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From Covid To COP26 – The Changing Role Of Financial Actors

Webinar

Tuesday 12 May 2020

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Agenda

14:00 – 14:05	Chairman Introduction
14:05 – 14:30	Keynote Address
14:30 – 14:45	Questions & Answers

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From Covid To COP26 – The Changing Role Of Financial Actors

Nick Mabey

Chief Executive Officer

E3G

Introduction to E3G

- European environmental thinktank working globally
- Offices in Brussels, Berlin, London and Washington DC
- Focus on analysing & shaping national and international politics of climate change. Expertise on diplomacy, security, finance, clean economy & resilience.
- Target systemic changes with high leverage e.g. UK Green Investment Bank; EU-China relations; EU sustainable finance reform & Multilateral Development Bank reforms
- Advise European governments on climate diplomacy and strategy
- Mainly grant funded by philanthropy and governments.
- My background: energy industry, academia (MIT, LBS), WWF, FCO & UK Prime Minister's Office.

Key Takeaways

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1. Paris climate agreement made us safer but not safe. COP 26 critical point to raise climate ambition.

2. COVID has upended the strategic landscape requiring a **complete rethink of climate ambition strategies.**

3. **Dynamics of COVID are hugely uncertain** and linked to second wave financial crises & third wave social stability impacts. **Too early to call geopolitical response to COVID;** major powers both cooperating and competing.

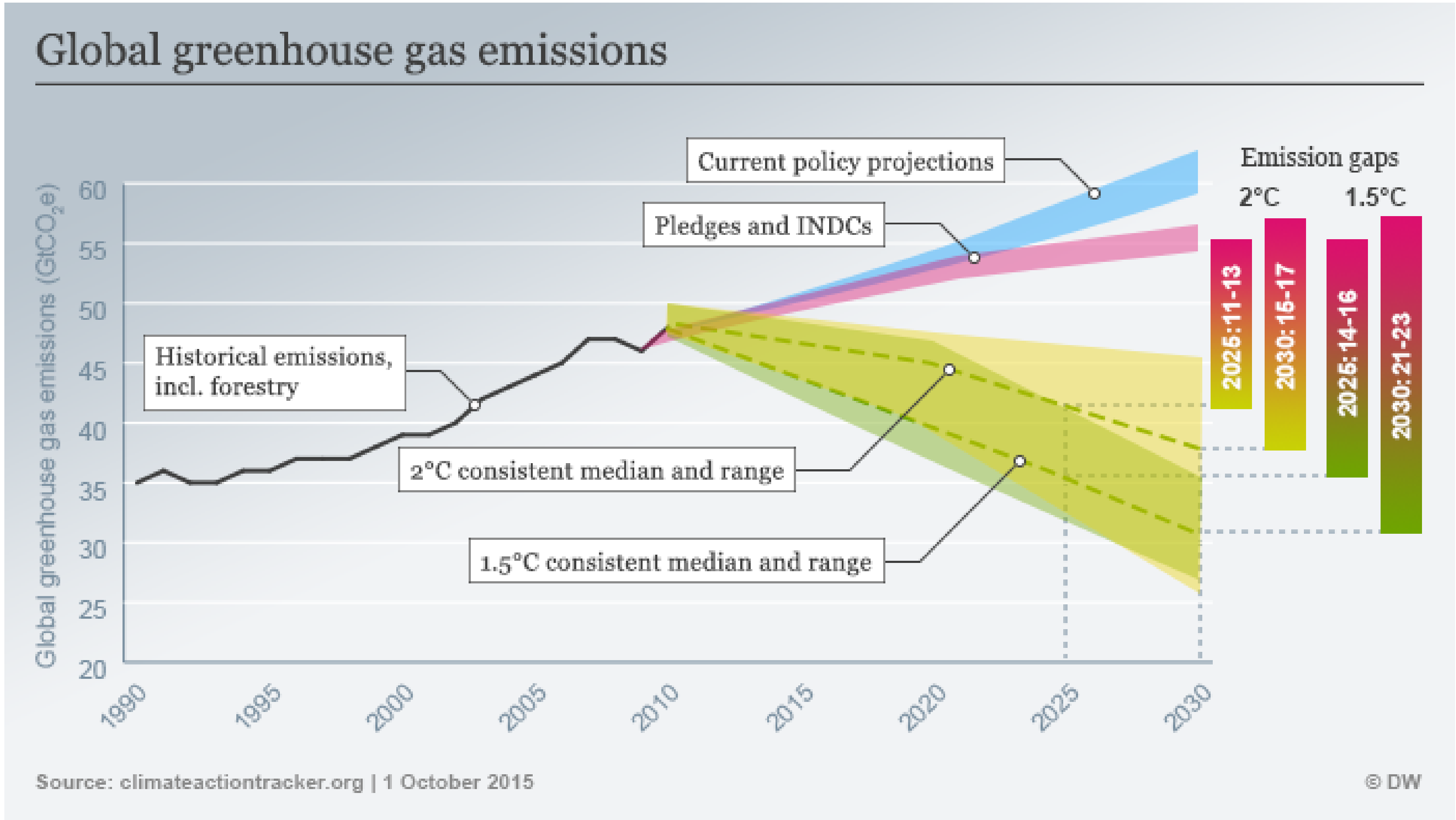
4. Before COVID climate ambition required COP 26 to drive geopolitical priorities. Now **climate action will only advance by riding the geopolitical and geo-economic waves** caused by COVID.

5. Decisions taken in next 3-6 months over recovery packages, and next 6-18 months on debt restructuring, will determine the **ability to stay within "safe" climate limits**. **COP 26 still critical to cement the credibility of the Paris regime** but big risks remain – especially with Trump 2 - as it will not deliver 2C>> or 1.5C.

6. **Delivering net zero, resilient alignment of UK and EU recovery packages** will be the biggest geopolitical and diplomatic asset for shaping climate ambition at COP 26 and in 2021 more broadly.

7. **Climate action now critically depends on major public financial decisions and reforms**. What is the role of finance actors in shaping these choices? What is the role of private finance intermediaries in financing the green recovery? What are the long term changes needed to the balance of public and private finance?

Paris made us safer but not safe. Emissions must be 40GT> by 2030; 15 GT "gap".



Probability of > 4C reduced by 80%; 2.7C-3.5C likely outcome

Where were we before COVID-19?

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A political and economic landscape dominated by rising headwinds:

↓ **Flat geopolitics**: vacuum of leadership on climate action

↓ **Low reputational leverage**: reputational hits for other issues priced in by leaders and publics in China, India, Brazil, Australia, Turkey, etc.

↓ **Legacy of distrust** in UNFCCC process from LDCs and Vulnerables due to exclusion at COP25 and lack of progress on loss and damage

↓ **UNSG power uncertain**: in wake of UN Climate Action Summit in 2019

↓ **Narrative that UNFCCC process is failing:** media seldom focused on country inaction – except for USA – but blame UN regime itself.

…with a few tailwinds:

↑ **Falling cost** of low carbon tech

↑ Growing commitments from **businesses/cities**

↑ **Public attention** on climate action unprecedented

↑ **Engagement** of central bankers

Pre-COVID expectations of COP 26/2021

- Even under most positive scenario of strong EU-China cooperation **E3G analysis suggested that country commitments for 2030 would fall well short of 2C>> trajectory**

- UK Presidency aiming to **support & supplement NDC ambition** through diplomatic campaigns on:

    - **Coal phase out**, new coal power moratoria and stopping public coal finance.

    - **Private sector finance regulation** (mandatory climate risk disclosure), central bank climate stress test commitments and private investor low carbon financing commitments.

    - **Public bank Paris-alignment** and increased capitalisation;

    - **Internal combustion engine phase out** commitments.

    - **Nature-based solutions** commitments including commodity supply chain reforms.

- **Strong action on resilience support planned** to show balanced Paris delivery and cement critical political alliances with Vulnerable Country Group and Africa.

Even optimistic scenarios for Glasgow had high risks that the Paris regime would be perceived to be failing to deliver by political leaders, finance actors and/or the public. <u>These risks remain</u>.

COP 26 Outcomes by the Numbers

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	High Ambition	Medium Ambition	Low Ambition
NDCs	Extra 5 GT	Extra 3.25 GT	Extra 1.0 GT
Long Term Strategies	50% Emissions Net Zero 2050 (China and India)	15% Emissions Net Zero 2050 (Japan, S Korea)	UK, EU & EEA with clear Net Zero Targets (10% GHG Emissions)
New Coal	200 GW New Coal paused or cancelled + 40+ governments commit to moratoria / 'no new coal by 2020', incl. Japan, Korea	100 GW New Coal paused or cancelled + ~20 governments commit to moratoria / 'no new coal by 2020'	219 GW New Coal paused or cancelled since 2015
Coal Finance	China, Japan and Korea stop coal finance and pivot to clean	Japan and Korea stop Coal Finance	Stop remaining EU coal finance + export credits:
Existing Coal	100 GW of closures / phase out commitments announced	50 GW of closures / phase out commitments announced	25 GW of closures / phase out commitments
Public Climate Finance	Development Banks given more "capital" to do more 150% more climate investment. 2-3 MDBs and all European DFIs stop all fossil finance	Development Banks announce 25% increase in climate finance and weak alignment with Paris	Development Banks announce framework for alignment with Paris
ICE	62% of 2018 car sales ICE phase out before 2030/35 (China & India)	22% of 2018 car sales ICE phase out before 2030/35 (Italy, Spain, Japan & California)	8% of 2018 car sales ICE phase out before 2040

Where are we now with COVID-19?

- **COVID-19 response is (rightly) dominating national discourse** and will continue to dominate for at least the next 6-18 months.
- **Economic Impacts are Spreading - t**here will be geopolitical tensions over who controls bailout and debt relief terms. The role of the IMF & MDBs will increase
- **Systematic lack of resilience thrown into the spotlight**
- **Global cooperation is being tested**. COVID-19 reveals vulnerabilities in global governance and exacerbates existing inequalities. The **diplomatic calendar is unsettled**

"First round" impacts:

- Lockdown leads to large 10% + falls in GDP in major economies
- Crisis packages will massively increase global debt
- Implications for fiscal space for government spending and investment.

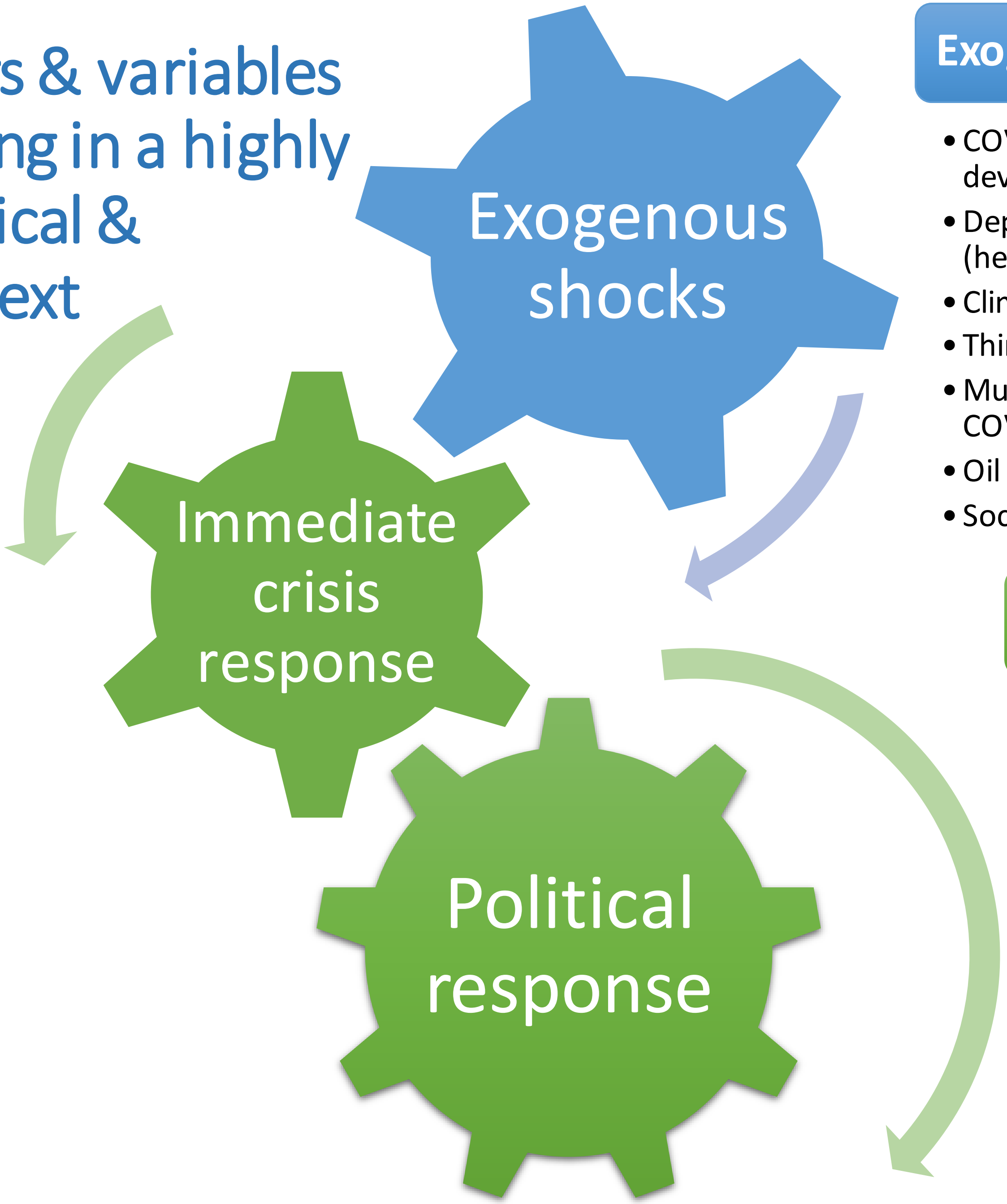
"Second round" impacts:

- **G**lobal economic slowdown
- Collapse of tourism
- Credit downgrades/higher cost of capital
- More downward pressure on oil prices impacts country balance sheets
- Risk of financial crises

"Third round" impacts:

- Risk of social instability rises due to food price rises and income shocks mirroring 2007/8 food crisis.
- Additional shocks from extreme weather impacts, locust infestation etc combine with COVID crisis

3 sets of drivers & variables interact resulting in a highly uncertain political & economic context



Exogenous shocks

- COVID-19 – mutation rate, severity of infection, development of vaccine, waves of pandemic
- Depth of the crisis – multiple compounded crises (health-economic-social) vs single crisis
- Climate impacts and extreme weather events
- Third order impacts e.g. food price crisis
- Multiple overlapping vulnerabilities (e.g. climate x COVID x debt x export crisis x food price crisis)
- Oil price & politics of energy
- Social consequences of mass changes in behaviour

Immediate crisis response

- Length of lockdown
- Depth of recovery packages – multiple rounds vs. one round
- Politics of normality vs politics of change (desire to return to normal)
- Leadership volatility
- Ability & agency to support vulnerable countries
- Tension between national interest and shared interest

Medium-term Political Response

- Ideological (e.g. ethnonationalism) and interest-based (e.g. fossil fuels) opposition
- Cooperation vs Isolation
- Role of the state & longer term public expectations
- Geopolitics of debt (tension over terms & control)
- Globalisation (national vs international division of labour)
- Politics of resilience and solidarity (national and international, in response to COVID-19 and climate impacts)
- Public support for climate action
- Siloed vs multi-crisis response
- Politics of freedom and public expectations on the role of the state

Too early to call the Geopolitics of Cooperation vs Isolation & Power

WORLD NEWS MARCH 26, 2020 / 8:21 AM / A MONTH AGO

G20 leaders to inject $5 trillion into global economy in fight against coronavirus

6 MIN READ

Trump Says China May Be 'Knowingly Responsible' for Virus

By Mario Parker
Updated on

Iranian, Russian, Chinese Media Push COVID-19 'Bioweapon' Conspiracies

AA FONT SIZE + PRINT AP PHOTO/EBRAHIM NOROOZI

COVID challenges Climate Actors to deliver same – or better outcomes – through different venues

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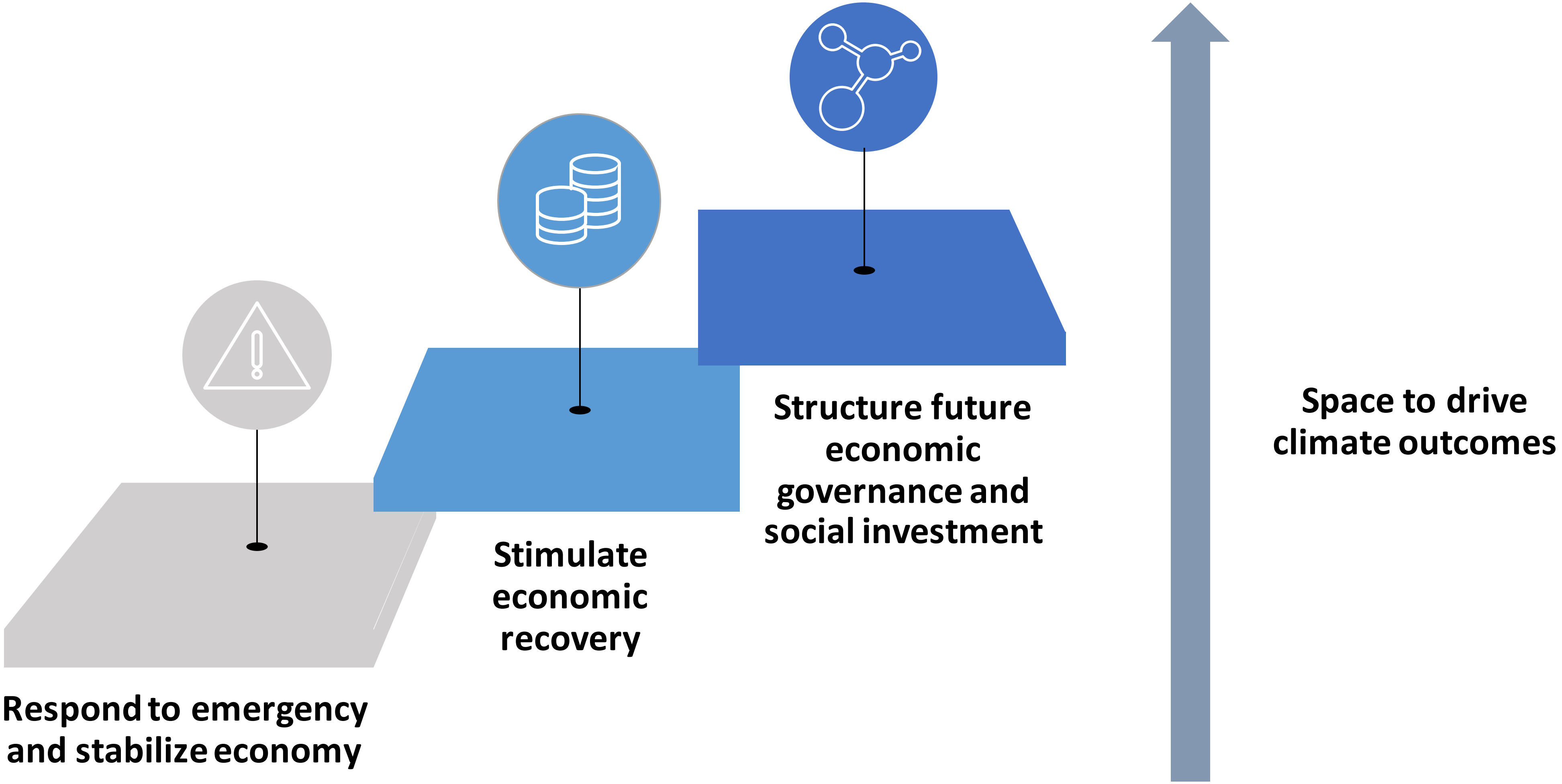
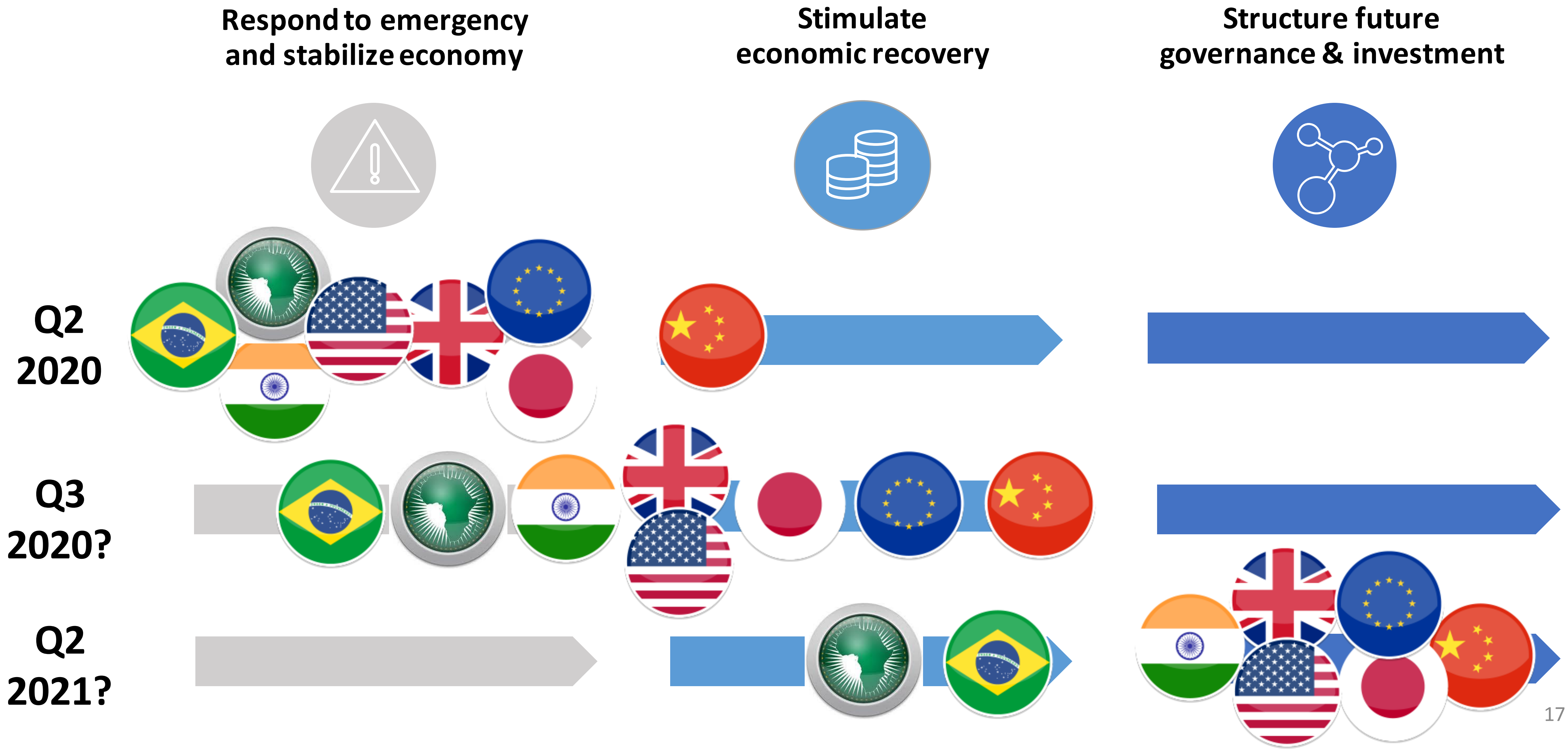
- **The theory of change has flipped.** Changes we expected to take 5-10 years will now be determined by actions taken in the next 18-24 months.
- **A window is now open to influence significant capital allocation and geopolitical dynamics** that will set the path of action for the next decade.
- **Big long term geo-economic questions are being asked now**:
  - Fiscal sentiment is being re-set by a big burst of government spending
  - Rapid transition in debt geopolitics calling into question how to manage debt relief, sovereign risk assessment, debt cooperation, stranded assets, and the role of China in managing global debt
  - Multiple interacting shocks are demonstrating the need to improve resilience across areas from public & environmental health, food security, economic resilience and social protection.

Climate actors - state and non-state - must influence unfamiliar venues and build new coalitions. <u>Will climate miss the wave of change?</u>

Ability to mainstream climate into COVID crisis responses will vary with phases of crisis



Countries will Move at Different Rates



Lessons from the 2008 financial crisis

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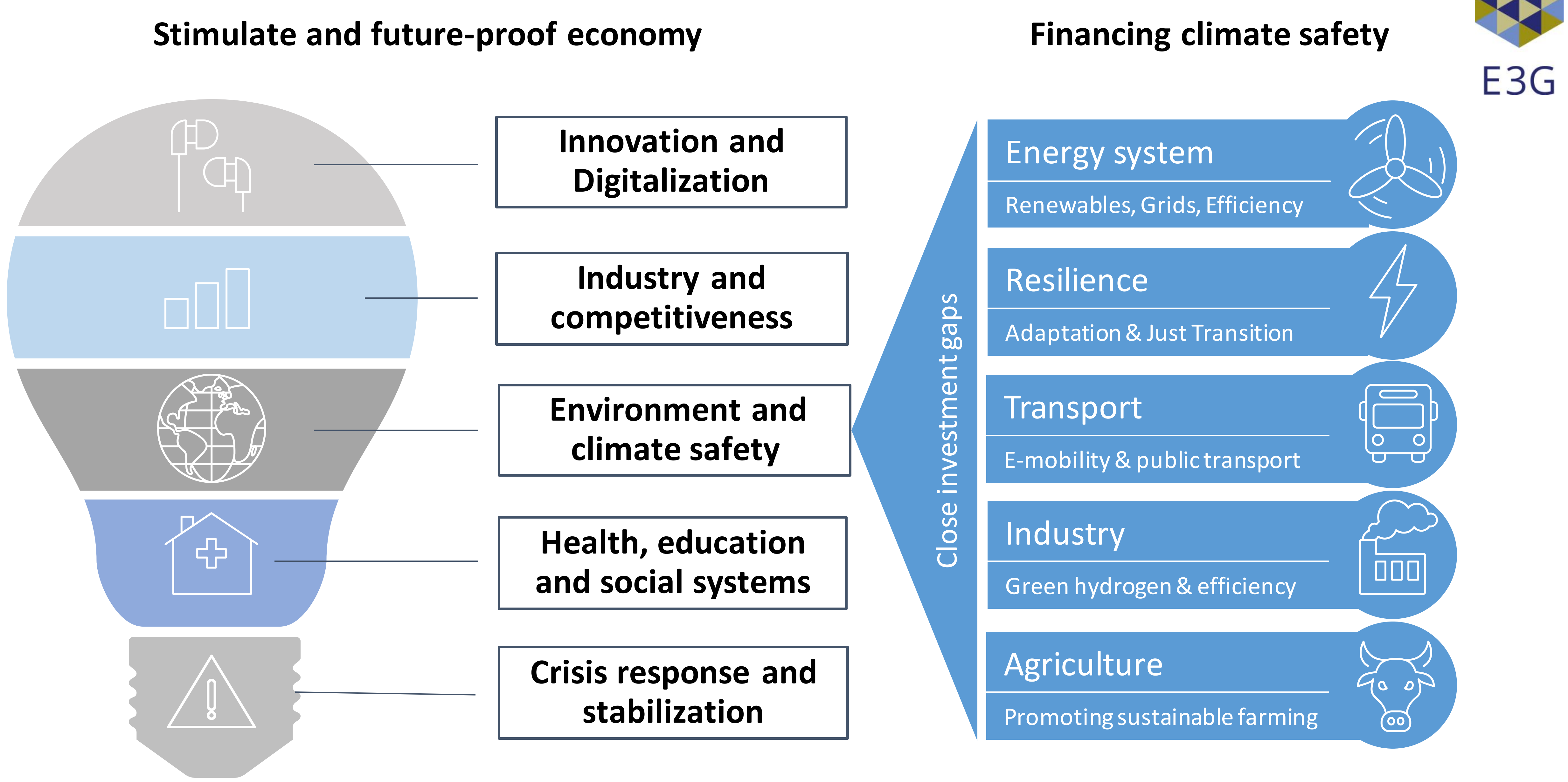
2008 ≠ 2020. Integrating climate outcomes demands unique strategies.
But what should we remember?

The stakes are high	Emissions drop in 2008 was short-lived. A repeat would jeopardise climate safety.
Political 'normality' returns quickly	Limited window of opportunity. Opponents of climate action will defend status quo. The politics of crisis rapidly becomes the politics of recovery (and retribution).
Process design will count as much as ideas	Stimulus package design process is dominated by institutions that undervalue climate/resilience & overvalue high carbon investment.
Design-in rapid delivery	Supporting policies and effective delivery must be designed-in from the start. Public banks & decentralised actors (e.g. regions, cities) are key for rapid delivery.

Reference: https://www.e3g.org/library/scorecards-on-best-and-worst-policies-for-a-green-new-01

We have much stronger political, institutional and economic assets to climate align recovery packages than in 2009

The Paris Agreement	• All countries have NDCs – and some long term strategies – often underpinned by domestic legislation which can guide and recovery spending and investment
Cheap Renewables	• Renewables are now cheaper than coal power which was the big beneficiary of 2009 stimulus packages. Coal power plants continue to be cancelled.
Finance actors more aware of climate risks	• Commitments to actively manage climate risk by IMF, ECB, NGFS Central Bank Group, Coalition of Finance Ministers; MDBs committed to Paris alignment; Private Investor groups.
Governance structures and mechanisms	• EU sustainable finance taxonomy; Helsinki Principles; TCFD Process and regulator guidance; Central Bank climate stress test scenarios
Support for climate action	• Widespread awareness and increasingly (though asymmetrically) mobilised populace
Non-state actor action	• Business and investor-led initiatives; city & subnational regions action & commitments including in laggard countries such as USA, Japan, Brazil, Australia etc
Climate becoming economically mainstreamed	• e.g. European Green Deal, South Korean Green Deal approach



Stimulate and future-proof economy
Financing climate safety
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Innovation and Digitalization
Industry and competitiveness
Environment and climate safety
Health, education and social systems
Crisis response and stabilization
Close investment gaps
Energy system
Renewables, Grids, Efficiency
Resilience
Adaptation & Just Transition
Transport
E-mobility & public transport
Industry
Green hydrogen & efficiency
Agriculture
Promoting sustainable farming

Economic Recovery – Some Green Shoots?

Broader economic recovery packages

- **Wealthy nations proposing enormous packages**
  - Packages worth significant % of GDP
  - ECB €1 trillion in QE
  - Japan (20%), UK (15%+), South Africa (10%)
- **Social safety nets the norm in wealthy countries**
  - US, Japan, Spain issuing pay-outs for all.
  - Extending welfare to those previously not covered (e.g. homeless, migrant workers).
- **A shift to monetary financing**
  - Many Central Banks directly financing programmes as countries unable to raise money on gilt markets.
- **Lower-income countries forced to turn to the world's creditors to support their economies – leading to rising debts**
  - IMF responding to 90+ countries emergency financing requests
  - World bank disbursing $160bn in budget support over next 6 months.

Green recovery measures

Many missed opportunities for green recovery

↓ **Short-term responses have not incorporated climate**

↓ **Bail-outs so far mainly granted without green strings**

↓ **Some push back against green financial regulation**

But a few green shoots:

✓ **European leaders have pledged to a green recovery** – 17 environmental ministers supporting a statement

✓ Some focus on green recovery measures from **South Korea, Japan and China**

✓ **IFIs support green recovery** – including Asian Infrastructure Investment Bank, IMF, World Bank, European Investment Bank and European Association of Public Banks

✓ **Cities taking the lead** – e.g. Amsterdam's 'donut economics' & Milan/Brussels looking to permanently reduce traffic

Elements of an EU Green Recovery

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- The EU has a €260bn annual investment gap to meet its current 2030 climate goals. EU 2030 climate goals likely to be increased in 2020.

- Pre-COVID the European Commission has already proposed a €1 trillion sustainable investment package to be leveraged through the EIB and other public banks. An additional €100bn Just Transition support package will support high fossil regions.

- **EU level** sees the European Green Deal as core stimulus package. European Council in April 2020: "restore *normal functioning of our societies and economies and to sustainable growth, integrating inter alia the green transition and the digital transformation, and drawing all lessons from the crisis.* ".

- Likely that funding devoted to recovery through the EIB & EU Budget will double post-COVID. All likely to be subject to the EU sustainable finance taxonomy which excludes most fossil fuel related investments. Commission focused on building renovation, nature based –solutions, stronger grids and EV charging networks.

- Lesson from the €500bn "Junker Plan" after 2009 crisis was that more intervention needed to drive investment into Eastern and Southern European and disadvantaged regions.

Delivering a fair and clean recovery will depend on strong public bank intervention into investment markets and pipeline creation.

The New Climate Diplomacy?

1. “Build Back Better” Diplomacy: UK & EU to build a joint approach with **China, Japan and South Korea to a Paris –aligned recovery** including stopping international coal financing as part of building effective international momentum behind Paris aligned recoveries.

2. Shape the design of stabilisation packages being delivered through the IMF & MDBs to avoid locking in high-carbon investments and keeping clean businesses & supply-chains open.

3. Build an approach to Climate-Aligned Debt Management to ensure that especially emerging economies have the fiscal space over the next decade for increased investment in climate action. Instruments such as “debt for nature/climate swaps” should **maximise the incentives for investment in climate transitions** and protection - especially in high coal-use & deforestation risk.

4. **Capitalise and reform international and national public banks** to ensure they can play a strong role in leveraging private capital into fair and resilient climate transitions.

5. Strengthen resilience governance at national and international level by developing a broad agenda for delivering complementary global action & reforms ay G7 & G20 in 2021 to improve resilience across the climate, health, development, energy, digital, food security and peacebuilding areas.

What Role for Financial Actors?

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Climate action now depends on major public financial decisions and reforms; arguments about dangers of "crowding out" private sector have disappeared.

- **What is the role of finance actors in shaping these choices?** Mix of finance industry voices pushing for & against climate financial regulation - what is the
- **What is the role of private finance intermediaries in financing the green recovery?** If public banks are doing the heavy lifting in bringing private assets into investments what is the added value of the private sector.
- **What are the long term changes needed to the balance of public and private finance?** Post-COVID will se many changes to the social contract and balance of state and private action in the economy. How will this impact finance?

About E3G

E3G is an independent climate change think tank accelerating the transition to a climate safe world.

E3G builds cross-sectoral coalitions to achieve carefully defined outcomes, chosen for their capacity to leverage change. E3G works closely with like-minded partners in government, politics, business, civil society, science, the media, public interest foundations and elsewhere. In 2018, for the third year running, E3G was ranked the fifth most globally influential environmental think tank.

More information is available at www.e3g.org

Questions, Comments & Answer(s)?

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Thank You

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14 May 2020 (14:30) In Safe Hands? – The Future Of Financial Services In 2020

15 May 2020 (12:30) Financial Centres Of The World 2020: Focus on Xi'an

15 May 2020 (14:30) Enterprise Management Incentives (EMIs) – Powerful Lessons From Five Practical Case Studies

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