“From Virus to Vitamin” Newsletter

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Who wants to foot the bill?

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Observatoire de la Finance

16, chemin des Clochettes
1206 Genève, Suisse
Tél.: +41 22 346 30 35

www.obsfin.ch
E-mail: office@obsfin.ch

QUESTION UNDER DISCUSSION

"The Emissions Gap Report 2021 (UNEP) shows that pre-COP 26 national climate pledges combined with other mitigation measures put the world on track for a global temperature rise of 2.7°C by the end of the century, which is well above the goals of the Paris climate agreement and would lead to catastrophic changes. To what extent can the financial system as such, or its main players, be held - morally or/and legally - responsible for insufficient progress in containing climate warming? What should, and what should not be done to rapidly change this state of affairs? By whom?"

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EDITORIAL

Who wants to foot the bill?

It has been 40 years since global warming became widely known and more than a decade since the Principles for Responsible Investment were created and the first green bonds issued. Yet capital markets are still supporting an unsustainable economy, with greenhouse gas emissions accelerating climate change.

The key issue, according to Ladislau Dowbor, is that "creating systemic disaster is more profitable than going according to long term basic sustainability demands, and money just flows to where it pays more." Against this background, the question boils down to carrots and sticks: sticks of legal constrains, stress testing and regulations; and carrots of incentives, including (carbon) price signals.

Another argument often used is that financial firms do not have enough information to make sustainable choices. However, companies have been disclosing large amounts of environmental information for years. Even worse, as pointed out by Kara Tan Bhala, "finance players knew about the devastating planetary effects of carbon emissions in the early twenty-first century. Despite this knowledge, the industry has funded fossil fuels globally for the past twenty years." This may lead to the conclusion that "the financial system can and should be held morally responsible for the dismal progress in mitigating climate change." The question remains, more responsible than the other stakeholders or as much as the rest.

However, the responsibility of the "financial system as such" for climate deterioration is difficult to settle, as explained by Etienne Perrot: "the IPCC has clearly established the consequences of global warming (the principle of affectability inherent in any responsibility), but the search for the link between cause and effect brings to light a number of actors, including governments, consumers, business leaders, professional unions, etc." In other words, responsibility is split between different players and across different sectors, which leads Valerio Bruno to consider that "the financial sector per se should not be seen as more responsible, legally or morally, than any other comparable sectors".

Ultimately, what is required may be a change of approach: climate change should not be viewed as a market failure anymore but as a systemic challenge calling for an unprecedented level of commitment and coordination between multiple actors (private and public) and instruments (eg. carbon pricing, stress testing, regulations, education). A first step in this direction would be a globally coordinated trend to steadily increase the carbon price, but who is going to foot the bill? Paradoxically, the answer seems to be "not me"

Virgile Perret & Paul H. Dembinski

"… the responsibility of the financial system for climate deterioration is difficult to establish …"

The responsibility of the "financial system as such" for climate deterioration is difficult to establish. The IPCC has clearly established the consequences of global warming (the principle of affectability inherent in any responsibility), but the search for the link between cause and effect (principle of imputability) brings to light a number of actors, including governments, consumers, business leaders, professional unions, etc. Legal responsibility (principle of judiciability) requires the establishment of binding regulations. This is in the hands of the legislator (e.g. carbon tax or a ban on financing research and extraction of fossil fuels). While waiting for such regulations, the moral responsibility of the actors remains, which comes up against the contradictory logic of their particular socio-political situations. For the most pugnacious among these actors, remains discernment.

Etienne Perrot

Jesuit, Dr. Economics sciences, editorial board of the magazine Choisir (Geneva), editorial adviser of the journal Études (Paris)

"… financial institutions can play a decisive role …"

Whatever the responsibilities for the past, **financial institutions can play a decisive role in changing the state of affairs from now on, especially by supporting the elaboration and promoting as quickly as possible the adoption of new reporting standards, through which environmental costs are integrated into profit and loss accounting. Their support will also be useful for the adoption of effective carbon pricing, a necessary step which will not be easily understood by voters.** This will translate into new credit criteria. A dose of technocratic discernment and governance is needed, in which the financial system plays the role of an indispensable transmitter. Financial leaders world-wide are prepared for that, they must be encouraged – and perhaps legally forced – by Governments.

Domingo Sugranyes

Director of a seminar on ethics and technology at Pablo VI Foundation, past Executive Vice-Chairman of MAPFRE international insurance group

"… apply the Polluter-pays Principle …"

If the market economy is to do its job correctly, every beneficiary of a good or service should pay what it costs to provide it, otherwise someone who has not benefited will have to pay. It is also a founding principle of the Protestant ethic: as Calvin said, "whatever means we use to enrich ourselves at the expense of others count as theft". **The short answer to the**

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question is therefore to apply the Polluter-pays Principle: it is fundamental, more far-reaching than its misleadingly narrow name. Countless international conventions - e.g. the Rio Declaration, Principle 16 - already require it.

Edouard Dommen

Specialist in economic ethics, former university professor and researcher in UNCTAD and president of Geneva's Ecumenical Workshop in Theology

"… a policy operating through the financial system can only be a second best …"

A policy operating through the financial system can only be a second best, less effective than a direct pricing of pollution. Regulators should ensure that financial intermediaries take due account of climate risk, for instance via stress testing scenarios. **Political authorities** could also edict guidelines applicable to the financial entities in their jurisdictions (including pension funds) on what sectors or firms should be avoided in investment decisions. **Public authorities** can play a coordination role by issuing official labels on various investment options. **Private investors** can also exert pressure on the providers of investments vehicles to offer options with limited climate footprint, a process that is already well underway.

Cédric Tille

Professor of macroeconomics at the Graduate Institute of International and Development Studies in Geneva

"… the USD 250 trillion+ investment industry should make changes …"

In the light of immediate and mid-term social and environmental challenges, as proxied through the 17 Sustainable Development Goals, **moral justice requires and society is entitled that the USD 250 trillion+ investment industry, directing capital flows and providing incentives, should make changes** 1) towards a more precise and enforced stakeholder governance, 2) towards roles and language fitting these times, 3) towards a more complete information sharing for society at large, 4) towards a real positive investment impact and 5) towards undoing injustice. This while the regulatory regime a) enforces equality, b) redefines fiduciary duties and c) bans green washing. This is not esoteric and can be implemented by the financial, legal and education systems now.

Eelco Fiole

Investment governance expert, board director and adjunct professor of Finance Ethics in Lausanne and Neuchatel

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"… systemic disaster is more profitable than long term basic sustainability demands …"

The key issue is that creating systemic disaster is more profitable than going according to long term basic sustainability demands, and money just flows to where it pays more. Free markets in times of corporate giants, massive-impact technologies, immaterial money and High Frequency Trading are creating chaos. The present reward system is wrong: corporate managers raise their bonuses if they improve dividends, not systemic sustainability. And institutional investors just move ahead to where dividends are higher. **A global new deal is long overdue. Make it green, too.** The way it is, wrongdoing is getting the best rewards.

Ladislau Dowbor

Economist, professor at the Catholic University of São Paulo, consultant to a number of international agencies

"… improved measures of climate risk …"

For the financial sector, major components of the policy program are the subject of proposed changes in regulation and other actions, some now broadly accepted and others more controversial. **The first set includes the improved measures of climate risk for the costs and prices on which accounting and regulatory policies are based, improved disclosures to investors and supervisors, and inclusion of targets for lowering climate risks in conditions for the provision of financing. The second set would involve extending stress testing for financial institutions to longer horizons to include the impact of climate risks as well as incorporating such risks in the macroeconomic models which serve as the basis of monetary policy.** Both of the latter have aroused concerns regarding the reliability of currently available models for such purposes.

Andrew Cornford

Counsellor, Observatoire de la Finance; past staff member of UNCTAD, with special responsibility for financial regulation and international trade in financial services

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"… To continue an act despite knowing it causes harm is to act unethically …"

The financial system can and should be held morally responsible for the dismal progress in mitigating climate change. Let's say finance players first knew about the devastating planetary effects of carbon emissions in the early twenty-first century (although, don't they arrogate to themselves extraordinary intelligence and learning?). Despite this knowledge, the industry has funded fossil fuels globally for the past twenty years. **To continue an act despite knowing it causes harm is to act unethically. Pricing carbon and using carbon markets may move an industry driven by market forces to get on the side of the planet. Developing a new theory of finance, climate finance, call it CliFin, that incorporates carbon into models and demotes profit maximization may be another way.**

Kara Tan Bhala

President and Founder of Seven Pillars Institute for Global Finance and Ethics

"… not more responsible, legally or morally, than any other comparable sector …"

The financial sector per se, or its main players, should not be seen as more responsible, legally or morally, than any other comparable sectors. When the financial sector engages a wide range of stakeholders, it has demonstrated capable of developing tools having great impact in containing climate warming, as the ESG (Environmental, Social, and Governance) criteria and related funds. On the contrary, when the initiative is left in the hands of private individuals, from the great hi-tech gurus to the case of the cryptocurrency Bitcoin, huge inefficiencies are mistakenly tolerated to the wildest speculation. **The impact of the financial sector can well play a positive role, provided it includes a wide range of actors and is not left in the hands of private initiative alone.**

Valerio Alfonso Bruno

Researcher in politics and Senior Research Fellow at the Centre for Analysis of the Radical Right (CARR)

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LIST OF CONTRIBUTORS

Valerio Alfonso Bruno is a Researcher in politics and a Senior Research Fellow at the Centre for Analysis of the Radical Right (CARR), member of AREF and AIESC. He provides regularly political analysis for, among others, the Fair Observer, Social Europe and Indus News.

Andrew Cornford (Counsellor, Observatoire de la Finance; from 1977 until 2003 staff member of UNCTAD, latterly with special responsibility for financial regulation and international trade in financial services)

Paul H. Dembinski is the initiator and Director of the Foundation of the Observatoire de la Finance. In parallel, he is partner and co-founder of Eco'Diagnostic, an independent economic research institute working for both government and private clients in Switzerland and elsewhere. Paul H. Dembinski is also Professor at the University of Fribourg.

Edward Dommen is a specialist in economic ethics, particularly Calvin's. He has been a university professor, a researcher in UNCTAD and president of Geneva's Ecumenical Workshop in Theology (AOT) – an adult-education programme.

Ladislau Dowbor, economist, professor at the Catholic University of São Paulo, consultant to a number of international agencies. His books and technical studies can be found free of charge (Creative Commons) at http://dowbor.org.

Dr. **Eelco Fiole**, CFA, LLM is an investment governance expert, board director and adjunct professor of Finance Ethics in Lausanne and Neuchatel. He was a CFOO for almost 10 years in (alternative) investment management and blockchain, and holds advanced degrees in various academic domains. Thriving on idiosyncrasies and deeply international in his outlook, he is increasingly currently focused on social innovation.

LIST OF CONTRIBUTORS

Dr. **Virgile Perret** holds a Ph.D in Political Science from the University of Lausanne and he is specialized in the study of monetary innovation from an interdisciplinary perspective. He collaborates with the Observatoire de la Finance where he is responsible for managing the global Prize “Ethics & Trust in Finance for a Sustainable Future”.

P. **Etienne Perrot**, Jesuit, Doctor in Economics sciences, member of the editorial board of the magazine Choisir (Geneva), editorial adviser of the journal Études (Paris).

Domingo Sugranyes Bickel, KCSG. Graduated from the University of Fribourg, Switzerland. Secretary General of UNIAPAC, Brussels, from 1974 to 1981. With MAPFRE international insurance group from 1981, Executive Vice-Chairman until 2008. From 2009 to 2019, Chairman of Vatican-based Foundation Centesimus Annus Pro Pontifice. Knight Commander of the Pontifical Order of Saint Gregory the Great (April 2019).

Dr. **Kara Tan Bhala** is President and Founder of Seven Pillars Institute for Global Finance and Ethics, the world’s only independent think tank for research, education, and promotion of financial ethics. Dr. Tan Bhala worked nearly twenty in finance, mostly on Wall Street, and has five degrees across three disciplines.

Cédric Tille is Professor of macroeconomics at the Graduate Institute of International and Development Studies in Geneva. Before joining the Institute in 2007 he worked during nine years as an economist in the international research department of the Federal Reserve Bank of New York.

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"FROM VIRUS TO VITAMIN" – JOIN THE DISCUSSION

The Observatoire de la Finance intends to seize this period of pandemic to step back and take a fresh look at our global economic system, dare to ask new questions which the current crisis brings to the fore and propose innovative ways to rebuild a more resilient and sustainable economy and society. In brief, we want to turn the virus into a vitamin for the future.

Our Discussion Board "From Virus to Vitamin" focuses on commenting issues relevant to finance and economy in relations to society, ethics and the environment from a variety of perspectives, of practical experiences and of academic disciplines. It has been designed to share and discuss information and opinions expressed in a short and concise manner.

Contributors (Discover the list of contributors) are invited to react on a question/issue that is submitted in parallel to a limited group of experts. This happens on a regular basis, through a dedicated mailing list. After the deadline for submission, the reactions are edited and published with signatures in one document on the website of the Observatoire de la finance and on its Linkedin page. If you would like to join the discussion, you may send an email to the editor, Dr. Virgile Perret <perret@obsfin.ch>.

OF Discussion Board – Questions addressed so far

- Question 21 : Rowing together to trim down the Gini coefficient
- Question 20 : Turning up the heat: can private insurance alone mitigate climate change damages?
- Question 19 : From the gold window to the global casino
- Question 18 : Turning point for the planet: can the G7 be trusted?
- Question 17 : Sustainable Finance: Hype or Hope?
- Question 16 : Universal basic income – an idea boosted by the pandemic?
- Question 15 : Multi-polarity: the best guarantee against falling (again) into the Thucydides Trap
- Question 14 : Special Drawing Rights: a drop of liquidity in an ocean of needs
- Question 13 : Trump's economic heritage: false promises setting the stage for populist disruption
- Question 12 : Will America drive the world again? A whish list for Biden's economic agenda

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