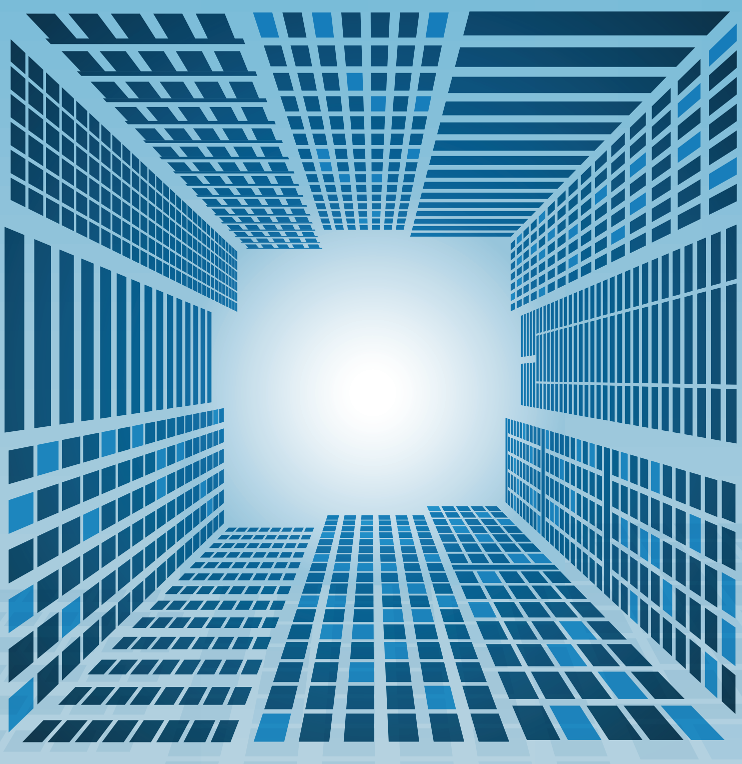
UN environment

Inquiry: Design of a Sustainable Financial System

Corporate Knights
The Company for Clean Capitalism

FINANCIAL CENTRES FOR SUSTAINABILITY

REVIEWING G7 FINANCIAL CENTRES IN MOBILIZING GREEN AND SUSTAINABLE FINANCE



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The UN Environment Inquiry

The Inquiry into the Design of a Sustainable Financial System has been initiated by the United Nations Environment Programme (UN Environment) to advance policy options to improve the financial system's effectiveness in mobilizing capital towards a green and inclusive economy—in other words, sustainable development. Established in January 2014, the Inquiry published its first global report, 'The Financial System We Need' in October 2015, with the second edition launched in October 2016. The Inquiry has worked in around 20 countries and produced a wide array of briefings and reports on sustainable finance.

More information on the Inquiry is at: *www.unep.org/inquiry* and *www.unepinquiry.org* or from:

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Corporate Knights

Corporate Knights Inc. (CK) has a media and research division, which includes the award-winning business and society magazine Corporate Knights, and a research division, which produces corporate rankings, research reports and financial product ratings based on corporate sustainability performance. Its best-known rankings include the Best 50 Corporate Citizens in Canada and the Global 100 Most Sustainable Corporations. In June 2013, Corporate Knights was named Magazine of the Year by Canada's National Magazine Awards Foundation.

For more information about CK, please visit *www.corporateknights.com*.

About this report

This report has been commissioned by Italy's Ministry of the Environment (MATTM) to explore the emerging agenda linking financial centres, climate action and sustainable development. It has been written by Nick Robins and Jeremy McDaniels of UN Environment's Inquiry and Toby Heaps and Fern Ramoutar of Corporate Knights. A first draft was prepared as a background paper for a G7 meeting on Financial Centres for Sustainability held at Borsa Italiana in Milan on 23-24 February 2017.

The report has benefited considerably from the presentations and discussions at the Milan meeting. Participants included Manuel Adamini, Anke Bauer, Marcello Bianchi, Timothy Bishop, Tatiana Bosteels, Gionata Castaldi, Davide Dal Maso, Carmina Di Noia, Pierre Ducret, Robin Edme, Paolo Garonna, Maurizio Gozzi, David Harris, Reo Kawamura, Cary Krosinsky, Adam Leff, Sara Lovisolo, Regina Maltry, Mike Manning, Jo Anne Matear, Jeremy McDaniels, Andrea Molocchi, Lucy Moran, Shinji Onoda, Frederick Packham, Stanislas Pottier, Aldo Ravazzi, Manfred Rosenstock, Anne-Claire Roux, PierCarlo Sandei, Henry Schaefer, Ludovica Soderini, Takehiro Sueyoshi, Alexandra Teisan, Alexandre Vinel, Alberto Visona, Amane Yamazaki and Philippe Zaouati.

The opinions expressed in this report remain those of the authors alone.

Feedback on this report is welcome. Comments should be sent to *nick.robins@unep.org*.

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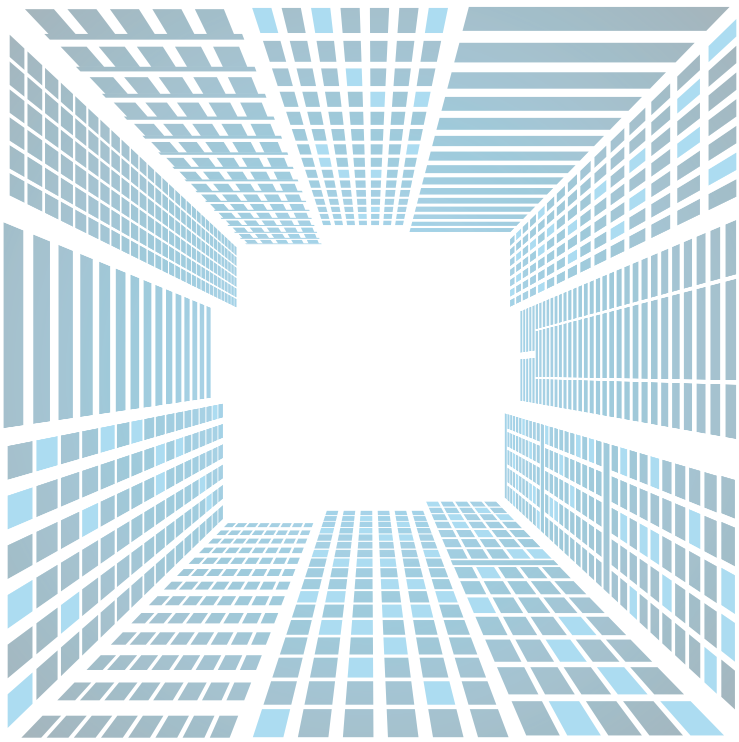

CONTENTS

EXECUTIVE SUMMARY 7

1 WHY SUSTAINABILITY IS SIGNIFICANT FOR FINANCIAL CENTRES 11

1.1 THE GROWING GLOBAL MOMENTUM 11
1.2 FINANCIAL CENTRES: WHERE GREEN AND SUSTAINABLE FINANCE BECOMES TANGIBLE 14

2 GREEN AND SUSTAINABLE FINANCE ACROSS LEADING G7 FINANCIAL CENTRES 17

2.1 MAPPING PRACTICE ACROSS THE G7 17
2.2 GREEN AND SUSTAINABLE FINANCE ACROSS LEADING G7 FINANCIAL CENTRES 18

3 LESSONS AND NEXT STEPS 29

3.1 FINANCIAL CENTRES AND SUSTAINABILITY – IDENTIFYING THE KEY FEATURES 29
3.2 LESSONS FROM PRACTICE 30
3.3 NEXT STEPS 31
3.4 LOOKING TO THE FUTURE 33

EXECUTIVE SUMMARY

Achieving sustainable development poses a strategic challenge for the world's financial centres. They are the places where the supply and demand for finance comes together and where action to connect finance and sustainability becomes tangible across banking, capital markets, insurance and institutional investment. This report has been prepared as part of Italy's G7 Environment programme to explore how financial centres can contribute to the delivery of the Sustainable Development Goals (SDGs) and the Paris Climate Agreement. It takes stock of the sustainability agenda that is emerging for financial centres, reviews current practice across leading centres in G7 countries and suggests priorities for further action. This report focuses on green and sustainable finance – in other words finance that delivers environmental benefits within the context of the wider transition to sustainable development.

The momentum in favour of sustainable finance is clearly accelerating. The value of investment assets committed to the Principles for Responsible Investment is now over US$65 trillion. In debt markets, issuance of green bonds has grown from US$11 billion in 2013 to US$81 billion in 2016. However, despite this impressive growth, green bonds still represent less than 1% of global bond issuance. Moreover, a number of strategic challenges continue to constrain the development of sustainable finance, including concerns over clarity and consistency of key definitions, incomplete disclosure, as well as market failures (such as environmental externalities and short-termism). Together, these can result in insufficient demand for sustainable financial services, as well as an inadequate pipeline of green financial assets.

To date, action to promote sustainable finance has mostly focused on separate financial sectors and on national policy frameworks. Now, there is growing realization that sustainability also has strategic implications for the world's more than 100 financial centres. Here, we define financial centres as cities with an intense concentration of financial activity involving an interlocking set of financial sectors and transactions. The case of green bonds illustrates how sustainability is becoming a cross-cutting issue for financial centres as a whole, involving local, national and international issuers, banks as underwriters and analysts, credit rating agencies, portfolio managers, asset owners, stock exchanges, specialist sustainability agencies, standard setters and market authorities, as well as civil society organizations and individual consumers. Importantly, financial centres are not just arenas for financial transactions – but are in many cases the locus of financial regulation as well as of public debate on financial performance, including on social and environmental metrics.

Over the past year, a number of financial centres (such as Casablanca, Frankfurt, Hong Kong, London, Luxembourg and Paris) have launched specific green or sustainable finance initiatives. These and other initiatives are responding to three different imperatives generated by the sustainability agenda:

- Policy: local and national governments are interested in how their financial centres are mobilizing capital to deliver key environmental, climate and sustainable development targets.
- Market: financial centres themselves are interested in how sustainability factors could create new opportunities as well as potential risks.
- Economic: more broadly, there is interest in how financial centres are serving the real economy as it makes its sustainability transition.

A review of the leading G7 financial centres – Toronto, Paris, Frankfurt, Milan, Tokyo, London and New York – and discussions with experts identified 10 key factors that contribute to the sustainability of financial centres. From this, a number of lessons can be drawn about the current state of practice.

1 **Diverse Drivers at Work:** A wide array of factors are prompting financial centre action, including city ambitions as well as national policy commitments, growing green bond issuance and innovation by institutions operating in the financial centre, including state green banks. Progress often requires the involvement of anchor institutions, such as major pension funds and stock exchanges as well as city authorities, who are willing to take a leadership stance to build momentum.

2 **Understanding the Financial Ecosystem:** Each centre operates in a distinctive financial ecosystem, with considerable diversity across the G7. For example, federal countries often have a number of different financial centres rather than a single hub. Some centres are more focused on capital markets; others focus more on banking, including financing small and medium enterprises (SMEs). This diversity is a real strength – and clearly illustrates that there is no single template for efforts to develop sustainable financial centres.

3 **The Clustering Effect:** Financial centres can add real value to the expansion of green finance by being place-specific, generating a cluster effect across sectors and institutions. This can help to ground green finance in the specific needs of the real economy and build long-term relationships. Here, the knowledge agenda is important, embedding green finance in the key professional associations and universities within the financial centre, so that expertise in sustainability becomes increasingly established.

4 **A Multi-Asset Opportunity**: The growth of the green bond market has certainly catalysed financial centres to start thinking strategically about sustainability. But green bonds are just one part of a much wider trend – starting with listed equities and now extending to bank lending, insurance markets as well as infrastructure, private equity, derivatives and fintech. A key unifying feature is the need for common definitions of financial flows across assets and sectors.

5 **The Public-Private Dynamic:** Public policy and regulation can play an important role in ensuring good sustainability practice in financial centres, notably through corporate governance, stewardship and disclosure requirements. In addition, policymakers can help to stimulate the growth of sustainable financial services, for example by encouraging public agencies to pump prime markets through the issuance of green bonds or support for green investment trusts. Dedicated initiatives by financial centres on sustainability can also act as focused interlocutors with national governments on policy design.

6 **From Early Stage Innovation to Transformation:** The greening of financial centres is still, however, at an early stage of development. Most financial centres have yet to consider how sustainability influences their future trajectory and even in those that have launched