Global Economy

Climate Change: *Tempus Fugit*

Expansión (Spain)

Arturo Fraile

The Paris Agreement (2015 UN Climate Change Conference) was a tipping point on how to address climate change to *breaking the tragedy on the horizon*. Last week's United Nations Summit and Climate Week NYC, among other things, have evidenced the widespread consensus on the fact that the impact of global warming and the transition to a low-carbon economy may involve significant risks to financial stability; and that the concrete actions taken for the time being, and their effects, are not sufficient to meet the goals of the 2030 Agenda for Sustainable Development or the net-zero CO2 emission target by 2050. Some analyses suggest that the likelihood of a late and abrupt transition is starting to be high.

From a of financial regulation and supervision perspective, at least three conditions seem to be essential for achieving the aforementioned goals without causing disruption or unintended consequences for the financial system or the real economy:

- A framework that allows for an orderly and a credible transition. Some clarity and ambition are needed to properly internalize and incorporate this new paradigm into financial and macroeconomic expectations and models.

- A flexible approach that considers different states, conditions and speeds among countries. This approach must be adapted to local conditions, as per the Paris Agreement, which for the first time explicitly allowed for different speeds and different requirements for emerging and developed countries, according to the capacity of each country to meet its commitments — which must be credible.

- Data generation and disclosing useful information to measuring, analyzing and managing climate-related financial risks, and other environmental, social and governance (ESG) risks. The prices of financial assets must adequately capture these risks, so that agents can take capital allocation decisions efficiently. Information about companies' long-term strategies, objectives, and degree of compliance with these over time is of the utmost importance.

On the one hand, some developments that suggest these trends will evolve from being voluntary to binding should be noted. Among them:

- The June status report by the Task Force on Climate-related Financial Disclosures (TCFD) notes that the volume of information disclosed by companies has increased since 2016. However; this is still insufficient, and more accuracy is needed on of how climate-related risks impact on companies, and their plans to address and to mitigate them. In Europe, there seems to be a chance that the Non-Financial Reporting Directive could be revised to align it with the TCFD recommendations (on disclosure of information).

- In April, the Central Banks and Supervisors Network for Greening the Financial System and the European Banking Authority, released their plans to integrate climate-related risks sequentially as a source of financial risk into the prudential framework: firstly, through market discipline (information and reporting); secondly, via risk management and supervision; and finally, if necessary, through the minimum capital requirements. The European Central Bank included climate-related risks for the first time in its banking supervision risk assessment for 2019 and has publicly announced the possibility of incorporating those risks in future stress tests.

- The ten key actions of the European Commission's Action Plan for Sustainable Finance are being materialized into three regulatory proposals of the highest level: a framework to promote sustainable investment through a taxonomy that clarifies what economic activities are considered to promote sustainable development; a proposal for the disclosure of information (on sustainable investments) and ESG risks; and a proposal for two new benchmarks.

On the other hand, time is running out, and we need to accelerate to achieve the 2030 and 2050 aforementioned targets. Nevertheless, the increase in speed must allow for adaptation to the new global financial trends: the importance of ESG issues and their demand wil increase for regulators, investors and society as a whole. All of us must work together towards a *new horizon*.

DISCLAIMER

This document has been prepared by BBVA Research Department. It is provided for information purposes only and expresses data, opinions or estimations regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

Any estimations this document may contain have been undertaken according to generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, either positive or negative, are no guarantee of future performance.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

With regard to investment in financial assets related to economic variables this document may cover, readers should be aware that under no circumstances should they base their investment decisions on the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

ENQUIRIES TO:
BBVA Research: Azul Street. 4. La Vela Building – 4th and 5th floor. 28050 Madrid (Spain).
Tel. +34 91 374 60 00 y +34 91 537 70 00 / Fax (+34) 91 374 30 25
bbvaresearch@bbva.com www.bbvaresearch.com