The EU Action Plan on Financing Sustainable Growth

In 2015, landmark international agreements were established with the adoption of the UN 2030 Agenda and Sustainable Development Goals and the Paris Climate Agreement. The Paris agreement, in particular, includes the commitment to align financial flows with a pathway towards low-carbon and climate-resilient development. To achieve the EU's 2030 targets agreed in Paris, including a 40% cut in greenhouse gas emissions, we have to fill an investment gap estimated at 180 billion EUR per year.

The EU is already providing impetus to help attract the required investments with the European Fund for Strategic Investments and other initiatives. In 2017, almost one third of investments mobilised by the European Fund for

Strategic Investments (EFSI) were channelled into energy, environment and resource efficiency projects and social infrastructure. The EFSI 2.0 extends the fund until 2020 and raises investment targets to EUR 500 billion, with at least 40% of EFSI financing for infrastructure and innovation to support climate action projects.

However, the scale of the investment challenge is beyond the capacity of the public sector alone. The financial sector has a key role to play in reaching those goals. It can

- re-orient investments towards more sustainable technologies and businesses
- finance growth in a sustainable manner over the long-term
- contribute to the creation of a low-carbon, climate resilient and circular economy

"Re-orienting private capital to more sustainable investments require a comprehensive rethinking of how our financial system works. This is necessary if the EU is to develop more sustainable economic growth, ensure the stability of the financial system, and foster more transparency and long-termism in the economy. This thinking is also at the core of the European Union's Capital Markets Union (CMU) project".

The EU Action Plan on sustainable finance adopted in March 2018 aims to address this investment challenge. It is part of the Capital Markets Union's (CMU) efforts to connect finance with the specific needs of the European economy to the benefit of the planet and our society.

Understanding the EU Action Plan on financing sustainable growth

Sustainable finance is the provision of finance to investments taking into account Environmental, Social and Governance (ESG) considerations. Sustainable finance includes a strong green finance component that aims to support economic growth while:

- reducing pressures on the environment
- addressing green-house gas emissions and tackling pollution
- minimising waste and improving efficiency in the use of natural resources

It also encompasses increasing awareness of and transparency on:

- the risks which may have an impact on the sustainability of the financial system
- the need for financial and corporate actors to mitigate those risks through appropriate governance

The Action Plan is part of broader efforts to connect finance with the specific needs of the European and global economy for the benefit of the planet and our society. It aims to:

1. Re-orient capital flows towards sustainable investment, in order to achieve sustainable and inclusive growth;
2. Manage financial risks stemming from climate change, natural disasters, environmental degradation and social issues; and
3. Foster transparency and long-termism in financial and economic activity.

Key features of the Action Plan include:

- Establishing a common language for sustainable finance – i.e. a unified EU classification system (or taxonomy) of climate, environmentally and socially sustainable activities, thus defining what is sustainable and which investment areas can be most effective in terms of impact on sustainability.
- Creating EU standards and labels (e.g. an EU Ecolabel) for green financial products on the basis of an agreed EU classification system: this will help investors to identify investments that comply with green or low-carbon criteria.
- Clarifying the duty of asset managers and institutional investors to make sure they consider, in an appropriate manner, environmental, social and governance (ESG) issues in their investment decision process and are more transparent towards their clients, including by enhancing disclosure requirements).
- Requiring insurance and investment firms to advise clients on the basis of their preferences on sustainability.
- Incorporating sustainability in prudential requirements: banks and insurance companies are an important source of external finance for the European economy. The Commission will explore the feasibility of recalibrating capital requirements for banks for sustainable investments (the so-called green supporting factor), when it is justified from a risk perspective, while ensuring that financial stability is safeguarded.
- Enhancing transparency in corporate reporting and improving accounting rule-making. The Commission will evaluate the current reporting requirements for issuers to make sure they provide the right information to market participants. It will also ensure that accounting rules do not directly or indirectly discourage sustainable and long-term investments.

Implementing the EU Action Plan on Financing Sustainable Growth

The European Commission has taken steps to implement its action plan on sustainable finance. These include the adoption (in May 2018) of:

- A proposal for a regulation on the establishment of a framework to facilitate sustainable investment. The proposed regulation sets out uniform criteria for determining whether an economic activity is environmentally sustainable, thus puts forward a process to establish a unified EU classification system ('taxonomy').
- A proposal for a regulation on disclosures relating to sustainable investments and sustainability risks and amending Directive (EU)2016/2341. The proposed regulation intends to establish a concise disclosure framework for institutional investors and asset managers in relation to the integration of ESG factors in risk processes in the financial services sector.
- A proposal for a regulation amending the benchmark regulation. The proposed amendment aims to address the risk of 'greenwashing' and to assist market players in the selection of benchmarks for their investment strategy. It establishes two categories of benchmarks, as follows: (i) 'low-carbon' and (ii) 'positive carbon impact'.

The Commission has also proposed amendments to delegated acts under the Markets in Financial Instruments Directive (MiFID II) and the Insurance Distribution Directive, with a view to including ESG considerations into the advice that investment firms and insurance distributors offer to individual clients.

On 18 April 2019, the European Parliament endorsed the legislation setting the building blocks of a capital markets union, including the regulation on disclosures relating to sustainable investments and sustainability risks.

The Commission has published new guidelines on corporate climate-related information reporting (June 2019), as a supplement to the existing guidelines on non-financial reporting (the non-financial reporting Directive - 2014/95/EU), which remain applicable. The guidelines provide practical recommendations on how companies can better report the impact of their activities on the climate, as well as the impact of climate change on their business.

The strategy set out in the Action Plan is a first essential step in moving finance towards sustainability; but it needs to be complemented by measures in other areas, requiring concerted efforts from all relevant actors, to reach its full potential.

INTERNATIONAL DIMENSION

Recognising the global dimension of the sustainable finance challenges, the European Commission calls for a coordinated, global effort involving other players, like the EU Member States, the private sector and major non-EU countries, to take decisive action to promote and lead transformation in their respective areas. In this context, the EU Action Plan on Financing Sustainable Growth sets a benchmark for relevant policies. It aims to be a blueprint for future discussions in international fora to promote a renewed approach to managing the financial system more sustainably, including in the Financial Stability Board, the G20, the G7, the United Nations and the International Organisation of Securities Commission (IOSCO).

The EU Action Plan on Financing Sustainable Growth echoes growing attention to sustainable finance in many other countries, including in developing economies. It also reflects the focus of development partners' initiatives supporting sustainable public and private finance, such as UNEP FI.

Transfer of EU experience (Relevance to development cooperation context)

The Action Plan on Financing Sustainable Growth complements other initiatives by the European Commission supporting investments contributing to the achievements of the United Nations 2030 Agenda for Sustainable Development and its Sustainable Development Goals (SDGs), notably the establishment of the European Fund for Sustainable Development (EFSD), as part of the External Investment Plan (EIP), to support investments in Africa and the Union's Neighbourhood. Under the EFSD, any decisions on guarantee agreements should be taken with due diligence paid to EU and international Environmental, Social and Governance (ESG) standards. Specifically, environmental sustainability shall relate to the protection (and where necessary the restoration) of all material components of the natural capital relating to air (including climate), water, land and biodiversity. Moreover, all investment windows under the EIP should profit from the EU's circular economy approach.