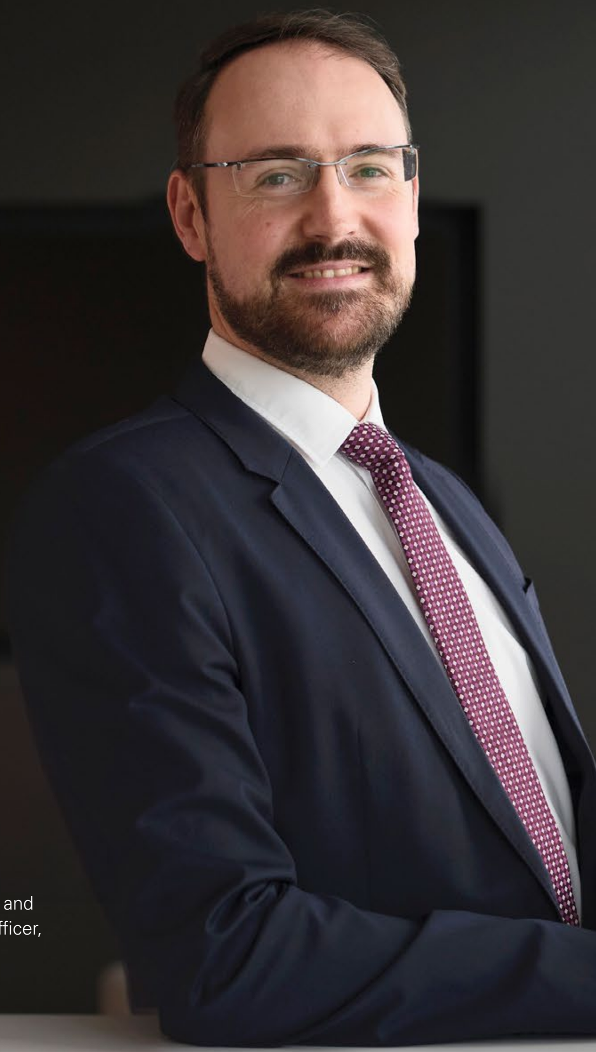
Mobilizing funds to address climate change

Patrick Schmucki, Director, Financial Services and Corporate Responsibility Officer, KPMG Switzerland spoke to Christoph Baumann, Envoy for Sustainable Finance at the State Secretariat for International Finance (SIF), on the opportunities of sustainable finance for the Swiss financial sector, the role of regulation and what is needed in the future to meet the ambitions of the Federal Council.



Patrick Schmucki
Director, Financial Services and Corporate Responsibility Officer, KPMG Switzerland

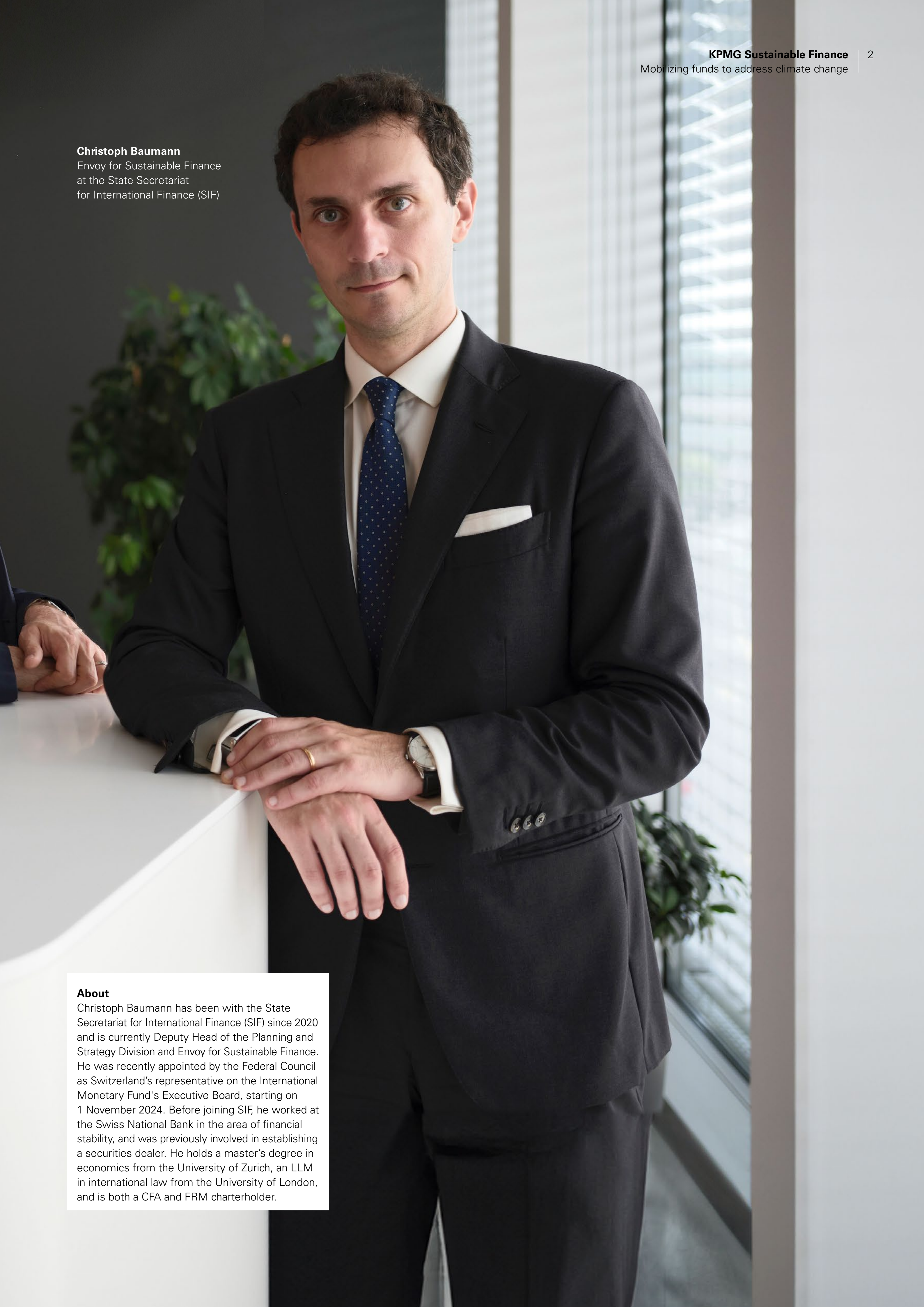
Mitigating climate change is a societal imperative requiring significant monetary investment. The Glasgow Financial Alliance for Net Zero (GFANZ) puts the figure at USD 3.2 trillion – a scale of financing that will only be possible through the mobilization of private capital.

While the funds needed to close the financing gap are available in the private financial sector, willingness of private investors to provide financing is linked to the investment-worthiness of individual projects. Investors expect – and demand – that invested funds generate a risk-adequate return.

Against this background, the role of governments in the mobilization of private capital has recently come into focus. Indeed, Switzerland's Federal Council identifies a need for action in its Sustainable Finance Strategy 2022 – 2025 to develop a leading Swiss sustainable financial market. Specifically, the Federal Council has identified two key measures in this regard:

- Promoting financial flows with a climate and sustainability impact in developing countries
- Exploring adaptation of financial market law for the dissemination of impact investments

Fotos: Geertjan van Beusekom



Christoph Baumann
Envoy for Sustainable Finance
at the State Secretariat
for International Finance (SIF)

About

Christoph Baumann has been with the State Secretariat for International Finance (SIF) since 2020 and is currently Deputy Head of the Planning and Strategy Division and Envoy for Sustainable Finance. He was recently appointed by the Federal Council as Switzerland's representative on the International Monetary Fund's Executive Board, starting on 1 November 2024. Before joining SIF, he worked at the Swiss National Bank in the area of financial stability, and was previously involved in establishing a securities dealer. He holds a master's degree in economics from the University of Zurich, an LLM in international law from the University of London, and is both a CFA and FRM charterholder.

Patrick Schmucki Mr. Baumann, could you briefly explain why sustainability is important to you personally and how you see your own role in this area?

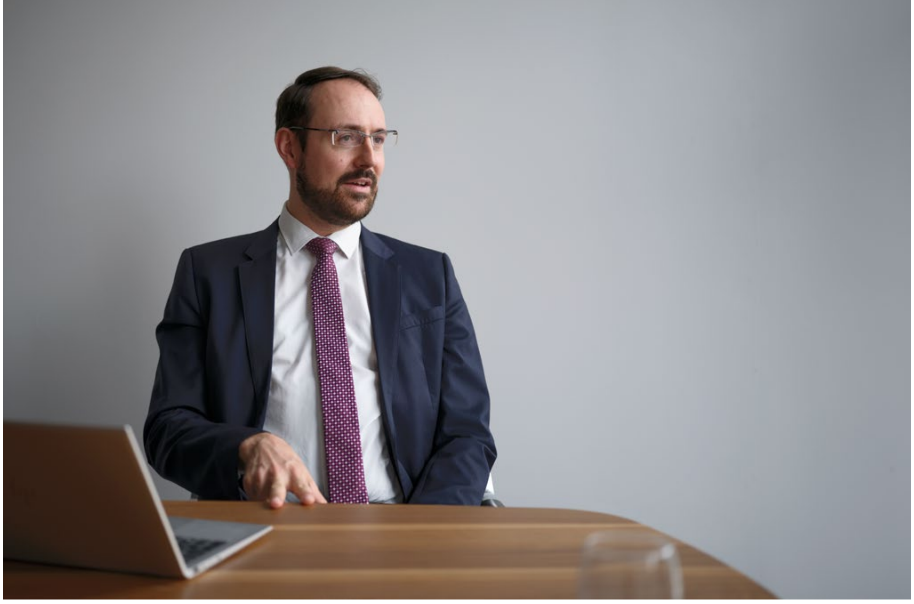
Christoph Baumann The transition to net zero and tackling biodiversity loss are two of the biggest challenges we face. In my position as Envoy for Sustainable Finance at the State Secretariat for International Finance, I can actively shape the framework conditions and that's personally very motivating, also as a parent of two daughters who will be much more exposed to the consequences of these global challenges.

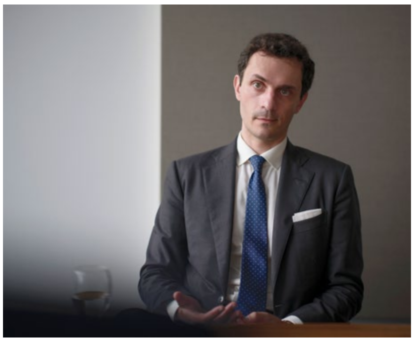
It is great that the Swiss financial industry is absolutely behind sustainable finance and sees the transition to net zero as an opportunity. I don't need to convince industry leaders on the overall direction. As a community, we are debating the most effective levers to reach the goals, but there is agreement about the goals themselves, in particular the transition to net zero by 2050. That aspect is very motivating. Obviously, there are challenges to overcome when dealing with lots of different stakeholders. People look at problems from different perspectives. It's part of my job to bring together what can be conflicting views and find a compromise that is both effective and pragmatic.

You said that industry leaders see the transition as an opportunity. Can you explain in more detail what this means for Switzerland and for our financial institutions?

Christoph Baumann The transition to net zero is probably the largest shift in capital we have seen globally since industrialization. Whenever there's a major shift in capital, there's also a huge opportunity for financial institutions to provide that capital. But to make the most of the possibilities, financial institutions need to position themselves credibly through their service offerings and the advice they provide to corporates, SMEs and private clients.

Personally, I see this shift as highly significant not only for the financial center itself, but also for Switzerland. We're very active on the sustainable finance front in many international organizations including the G20, the International Platform on Sustainable Finance and the Coalition of Finance Ministers for Climate Actions. Switzerland is one of a small group of countries actively shaping international policy-making in the area of sustainable finance.





«As a community, we are debating the most effective levers to reach the goals, but there is agreement about the goals themselves, in particular the transition to net zero by 2050.»

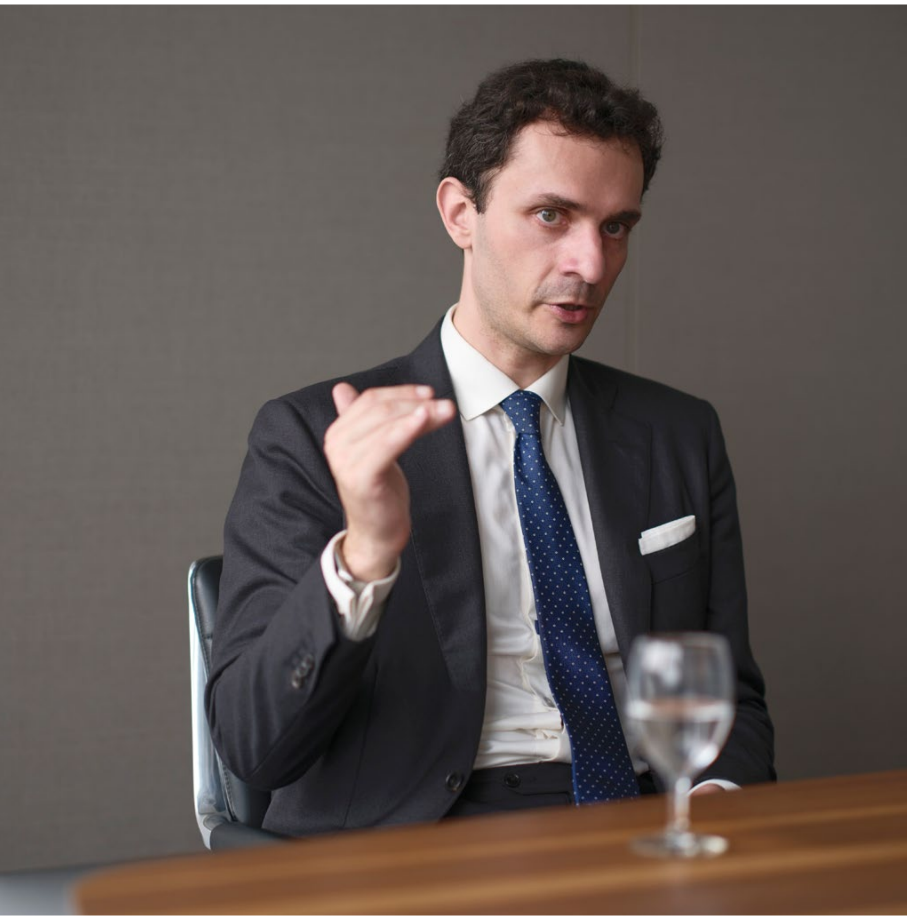
If Switzerland is making such a mark behind the scenes, how is our sustainability performance in the market? How do we compare to the US and Europe?

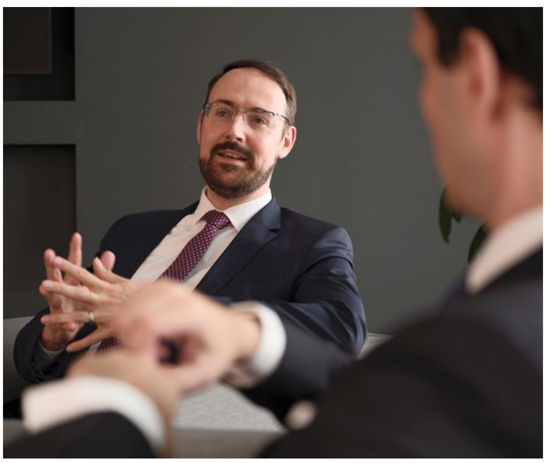
Christoph Baumann That's a difficult question. I think we have shown ourselves to be pioneers in impact investment over the past thirty years, that's positive. For example, Switzerland is the world leader in private impact investment in developing countries, with a market share of approximately 35%. However, impact investment accounts for only a small, albeit rapidly growing, slice of the total Swiss sustainable finance market. Also, we're probably the only large financial center to measure our financial institutions' alignment with the Paris Agreement on a regular basis. It's a voluntary exercise, but more than 80% of institutions regularly participate. In terms of where we stand, there's still a long way to go but we are seeing clear progress over time. In Switzerland, we know where we stand but not all other countries have the same quality of data to enable a comparison.

Overall, comparison with other financial centers is difficult. There are different approaches, with more regulation in Europe, for example. In Switzerland, we follow a more principle-based approach with a mixture of regulatory and voluntary measures.

It has been suggested that Switzerland is a laggard when it comes to regulation. What's your take on that?

Christoph Baumann We're a laggard in terms of bureaucracy – and that's a very good thing. If you overdo the red tape, sustainable finance risks becoming a tick-the-box exercise. We're the only country to have had a popular vote on net zero by 2050. To my knowledge, we're the only country that requires every company headquartered in Switzerland to be net zero by 2050 in terms of Scope 1 and Scope 2 emissions. And we're the only country in the world to have enshrined in law that financial flows need to be aligned with the goals of the Paris Agreement. The law also mandates the government to ensure that financial institutions contribute to climate change mitigation. All this already puts us in a strong position. Then you have our Climate Reporting Ordinance, which includes mandatory transition plans in accordance with the TCFD recommendations across the economy for larger companies. On the product side, for example when it comes to greenwashing, we rely on self-regulation to a large degree while we await further developments in EU regulation. But the Swiss Bankers Association and AMAS regulations are mandatory as well, it's just that they are authored by the industry rather than the government. I don't believe that more state regulation necessarily means more impact on the market. The Swiss financial center should be measured by its progress on the path to sustainability, not by the number of pages of regulation in place.





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High-quality, comparable, accessible information is key for business and investment decision-making. Especially transition plans play an increasingly important role. How is the Swiss government supporting the development of respective solutions?

Christoph Baumann We have already mandated transition plans, and the Federal Council has asked us to add minimum criteria for financial institutions' transition plans. We plan to launch the consultation on revision for this by the end of the year. Given that it's quite a new topic, we don't yet have final best practices for what a transition plan should look like. We should avoid being too prescriptive and specific for Swiss transition plans as global financial institutions cannot transition in multiple directions. Our aim is to remain principles-based with regard to transition plans, while very much supporting convergence toward international best practice. We need to work toward a world where transition plans of companies across all sectors and countries are comparable.

On the other hand, institutions also need data. One big development we've been supporting since the beginning is the Net-Zero Data Public Utility (NZDPU). It's an initiative that aims at providing a public repository of climate data for everyone to use for free. It will be an absolute game changer once enough data is available.

As of this year, public interest entities are required to report on climate matters, including transition plans. A large portion of financial institutions' business is lending. How can we ensure transparency in the mortgage and SME lending markets?

Christoph Baumann I'm encouraged by the recent developments making the federal building and housing register include for every privately held home transparency on the heating source and energy efficiency. I hope financial institutions will increasingly make use of this registry to understand the energy status of their mortgage book and to help clients when they want to update their heating source.

In terms of lending to SMEs, such companies are often very willing to transition but they need advice – and financial solutions – to take action. They need help to develop a long-term financing plan for updating the factory or business processes. That's a phenomenal opportunity for financial institutions.

More generally, I would hope that sustainability preferences are not gathered in a tick-the-box exercise during client onboarding – that would be such a waste of opportunity.

One way the government can promote impact investing in Switzerland is by making changes to financial market regulation. Can you tell us a bit about what's happening in this space?

Christoph Baumann Our overarching goal is to take impact investments mainstream. And by that, I mean also traditional impact investments – those that are less liquid and on the primary market. It's usually philanthropists, family offices, etc. making these investments. Given that the perceived risk of such investments is sometimes overestimated, we want to understand why they aren't being applied more broadly in wealth and institutional asset management. There's huge demand for impact. But as a retail investor or even as a high-net-worth investor, you will often be offered investment products focusing on high liquidity and, therefore, with limited impact. There is poor access to products with the highest impact. I'm not saying it's necessarily right for every client, but for those who really want to make the biggest impact, the option should be available. So, what's the issue? We don't believe that there is a regulatory barrier, which is good news in a way. Our current understanding is that you can absolutely have an illiquid portion in a very diversified portfolio; it's just not happening. We're in discussions with the industry about this. Is it just about building awareness? Or risk awareness at the level of the Chief Investment Officers? It will be interesting to dive deeper and understand what's happening.