



HLEG Final Report: Roadmap for a sustainable financial system

Topic of the month April 2018

Sustainability is the topic of our time – and the financial system plays a key role in view of its allocation and multiplier function. Sustainability means making economic wealth more robust in the long term, more socially integrated and less dependent on the exploitation of finite resources and the natural environment.

This transition to a more sustainable economic model requires substantial investments. The European Commission estimates that an additional sum of € 170-180 billion per year is needed to achieve the EU's energy and climate policy goals alone. The investment needed to achieve the Sustainable Development Goals (2020 United Nations Agenda) will be even higher. The current investment gap requires rapid and substantial redeployment of capital into sustainable activities, which should also promote employment, productivity and competitiveness of the EU economy.

This imperative of a sustainable financial system is nothing new – what is new is the momentum to its implementation. With the adoption of the 2030 Agenda for Sustainable Development and the Paris Climate Agreement, the global community has set itself concrete, universally valid goals – and ever since there has been increasing impetus for action.

What is striking about this new dynamic is how many organizations and institutions are working towards a common reform agenda. [The European Commission's High Level Expert Group on Sustainable Finance \(HLEG\)](#) is an example of how different stakeholders are involved in financial reforms.

The European Commission set up the HLEG to develop a comprehensive roadmap for a sustainable financial system in the EU. The HLEG was asked to develop concrete recommendations, as to a) how to steer the flow of capital towards sustainable investment, b) what steps financial institutions and supervisors should take to protect the financial system from sustainability risks and c) how this policy can be transposed to a pan-European level.

A roadmap for a sustainable financial system must therefore be multi-dimensional, reflecting the complexity of the system and the diversity of needs and capacities in the EU.

When the HLEG deepened its work after its interim report of July 2017, four common themes emerged, permeating all of the final recommendations of the group.

Speed up the change

These four themes should accelerate the transformation towards a sustainable financial system:

- 1. The need to achieve a fully coordinated approach to sustainable development in Europe that reconciles changes in the financial system with activities in the real economy.**

It is essential for European governments to ensure that price signals reflect both positive and negative externalities, for example in the form of changes in taxation, subsidies and performance standards, notably in agriculture, the real estate sector, the energy sector, the manufacturing, transport, water and waste disposal industries.



2. The central role of the financial industry as a service provider, serving the needs and preferences of its clients.

A common thread in the final report is the requirement for financial institutions, customers and beneficiaries to ask about their sustainability preferences and ethical values. It will also restore confidence in the financial sector and its ability to channel capital to the real needs of the economy and citizens.

3. The importance of bringing sustainable financing together with the specific needs of Europe's regions.

A decentralized and interactive approach is needed, which could also be used by suitable local banking networks and the best features of FinTechs.

4. The urgent need to extend the time horizon of decisions in the financial sector.

In this way, further, but profound, structural changes that are related to the sustainability agenda can be anticipated. The associated opportunities can be better grasped and the risks minimized. The HLEG has already highlighted in the interim report a „double compression“ as a fundamental problem for sustainable finance, namely that the time horizon of decisions is too short and risk understanding too narrow. This results in real effects in the form of a misallocation of capital at the expense of long-term value creation.

Interconnected by these aspects [the final report](#) (published at the end of January 2018) has a total of 28 recommendations:

- Eight key recommendations with the highest priority,
- eight cross-cutting recommendations and
- eight financial institutions and sectoral recommendations;
- four further recommendations also deal with social or other environmental content.

This shows that given the complexity of the European financial system and its political and regulatory environment, there is not one single lever to make the financial system more sustainable – the issues are too closely interlinked.

Accordingly, the report respectively the recommendations contained therein should not be considered as a modular set of individual recommendations.

Rather, the core and cross-sectional recommendations can be summarized in three major fields of action (the numbers in parentheses indicate the number of each key or cross-cutting recommendation in the HLEG report):

- Definitions and standards: taxonomy, standards and labels, retail / private investor market; global level
- Culture and behavior: investor duties, governance and leadership, supervisory authorities, retail / private investor market; short- vs. long-termism, citizen engagement, „think sustainability first“ principle
- Transparency and impact: disclosure obligations, „Sustainable Infrastructure Europe“, retail / private investor market; „EU observatory“, transparency in benchmarks, accounting standards, investing in energy efficiency.



And last but not least – despite all the complexity and interdependence – one must not forget why this and future efforts are being undertaken: A sustainable financial system is not an end in itself but serves a sustainable economy. Working towards this end is a formidable opportunity for the financial industry to reinstall purpose into its activities and thereby regain the trust of society that was so damagingly lost in the financial crisis.

On the basis of the recommendations set out by the High-Level Expert Group on Sustainable Finance, the Commission has drawn up a roadmap to boost the role of finance in achieving a well-performing economy that delivers on environmental and social goals as well. This “[Action Plan](#)” on sustainable finance (published early March 2018) 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. It is also one of the key steps towards implementing the historic Paris Agreement and the EU’s agenda for sustainable development.



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