MARCH 2024

# EXECUTIVE SUMMARY: INVESTING IN EUROPE'S PROSPERITY[1]

## A VISION FOR FINANCING THE TRANSITION TO SUSTAINABILITY 2024–2030

E3G – SHAREACTION – WWF

The transition to sustainability will enable social, economic and financial prosperity and stability in the European Union (EU). The EU's climate targets set out in the European Green Deal demonstrate its commitment to achieving a fair and prosperous future for all citizens. Achieving those goals requires mobilising significant private finance towards the sustainability objectives. Public finance also needs to work harder and smarter to shift the system and bring in more private finance. Policy choices will have to be made against a backdrop of challenging geopolitical, economic and social dynamics.

In the 2023 Strategic Foresight Report, the European Commission estimates the need for additional €620bn investments per year to meet the objectives of the European Green Deal and REPowerEU.[2] Those objectives include decarbonisation targets, but also creating a sustainable and competitive economy that protects the EU's natural capital, and the health and wellbeing of its citizens. The intensity of climate impacts is already showing us the costs of inaction – in both economic and human terms.

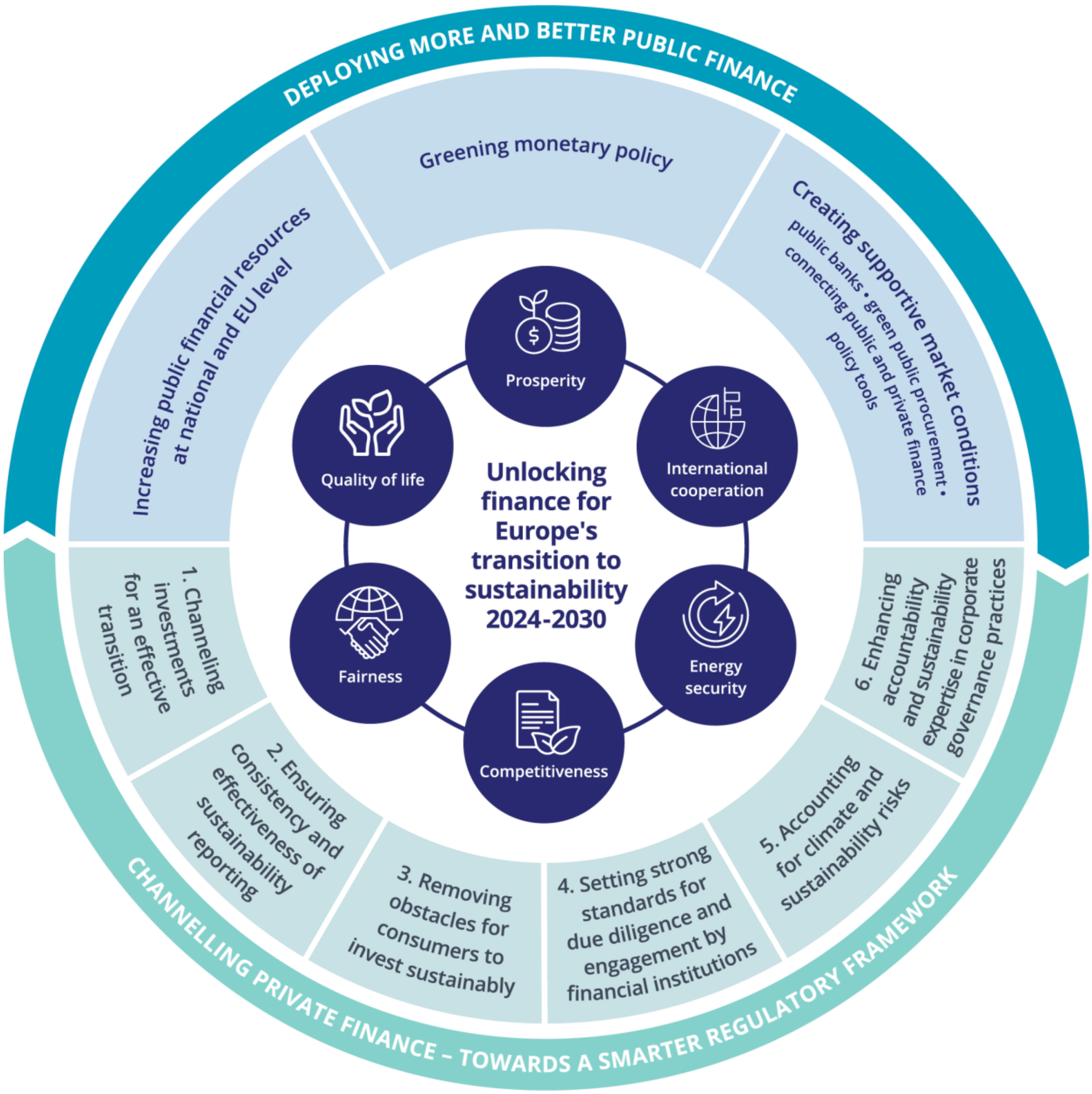
The funding needs are significant, but far from insurmountable. Much can be achieved by making sure more existing finance – both private and public – ends up in the right place. However, the conditions under which these decisions will have to be made in the coming five years have become challenging. Multiple crises, increased inflation and social inequality, and geostrategic competition have affected the political space and support for the sustainable transition in

[1] This is a summary of the report of the same name, available from E3G, March 2024, **Investing in Europe's prosperity**

[2] European Commission, July 2023, **2023 Strategic Foresight Report** (PDF)

Europe. To achieve sustained political and popular support for the transition, its benefits must be confidently communicated, including inclusion, safety and economic competitiveness.

Our report makes recommendations for developing a smarter and better regulatory framework for sustainable finance in the EU, and explores opportunities for deploying public finance more effectively and at scale.



# Achieving a harmonised sustainable finance regulatory framework

Too much money is still paying for activity that runs counter to the goals of the transition. Estimates show that three-quarters of the funding gap for decarbonisation by 2050 can be filled simply by diverting existing finance from harmful or superfluous activities, into those that will deliver the transition.[3]

The EU has already shown excellent leadership in promoting ambitious sustainable finance legislation, and the existing regulatory framework is a good basis to work from to make it more coherent and workable. To date the EU's focus has been on encouraging transparency and making it easier for investors to identify sustainable activities to invest in. Now, action needs to move to providing stronger incentives for investors to put their money towards sustainability objectives.

The system needs to be coherent, easy to navigate, and speak to all potential users from consumers to financial institutions. We provide detailed recommendations in support of six key objectives for private financing.

### 1. Channelling investment for an effective transition

> Establish a single mandatory transition plan framework to streamline reporting, target-setting and implementation requirements for corporate transition plans. Currently these are too fragmented and unclear, creating legal ambiguities and administrative challenges for organisations.

> Expand the scope of the EU taxonomy to make it more comprehensive and robust. It should cover activities that are not environmentally sustainable but may be in the future, and those that will never be sustainable and should therefore be decommissioned. The taxonomy should also define socially sustainable activities.

> Further align the EU Green Bond Standard with the EU taxonomy and make the standard mandatory.

### 2. Ensuring consistency and effectiveness of sustainability reporting

> Prioritise the development and adoption of robust sector-specific corporate sustainability reporting standards and enhance requirements and reporting quality.

[3] Institut Rousseau, January 2024, **Road to Net Zero, Bridging the Green Investment Gap**

> Embed sustainability disclosure requirements in relevant legislation beyond the Corporate Sustainability Reporting Directive and European Sustainability Reporting Standards, to ensure consistency.

### 3. Removing obstacles for consumers to invest sustainably

> Create a mandatory product categorisation system that includes minimum criteria for sustainable investment products under the Sustainable Finance Disclosures Regulation.

> Strengthen sustainability provisions in the retail investment strategy.

> Better define and integrate sustainability into product and sectoral legislation such as the Mortgage Credit Directive, Distance Marketing of Consumer Financial Services Directive and Unfair Consumer Practices Directive.

### 4. Setting strong standards for due diligence and engagement by financial institutions

> Set mandatory due diligence requirements for financial activities.

> Set more comprehensive due diligence requirements for environmental matters.

> Ensure a higher standard for investor engagement.

### 5. Accounting for climate and sustainability risks

> Reflect the risks of activities that are not aligned with the EU climate objectives in the risk-based capital requirements.

> Ensure that credit ratings adequately integrate sustainability risks.

### 6. Enhancing accountability and sustainability expertise in corporate governance

> Ensure that companies' remuneration structures do not incentivise directors to favour short-term financial gains.

> Better regulate corporate lobbying, which weighs EU policy decision-making towards short-term industry interests.

> Engage stakeholders in a debate on corporate purpose to maximise shareholder value.

# Putting public finance to work in support of the transition

Public investment is crucial to achieving the transition. There are many situations – such as public transport, and home retrofits for people on low incomes – where public funding is the only viable solution. Moreover, investments in resilient public services, and providing financial support for regulatory initiatives, are essential to maintain social cohesion.

**Raising public investment at national and EU level**

There are significant opportunities to free up public funds at the national level:

1. Phase out environmentally harmful subsidies.
2. Reduce public budgets' exposure to fossil fuel price volatility and anticipate costs for climate risks and damages in multi-year budgetary planning.
3. Apply progressive taxation on carbon-intensive consumption.
4. Use corporate tax policy to encourage sustainability, aligned with the EU taxonomy.
5. Include the cost of inaction in debates about investments.

EU-level funding is also crucial, to protect the single market in the face of mounting international competition, and to invest in European public goods as well as private sector sustainable projects. The pressures of EU enlargement and debt repayment also mean there will be more strain on EU budgets. There are two principal ways to leverage additional EU public funding:

1. Issuance of common debt, the effectiveness of which has been demonstrated by the Recovery and Resilience Facility.
2. EU levies and tax transfers, following the pioneer examples of the plastics tax and the Carbon Border Adjustment Mechanism.

**Greening the European Central Bank's monetary policy**

Monetary institutions need to find a way to address the high interest rates and increased capital costs that are likely to arise in the shift towards the transition to sustainability. The current ECB approach of tightening monetary policy restricts the fiscal space for investment.

In a high-interest rate environment, central banks should consider tools to incentivise borrowing and investment in green projects, for example dual interest rates.

In its review of its collateral framework, the ECB should recognise that environmentally harmful assets are at high risk of losing some or all of their value in the transition. It should integrate this risk into the framework by excluding such assets, or applying haircuts according to the level of environmental impact of the asset.

### Smarter deployment: leveraging the system towards the future

It is not enough to have public funding available for investments into the transition – it is necessary to effectively deploy it to crowd in private finance, create market demand for activities and solutions that support the transition and provide strong signals to financial market players. There are three areas where the EU's public institutions, policy levers and tools can be strengthened to better deploy public funding for the transition:

1. **Public banks**. European public banks should be utilised more for their knowledge to spur the transition at EU, national and sectoral level. They should take on more ambition and go beyond just aligning with existing EU legislation to address the EU's deep decarbonisation challenge. In addition, the mandate of public banks should be revised to attract a more diverse team of personnel, able to provide tailored and cutting-edge technical assistance. This will support both the project ideation and the financial modelling needed to finance transition-related solutions. Enhancing and mainstreaming the use of innovative financial instruments, and financing resilience and adaptation across Europe, should also be core functions of EU public banks.
2. **EU green public procurement.** This should be an appealing prospect as it entails changing the conditions for existing public finance, rather than increasing the amount of finance. Public procurement could be an especially powerful tool for driving the transition in heavy industries such as steel and cement, where public investment can help de-risk investment in low-carbon production methods.
3. **Linking public finance more explicitly to the EU sustainable finance framework.** National and EU-level financing could additionally both leverage private investments and support companies in their transition by aligning those mechanisms with the current sustainable finance policies and tools for the private sector. Notably the taxonomy's 'do no significant harm' principle and criteria, and transition plan supervision under the due diligence directive (CSDDD) would be powerful incentives if mainstreamed into public spending.

*This report is a joint publication by E3G, ShareAction and WWF Europe Policy Office. Our organisations have drawn on our respective areas of expertise to address the opportunities and challenges of the transition in this holistic way. The three organisations jointly developed the content and recommendations in the Introduction and Chapter 1 on private finance. Chapter 2 on public finance was led by E3G and reflects its views alone.*

## About E3G

E3G is an independent climate change think tank with a global outlook. We work on the frontier of the climate landscape, tackling the barriers and advancing the solutions to a safe climate. Our goal is to translate climate politics, economics and policies into action.

E3G builds broad-based coalitions to deliver a safe climate, working closely with like-minded partners in government, politics, civil society, science, the media, public interest foundations and elsewhere to leverage change.

**www.e3g.org**

## About ShareAction

ShareAction is an NGO working globally to define the highest standards for responsible investment and drive change until these standards are adopted worldwide. We mobilise investors to take action to improve labour standards, tackle climate change, protect the natural world and address pressing global health issues. For nearly 20 years, ShareAction has used its powerful toolkit of research, corporate campaigns, policy advocacy and public mobilisation to drive responsibility into the heart of mainstream investment. Our vision is a world where the financial system serves our planet and its people.

**www.shareaction.org**

## About WWF

WWF's mission is to stop the degradation of the planet's natural environment and to build a future in which humans live in harmony with nature. The European Policy Office contributes to this by advocating for strong EU environmental policies on sustainable development, nature conservation, climate and energy, marine protection, sustainable finance and external action.

**www.wwf.eu**