Topic: The Bank of Finland's position regarding the decarbonization of the ECB

11th March 2021

Dear Governor Rehn,

2021 will be a decisive year for climate action. The COP26 in sight, it is now agreed-upon that the next few years will determine whether we keep global warming under 1.5 or even 2°C[1]. The European Union and other major world powers like the United States and China are strengthening their climate pledges[2] and building the tools to follow them.

Finance will be key in achieving these goals. In fact, "Building a private finance system for net zero[3]" is one of the priorities of the COP26.

Fossil fuel production needs to decrease by at least 6% each year from 2020 to 2030 to keep global warming under 1.5°C[4]. Therefore, reducing financial support to these high-carbon energies to redirect it to sustainable alternatives should be the utmost priority and ending all support to new fossil fuel project a pre-requisite to meaningful climate action.

The European Central Bank cannot ignore this Momentum for climate action. In 2020, a growing number of voices have risen to make a simple point: climate action is not only compatible with the ECB's mandate, it is needed to fulfill it and a responsibility of the bank.

More than 167 000 Europeans[5] are already calling on the ECB to stop supporting fossil fuel companies[6] through its monetary operations and 80% of 24 000 Europeans surveyed by NGOs think climate should be the ECB's top priority[7]. They are backed by European MEPs that are asking the ECB to justify its carbon bias and to change its ways[8].

ECB President Lagarde[9], and prominent ECB board members[10], have all stressed the necessity to integrate climate to the bank's operations, notably by reviewing its "market neutrality" doctrine. The governor of the Banque de France even claimed he wanted to make the ECB "a pioneer central bank in the fight against climate change[11]". Following this dynamic, the NGFS now distinguishes between

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[1] See for example Fatih Birol's interview to the Guardian in June 2020 and data from the Net Zero Economy Index.
[2] The EU pledged to cut GHG emissions by 55-60% by 2030, China adopted carbon neutrality objectives and the US is getting back on the Paris Agreement.
[3] For a detailed outline of this priority, see the document coordinated by Mark Carney.
[4] Data from the Production Gap Report 2020.
[5] See the petition from SumOfUs, 350.org and Reclaim Finance.
[6] The ECB's asset purchases support 38 fossil fuel companies planning at least 67 new fossil fuel projects and have a dangerous carbon bias. Furthermore, current refinancing operations do not account for climate risks and impact.
[7] The results of this survey was conducted to mirror the ECB strategy review consultation and provide the opportunity for a wider audience to participate. Its results are available here.
[8] See for example Christine Lagarde's response to MEPs on asset purchases and their question on ECB's disclosure of climate related risks.
[9] See Christine Lagarde's interview with the Financial Times.
[10] For examples Isabel Schnabel and Luis de Guindos.
[11] See the interview of the French governor in Alternatives Economiques (in French).

"protective" and "proactive" measures[12], thus admitting that central banks and supervisors can have an active role in mitigating climate change.

After announcing an ambitious carbon neutrality objective by 2035[13], Finland cannot stay silent. The Bank of Finland as the power to push the ECB to take bold steps to fight the climate crisis.

A few key measures[14] should be supported to make the ECB work for – and not against – climate without requiring any changes to its mandate:

1. Align its asset purchasing programs and collateral frameworks with the Paris Climate Agreement, to support the low carbon transition[15].
2. Align its refinancing operations to the banking sector with the Paris Agreement to encourage more sustainable bank lending and fill the green investment gap[16].
3. Support asset markets for sustainable investment and coordinate operations with the European Investment Bank (or other equivalent European institutions) to ramp up green investment and lock-in a low carbon future.
4. Implement prudential measures to increase the resilience of the European banking sector to climate risks and reduce brown financial flows[17] (e.g. financing of fossil fuels).
5. Lead by example on climate disclosures and transparency by assessing and regularly communicating to elected officials the alignment of its operations with the Paris Agreement and that of the European banking sector.

Recent studies by Banque de France and the ECB[18] showed that decarbonizing both asset purchases and the collateral framework would have concrete effects on emissions. Furthermore, several central banks started using climate conditions on their monetary policy[19]. If these first measures are far from sufficient, they show that climate criteria can be used without further delay.

"Market neutrality[20]" should not be an obstacle. As you rightfully underlined, the market is not pricing climate risks[21], and therefore the current "market neutrality" principle rigs ECB operations with a carbon bias. Christine Largarde[22], Isabel Shnabel[23], François Villeroy de Galhau, Klaas Knot[24] all suggested that market neutrality should be reviewed. We hope that The Bank of Finland will push for an ambitious revision of this principle, to allow the ECB to contribute to the fight against climate change, not to block it.

[12] This distinction is made by the NGFS in its publication *Survey on monetary policy operations and climate change: key lessons for further analyses*
[13] Prime Minister Antti Rinne pledged to reach carbon neutrality by 2035 in 2019.
[14] A network of EU NGOs agreed on 5 key demands to make the ECB work for climate. The Veblen Institute also provide a note highlighting various "greening" options that fits into these 5 key demands.
[15] For precise measures to do so see Reclaim Finance's demands and the NEF and Greenpeace report.
[16] For precise measures see Positive Money Europe's report and Reclaim Finance's demands.
[17] See the analysis of Finance Watch on the need to increase prudential requirements for fossil fuel holders.
[18] See the study on collateral and on asset purchases.
[19] The Swiss National Bank excludes coal mining companies from all its portfolios. Sveriges Riksbank has been using GHG criteria to shift its monetary reserves since 2019, thus leaving behind the bonds of regions significantly involved in coal and unconventional oil and gas, and recently started conditioning its asset purchases to the respect of international norms.
[20] See CEP's analysis of market neutrality.
[21] See Olli Rehn's response to Central Banking.
[22] See Christine Lagarde's interview with Bloomberg.
[23] See Isabel Schnabel's speech.
[24] See the article quoting both François Villeroy de Galhau and Klaas Knot in the Financial Times.

As the ECB's response to Covid will exceed 5 000 billion euros in 2020-2022[25], we cannot wait for the end for the strategy review to end. If some of the proposed measures could be difficult to immediately implement, a few emergency measures could be taken to mitigate the climate impact of the ECB's Covid response and back its climate pledges. The ECB could notably exclude fossil fuel companies from its asset purchases and set-up a "green TLTRO" pilot program to support energy efficiency work all around the Union[26].

The Bank of Finland has the influence to drive a swift and meaningful decarbonization of the European monetary policy. It should launch this dynamic by implementing strong climate requirements on its own portfolios. Building on its the Principles for Responsible Investment the bank signed in 2019 and the ESG criteria it already applies[27], The Bank of Finland could easily adopt criteria to reduce its investments in fossil fuels, thus advertising its climate commitment and sending a positive signal to Italian financial institutions. It could notably take up the Banque de France's decision to drastically reduce its fossil fuel investments, with a swift exit of coal, divestment from companies significantly involved in unconventional hydrocarbon and the opposition to any new fossil fuel project of investee companies[28]. By doing so, the bank would also contribute to the recent pledge of Eurosystem central banks to improve and harmonize their investment policies[29].

We would like to discuss these propositions with your teams during a call and are at your disposal to provide more detailed recommendations and analysis.

Sincerely,

Paul Schreiber
Campaigner
Reclaim Finance

Vera Kauppinen
Campaign specialist
Coal-free Finland

[25] More than 3 000 billion in refinancing operations, 1850 in PEPP, 120 in other APP and at least 30 billion in prudential easing measures.
[26] For details on easy to implement and short-term solutions, see the open letter sent to the ECB by EU NGOs on November 19th 2020.
[27] See The Bank of Finland 's ESG policy.
[28] See Banque de France's press release.
[29] See ECB's press release.