CCA SUSTAINABILITY SOLUTIONS

A Backgrounder on Green Finance

Definition

Green Finance is investment in projects, organizations or assets which deliver positive climate or other environmental benefits in the broader context of environmentally sustainable development. This can include renewable energy, energy-efficient infrastructure, or measures to adapt to the impact of climate change. Many believe that impact should include efforts to internalize environmental externalities and adjust risk perceptions. Green finance can take several forms:

Green Bonds
A fixed income financial instrument with which the proceeds will fund projects, organizations or assets which address climate change or environmental issues.

Green Investment
Investment in an organization, project or asset which addresses climate change or other environmental issues.

Climate Finance
Driven by bilateral and multilateral concessionary finance or aid, climate finance assists developing countries to make more sustainable choices in their economic development.

Green Funds
Investment funds managed by multilateral agencies such as the UN's Green Climate Fund. It may also refer to mutual funds that will only invest in companies that are deemed socially conscious in their business dealings or directly promote environmental responsibility.

Green Banks
Public or quasi-governmental institutions set up to fund and leverage private-sector funds for green investments, so far mostly for renewable energy projects.

Driving Forces

The Paris Agreement
signed by 195 nations, requires climate action by all ratifying nations to limit global warming to well below 2°C above pre-industrial levels, leading to new laws, incentives and investment programmes in order to achieve countries' commitments to GHG reductions.

Regional and City-based Targets
are a key part of the realization of the Paris Agreement. Hundreds of local and city governments are now committed to surpass national emissions, renewables and efficiency targets.

Institutional Investors
including pension funds, universities, and sovereign funds divesting from carbon-intensive activities out of ethical concerns, public pressure, rising expectations from investors, and the need for risk-hedging.

Green Growth Opportunities
and the worldwide transition to greener energy use are creating new jobs, driven by market forces as a result of accelerating advancements in green technologies.

Climate Risk Mitigation
is becoming a necessity in the investment and insurance sector. Risks include physical risk to future assets, liabilities arising from stranded assets, and transition risk of costly late adjustment to incoming GHG and energy regulations.

Challenges

Environmental Integrity

Green finance organizations are working on ways to ensure robust standards which provide reliable evidence of the positive climate impact of activities funded with green finance. Poor, divergent or weak environmental integrity poses the risk of discrediting the concept of green finance, confusing investors and risking accusations of 'greenwashing' from the public.

Disclosure Standards

Consistent standards of monitoring, verification and reporting are not yet universally applied. To maintain a green label, projects seeking green finance will need environmental impact assessment at the outset, as well as measurement of the concrete achievements post-funding.

Measurement of Externalities

The benchmarking of green programmes demands consistent rating of environmental externalities. Government-led initiatives such as subsidies, tax credits, feed-in-tariffs, renewable portfolio standards, emissions trading systems and carbon markets attempt to go some way to address the issue.

Liquidity Alignment

There is often a mismatch between the investors requiring liquidity, and the long-term maturity of green infrastructural investment, although this can occur in conventional infrastructural investment as well. Energy efficient buildings and renewable energy projects may require more up-front capital but less operating capital than their non-green counterparts.

Limited Deal Flow

The lack of an insufficient pipeline of well-packaged, investible green projects with positive climate and environmental characteristics may hamper the green fund initiatives from government and the private sector.

Information Asymmetry

Compounding many of the issues above is an asymmetry of environmental data and the need to build analytical capacity in many government and financial institutions.

Key Statistics

- Global green bond market increased from US$11 billion in 2011 to almost US$42 billion in 2015.[i]
- Less than 1% of global bonds are labeled green.[ii]
- Renewables represented 62% of net additions to global power capacity in 2015.[iii]
- $53 trillion capital on energy supply and energy efficiency is needed over next 20 years to stay within the 2°C limit.[iv]
- Chinese-funded entities issued US$11.2 billion in green bonds, representing 33% of the global total during first half of 2016.
- By 2020, China will issue RMB 300 billion of green bonds annually.

I Huan Chaoni. "What do China's new green bond rules mean for sustainable investment." China Dialog. 12.01.2016
Ii G20 Green Finance Study Group. Green Finance Synthesis Report. July 2016
Iii REN21, 2016, "Renewables 2016, Global Status Report".
Iv Xu Nan and Wang Yao. "China's green bond market booms with more clarity in policy." China Dialog . 29.07.2016

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