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Leading the way to a green and resilient economy

A Swiss-quality approach to sustainable finance

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The core team of editors wants to thank all the contributors to this paper.

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Foreword

> A crisis is a productive state; you simply have to get rid of its aftertaste of catastrophe.
>
> Max Frisch, Swiss playwright and novelist

Since our first joint PwC and WWF sustainable finance reports in 2019 (Paradigm Shift in Financial Markets) and in early 2020 (Nature is Too Big to Fail), the world we live in has changed dramatically. The COVID-19 pandemic has swept across the world, impacting lives and livelihoods and exposing how fragile our economies and societies are to external shocks. At the societal level, the COVID-19 crisis gave rise to much uncertainty and reminded us of the urgency to act that many of us already felt long before in light of the looming ecological crisis. On the other hand, the COVID-19 crisis showed that states can act rapidly and boldly and that people around the world can unite to fight against the pandemic. Recent developments can thus be seen as a catalyst for change and renewal. It is now more important than ever to change our unsustainable relationship with nature and to limit the averse impacts of mankind on the environment. As governments around the world are restarting their ecnomic engines and mulling post-pandemic recovery plans, it is fundamental to acknowledge that these must address long-term prosperity while advancing our capacity to deal with future shocks. Only then will our societies and economies become greener and more resilient.

The transition to a climate-safe world with net zero greenhouse gas emissions and fully recovered biodiversity is steadily gathering pace. More and more forward-looking businesses and financial institutions recognise the strategic imperative to act on climate change and biodiversity loss. However, the pace and scale at which this transition is happening is still far from sufficient. The financial sector has a critical role to play in this transformation by how it allocates capital and manages risks, thereby impacting the current and future shape of our economy. This has been recognised by the Paris Agreement, which acknowledges the instrumental role of aligning financial flows with a pathway towards low greenhouse gas emissions and climate-resilient development. While the political momentum and scientific evidence on financial risks related to biodiversity loss are less advanced compared with climate change, it is evident that the two challenges have to be addressed simultaneously.

Most sustainable finance discussions in Switzerland perceive action as a vehicle to strengthen the competitiveness of the financial sector. There is nothing to be said against this. The authors believe however that when approaching the climate and biodiversity crises, the financial sector's broader role should also be considered to ensure consistency and credibility. PwC and WWF are convinced that financial flows should, first and foremost, serve to create a green and resilient economy. To realise this objective, financial flows managed or controlled by Swiss financial institutions need to follow a well set out and measurable transitional pathway to achieve net zero greenhouse gas emissions and recover biodiversity fully by no later than 2050. We have a long way to go, knowing that Swiss financial flows currently are far from being aligned with international agreements such as the Paris Agreement and the Convention on Biological Diversity.

Our idea is not targeted exclusively at the Swiss financial sector and may be adapted to other contexts. However, we are convinced that Switzerland in particular would benefit from it. First, the alignment of financial flows with global environmental goals triggers transformational change in the real economy, thereby creating new economic opportunities, while at the same time honouring Switzerland's international commitments. Furthermore, when based on measurable progress, it strengthens the competitiveness and long-term viability of the Swiss financial sector, which is hard-pressed to find a new identity and competitive edge after the end of Swiss banking secrecy. Focusing on the positive environmental impact of financial flows would provide Switzerland a unique selling point, increasing its positive reputation while building on typical Swiss attributes such as high quality, competence and credibility. At the same time, the transition to a sustainable financial sector will provide benefits to both financial players and their clients.

PwC and WWF agree that building the economy of the future and making our financial system greener and more resilient will only be possible if a broad coalition of relevant actors come together to rally behind a common goal and jointly develop concrete solutions. While there is no single "silver-bullet" solution, we are convinced that there are critical leverage points in the system that need to be activated without further delay. This paper calls all actors involved in sustainable finance in Switzerland to embrace and publicly endorse the idea of putting the positive environmental impacts of financial flows at the centre. By proposing a suite of concrete measures, the authors intend to kickstart a discussion between the financial sector, companies, policymakers and civil society actors to build a fully-fledged action plan with clear roles, responsibilities and timelines. Only a concerted effort by a broad coalition of actors will bring to life a new quality approach to sustainable finance with which Switzerland can make a pioneering contribution to building a healthy planet for future generations.

Andreas Staubli,
CEO PwC Switzerland

Thomas Vellacott,
CEO WWF Switzerland

Executive summary

Attention to sustainable finance is at an all-time high in the news and sustainably managed assets have hit a new peak both internationally and in Switzerland. Multiple initiatives have emerged since the last two PwC/WWF joint reports (Paradigm shift, 2019; Nature is too big to fail, 2020). Despite this increasing attention and the impressive array of publications from actors such as the Swiss Bankers Association and the Federal Council, the significant direct and indirect impacts of financial flows on climate change and biodiversity loss still need to be addressed with more concrete actions. Financial flows, particularly in Switzerland, still have significant negative environmental impacts. And while progress is being made in relation to the integration of climate risks, financial flows are still far from being aligned with international agreements such as the Paris Agreement and especially the Convention on Biological Diversity. PwC and WWF believe this has to change and suggest a Swiss-quality approach to sustainable finance: all financial flows managed or controlled by Swiss financial institutions contribute to a green and resilient economy, thus facilitating the achievement of the Paris Agreement and the Convention on Biological Diversity.

The World Economic Forum underlines it clearly: "There is no future for business as usual – we are reaching irreversible tipping points for nature and climate, and over half of the global GDP, $44 trillion, is potentially threatened by nature loss."[1] Thus, there is no other issue that is as pressing as safeguarding humanity's capacity to sustain life on earth. This can only be achieved if climate change and biodiversity loss are addressed effectively and simultaneously via transforming the economic system. As the financial sector is at the heart of the economic system, it has a privileged position to encourage, demand and create the necessary incentives for the transformation of the real economy. Substantial progress needs to be made to ensure that the financial sector genuinely supports businesses on their transition path towards sustainability.

There is no better place than Switzerland to kickstart this reflection. Switzerland boasts an important financial sector (managing over CHF 6200 billion[2]), a long-standing tradition in sustainable finance, an innovative market space, lean framework conditions and excellent universities. Furthermore, Switzerland is known for its attributes such as excellence and competence. Lastly, reducing the negative environmental impacts of financial flows is associated with a number of economic and social benefits such as increased financial stability, equivalence with EU legislation and protection of consumers against greenwashing.

Despite this excellent initial position, the sustainable finance debate in Switzerland is still characterised by a number of contrasting views with regards to the purpose that sustainable finance should serve (e.g. competitiveness of the financial sector vs. contribution to sustainability goals), the scope it encompasses (e.g. ESG vs. climate change), the business lines it focuses on (e.g. lending vs. investment) and the type of intervention that is required or desirable (e.g. regulation vs. voluntary action).

The authors claim that financial flows should, first and foremost, serve to create a green and resilient economy. To achieve this, all financial flows (investment, lending and underwriting business) managed or controlled by Swiss financial institutions need to follow a well set out and measurable transitional pathway to achieve net zero greenhouse gas (GHG)[3] emissions and fully recover biodiversity by no later than 2050. This basically means translating the scientific findings on climate change and biodiversity loss to the financial sector. Building the economy of the future and making our financial system greener and more resilient does not happen overnight and requires the buy-in of all relevant sustainable finance actors.

PwC and WWF therefore suggest that until 2030 the combined efforts are geared towards creating a net zero GHG-emitting and full biodiversity-recovering real economy. The financial sector plays a pivotal role in this transformation by reducing its exposure to high-emitting economic sectors and activities, by engaging vigorously with the invested companies and policymakers and by creating new financial vehicles for a net zero, biodiversity-recovering economy. But the financial sector also depends deeply on the transformation of the real economy, which currently is far from being climate- and biodiversity-friendly. At the same time, the transformation needs to be based on ambitious, practical measures for the financial sector and a clear policy framework (common standards for defining sustainability, sustainability disclosure requirements and sufficient granular data). Therefore, the authors suggest that until 2030 the negative impacts on climate and biodiversity should be decreased, acknowledging that GHG emissions and biodiversity destruction will continue, albeit at a slower growth rate. To reverse this trend, it is imperative that from 2030 onwards all new financial flows or refinancing activities emit net zero GHG and restore and enhance biodiversity. This creates a second strong, necessary push to achieve the final goal by 2050. Furthermore, it gives the real economy until 2030 to adapt and transform towards the set-out goal.

1 https://www.weforum.org/reports/new-nature-economy-report-ii-the-future-of-nature-and-business

2 https://www.six-group.com/exchanges/download/about/div_pub/ssx_financialcenter_en.pdf

3 In this paper we consistently use the term "greenhouse gas emissions", which broadly refers to gases that trap heat in the atmosphere. There are several types of GHGs with different global warming potentials, with CO2 being the most important GHG.

The years until 2030 are crucial to set the stage and start moving in the right direction. Missing this window makes it almost impossible to reach the formulated goals in time. To kickstart this transition, all actors (financial institutions, federal administration, industry associations, policymakers and civil society) need to join forces and push in the same direction. Focusing solely on voluntary measures by market players falls short, given that the Swiss financial sector is way off track from meeting global environmental targets.[4] The sheer size of the challenge at hand also requires clear and predictable policy signals and regulatory framework conditions, which should be complemented by ambitious, targeted self-regulation. A smart mix of measures is therefore most likely to produce the desired outcomes. The authors propose to place the short-term focus on the following leverage points, which in their view are the most impactful:

Leverage point 1	Turn Switzerland's political commitment to net zero GHG emissions by 2050 into a legal obligation for financial actors and set a political goal for aligning financial flows with full biodiversity recovery.
Leverage point 2	Revise the fiduciary duty such that financial actors and regulators need to integrate the financial risks associated with climate change and biodiversity loss and are responsible for minimising the negative impacts of financial flows on climate and biodiversity.
Leverage point 3	Promote meaningful metrics for climate- and biodiversity-related financial risks and impacts and define clear standards determining what can be considered climate- and biodiversity-friendly and unfriendly.
Leverage point 4	Request real economy companies and financial actors to establish measurable strategies and targets for reducing GHG emissions and negative biodiversity impacts and to disclose their climate- and biodiversity-related financial risks and impacts.
Leverage point 5	Rapidly align asset owners' and banks' investment, lending and underwriting portfolios with net zero GHG emissions and full biodiversity-recovery pathways and adjust capital requirements for banks and (re-)insurers accordingly.
Leverage point 6	Advocate for correctly pricing negative climate and biodiversity externalities and for adopting preferential tax policies for climate- and biodiversity-friendly activities, thus facilitating the transition to a green and resilient economy.

[4] Current estimates by the Federal Office for the Environment (FOEN) indicate that the Swiss financial flows contribute to global warming of between 4 and 6 degrees Celsius.

“This new report from PwC and WWF draws up a much-needed action plan outlining concrete measures for achieving the Swiss Federal Council’s ambition of making Switzerland a leading place for sustainable finance. When it comes to climate change and biodiversity loss, we cannot afford to waste time and wait for self-regulation.”

Vincent Kaufmann, CEO of Ethos Foundation and of Ethos Services

“Following J. Safra Sarasin Asset Management’s Climate Pledge for a net-zero carbon footprint across its portfolios by 2035, we share the authors’ view that the next milestone will be to create a framework to report and manage the financially-material risks of biodiversity loss in portfolios in order to mitigate a negative impact.”

Jan Amrit Poser, Chief Strategist & Head Sustainability, Bank J. Safra Sarasin

1. Global climate and biodiversity goals and the role of the financial sector

> "If we do not [take action] we will surely see a rebound in emissions. If emissions rebound, it is very difficult to see how they will be brought down in future. This is why we are urging governments to have sustainable recovery packages."[5]
>
> Fathi Birol, IEA CEO, in The Guardian

1.1 Global legal environmental architecture

The biggest challenge of mankind is to effectively address the self-imposed threats of climate change and biodiversity loss in order to ensure the ability to sustain all life on Earth. As climate change and biodiversity loss are two sides of the same coin, these issues cannot be looked at nor managed separately. In fact, the massive loss of nature that we see today not only directly threatens human health and wellbeing, for instance through a decline in food production and freshwater availability. By destabilising our climate, the ecological crisis also threatens the stability of the entire planet. There is thus a connection, and to some degree an overlap, between climate-related and environmental risks.[6] This relationship is mirrored at the institutional level with the United Nations Framework Convention on Climate Change (UNFCCC), the Convention on Biological Diversity (CBD) and the United Nations Convention to Combat Desertification (UNCCD), known as the Rio Conventions, together making up the legal framework that governs the natural environment.

Building on the UNFCCC and entering into force on 4 November 2016, the Paris Agreement for the first time brings all nations into a common cause to undertake ambitious efforts to combat climate change and adapt to its effects. As such, it charts a new course in the global climate effort. The Paris Agreement's central aim is to strengthen the global response to the threat of climate change by keeping a global temperature rise this century well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5°C. Additionally, the agreement aims to strengthen the ability of countries to deal with the impacts of climate change.[7] The year 2020 marks the first litmus test for the Paris Agreement as parties are expected to submit their long-term net zero climate strategies as well as shorter-term 2030 goals (Nationally Determined Contributions).

With its ratification of the Paris Agreement on 6 October 2017, Switzerland committed itself to an emissions reduction target of minus 50% by 2030 in comparison with 1990 levels. At the national level, these reduction commitments are implemented in the national climate legislation. At the time of writing, the full revision of the CO2 Act for the post-2020 period is still being debated in the Swiss Parliament, with discussions expected to terminate in autumn 2020. Referencing the findings of the IPCC and Switzerland's ratification of the Paris Agreement, the Federal Council announced on 28 August 2019 its decision to aim for a climate-neutral Switzerland by 2050. Hence, Switzerland should not emit more GHGs than can be absorbed naturally or by technical means. This means that net emissions will have to be reduced to zero by 2050.[8] It is expected that Switzerland will submit its 2050 climate strategy to the UNFCCC Secretariat by the end of 2020.

The Convention on Biological Diversity (CBD) entered into force on 29 December 1993 and was later complemented by the Cartagena and the Nagoya Protocols. The CBD is the legal instrument for "the conservation of biological diversity, the sustainable use of its components and the fair and equitable sharing of the benefits arising out of the utilization of genetic resources"[9] and today has 196 parties. In 2020, the CBD was set to review the achievement and delivery of the CBD's strategic plan for biodiversity 2011-2020 and to adopt the post-2020 global biodiversity framework. However, against the backdrop of the COVID-19 pandemic, the 15th meeting of the Conference of the Parties (COP15) to the CBD had to be deferred to 2021.

Switzerland became a party to the CBD in 1994. However, unlike the CO2 Act, no single legal framework exists at the national level that directly transposes Switzerland's international commitments on biodiversity. Rather, the conservation and promotion of biodiversity is referenced in various federal acts.[10] Recalling the existential and economic importance of biodiversity as the basis of human existence and the risks that a reduction in biodiversity poses to human welfare and the functioning of the economy, the Federal Council adopted an action plan for the Swiss biodiversity strategy on 6 September 2017. Substantiating the objectives of the Swiss biodiversity strategy, which was passed by the Federal Council on 25 April 2012, the action plan proposes a set of 27 measures to be implemented over two phases, 2017-2023 and 2024-2027 respectively.[11]

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5 https://www.theguardian.com/environment/2020/jun/18/world-has-six-months-to-avert-climate-crisis-says-energy-expert

6 https://www.ngfs.net/sites/default/files/medias/documents/ngfs_guide_for_supervisors.pdf

7 https://unfccc.int/process-and-meetings/the-paris-agreement/the-paris-agreement

8 https://www.bafu.admin.ch/bafu/en/home/documentation/news-releases/anzeige-nsb-unter-medienmitteilungen.msg-id-76206.html

9 https://www.un.org/en/observances/biological-diversity-day/convention

10 These federal acts include the Protection of Nature and Cultural Heritage Act, the Environmental Protection Act, the Hunting Act, the Water Protection Act, the Fisheries Act and the Gene Technology Act.

11 https://www.bafu.admin.ch/dam/bafu/de/dokumente/biodiversitaet/fachinfo-daten/aktionsplan-strategie-biodiversitaet-schweiz.pdf.download.pdf/Aktionsplan_SBS_final_Deutsch.pdf

Net zero GHG emission targets

Targeting net zero GHG emission or climate neutrality can be defined as reducing the overall greenhouse gas emissions in alignment with the Paris Agreement objective to keep the global temperature increase to below 2°C and pursue efforts to keep it to 1.5°C. In the financial industry context, the UN-convened Net-Zero Asset Owner Alliance defines net zero transitioning in the investment portfolio context as reducing the overall emissions contained in the portfolio by 2050 consistent with a maximum temperature rise of 1.5°C above pre-industrial temperatures.[12]

1.2 Role of the financial sector

It is broadly understood that the direct biodiversity and climate impacts of the financial sector are rather limited in comparison with the real economy. However, through the indirect impacts of allocating capital to businesses and projects via investments, loans and underwriting activities, actors from the financial sector play a key role in shaping the current and future economic system. In fact, they catalyse behaviour changes and influence economic pathways, business models and practices, thereby influencing business activities. Since the economic system is the most important driver of climate change and biodiversity loss,[13] the financial sector has a large indirect influence on our natural environment. It appears therefore obvious that the financial sector should be leveraged in the transformation of the real economy. Being ahead of the curve and anticipating the transformation of the real economy is also in the interest of the financial sector. By aligning its investment, lending and underwriting activities with climate and biodiversity goals,

> "Baloise is a Swiss insurance company with a rich tradition and a business model that takes responsibility for the current generation and those to come. We strongly believe that all Swiss players will have to rethink if we are to be able to live together in a successful country that is fit for the future. We wish to work alongside our clients to make our contribution to this through our value creation model and our responsible investments."
>
> Dr. Agnes Neher, Head Responsible Investment, Baloise Asset Management

the financial sector reduces its exposure to financial risks associated with climate change and biodiversity loss. This in turn enhances the stability of the financial system. Secondly, supporting the transformation of the real economy comes with important investment opportunities for the financial sector. The financing gap for addressing climate change alone has been estimated by the Global Environmental Facility and the Green Climate Fund to be about USD 6 trillion per year. Regarding the restoration and conservation of biodiversity, PwC and WWF estimated in their last report that over USD 0.5 trillion is needed annually.[14] This misallocation of capital creates important opportunities for the financial sector to develop new financial vehicles steering financial flows into climate change mitigation and adaptation as well as biodiversity restoration and conservation.

The critical role of financial flows in the transition to a more sustainable world is acknowledged in the Paris Agreement, which states in article 2.1, paragraph c) that financial flows should be made consistent with a pathway towards low greenhouse gas emissions and climate-resilient development. An equivalent goal does not (yet) exist in the CBD. This is reflective of the fact that the relationship between sustainability themes and financial flows has been particularly well discussed and researched regarding climate change and less so on biodiversity.[15] However, the United Nations Environment Programme Finance Initiative (UNEP FI) considers biodiversity to be the next frontier of sustainable finance, and business and finance sectors are increasingly aware of risks arising from biodiversity loss and shifting their attention to more biodiversity-positive practices.[16] It is against this backdrop that UNEP FI is set to release guidance for banks to set targets on biodiversity in 2021.[17] In the same vein, the launch of an informal working group in July 2020 by the UK and Swiss governments and ten financial institutions that is supposed to lead to the creation of a Task Force on Nature-related Financial Disclosures (TNFD) is a further point in case illustrating the growing awareness of the materiality of nature-related risks for business and finance. Going forward, it is likely that the new Global Biodiversity Framework 2021-2030 that is up for negotiations at the 15th Conference of the Parties to the CBD will address the financial sector's role in contributing to a positive impact for biodiversity.

Looking at the facts it becomes clear that the financial flows managed or controlled by Swiss financial institutions are still not in line with reaching the targets set by the Paris Agreement and especially the Convention on Biological Diversity. According to the most recent voluntary climate compatibility test of pension funds and insurances companies conducted by the Swiss Federal Office for the Environment (FOEN), the Swiss financial sector currently invests in an economy that encourages global warming of between 4° and 6°C.[18] Greenpeace further highlighted in its latest report that despite a small reduction, the two largest Swiss banks (UBS and Credit Suisse) still heavily invest in fossil fuels.[19] With regards to the biodiversity impacts of financial flows, no quantitative assessment has been conducted for Switzerland yet.

[12] https://www.unepfi.org/wordpress/wp-content/uploads/2019/09/AOA_FAQ.pdf

[13] IPCC (2018): https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc_wg3_ar5_chapter5.pdf

[14] Based on the estimates by the High-level Panel on global investment required for biodiversity conservation (2014).

[15] Nature is too big to fail (2020): https://www.pwc.ch/en/publications/2020/nature-is-too-big-to-fail.pdf

[16] For an overview of the developments in the financial sector regarding integrating biodiversity-related financial risks, see the 2020 report from UNEP FI and Global Canopy, "Beyond 'Business as Usual': Biodiversity targets and finance. Managing biodiversity risks across business sectors." https://www.unepfi.org/publications/banking-publications/beyond-business-as-usual-biodiversity-targets-and-finance/

[17] https://naturalcapital.finance/wp-content/uploads/2020/06/Beyond-Business-As-Usual-Full-Report.pdf

[18] https://www.newsd.admin.ch/newsd/message/attachments/50023.pdf A new round of climate compatibility tests is currently being run by the FOEN with results expected to be released towards the end of 2020.

[19] https://www.greenpeace.ch/de/publikation/53979/klimaschaedliche-geschaefte/

2. Sustainable finance in Switzerland and globally: recent developments and current debate

> "Achieving net zero will require a whole economy transition – every company, every bank, every insurer and investor will have to adjust their business model. This could turn an existential risk into the greatest commercial opportunity of our time."[20]
>
> Mark Carney, former Governor of the Bank of England

The PwC/WWF report "Paradigm Shift in the Financial Market"[21] highlighted sustainable finance developments in Switzerland, stressing notably the different market-led initiatives, the importance of conducive framework conditions and the increasing political and public pressure. Since 2019 these developments have gathered further pace as evidenced by a series of actions at the national level[22]:

- **Market-led initiatives:** In June 2020, the Swiss Bankers Association (SBA) published an updated position paper on sustainable finance alongside a set of guidelines on how to integrate ESG criteria into the private client advisory process. Stressing the excellent opportunities for a sustainable Swiss financial centre and the industry's own initiatives, the SBA suggests ten action areas for improving the framework conditions. Further in June 2020, the Swiss Funds and Asset Management Association (SFAMA) together with Swiss Sustainable Finance (SSF) issued some high-level key messages accompanied by a set of technical recommendations for the Swiss asset management industry on how to implement a sustainable investment process. This publication came on the heels of the Swiss Sustainable Investment Market Study 2019, launched earlier by SSF and providing in-depth insights into recent developments in the Swiss sustainable investment market. A few examples of action on the business side: in May 2020, J. Safra Sarasin Asset Management pledged to aim for a carbon-neutral outcome in assets under management by 2035. Swiss Re, in February 2020, announced further measures to support the transition to a low-carbon economy in line with its commitment as a member of the UN-convened Net-Zero Asset Owner Alliance and a signatory to the UN Business Ambition for 1.5°C pledge. Also the pure-player sustainable finance institutions have been active. Notably, the Alternative Bank Schweiz organised the high-level event "Every degree matters" and launched its vision for a sustainable economy.[23]

- **Framework conditions:** In general, the Federal Council's financial market policy is guided by the primacy of market-based solutions and the subsidiarity of government action. Prompted by the regulatory developments on sustainable finance in the EU, the Federal Council announced in June 2019 the set-up of an internal working group tasked with examining climate and environmental risks and impacts, specifically regarding transparency, due diligence and financial market stability. In June 2020, the Federal Council published a long-awaited report and guidelines on sustainability in the financial sector, providing for the first time a comprehensive overview of international developments and Switzerland's position.[24] Highlighting the great opportunity that sustainable finance offers for the Swiss financial centre and the importance of optimal framework conditions, the report fails, however, to take concrete action on the discussed measures. At the level of the supervisory bodies, in December 2019 the Swiss Financial Market Supervisory Authority (FINMA) released for the first time its annual risk monitor, where it acknowledged financial risks arising from climate change as one of the most important long-term risks. At the same time, FINMA declared its intent to refine its analysis of climate-related risks on the balance sheets of financial institutions and to develop approaches for improved voluntary or regulated disclosure of financial climate risks.

> "The Swiss financial sector has until now demonstrated what could best be described as "compliance" ambition. It does not act; it reacts. PwC and WWF are making an urgent plea for "leader" ambition: we can drive the agenda faster, smarter and with greater courage than others. If we take direct action to redirect capital, this will benefit humankind and the environment. And our economy will be strengthened."
>
> Peter Zollinger, Head of Impact Research, Globalance Bank

- **Political and public pressure:** In June 2020, the National Council largely followed the Council of States in its deliberations on the full revision of the CO2 Act for the period after 2020, thereby overturning its decision of December 2018 when it had repealed the bill. While the modified CO2 Act contains relatively few provisions specifically targeting the financial sector, it nevertheless marks a small step forward by stating in article 1 the aim of aligning financial flows with a low-carbon and climate-resilient development, consistent with article 2.1c of the Paris Agreement. Furthermore, the National

[20] https://www.bankofengland.co.uk/-/media/boe/files/speech/2020/the-road-to-glasgow-speech-by-mark-carney.pdf?la=en&hash=DCA8689207770DCBBB179CBADBE3296F7982FDF5

[21] https://www.pwc.ch/en/publications/2019/paradigm-shift-in-financial-market-EN-web.pdf

[22] These examples from the recent past serve a purely illustrative purpose and are not intended to be exhaustive.

[23] https://www.abs.ch/?id=931

[24] https://www.admin.ch/gov/en/start/documentation/media-releases.msg-id-79606.html

Council accepted the requirement for FINMA and the Swiss National Bank (SNB) to regularly assess and disclose climate-related financial risks at micro- and macroprudential level. The fact that an overwhelming majority of the National Council endorsed the revised CO2 Act can be attributed to different reasons, the main ones being the landmark gains by the green parties in the 2019 Swiss federal elections and the renewed commitment of the centrist liberal party (FDP) to environmental and climate protection. It is fair to assume that this political turn of the tide was facilitated by a series of protests around the world, including Switzerland, referred to as the global climate strikes, and which demand that political decision-makers take urgent and effective action to combat climate change.

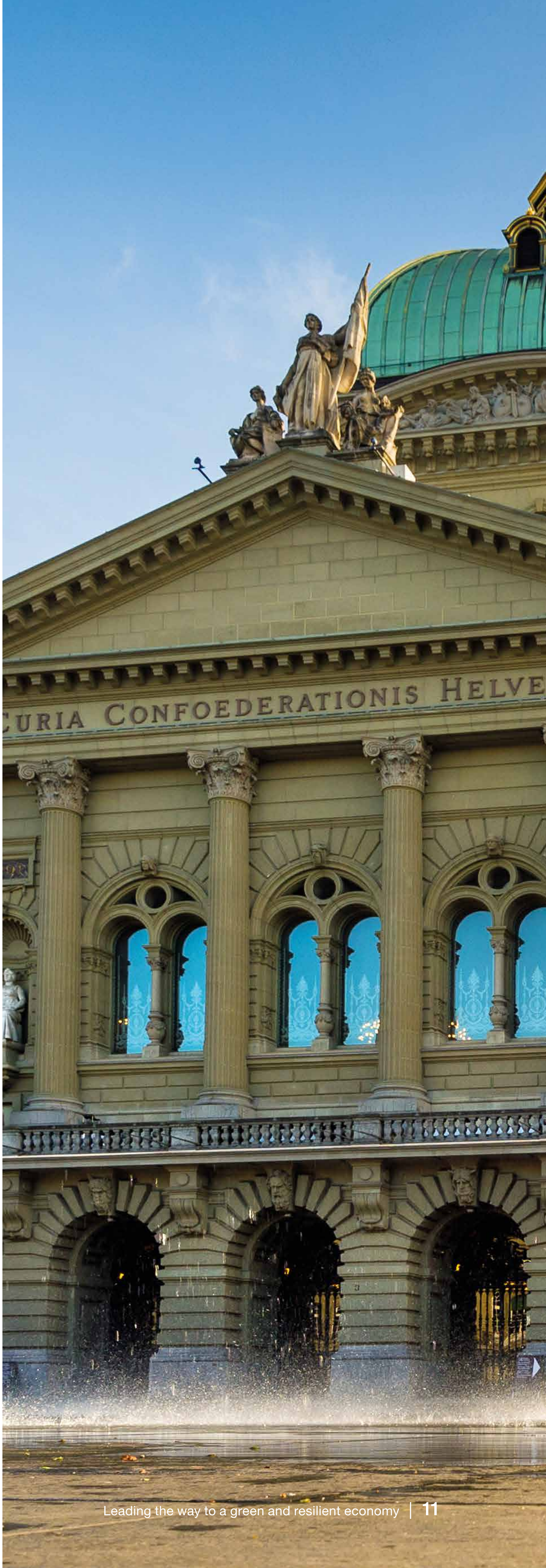
Over the recent years a wide array of actors have expressed their opinion on sustainable finance and sharpened their positions. This comes against the background of an impressive growth in sustainable investments in Switzerland, as evidenced by the latest Swiss Sustainable Investment Market Study 2020.[25] When analysing the current debate it appears that most actors agree on the following statements:

1. sustainable finance has the potential to become the new unique selling point of the Swiss financial sector as it is strongly tied to Swiss qualities such as high quality and excellence;
2. Switzerland is well equipped to be a frontrunner in the sustainable finance space;
3. the Swiss financial sector is increasingly asked to integrate sustainability considerations into financial decision-making and to position itself with regards to sustainable finance;
4. financial flows play a crucial role for the achievement of international commitments such as the Paris Agreement and the Sustainable Development Goals (SDGs);[26]
5. the financial sector and the real economy are closely interdependent and the transformation of the one requires the transformation of the other.

> “The financial sector can contribute to ensuring that capital is invested in sustainable projects, companies and countries. Against the backdrop of the major challenges faced today, it is extremely important and urgent that we implement the necessary changes that will lead to a more sustainable allocation of capital.”
>
> H.S.H. Prince Max von und zu Liechtenstein, CEO LGT

[25] According to this study, between 2018 and 2019, sustainably managed assets have increased by 62%, reaching around CHF 1,163 billion of sustainable investments in 2019. https://www.sustainablefinance.ch/en/swiss-sustainable-investment-market-study-2020-_content---1--3037--35722.html

[26] As a member of the UN, Switzerland has committed itself to implementing the UN 2030 Agenda for Sustainable Development with the 17 Sustainable Development Goals (SDGs) at its core. They balance the economic, social and ecological dimensions of sustainable development and place the fight against poverty and sustainable development on the same agenda for the first time. https://www.eda.admin.ch/agenda2030/en/home.html



Despite these agreements the Swiss debate is still characterised by a number of contrasting views with regards to the purpose that sustainable finance should serve (e.g. competitiveness of the financial sector vs. contribution to sustainability goals), the scope it encompasses (e.g. ESG vs. climate change), the business lines it focuses on (e.g. lending vs. investment) and the type of intervention that is required or desirable (e.g. regulation vs. voluntary action).

The increasing momentum in sustainable finance is not only being seen in Switzerland. The two most interesting developments in recent years pertain to the EU and to the Network on Greening the Financial System (NGFS) and some individual central banks. Despite this common trend, the approach of the EU[27] and the NGFS[28] on sustainable finance is clearly grounded in the aim to increase environmental policy ambitions and to mobilise investment capital at scale for sustainable activities.

- **European Union (EU):** With its Action Plan on Sustainable Finance, the EU is one of the pioneers in sophisticated sustainability regulation. The introduced measures and proposals are bold and have far-reaching consequences for the financial industry and the broader economy not only in EU member states but also in Switzerland.[29] They include a legally defined classification system for environmentally sustainable economic activities (green taxonomy), extensive sustainability-related disclosures for financial products and services, as well as various amendments to existing regulatory frameworks such as MiFID II, UCITS, AIFMD, IDD and Solvency II.[30] The amount of legislative proposals and the fast pace at which they are adopted shows the EU's high level of ambition. A renewed Sustainable Finance Strategy with further extensive proposals is currently in public consultation. In addition, the European Green Deal provides a new European growth strategy with actions for preserving ecosystems and biodiversity and mobilising the industry for a circular economy. Further initiatives include the EU Biodiversity Strategy for 2030 and the associated action plan, a proposal for a European climate law and a proposal for a circular economy action plan. From a supervisory perspective, the European Central Bank (ECB) has also signalled strong support in the field and is consulting on its guide on climate-related and environmental risks.
- **Network for Greening the Financial Systems (NGFS) and others:** Since its creation and the publication of its "call to action" in April 2019, the NGFS and its constituting members have been very active. In its Guide for Supervisors published in May 2020, the NGFS explicitly warned of potential greater impacts due to the combined effects of climate-related and environmental risks, as they may reinforce each other through a negative feedback loop.[31] Individual central banks and financial regulators have complemented the action from the NGFS with important steps at the national level. Particularly noteworthy in this context are the report of the Dutch central bank (DNB) which highlights biodiversity-related financial risks as the next frontier[32], the clear signals from ECB President Christine Lagarde regarding putting green policy at the top of the agenda[33] and the trailblazing study "Green Swan – Central banking and financial stability in the age of climate change"[34] by the Bank for International Settlements.

"The purpose of finance is to serve society. Sustainability encompasses many aspects. We therefore welcome biodiversity being included in a transitional pathway. The financial centre in Switzerland is still a long way off having the necessary measures to address climate and biodiversity issues effectively. At ABS we therefore welcome the PwC/WWF report identifying possible routes to a more binding action plan."

Michael Diaz, Head Investing, Member of the Management Board, Alternative Bank Schweiz

"Creating a green and resilient economy is a complex but increasingly pressing challenge, which requires broad collaboration, dialogue and mobilisation of all stakeholders. A clear and well-structured framework is critical to characterise, measure and represent the sustainability performance of financial portfolios on climate, nature and biodiversity."

Michaël Lok, Co-CEO Asset Management and Head of Investment Management, Union Bancaire Privée

Nicolas Faller, Co-CEO Asset Management and Head of Institutional Clients, Union Bancaire Privée

27 EU Action Plan "Financing Sustainable Growth": "Sustainability and the transition to a low-carbon, more resource-efficient and circular economy are key in ensuring long-term competitiveness of the EU economy. Sustainability has long been at the heart of the European Union project and the EU Treaties give recognition to its social and environmental dimensions. The EU is committed to development that meets the needs of present and future generations, while opening up new employment and investment opportunities and ensuring economic growth." https://ec.europa.eu/info/publications/sustainable-finance-renewed-strategy_en

28 On their website the NGFS mentions: "The Network's purpose is to help strengthening the global response required to meet the goals of the Paris agreement and to enhance the role of the financial system to manage risks and to mobilize capital for green and low-carbon investments in the broader context of environmentally sustainable development. To this end, the Network defines and promotes best practices to be implemented within and outside of the Membership of the NGFS and conducts or commissions analytical work on green finance." https://www.ngfs.net/en/about-us/governance/origin-and-purpose

29 For a discussion of the impacts of the EU Action Plan on Sustainable Finance on Swiss banks, see Jean-Luc Chenaux and François Piller, Does the EU Action Plan on Sustainable Finance Impact Swiss Banks?, in: Jusletter, 25 May 2020

30 Markets in Financial Instruments Directive (MiFID II), Undertakings for the Collective Investment in Transferable Securities Directive (UCITS), Alternative Investment Fund Managers Directive (AIFMD), Insurance Distribution Directive (IDD)

31 https://www.ngfs.net/sites/default/files/medias/documents/ngfs_guide_for_supervisors.pdf

32 Indebted to Nature https://www.dnb.nl/en/binaries/Indebted%20to%20nature%20_tcm47-389172.pdf

33 https://www.ecb.europa.eu/ecb/orga/climate/html/index.en.html

34 https://www.bis.org/publ/othp31.pdf

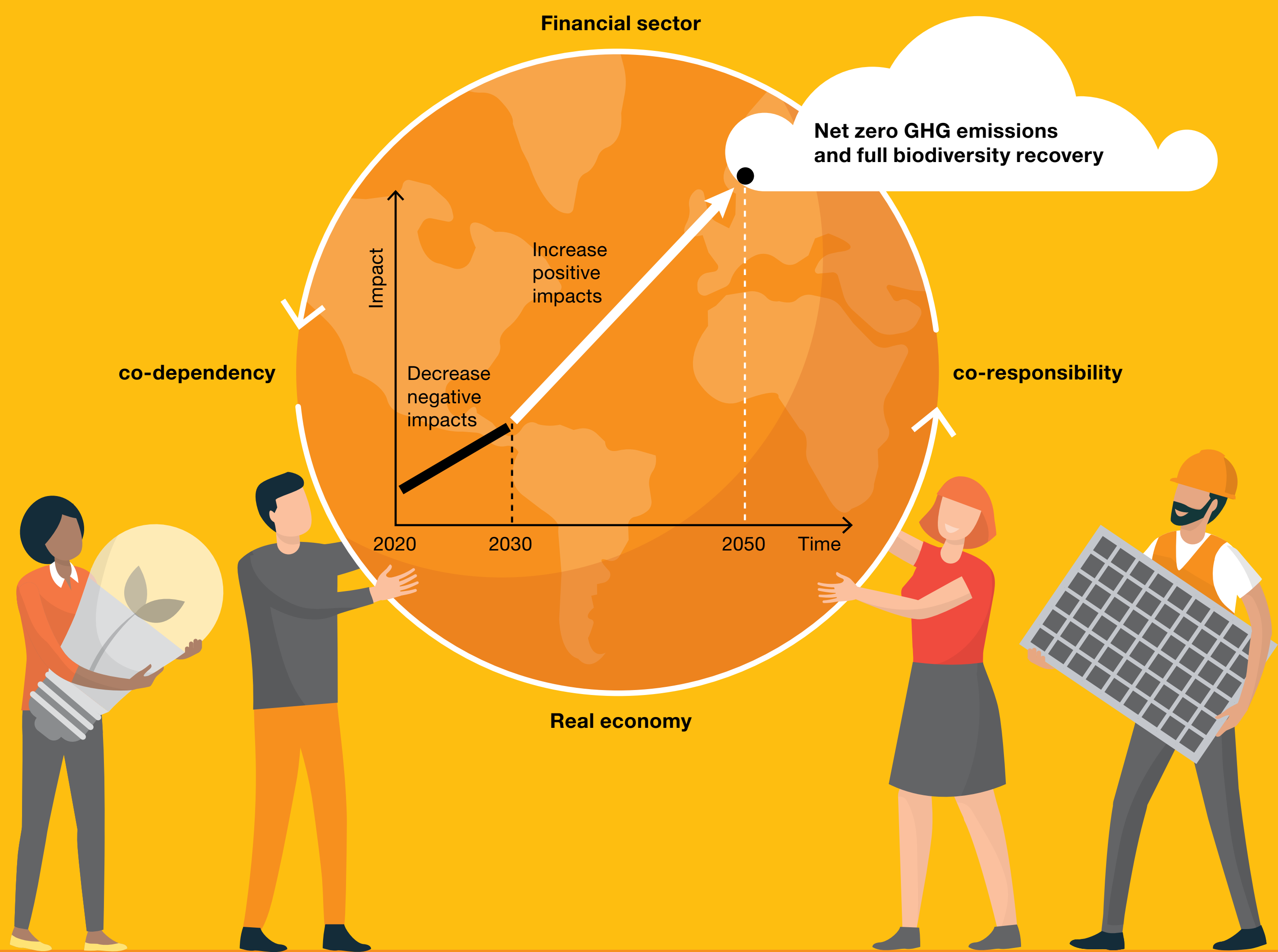
3. Financial flows for a green and resilient economy: the core of a Swiss-quality approach to sustainable finance

> "Moments of crisis are often also moments of opportunity. The Federal Council recognized sustainable finance as part of the national strategy to promote the competitiveness of the Swiss financial industry. It should now ensure that Switzerland does not miss this milestone and seize all opportunities it implies. For this to happen, a clear, proactive and forward-looking approach should be taken."
>
> Jean-Luc Chenaux and François Piller, Does the EU Action Plan on Sustainable Finance Impact Swiss Banks?, in: Jusletter, 25 May 2020

3.1 Rationale for a Swiss-quality approach

We live today in an era of high uncertainty and disruption. The COVID-19 pandemic has revealed the high fragility and limitations of our economic model, which have already been displayed by the environmental challenges. These challenges heighten the need to adapt to systemic changes and to innovate ahead of the curve. The bottom line is that we must seek alternatives to our current unsustainable production and consumption pattern to achieve the goals set by the Paris Agreement and the Convention on Biological Diversity. Thanks to its pivotal role at the interface with the real economy, the financial system can act as an engine in the global economy's transition towards sustainable development.

Figure 1: Leading the transition to a greener and more resilient economy

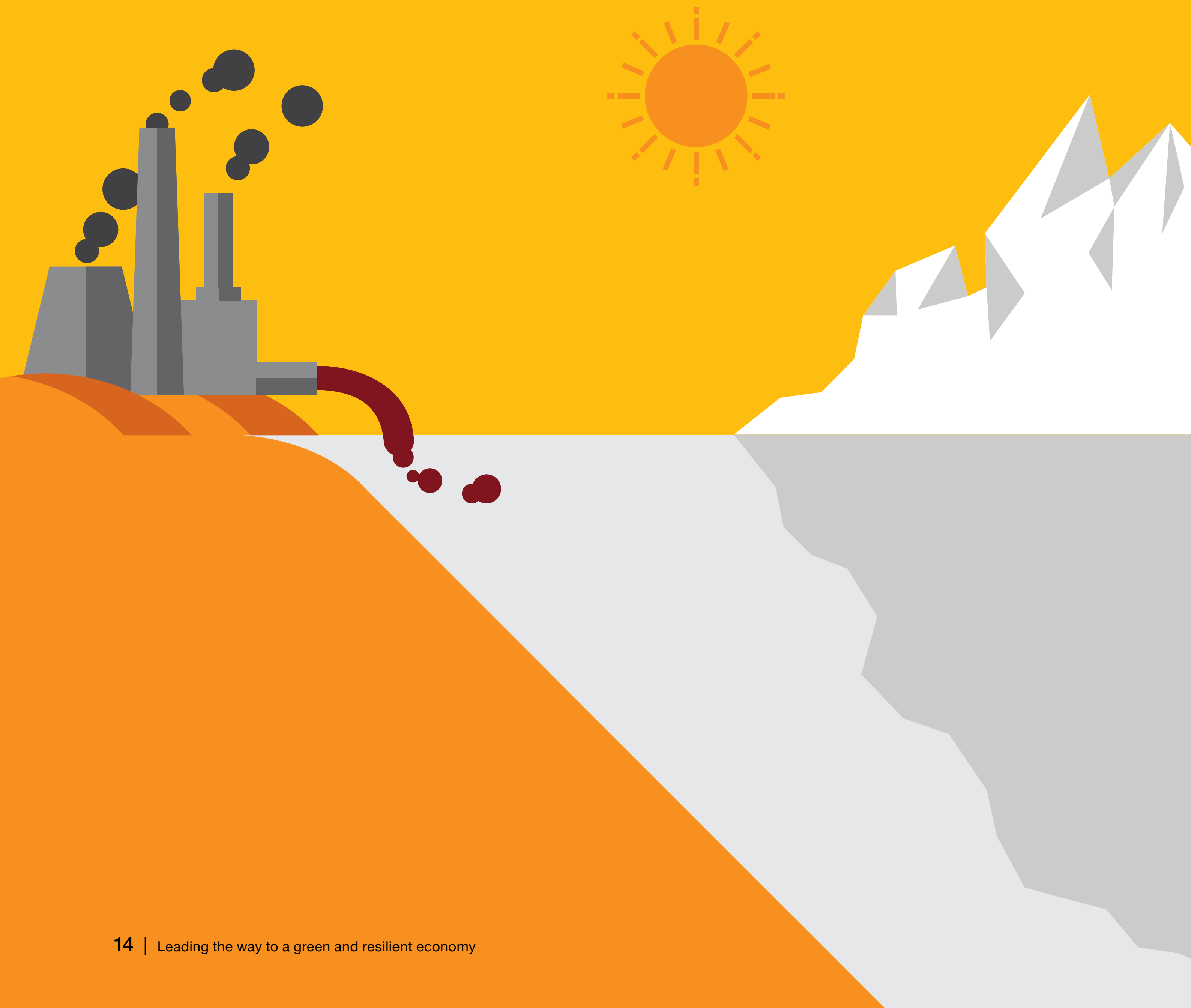


Realising the shift towards a financial system that encourages a greener and more resilient economy is, however, not a random process. Rather it must rely on a strategic approach that delivers clarity of direction and quality and can be used by all financial market stakeholders as a common reference point. For the financial sector to play its part in the transformation of the real economy, the relevant actors need first to agree on a common objective and a credible game plan for getting there. In our view, the financial sector's contribution to addressing the climate and biodiversity challenges will have to take centre stage. Realising the goals set out in this paper will have a positive impact not only on climate and biodiversity. It will also generate several economic and social benefits. Failing to align financial flows with global environmental goals will inevitably derail us from a sustainable path and result in dangerous consequences for our economies and societies.

Based on this, PwC and WWF emphasise the need for a Swiss-quality approach to sustainable finance with the following goal (see Figure 1):

Leading the transition to a greener and more resilient economy: financial flows managed or controlled by Swiss financial institutions align with a transitional pathway to achieve net zero GHG emissions and fully recover biodiversity by no later than 2050. To achieve this goal, all new and renewed financial engagements need to prove from 2030 onwards that they cause net zero GHG emissions and restore and enhance biodiversity.

> “We believe that all actors need to join forces to solve the existential challenge of climate change and endangered biodiversity. As a global investment manager we are fully committed to playing a proactive role in the transition towards a more sustainable economy and society.”
>
> Andreas Knörzer, Head Vontobel ESG Investment Governance Committee



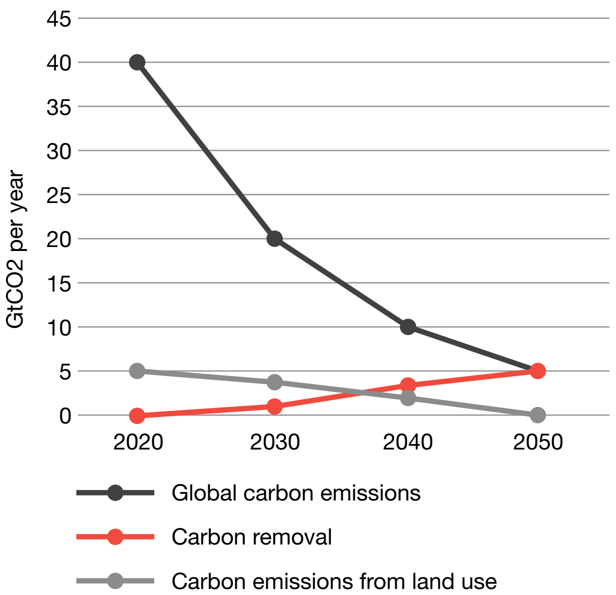
3.2 How to operationalise "financial flows for a green and resilient economy"

3.2.1 The scientific findings

With regard to climate change, the Intergovernmental Panel on Climate Change (IPCC) is the key authoritative source. In its special report on global warming of 1.5°C, published in October 2018, it concluded that net CO2 emissions need to be reduced to zero globally by around 2050 in order to stabilise global temperatures and avoid serious changes in ecosystems and negative consequences for humankind and biodiversity.[35] The same report states that the atmosphere can absorb no more than 420 gigatonnes (Gt) of CO2 as of the end of 2017 if we are to stay below the 1.5°C threshold. Since around 42 Gt of CO2 is emitted globally every year, less than ten years remain before this budget is expected to be used up.[36] It is therefore of utmost importance to accelerate the full decarbonisation of our world without further delay. The steeper the decrease in CO2 emissions now, the higher the probability that global warming will not exceed the 1.5°C target by 2050. Further, a significant decrease now will buy us more time to exhaust our remaining carbon budget. If annual CO2 emissions remain at today's level of around 42 Gt, the subsequent decrease will have to be disproportionally higher for us to have a chance to stay within the 1.5C° target. Hence, resolute action that reduces our annual CO2 emissions is needed now.

Figure 2: Global carbon law guiding decadal pathways

Source: Adapted from Rockström et al. (2017).



However, even if GHG emissions are reduced at rocket speed now, it is not certain that the global targets will be met without relying on so-called negative emissions. This has to do with the fact that our atmosphere has already accumulated a large amount of CO2 that needs to be removed in order to pay off our growing carbon debt (see Figure 2). There are different negative emissions technologies that remove CO2 from the atmosphere. However, all options that are discussed or already applied today are associated with considerable uncertainties and imply potentially significant trade-offs, for instance regarding land use.[37]

Regarding the loss of biodiversity[38], the scientific community has not yet agreed on a clear, quantified target that must be respected in the long run, unlike the 1.5°C threshold in the case of climate change. Yet there is ample scientific evidence that never in human history has biodiversity declined as fast as today. Nature across most of the globe has been significantly altered by multiple human drivers, with the great majority of indicators of ecosystems and biodiversity showing rapid decline. 75% of the land surface has been significantly altered, 66% of the ocean area is experiencing increasing cumulative impacts, and over 85% of wetlands (area) has been lost.[39] In addition, in the last 50 years global wildlife populations have declined by 60%, leading to a global environmental crisis which is often referred to as the sixth mass extinction. The massive degradation of oceans, forests, freshwater bodies and other ecosystems is undermining nature's ability to provide vital goods and services for all societies to thrive. The same logic that applies to climate change thus also holds true for biodiversity: the negative trend needs to be reversed rapidly and the curve of biodiversity loss be bended as soon as possible. By 2030 the decline of natural habitats and the loss of species must reach an inflection point from which the trend leads upwards on a path to full recovery by 2050.

It is worth emphasising that **climate stability and biodiversity are closely interconnected** and ultimately two sides of the same coin. In fact, climate change further accelerates the extinction of species and leads to rapid changes in ecosystems.[40] Conversely, the loss of biodiversity substantially reduces the capacity of ecosystems to sequester carbon, hence further worsening climate change.[41] The result is a negative spiralling loop. The negative impacts that arise from biodiversity loss and climate change are felt by nature and people across the globe. However, the relation between climate stability and biodiversity could also be a virtuous cycle.

3.2.2 Translating the scientific findings into goals for the financial sector

This paper claims that financial flows should, first and foremost, serve to create a green and resilient economy. To achieve this, financial flows managed or controlled by Swiss financial institutions need to follow a well defined out and measurable transitional pathway to achieve net zero greenhouse gas (GHG) emissions and fully recover biodiversity by no later than 2050. This basically means translating the scientific facts on climate change and biodiversity loss into goals and guiding principles for the financial sector.

35 https://www.ipcc.ch/sr15/

36 See MCC carbon clock for more details https://www.mcc-berlin.net/en/research/co2-budget.html

37 https://www.mcc-berlin.net/en/research/policy-briefs/negativeemissions.html

38 The most commonly used definition of biodiversity – from the Convention on Biological Diversity (CBD) – is diversity of species, variation of genes and different ecosystems.

39 https://ipbes.net/global-assessment

40 According to the precited IPBES report, the direct drivers of change in nature with the largest global impact during the past 50 years have been (starting with those with most impact): changes in land and sea use; direct exploitation of organisms; climate change; pollution; and invasion of alien species.

41 https://www.pwc.ch/en/publications/2020/nature-is-too-big-to-fail.pdf

PwC and WWF therefore suggest that until 2050 the combined efforts from all relevant actors are geared towards creating a net zero GHG-emitting and full biodiversity-recovering real economy, which presently does not exist. The financial sector and the real economy are in a co-dependent relationship. Only if the real economy transforms will the financial sector be able to achieve the set goals. On the other hand, the financial sector plays a pivotal role in this transformation of the economic system by reducing its exposure to high-emitting economic sectors and activities, by engaging vigorously with the invested companies and policymakers and by creating new financial models and vehicles for a net zero, biodiversity-recovering economy. This does not mean that each investment, loan or insurance policy that is available on the market today will comply with the goal set for 2050. However, it is crucial that the negative environmental impacts of financial flows decrease substantially over the next ten years. While the real economy is far from being compliant with the net zero GHG emission and full biodiversity recovery goal, the significant decrease in negative impacts is a goal that can be reached. Charting a pathway to sustainability is key to allow the financial sector and the real economy to adapt and reorient their activities and avoid any disruptive changes. It is indispensable to advance and accelerate the transition to a greener and more resilient economy. However, in the near future, carbon emissions and biodiversity destruction are expected to continue. To reverse this trend over the longer term, it is imperative that from 2030 onwards all new financial flows or refinancing activities cause net zero GHG emissions and restore and enhance biodiversity. This creates a second strong, necessary push to achieve the final goal by 2050. Furthermore, it builds on the premise that by 2030 the real economy will have had the time to adapt and transform with regards to the net zero GHG emission and full biodiversity recovery goal, which would again facilitate the task of the financial sector. Figure 1 indicates this co-responsible relationship between the financial sector and the real economy for the transformation towards a green and resilient economy. At the same time, further dialogue and collaboration between the financial sector, the real economy and the scientific community is needed in order to define universal, scientifically-driven standards for the measurement of biodiversity impacts and the required data.

3.2.3 Levers of the financial sector

In our view, the financial sector has three main levers at its disposal that it can use to contribute to achieving the set-out goal.

Biodiversity risks in the financial sector:

Similar to climate risks, biodiversity loss can translate into material financial risks (taking form of transition, physical, litigation and systemic risks) and can transform into the established risk management types. Further information can be found in the PwC / WWF Report Nature is too big to fail (2020).

Reduce negative climate and biodiversity impacts: Financial institutions can significantly reduce their climate and biodiversity impacts by screening their portfolios for “transformation-incompatible” investments, loans and insurance claims. By decreasing and progressively stopping financing harming activities, the financial sector contributes to the necessary shift of financial flows from financing “dirty” activities (i.e. activities which are not consistent with a low-carbon, nature-positive transition) toward “green” activities.[42]

Encourage transformation: With regard to the “transformation-compatible” sectors, industries and economic activities, the financial actors should have clear transformation plans providing engagement and voting strategies for the investee companies. Only by engaging with off-the-course companies and credibly raising the threat of divesting from a company will it be possible to further decrease the negative climate and biodiversity impacts of financial flows. Furthermore, it is inherently in the financial industry’s interest to advocate for clear policy directions and smart regulatory frameworks that facilitate the transformation of the real economy and it should therefore make its voice heard. Signalling support to those business actors that call for effective carbon pricing as a critical enabler to raise climate ambition is a case in point.

Enable a net zero, biodiversity-recovering economy: As there are currently hardly any net zero, biodiversity-recovering economic practices, the financial sector has a chance to kickstart and nurture this kind of activity, by providing new and innovative investment, lending or underwriting vehicles and opportunities. The financial sector could, for instance, engage in ways to unlock capital for the development and deployment of the technologies and infrastructure required for the transition to a sustainable economy, such as the roll-out of electric cars, offshore wind and low-carbon heating options.

3.3 Associated economic and social benefits

Healthy nature and ecosystems are key for human wellbeing and development. Aligning financial flows such that by 2050 global warming does not exceed 1.5°C and biodiversity is fully recovered seems imperative for sustaining life on earth. Additionally, realising the overarching goal is associated with a series of economic and social benefits.

> “To preserve our planet, we must take responsibility for our investments. The transformation of the financial system thus requires a sound sustainability analysis of companies, supported by key legal standards that are feasible.”
>
> Doris Hauser, Head of Sustainability Research, Forma Futura Invest

[42] For a discussion of the role of the financial sector and the potential of financial regulation to support the financing of the transition, see https://www.i4ce.org/wp-core/wp-content/uploads/2020/06/RegulationBasCarbone_VA.pdf

3.3.1 Micro- and macroeconomic benefits

Open new market opportunities and create jobs: The financial sector can play an important role in encouraging and accompanying companies in their green transition by offering financial products and services for a net zero GHG-emitting and full biodiversity-recovering economy. This equates to what Patrick Odier, Chairman of Swiss Private Bank Lombard Odier, calls the "biggest investment opportunity" for the financial sector over the coming decade.[43] Nature-based solutions are a good case in point. Preserving and restoring ecosystems can lead to enhanced carbon sinks on land and in the oceans, which in turn helps to limit global warming. Recent science shows that natural climate solutions could provide around 30% of climate mitigation by 2030.[44] As evidenced in a new report from WWF Netherlands, there is a quest for bankable nature solutions which have the ability to create positive environmental returns that lead to improved biodiversity and climate mitigation and/or adaptation, while also being attractive for financial institutions to invest in.[45] With regard to the employment impact of the transition to a green economy, the International Labour Organization (ILO) estimated in 2018 that 18 million jobs could be created by achieving sustainability in the energy sector alone.[46]

Reduce the financial risks and strengthen the resilience of financial markets and the economy as a whole: Environmental risks such as climate change and biodiversity loss entail important financial risks which can materialise in different financial products. However, conventional risk management has marginal interest for "non-traditional", long-term risks such as climate change or biodiversity loss. Various institutions such as the Bank for International Settlements, the European Central Bank, NGFS, IOSCO,[47] UNEP and the World Bank have highlighted the necessity to address these, recognising that "traditional" risk categories are also affected by environmental financial risks. Moreover, climate change and biodiversity loss are a systemic risk in that they jeopardise the stability of the financial system.[48] This is even more the case as the costs associated with these risks increase with every day of inaction.[49] The later measures are taken, the more drastic they need to be, which again increases the risk of a financial crisis ("too late, too sudden" problem).

Ensure level playing field by granting market access and strengthen competitiveness of the Swiss financial sector: Digitalisation, the decline of investment banking, increased regulatory pressure and the unclear legal relationship with the European Union could all tamper the competitiveness of the Swiss financial sector. Emphasising the positive environmental impact of financial flows should allow Switzerland not only to ensure its alignment with international agreements and new regulatory developments such as the EU Action Plan on Sustainable Finance. It would also help the Swiss financial centre to distinguish itself from fierce competitors such as France, Great Britain and Singapore, which are all intent on making sustainable finance their unique selling point.

3.3.2 Social benefits

Investor/consumer protection: From an investor/consumer perspective, a sustainable Swiss financial sector should target higher investor protection[50] related to sustainability features in all financial services and products ranging from mainstream ones to those targeting a sustainability impact, and everything in between. In the sustainability context, this includes especially the areas of asymmetric information[51], conflicts of interest, and knowledge and competence. It should be emphasised that although the primary target group might be individual retail investors, institutional investors will ultimately also benefit from such a framework and need to be included.

Respect and align with consumer preferences: The rising public demand for investments that build a better world is a clear reflection of the changing mindset that is going on in our society. In particular, millennials tend to show a strong interest in sustainability themes related to their investments.[52] The latter are the customers of tomorrow and form the generation that will inherit significant wealth over the coming decades. As many millennials care deeply about the climate, biodiversity challenges and the positive impact of their money, financial institutions are challenged to respond to the new consumers' preferences and to suggest suitable products and services. These customers expect sustainable products to have a tangible positive impact on the environment and society. Hence, issues such as consumer protection and greenwashing with regards to financial products and services have gained much attention.

[43] https://www.businessinsider.com/best-investment-opportunity-of-last-25-years-patrick-odier-davos-2019-2019-1?r=US&IR=T

[44] https://www.pwc.ch/en/publications/2020/nature-is-too-big-to-fail.pdf

[45] https://wwfeu.awsassets.panda.org/downloads/bankable_nature_solutions_2__1.pdf

[46] https://www.ilo.org/global/publications/books/WCMS_628654/lang--en/index.htm

[47] International Organization of Securities Commissions

[48] The financial system can be affected through the institutions themselves (endogenous risk). Failure in financial institutions' functions (risk management) as a result of not taking biodiversity risks properly into account can lead to risk feedback loops and contagion, which can spiral out of control and impede the smooth functioning of the financial system.

[49] https://www.bafu.admin.ch/dam/bafu/de/dokumente/wirtschaft-konsum/externe-studien-berichte/cost-of-inaction-einschaetzung-zum-forschungsstand-und-anwendung-fuer-die-umweltpolitik.pdf.download.pdf/Cost-of-Inaction-Einschaetzung-zum-Forschungsstand-und-Anwendung-fuer-die-Umweltpolitik.pdf

[50] Investor protection refers to protecting the underlying trust of investors against misuse or malfunction. "In particular, 'small depositors' and institutional clients (such as pension funds), which together provide a bank with available liquid deposits, are affected" see Koumbarakis, A. (2018): "The Economic Theory of Bank Regulation and the Redesign of Switzerland's Lender of Last Resort Regime for the Twenty-First Century", Schulthess Verlag.

[51] Generally, there are three phenomena of asymmetric information, namely "adverse selection", "moral hazard" and "ruinous competition", that justify any form of intervention see Koumbarakis, A. (2018): "The Economic Theory of Bank Regulation and the Redesign of Switzerland's Lender of Last Resort Regime for the Twenty-First Century", Schulthess Verlag.

- Adverse selection indicates that clients cannot evaluate the quality of the financial product, which is also referred to as hidden information and can be understood as "green/impact-washing". In other words, green/impact-washing is a source of market failure. Moral hazard arises due to uncertainty about the quality of sustainable financial products and sustainability preferences because on one hand, financial institutions cannot observe their clients' sustainability preferences properly and, on the other hand, due to behaviour uncertainty financial institutions have difficulty identifying the target market of the sustainability product (see Koumbarakis 2018). Therefore, requirements need to be emphasised regarding the integration of clients' sustainability preferences (climate and biodiversity) into the advisory process (see SBA 2020) and into the product approval and review process.
- Conflict of interests: As an external party, investors need to be protected from such conflicts including possible misselling practices within the distribution of sustainability products, remuneration-related conflicts of interest or those arising in the course of managing sustainability portfolios.
- Knowledge and competence: Not only investors need to be better educated on ESG investment features for a sustainable financial system in Switzerland to function well. It needs to be ensured that all relevant employees at financial institutions possess the necessary knowledge and competence to understand the sustainability-related risks and opportunities.

[52] https://www.msci.com/documents/10199/07e7a7d3-59c3-4d0b-b0b5-029e8fd3974b

"No problem can be solved from the same level of consciousness that created it."

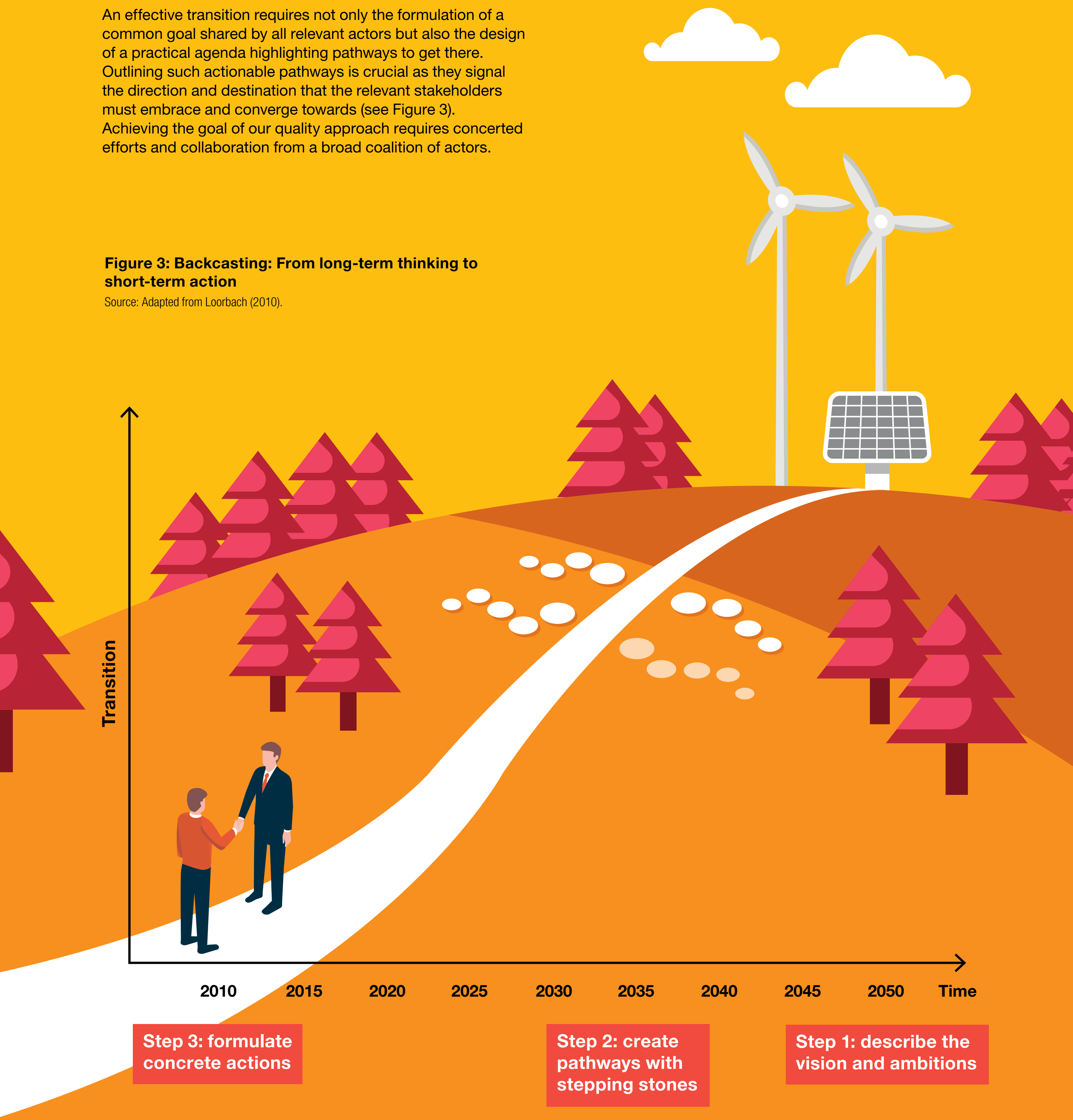
Albert Einstein

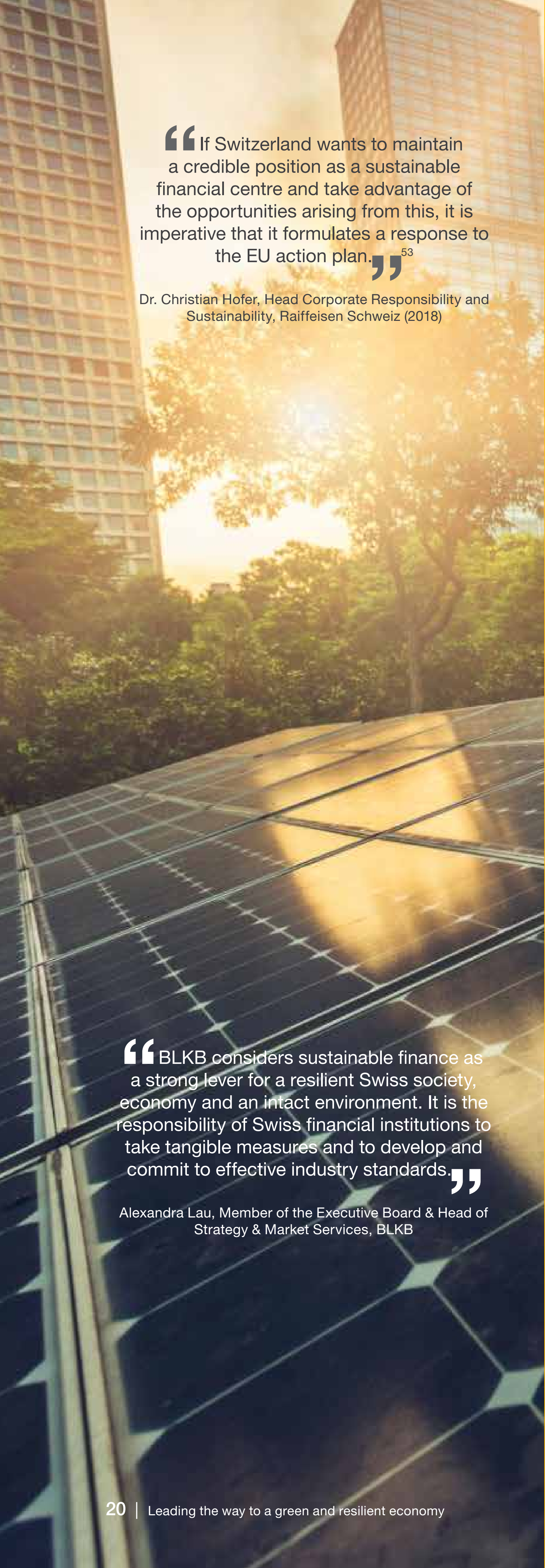
4. An action agenda to build a green and resilient economy

An effective transition requires not only the formulation of a common goal shared by all relevant actors but also the design of a practical agenda highlighting pathways to get there. Outlining such actionable pathways is crucial as they signal the direction and destination that the relevant stakeholders must embrace and converge towards (see Figure 3). Achieving the goal of our quality approach requires concerted efforts and collaboration from a broad coalition of actors.

Figure 3: Backcasting: From long-term thinking to short-term action

Source: Adapted from Loorbach (2010).





“If Switzerland wants to maintain a credible position as a sustainable financial centre and take advantage of the opportunities arising from this, it is imperative that it formulates a response to the EU action plan.”[53]

Dr. Christian Hofer, Head Corporate Responsibility and Sustainability, Raiffeisen Schweiz (2018)

“BLKB considers sustainable finance as a strong lever for a resilient Swiss society, economy and an intact environment. It is the responsibility of Swiss financial institutions to take tangible measures and to develop and commit to effective industry standards.”

Alexandra Lau, Member of the Executive Board & Head of Strategy & Market Services, BLKB

This final chapter proposes an action agenda with a set of outcome-oriented, practical measures that need to be implemented over the coming years. Collectively, they have the potential to lead the way to a greener and more resilient financial system that protects our natural ecosystems and ensures climate stability in the long run. To produce the desirable effects, it is imperative to start working on all measures simultaneously. Only by adopting a comprehensive view and engaging on all fronts will we have a chance to successfully transition from the status quo to a world with net zero emissions and healthy ecosystems. For a successful achievement, we encourage taking an ambitious but also realistic approach when implementing any measures and providing a clear policy framework consisting of, at the minimum, a common understanding of sustainability, enhanced disclosure requirements and sufficient data basis from the real economy.

As outlined previously, realising the transition towards a green and resilient financial system is not possible without fundamentally altering the way in which our economic system works. Aligning financial flows with a net zero GHG emissions and full biodiversity goal is thus intimately linked to the transformation of the real economy. The proposed action points are therefore divided into two broad sets: one containing measures aimed at aligning financial flows with climate and biodiversity goals, and one encompassing measures that are expected to support and accelerate the transition to a greener and more resilient financial system. Regarding the first set of measures, they are broken down along four principles, namely “define”, “disclose”, “measure” and “manage”. The logic underpinning this categorisation is that several results need to happen before being able to make financial flows consistent with a carbon-neutral and biodiversity-friendly future. The measures contained in the second set have in comparison a wider focus by targeting sectors and policy areas outside the financial system as well. The buy-in from the financial sector is nevertheless essential for their successful implementation.

What appears clear from the proposed menu is that concerted efforts from all relevant stakeholders are required to realise the action agenda. Cognisant of this co-responsibility of the various actors (regulator, policymakers, financial industry, data providers, academia, civil society, etc.) we have renounced to specify which measure should be taken forward by which actor. In our view, developing a fully-fledged action plan with clear roles, responsibilities and timelines is a follow-up task that should be taken on by all relevant sustainable finance actors jointly. It is important to stress that the proposed measures are neutral in terms of the type of intervention approach (market vs. regulation). In our view, a smart mix of voluntary, self-regulatory and regulatory action is most conducive to make ends meet and ultimately attain the stated objectives.[54] We have, however, indicated for each measure how it relates to the EU regulatory framework.

We are aware that some of the listed measures are more relevant and urgent than others to achieve the goals set out in this paper. We have therefore singled out what we consider to be the most impactful leverage points. This assessment is based on a judgment by over 20 sustainable finance experts whom we have asked to rate the different measures according to their presumed effectiveness. Acting with resolve and determination on these measures will significantly increase the chances of success. They deserve therefore high priority and should be implemented right away.

[53] https://dievolkswirtschaft.ch/de/2018/10/hofer-11-2018/)

[54] For more information on the discussion of the type of intervention approaches, see the Annex of this report.

1. Aligning financial flows with net zero GHG emissions and full biodiversity recovery by 2050

Principle	Measure	Relationship with EU regulatory framework	Estimated effectiveness
Define	Political goals and institutional arrangements		
	• Turn Switzerland's political commitment to **net zero GHG emissions by 2050** into a legal obligation for financial actors in Switzerland and set interim emission targets.	More ambitious	+++
	• Support the adoption of a **new target in the Convention on Biological Diversity (CBD)** on alignment of all financial flows with global biodiversity goals, similar to article 2.1(c) of the Paris Agreement and make it as a legal obligation for financial actors in Switzerland.	More ambitious (although plans in the EU are underway)[55]	+
	• Set up a **permanent technical expert group** at national level with members of civil society, academia and the finance industry to advise the Federal Council on sustainable finance and define an action plan to implement the proposed Swiss-quality approach to sustainable finance.	Similar measures in the EU (Sustainable Finance Platform)	++
	Mandates and legal duties		
	• Revise current law regarding **fiduciary duty** to make it mandatory for asset managers to: 1) consider climate- and biodiversity-related financial risks in and impacts from investment and financing decisions; 2) check and take into account clients' sustainability preferences; 3) exercise active voting and engagement strategies with regards to net zero GHG emissions and full biodiversity recovery.	Required for equivalence More ambitious[56]	+++
	• Adjust the **mandates of the SNB and FINMA** to clarify that addressing climate- and biodiversity-related financial risks and impacts are part of their mandate.	Similar developments in the EU[57]	+++
	• Require **credit rating agencies** to integrate climate- and biodiversity-related financial risks and impacts into their credit risk analyses and ratings.	More ambitious	+++
	• Review **financial accounting standards** (such as the IFRS framework) to reflect climate- and biodiversity-related financial risks and impacts.	Currently more ambitious[58]	++
	Methodologies and metrics		
	• Develop and adopt a comprehensive, nuanced **classification system of climate and biodiversity-friendly and unfriendly economic activities (taxonomy).**	Required for equivalence	++
	• Drive the development of **science-based, forward-looking, and outcome-oriented metrics and indicators** for climate- and biodiversity-related financial risks and impacts and promote open access to more and better-quality data.	Required for equivalence	+++

55 See the 2020 EU Biodiversity Strategy. https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal/actions-being-taken-eu/eu-biodiversity-strategy-2030_de#documents

56 Current obligations in the EU regarding voting and engagement are generally focused on transparency.

57 See draft ECB Guide on climate-related and environmental risks, 2020. https://www.bankingsupervision.europa.eu/legalframework/publiccons/html/climate-related_risks.en.html

58 However, such plans are currently being discussed as part of the EU's Renewed Sustainable Finance Strategy.

Principle	Measure	Relationship with EU regulatory framework	Estimated effectiveness
Disclose	Strategies and targets		
	• Require companies and financial institutions to enhance transparency by establishing **measurable, science-based and time-bound strategies and targets** for reducing GHG emissions and negative biodiversity impacts, to have **asset-level transition plans and to report on progress against these targets/plans.**	Required for equivalence	+++
	Climate- and biodiversity-related information		
	• Introduce **mandatory, forward-looking disclosure of climate- and biodiversity-related financial risks and impacts at corporate and product level**.	Currently more ambitious, but planned in EU[59]	+++
	• Require asset managers to integrate climate- and biodiversity-related financial risks and impacts in **client-onboarding activities and advisory processes**.	Partly required	+
	Financial flows and data		
	• Require financial institutions to report on a yearly basis on **financial flows by economic sector, activity and asset class.**	Required for equivalence	++
Measure	Exposure to climate- and biodiversity-related financial risks		
	• Conduct and publish science-based and forward-looking **scenario analyses and standardised net zero GHG emissions and full biodiversity-recovery stress tests** to determine the exposure of financial institutions to climate- and biodiversity-related financial risks and the effects on their financial stability.	More ambitious	+
	Alignment with net zero GHG emissions and full biodiversity recovery		
	• Assess the **compatibility of all investment portfolios and outstanding credit and insurance claims** with the net zero GHG and full biodiversity recovery goal and track the alignment of all Swiss financial flows periodically.	More ambitious	++

[59] Several requirements impose transparency requirements on sustainability risks, with more details planned to be published at a later stage. EU non-financial disclosures are currently under review.

Principle	Measure	Relationship with EU regulatory framework	Estimated effectiveness
Manage	Portfolio alignment with net zero GHG emissions and full biodiversity recovery		
	• **Align asset owners' and banks' investment, lending and underwriting portfolios** with net zero GHG emissions and full biodiversity-recovery pathways and track progress.	More ambitious	+++
	• Adjust **capital requirements for banks and (re)insurers** based on the integration of climate- and biodiversity-related risk factors.	More ambitious	+++
	• Adapt the **credit and mortgage risk assessment** of financial institutions by requiring them to assess the "transformation compatibility" of each loan.	More ambitious	++
	• Amend **collateral frameworks** for financial institutions borrowing from the SNB according to their aggregate climate and biodiversity-related financial risks and impact.	More ambitious	++
	Financial products and value chains		
	• Increase the demand for net zero GHG emissions and full biodiversity recovery financial products by offering these as the **default option.**	Currently more ambitious[60]	++
	• Encourage the **development of** net zero GHG emissions and full biodiversity-recovery **financial products** of all types, correctly labelled and easily accessible for retail customers.	Similar developments in the EU[61]	+
	Awareness and capacity building		
	• Define **appropriate governance structures** within financial institutions that mainstream responsibility for climate and biodiversity financial risks and impacts across all levels.	Required for equivalence	+
	• Deploy **specific training and capacity building to all staff members working in financial institutions** on climate- and biodiversity-related financial risks and impacts, and reward climate and biodiversity expertise at the management level.	Required for equivalence	+
	• Offer **guidance and tools** for financial institutions to comply with international best practice regarding climate- and biodiversity-related financial risks (e.g. TCFD recommendations) and impacts.	More ambitious (but similar developments in the EU)	+

60 This option is currently under discussion in the EU's Renewed Sustainable Finance Strategy.

61 See, for example, the EU's ecolabel for retail financial products, EU Green Bond Standard.

2. Supporting the transition to a green and resilient financial system

Principle	Measure	Relationship with EU regulatory framework	Estimated effectiveness
Transformation of the real economy	• Include the **cost of negative climate and biodiversity externalities** into the pricing of goods and services and remove harmful subsidies.	More ambitious	+++
	• Build up **pipeline of investable projects and companies** (e.g. scale up **nature-based solutions** for mitigation, resilience and adaptation in key areas)	Similar developments in the EU	++
	• **Adopt preferential tax policies** for low-carbon infrastructure and biodiversity-friendly land uses.	More ambitious	+++
	• Revise **public procurement standards** by integrating climate- and biodiversity-related financial risks and impacts for screening public investment programmes.	Similar developments in the EU	++
	• Implement **targeted re-/financing lines/facilities** to promote credit for sectors and economic activities that contribute to the net zero GHG emissions and full biodiversity recovery goal.	More ambitious	++
Increase long-termism	Financial incentives		
	• Link a significant part of the variable **remuneration and promotion of senior management** to the achievement of net zero GHG emission and full biodiversity-recovery strategies and targets.	More ambitious, but similar developments in the EU[62]	++
	• Link part of the **dividend payout policy** at corporate level to climate and biodiversity performance.	More ambitious	++
	• Tax **short-term ownership of assets**	More ambitious, but similar developments in the EU	++
	Reporting		
	• Shift **from quarterly to half-yearly financial reporting.**	More ambitious, but similar developments in the EU	+

"In addition to achieving climate targets, biodiversity conservation is of great importance to ZKB. Protection of habitat and species diversity is firmly anchored in our sustainability policy. We discuss this aspect with our clients and contribute to regional biodiversity with gardens at our locations designed to support wild bees' habitat."

Marit Kruthoff, Head Public Service Mandate, Zürcher Kantonalbank

[62] The current obligations require more transparency on how sustainability risk is incorporated in the remuneration policies, but does not explicitly pose cer-tain KPIs or achievements.

Principle	Measure	Relationship with EU regulatory framework	Estimated effectiveness
Foster research & innovation	Research and education		
	• Foster **research & development on net zero GHG-emitting and full biodiversity-recovery technologies and products**, especially in hard-to-abate industries (steel, cement, chemicals, etc.).	More ambitious	++
	• Conduct analyses on the **interplay between climate change and biodiversity loss** and how these interdependencies affect the financial bottom line.	Similar developments in the EU	+
	• **Foster cooperation and exchange between Swiss research institutions** on sustainable finance issues through dedicated requests for proposals and mixed advisory boards at project level.	Similar developments in the EU	+
	Innovative financing mechanisms		
	• Set up funds that invest in **sustainable fintech**, thus contributing to scaling up net zero GHG-emitting and full biodiversity-recovery ventures.	Similar developments in the EU	++
	• Devise and market **de-risking schemes for business models based on a circular economy and early-stage projects.**	More ambitious, but similar developments in the EU	+
	• Encourage the **issuance of debt products with adjusted interest rates** based on pre-determined climate and biodiversity performance.	More ambitious	++
International cooperation	International engagement	n/a	
	• Promote **ambitious and stringent sustainable finance regulation** at the international level and be active in all **international financial fora and initiatives** to which Switzerland is a party (e.g. Coalition of Finance Ministers for Climate Action, International Platform on Sustainable Finance, NGFS etc.).		n/a[63]
	• Provide **technical assistance to developing countries** to help devise and implement impact-oriented sustainable finance regulation and related activities.		n/a[64]
	• Endorse the **UN-backed initiative to create a Task Force on Nature-related Financial Disclosures (TNFD).**		+

[63] This measure was not included in the evaluation by the sustainable finance experts.

[64] This measure was not included in the evaluation by the sustainable finance experts.

Conclusion

> "Sustainability is the only option for the future. And it can only be achieved if we work together."
>
> Jörg Gasser, CEO Swiss Bankers Association, 26 June 2020[65]

The Federal Council's new report "Sustainability in Switzerland's financial sector", presented at a press conference by Federal Councillor Ueli Maurer on 26 June 2020 in the presence of all relevant financial industry associations, gives a fair account of the current state of debate on sustainable finance at the national level. In short, it hails sustainable finance as the market opportunity for Switzerland that the Swiss financial sector needs to harness if it wishes to remain competitive globally. This positioning comes at a critical juncture after other European financial centres such as Frankfurt, Paris and London have made bold announcements about becoming leaders in sustainable finance.

In order to be able to distinguish itself and carve out a 'sweet spot' in this competitive landscape, PwC and WWF are convinced that Switzerland should focus on typical Swiss attributes like excellence, innovation and credibility. A new quality-approach for the Swiss financial sector is therefore needed: financial flows for a green and resilient economy. Such an approach differs significantly from the dominant political narrative as epitomised by Federal Councillor Maurer's announcement on 26 June.

Firstly, the authors believe that Switzerland can only position itself as a leading place for sustainable finance if it builds its strategy on aligning financial flows with global climate (Paris Agreement) and biodiversity goals (Convention on Biological Diversity). Making sure that by 2050 all Swiss financial flows are consistent with a net zero GHG-emitting and fully biodiversity-recovering economy is likely to give Switzerland a competitive edge over its contenders.

Secondly, PwC and WWF challenge the belief that voluntary market action alone is sufficient to mainstream sustainable finance and align financial flows with environmental objectives in a sufficiently timely manner. A smart tool mix combining a variety of different policy, regulation and voluntary actions needs to be implemented simultaneously to achieve the stated goal.

Thirdly, it is not only incumbent on financial market participants to make headway on the transition to a GHG-neutral and biodiversity-friendly future. Other actors need to move too and take their share of responsibility. Only concerted and coordinated efforts by all stakeholders (government, policymakers, market actors, civil society, etc.) will produce the desired outcomes. Clear and ambitious policy signals and a conducive regulatory framework are key in this context to facilitate and accelerate the sustainable transformation of the financial sector and the real economy alike.

Fourthly, "the future is now". If the goal of aligning financial flows to create a greener and more resilient economy is to be achieved by 2050, action needs to happen now. In view of the environmental crisis unfolding before our eyes, there is no point in wasting more time.

Lastly, PwC and WWF argue that a multiplicity of effective actions can and should be taken today to gradually move towards a net zero GHG-emitting and full biodiversity-recovering economy. For a true success, these actions should be ambitious and at the same time realistic and based on a solid policy framework. In our view, the following leverage points are likely to deliver the biggest impact and should therefore be implemented without further delay:

Leverage point 1	Turn Switzerland's political commitment to net zero GHG emissions by 2050 into a legal obligation for financial actors and set a political goal for aligning financial flows with full biodiversity recovery.
Leverage point 2	Revise the fiduciary duty such that financial actors and regulators need to integrate the financial risks associated with climate change and biodiversity loss and are responsible for minimising the negative impacts of financial flows on climate and biodiversity.
Leverage point 3	Promote meaningful metrics for climate- and biodiversity-related financial risks and impacts and define clear standards determining what can be considered climate- and biodiversity-friendly and unfriendly.
Leverage point 4	Request real economy companies and financial actors to establish measurable strategies and targets for reducing GHG emissions and negative biodiversity impacts and to disclose their climate- and biodiversity-related financial risks and impacts.
Leverage point 5	Rapidly align asset owners' and banks' investment, lending and underwriting portfolios with net zero GHG emissions and full biodiversity-recovery pathways and adjust capital requirements for banks and (re-)insurers accordingly.
Leverage point 6	Advocate for correctly pricing negative climate and biodiversity externalities and for adopting preferential tax policies for climate- and biodiversity-friendly activities, thus facilitating the transition to a green and resilient economy.

[65] https://www.swissbanking.org/en/media/positions-and-press-releases/sustainable-finance-firmly-em-bedded-in-the-swiss-financial-sector?set_language=en

Annex

Market, governmental and societal actors have a variety of mechanisms to influence the transition towards a green and resilient economy in Switzerland. The authors argue that a smart mix of voluntary, self-regulatory and regulatory action will be most effective.

- **Voluntary actions** in form of voluntary commitments by individual institutions or a group thereof

Advantages	Limitations
• potential for highly ambitious commitments • high degree of flexibility allowing for innovative solutions and individual target setting • takes into account specifics such as size, business model and client base of the financial institution • industry knowledge and expertise	• not binding • commitments could be too vague • limited external monitoring that is highly dependent on the degree of information selected by the institution • insufficient transparency could lead to greenwashing

- **Self-regulation** of the Swiss financial market via industry standards and guidelines:
  These are already a priority for major Swiss finance associations such as Swiss Bankers Association, Swiss Funds & Asset Management Association and Swiss Insurance Association (SSF 2020)[66]

Advantages	Limitations
• potential for highly ambitious commitments • high degree of flexibility allowing for innovative solutions and individual target setting • takes into account specifics such as size, business model and client base of the financial institution • industry knowledge and expertise	• not binding • commitments could be too vague • limited external monitoring that is highly dependent on the degree of information selected by the institution • insufficient transparency could lead to greenwashing

- **Regulation via legislative initiatives:**
  Although the task can be challenging, examples from other jurisdictions such as the European Union with the EU Action Plan on Sustainable Finance or the Renewed Sustainable Finance Strategy demonstrate that **sustainability-related financial services regulation is possible**

Advantages	Limitations
• legal certainty • potential to impose sustainability standards coherently across the market • captures both public and private financial flows • possibility to oversee effective implementation and intervene if the defined objectives are not met • imposes effective obligations on the real economy, such as enhanced sustainability disclosure standards to deliver the ESG data Swiss financial players need • ensures legal equivalence of Switzerland with other jurisdictions (such as the EU) and related market access	• subject to political majorities • prone to influence from different lobbying efforts (including from parties that would be negatively impacted by the introduction of sustainability-related regulation) • lengthy legislative process • risk of overregulation (leading to disproportionate burdens for smaller financial players)

[66] https://www.sustainablefinance.ch/upload/cms/user/2020_06_08_SSF_Swiss_Sustainable_Investment_Market_Study_2020_E_final_Screen.pdf

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