Fostering green investments and tackling climate-related financial risks: which role for macroprudential policies?

Discussion

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Overview

1. What does the paper do?

2. Should we implement prudential tools to achieve climate goals?

3. Addressing the desirability of prudential tools in the paper

NOTE: the views expressed in this presentation are those of the author and do not necessarily reflect the official position of the Dutch Central Bank (DNB)

What does the paper do?

- The paper starts with the problem of the “green finance gap”, i.e. additional financial resources needed for green investments (~ USD 14 trillion between 2010 and 2030)

- The study focuses on the question to which extent <u>prudential regulation</u> is a tool that policymakers <u>could</u> and <u>should</u> use to <u>foster green investments</u> and <u>mitigate climate related financial risk</u>.

- To that end it reviews the official central banks documents to map current green prudential regulations and then reviews the existing and novel prudential approaches to align finance with sustainable growth objectives.

What does the paper do?

- Possible prudential measures are put forward in a structured way, and innovative new potential options are identified.

- The paper also makes interesting points on differences in goals (and functions) between global central banks and policies that they already implement → interesting to elaborate upon a bit more

- Even though the paper mostly focuses on identifying what central banks <u>could</u> do, it also makes some statements about what they <u>should</u> do.
  - “macroprudential policy … should be concerned with financial stability and a climate-related objective”
  - “we suggest the implementation of a set of regulatory tools …”

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Should we implement prudential tools to achieve climate goals?

From a policy perspective, two key ways to increase financial flows to green projects:

1. Improving profitability of green projects
2. Removing barriers to otherwise profitable investments (e.g. barriers to long-term investments)

- Improving profitability: most obvious instrument is to tax brown projects and put subsidies on green ones (e.g. a carbon tax and innovation subsidies)
- Profitability could also be improved by decreasing the cost of funding, which is something that could potentially be achieved with monetary and/or prudential means. But effectiveness of these instruments is questionable and likely there are trade-offs with other policy objectives.
- Removing barriers in this paper seems to focus on impediments to long term investments. However potential trade-offs to financial stability (e.g. with respect to liquidity requirements).

Addressing the desirability of prudential tools in the paper

- Open question: in the whole spectrum of policy instruments, is prudential policy the most effective and efficient tool to use? How severe are unintended consequences?

- If the intention is to convince prudential policymakers to implement these measures, two additional pieces of analysis would be valuable (besides addressing questions about mandates):

1. The role of fiscal policies (why not use a much simpler/effective carbon tax?)
2. A framework to evaluate green prudential instruments, going a bit futher than pro’s and con’s

- NB: In case there is full alignment of objectives, a more straightforward case can be made – this is especially so if green policies also better address risks (e.g. a brown penalizing factor)

Recap

- Nice paper, puts forward innovative prudential policies that could stimulate green investments
- It would be interesting to elaborate a bit more on the green regulations that already exist (which types of regulations are we talking about; perhaps make it a full section?)
- Discuss the role of fiscal policies in relation to prudential policies and work towards a more elaborate evaluation framework (could be in this paper, or future research)

Thank you