

## **Sustainability: a role for central banks?**

Speech by Klaas Knot at the CEP/DNB workshop 'Central banking & Green Finance'

Amsterdam, 28 November 2017

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Ladies and gentlemen,

Welcome to the workshop on 'Central banking and green finance'.

I would like to thank all of you for participating, specifically the Council on Economic Policies for initiating a workshop on this important topic and the authors and discussants for their contributions.

Green finance, and in a broader sense, sustainability, is a topic we consider as very important here at DNB. Before explaining why DNB focusses on sustainability, it's good to know what kind of an organization DNB is.

DNB is an independent central bank, supervisor of banks, pension funds and insurers, as well as the resolution & DGS authority. The official mission of DNB is to safeguard financial stability and thereby contribute to sustainable prosperity in the Netherlands.

But what is sustainable prosperity? Prosperity that is durable in the long run.

There are both financial and non-financial elements to this. If financial institutions have insufficient buffers to cover unexpected significant losses, this may hamper sustainable development. Furthermore, the debt driven growth model from before the financial crisis is another example of prosperity that is not sustainable in the long run. At the same time, prosperity that results in major ecological damage, or prosperity that even puts a severe strain on a nation's social cohesion, is not durable in the long run either.

But even though we've existed for over 200 years, and even though we've always had the long-term view, this emphasis on sustainability is still relatively new. It started about 5 years ago, with a new board. But our focus on sustainability shouldn't be surprising. After all, our supervision is in part aimed at ensuring that financial institutions are able to meet their commitments, now but also in a few decades' time. And as a central bank we work to promote price stability and financial stability for today and in the future. Not taking relevant long-term risks and long-term prosperity into account, would be contrary to our mandate.

Therefore, in recent years we have done a lot of research on the topics of sustainability and climate change. DNB has published research and policy papers about a broad range of related topics, such as:

- the impact of the energy transition on the macro-economy,
- the risk of a carbon bubble,
- ESG investments by institutional investors,
- bottlenecks in green finance
- and most recently, the implications of climate change and climate policies for the financial sector.

Currently, we are developing a stress test for climate-related risks, which will build on the work done by our economic researchers on incorporating climate policies in macroeconomic models.

We believe the transition to a carbon neutral economy to be one of the most important long-term challenges for the economy. Changes in energy systems potentially have a major impact on the economy. And the Paris Climate Agreement implies that the transition to a carbon-neutral economy must be completed well before the turn of the century, within the expected life span of the homes and offices we are building today.

However, the world is still far removed from reaching the objectives of the Paris Climate Agreement. It is clear that much more investments are needed to reach our climate goals. This also raises the question which role central banks and financial supervisors should play in facilitating these investments.

We believe there is an important role here for central banks and financial regulators. For example, in our role of economic advisor to the government we have publicly advocated a climate law in the Netherlands to ensure a more attractive green investment climate. In our role as prudential regulator we are making sure that banks, insurers and pension funds are taking climate-related risks into account. And we've also played a catalyzing role by launching the Platform for Sustainable Finance. A platform where the financial sector and the public sector can cooperate in seeking ways to increase sustainable investments.

Recently, there has been debate about whether central banks and regulators should also directly use their monetary policy tools and macro-prudential policy tools to facilitate green finance. Should climate goals be taken into account when implementing QE measures? Should capital requirements be used to stimulate green investments or to discourage fossil investments?

Central banks are generally cautious when it comes to using its main policy tools for goals other its main objectives: inflation, financial stability. This is mainly because we believe that due to our independence – and with little democratic oversight – it is important for us to have a clear and limited mandate. A mandate to which we can be held accountable.

However, we do see the enormous challenge of limiting global warming, and the potential disastrous consequences if we do not act sufficiently to meet this challenge. We therefore think it is important to ask ourselves whether central banks and financial supervisors should play a more active role in facilitating green finance.

It's good to see that we are here today with a diverse group of academics, policymakers, financial sector representatives, central bankers and others to discuss these issues, on which I urge you all to have an open and interesting debate.