

Climate Risks and Business Opportunities – Report on the International Green Finance Conference in Budapest, November 2019*

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Financial and environmental factors are interrelated, and climate change, which already affects the economy and financial markets, may function as an increasingly important driver behind credit risks and other traditional financial risks in the future. This leads to a new risk management task for market players, central banks and financial supervisors: establishing the financing conditions for a sustainable, climate-friendly economy also represents a business opportunity for financial institutions. At the International Green Finance Conference in Budapest, organised by the MNB and the European Bank for Reconstruction and Development (EBRD), these issues were addressed in three sections by renowned Hungarian and foreign speakers, opening up new perspectives for everyone concerned.

Relationships between environmental and financial risks

From the aspect of financial stability, it is vitally important to mitigate the pace of climate change and this should be supported by market players, regulators and supervisory institutions, including central banks, each using the instruments they have available, according to *György Matolcsy*, Governor of Magyar Nemzeti Bank (MNB), in his opening statement. The first section of the conference focused on the interaction between environmental and financial risks. *Irene Heemskerck*, Advisor to the Chair of the Central Banks and Supervisors Network for Greening the Financial System (NGFS), also stressed the importance of national banks and financial supervisors assuming new responsibilities in connection with climate change. She pointed out that if we fail to curb climate change, increasingly frequent extreme weather conditions and other physical impacts will cause damage to the economy and hence to the financial system. However, if we manage to ‘decarbonise’ the economy through radical measures, financial institutions will need to be able to cope with the related regulatory, technological and social changes. Heemskerck also pointed out that the NGFS, originally established by just eight central banks, now has fifty members (for quite some time the MNB was its only member from

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Central and Eastern Europe) and that observers in the organisation now include the IMF and the Basel Committee on Banking Supervision.

Csaba Kandrács, MNB Deputy Governor responsible for financial supervision and consumer protection, summed up the measures taken by the Hungarian central bank to date and the planned actions to support the greening of the financial system. Some of the MNB's actions focused on the management of environmental and climate change-related risks. In the upcoming period, the central bank intends to analyse and model the climate-related exposure of banks' balance sheets and will issue recommendations on how to address environmental risks in connection with standard best practices. The central bank also intends to increase the ability of the financial system to take part to the greatest possible extent in financing climate neutrality and other sustainability-related investments worth thousands of billions of forints. Measures concerning the latter will be drawn up in several segments, the first of which will include preferential capital requirements for loans financing green (i.e. energy-efficient) buildings and energy efficiency renovation.¹ This programme is unique even by international standards. In his presentation, Csaba Kandrács emphasised that the MNB is keen on playing a pioneering role.

In the same section, *Christopher Perceval* of Trucost, representing a division of S&P specifically dedicated to environmental risks, presented the latest trends and state-of-the art methods of data analysis. ESG-based investment policies, based on a large volume of non-financial data, with a strong focus on environmental (E), social (S) sustainability and corporate governance (G), are becoming increasingly dominant on the global markets. Businesses will be increasingly required to measure, generate and disclose such data on account of the expectations of investors (and regulators).

Green lending as a new opportunity

On behalf of the Raiffeisen International Group, *Ralf Zymanek* and *Christine Würfel* focused on the conditions regulators should guarantee in order to enable banks to boost green lending. Such structural requirements include the widely accepted definition of green economic practices ('taxonomy') and the encouragement of green financing through prudential regulation (in particular the capital requirements for loans). According to Raiffeisen International, demand for sustainable investment and financial products may also rise in Central and Eastern Europe, especially in the private and premium banking sectors.

Nancy Saich, senior advisor to the European Investment Bank (EIB), gave a first-hand account of the decision made a day before by her bank's Board of Directors

¹ For more information, see: <https://www.mnb.hu/letoltes/green-retail-lending-in-hungary.pdf>

on putting their entire operation at the service of the Paris Climate Agreement and ultimately ceasing to finance fossil energy projects after 2021, while at the same time planning to mobilise green investments and lending a total of one thousand billion euros by 2030.² In the second part of her presentation, she described the new expert taxonomy of the European Union, i.e. essentially the set of criteria (encouraged by Raiffeisen International as well in their presentation), which provides a green definition of prospective green financing.

New initiatives by large global, universal banks were presented by *Luca Leoncini Bartoli* (Intesa San Paolo Group) and *Cecilia Moitry* (BNP Paribas). While they are active in different areas of green lending (renewable energy, energy efficiency, etc.), both banks support innovation to increase environmental sustainability. For example, ISP has established the Circular Economy Lab in order to improve the circular economy, whereas BNP Paribas has set up a spin-off business to collect voluntary carbon offset projects.

ESG asset management, green investments

The afternoon programme was opened by a keynote presentation by *Wang Yao*, Director General of the International Institute of Green Finance (IIGF), China's top think-tank on green finance. In addition to its research, education and analysis activities, the Institute specialises in providing assistance to Chinese government institutions, the central bank and supervisory authorities through advising and recommendations concerning public policies. The presentation covered a wide range of topics related to China's green financial regulations: As opposed to the prevalence of market-based initiatives and self-regulation typical of Western Europe or the US, government and central bank regulations play a crucial role, even though the best international practices are taken into consideration in drawing up new pieces of legislation. Wang Yao also referred to a potential green financial cooperation between China and Hungary in connection with various issues.

Investor considerations came up for discussion in the closing section. *Sergei Strigo* of Amundi Asset Management described the operation and the achievements of Emerging Green One, one of the world's largest green investment funds. He provided an insight into trends on the global green bond market, highlighting the challenges faced by emerging markets (a category Hungary is part of). Currently, only a few green bond issuances have taken place in Central and Eastern Europe. Pioneers include the PKO mortgage bank in Poland, which recently issued green mortgage bonds. (These instruments are 'more' than traditional mortgage bonds to the extent that, in addition to other process management

² <https://www.eib.org/en/press/all/2019-313-eu-bank-launches-ambitious-new-climate-strategy-and-energy-lending-policy>

and reporting commitments in accordance with international standards, they also offer green (energy-efficient) mortgage credit on par with the nominal value of the mortgage bond.) The Polish institution was represented by head of treasury *Agnieszka Zdziennicka*, who explained the rough path of the bond issue and their achievements to date.

Hungarian speakers also included *Péter Szabadhegy*, head of risk management at Susterra Capital, the company managing the Water Impact Fund (and former Ambassador to London). The Water Impact Fund finances innovative enterprises specialising in sustainable water management through equity investments. These are companies employing proven technology suitable for international distribution. A good indication of the business viability of these investments is that almost two billion people already have only limited access to clean water, while research has shown that 70 per cent of the global population will be affected by water scarcity in 10 years. State-of-the-art water management solutions will thus be in high demand and providing these firms with access to sufficient capital will clearly have a positive social and environmental impact.

On behalf of the EBRD, Associate Director *Dana Kupova* and Managing Director *Francis Maliq* pointed out that public funds alone are insufficient to meet the challenges posed by climate change. Cooperation with a number of other stakeholders, firm regulatory measures and the mobilisation of private sector investments – a sector where the EBRD has significant experience – are also called for.

Central banks and financial supervisors from thirteen countries, including Austria, the Netherlands, Poland and Germany, the EBRD, the European Central Bank, the European Investment Bank, the International Investment Bank, the Global Green Growth Institute and China's Asian Financial Cooperation Association were also represented at the conference which hosted more than 250 participants. Participants included the representatives from the entire Hungarian banking system, various foreign credit institutions and credit rating agencies and governmental organisations. The MNB, working with WWF Hungary, intends to carry out a complex, long-term ecological habitat restoration project in order to offset the unavoidable environmental burden associated with the conference.

The conference presentations are available at <https://www.mnb.hu/greenfinance/english/>.