



## Central banks cannot solve climate change on their own

Guest contribution by Jens Weidmann published in Financial Times

19.11.2020 | Jens Weidmann

Imagine you had magical powers that could make the global climate crisis disappear. Wouldn't you use them? I certainly would. Without a doubt, tackling this crisis is one of the greatest and most pressing challenges of our time. Every one of us should be doing more to curb global warming.

This goes for central banks, too. It includes shrinking their carbon footprints as institutions but our response cannot stop there. In particular, it is essential for us to learn more about the implications for monetary policy of climate change and efforts to address it. Climate-related financial risks are another factor that central banks need to consider. In our role as prudential supervisors and guardians of financial stability, we have to ensure that banks adequately incorporate these risks into their risk management.

Central banks must also practise what they preach. We owe it to our taxpayers to keep the financial risks that arise from our monetary policy operations in check. That's why central banks should make sure that climate-related financial risks are given due consideration in their own risk management.

To this end, it is legitimate to expect securities issuers and rating agencies to provide better information. The Eurosystem — the European Central Bank and the national central banks — should consider only purchasing securities or accepting them as collateral for monetary policy purposes if their issuers meet certain climate-related reporting obligations.

We could also examine whether we should use only those ratings issued by rating agencies that appropriately include climate-related financial risks. With such measures, the Eurosystem would help foster market transparency and standards at rating agencies and banks. We would act as a catalyst for “greening” the financial system and support climate policies.

Economists widely agree that raising the price of carbon is key to slowing global warming. This is a matter for governments and parliaments to address. They have the right tools at their disposal, such as taxes or “cap and trade” schemes, and also have the democratic authority to use them.

It is not the task of the Eurosystem to penalise or promote certain industries. Our primary objective is to maintain price stability. To achieve this goal in an economic crisis like the one we face today, it is imperative for monetary policy to keep interest rates low and support the whole economy. Asset purchase programmes are a component of our expansionary monetary policy. To be effective, they need to be broad-based. The principle of “market neutrality” aims to ensure this and prevent us from distorting market outcomes. We must check whether we have unintentionally allowed bias to creep into our securities portfolio, compared to the universe of eligible bonds. But it is not up to us to correct market distortions and political actions or omissions.

Elected politicians have staked out the goals of the Paris Agreement. It is unfortunate that they have not yet agreed on a concrete adjustment path. As a father of two, I very much regret seeing often halfhearted climate policies and a lack of credible commitment to a clear transition. But should central banks make up for a lack of political will? And how would their intervention be seen? As a form of support for policies? As an attempt to overturn them? Or as a way of letting politicians off the hook? Would central banks become engulfed in politics and undermine their own independence?

Central bank independence is not an excuse for inaction. It is an obligation to stay focused on our primary objective. It follows from the insight — and a broad consensus — that price stability is the best contribution monetary policy can make to overall welfare. Monetary policy has often been credited with extraordinary powers. That adulation has never really rung true. When it comes to saving the planet, central banks do not have a magic wand.