# Why 'greening' the EU's institutions remains far from straightforward

*In response to the increasing salience of climate change, there have been renewed efforts to enhance the green credentials of the EU's institutions. As* **Tobias Tesche** *writes, these efforts include proposals for the European Central Bank and European Investment Bank to take climate change into greater consideration when making decisions. Yet not all of these proposals have been well received and there remains the potential for significant controversy to be generated over how this 'green turn' is implemented.*

The issue of climate change has taken over the European political agenda and will likely dominate it for the coming years. The new European Commission has outlined its plan to 'green' the European economy in its communication for a European Green Deal, which partially reflects the new balance of power within the European Parliament.

The European Investment Bank (EIB) has also announced that it will turn into a 'climate bank' to finance the transition towards a low-carbon economy. In November 2019, the EIB's Board agreed on a new climate strategy and energy lending policy promising to end financing for fossil fuel energy projects by the end of 2021. However, the agreement was controversial and was not supported by certain countries with a large coal industry. In addition, exemptions could be made for continued financing of certain gas projects.

The European Central Bank's new President, Christine Lagarde, has similarly made climate change a key priority. She hinted at climate change becoming part of the upcoming strategic review of the ECB's monetary policy toolkit. In addition, the European Commission and the European Parliament have agreed on a common classification system for environmentally-sustainable investments. This commonly agreed taxonomy is supposed to end 'greenwashing', i.e. the practice of pretending that a product is more environmentally sustainable than it is in reality. A Technical Expert Group on Sustainable Finance will be tasked with working out the details of the agreement.

In May 2018, the Commission presented a package that aimed at (1) establishing a taxonomy for environmentally-sustainable investments, (2) increasing transparency with regard to how institutional investors use environmental, social and governance (ESG) factors in assessing risks, and (3) making the carbon footprint of different investments comparable. Unfortunately, the 'green turn' has also provided a window of opportunity for banks to lower their capital requirements in a socially acceptable way. Commission Vice-President Valdis Dombrovskis favours a 'green supporting factor' for banks that engage in climate-friendly lending, which has generated pushback from the Single Supervisory Mechanism.

**The 'greening' of central banking – controversy ahead?**

In addition to climate change becoming part of the ECB's review of its monetary policy strategy, Lagarde also made several proposals in her first hearing at the European Parliament's ECON Committee. First, she proposed that the ECB's macroeconomic analysis should account for climate change risks. Second, she argued that banking supervision needs to take climate risks seriously. Third, she pointed out that climate change considerations need to feature in the ECB's own portfolio of investment operations and the management of its pension fund. Finally, she acknowledged that climate change also merits consideration by the Governing Council when discussing the asset purchasing programme (Quantitative Easing – QE).

But not all of these proposals have been well received, suggesting that the 'green turn' cannot be implemented without controversy. Bundesbank Governor Jens Weidmann has argued that prioritising green assets via 'green QE' could violate Art. 127 of the EU treaty to observe the principle of 'market neutrality'. He cautioned that if monetary policy explicitly took into account environmental policy objectives, it might become overburdened and central bank independence could ultimately be undermined. He further questioned why environmental goals should only be pursued during times when the underlying price pressures were weak and called on credit rating agencies to improve their assessments of climate change related risks.

Some observers have rejected the argument of market neutrality on normative grounds. Adam Tooze, for instance, points out that 'the ECB has the responsibility to lean on the markets to bring them into line with the glide path to decarbonisation that Europe has collectively decided on'. He also notes that the acquisition of large fossil fuel-intensive portfolios by the central bank was the consequence of relying on the judgement of credit rating agencies.

**The rise of green macroeconomic indicators**

As Willem Buiter explains, there are two separate risks arising from the success or failure of fighting climate change. First, if climate change policy is successful, it could create 'stranded assets' that would lose value due to being carbon-intensive. Some credit rating agencies have already started to downgrade some of these non-green assets in anticipation of regulatory changes. Second, failed attempts to tackle climate change effectively would lead to physical risks. These risks would entail 'the destruction of real commercial and natural assets as well as human capital' with adverse consequences for insurance companies.

Yet, measuring the impact of climate change is not straightforward and these difficulties have yet to receive sufficient attention. In China, attempts to create a 'green GDP' that would measure the environmental impact of economic growth have largely failed. Weidmann acknowledged that 'both climate change and climate policy can have a bearing on macroeconomic indicators such as output and inflation'. In his view, climate change could have a strong bearing on the volatility of growth rates, inflation figures and financial markets in the long run.

The 'green turn' in the EU's institutions might revive the creation of macroeconomic indicators that better account for risks related to climate change. While in the past, macroeconomic indicators have had a rather depoliticising effect, new macroeconomic indicators that will take a more comprehensive view of societal developments might encounter contestation along the way and may end up leading to more politicisation.

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*Note: This article gives the views of the author, not the position of EUROPP – European Politics and Policy or the London School of Economics. Featured image: Greta Thunberg visiting the European Parliament in 2019, Credit: European Parliament (CC BY 2.0)*

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