate risks a priority
  - Reviewing how credit ratings reflect climate risks
- **Third milestone: Action**
  - Including climate risks into collateral framework
  - Making own asset purchases greener

# Bank of Finland's investment activities and new climate targets

# Decision-making depends on the portfolio

*Joint decision making*



*Independent decision making*

# Investment objectives

**Euro-**  
**denominated**  
**assets and**  
**long-term**  
**investments**

- **Liquidity**
- **Security**
- **Responsibility**
- **Return**

**Foreign**  
**Reserves**

# Developments within Responsible Investment at the Bank of Finland

## Action points delivered

- Responsible Investment strategy and norm-based screening
- Internal responsible investment working group
- NGFS-membership
- Signatory to the UN backed Principles for Responsible Investment (PRI)
- Full-time Responsible Investment Specialist
- Publishing Responsible Investment Policies
- Finsif (Finland's Sustainable Investment Forum) membership
- Carbon intensity calculations
- Using norm-based screening on external fund managers and own investment counterparties

## Current and future action points

- Publishing own investment climate targets (09/2021)
- Extensive climate data procurement (2021) and implementation (2022)
- Wider use of TCFD-recommendations on climate risk and opportunities reporting
- Active participation in working groups to promote sustainability (Eurosysteem, NGFS, Finsif)
- Common goals within the Eurosysteem to disclose climate risks

# The new climate targets for our own investments

- Broad target covering all own investments (initially excl. gold)
  - Fixed income incl. government bonds
  - Equities
  - Real estate
- Carbon neutrality by 2050 at the latest
  - All Kyoto protocol greenhouse gases
  - Scope 1+2 to start with, Scope 3 can be added once calculations, methodologies and coverage increase
- Interim targets to be published later this year
  - Exclusion thresholds on fossil fuel investments
  - Emission reduction targets on equity investments
  - Qualitative targets on external fund managers and supranational investments

# Concluding remarks

- Climate change is a long-term phenomenon that permanently changes the operating environment of central banks.
- The new ECB strategy highlights climate change topics.
  - The roadmap that sets out the practical action plan is ambitious but realistic.
- The Bank of Finland has set a carbon neutrality target for its own investments.
  - This complements the Bank's own climate programme relating to the Bank's own activities.



*Thank you!*

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