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International Sustainable and Climate Finance: Where are we and which is the role of China on this?

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BRICS Policy Center Centro de Estudos e Pesquisas - BRICS

SOCIO ENVIRONMENTAL PLATFORM

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Summary

Abstract

Sustainable finance and climate finance have a large role to play on the effectiveness of the implementation of both the UNFCCC and the Agenda 2030. Sustainable finance is a large and growing field, both in terms of theoretical debate and in volume of resources involved. However, there is still no agreed global agreement of which specific criteria and transparency standards must be followed by financial institutions to allow them labelling the financial instruments under each of these categories. This brief focus on climate finance, as it encompasses a substantive part of the resources in this broader sustainability agenda. Having a better understanding of this field is important given the possible risk of other development resources being hijacked by the climate finance rhetoric. The paper also presents updated data on climate finance flows and for the implementation of the 2030 Agenda. Finally, it presents some evidence of how China and Chinese-led financial institutions are becoming key players in this field.

Key-words

Sustainable finance, Climate finance, 2030 Agenda, Development Banks, China

International sustainable and Climate Finance: Where are we and which is the role of China on this?

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1. Introduction

The year 2015 saw two landmark achievements in the global context of sustainable development: the adoption of the 2030 Agenda for Sustainable Development, and the Paris Agreement under the United Nations Framework Convention on Climate Change (UNFCCC). These two processes set the landscape of global development for the next generations. Efforts to tackle climate change are critical to meet the targets set by the Agenda 2030[1] and vice-versa. Given the risk that climate impacts impose on the poor and the benefits that climate adaptation action may have to improve their livelihoods, it is clear that, for policy interventions, there should be made efforts to tighten the relationship between climate and sustainable development initiatives.

Sustainable finance and climate finance have a large role to play on the effectiveness of the implementation of both the UNFCCC and the Agenda 2030. Theoretically, climate action may be more contentious; but there is a global consensus about the desire to meet the targets set by the Sustainable Development Goals (SDGs). The issue is how to channel more effectively funds to projects that contribute to these broad agendas in a global context of public resources scarcity, loose policy coordination, decentralized governance and where there are competing priorities and heavy private interests involved.

The sustainable finance field – both in theoretical terms and in practice - have been developing sharply in the last decades, in a movement driven by efforts of non-state actors, such as financial institutions, business associations, NGOs and academics, mostly from developed countries. In the past two-years, new players are entering in this debate, with the notable leadership of China.

The country has been showing a prominent role in the sustainable finance agenda in different fronts: In development finance, is the founder of two large multilateral development banks – the Asian Infrastructure Investment Bank (AIIB) and the New Development Bank (NDB) – both explicitly committed to advance the sustainable development agenda; in capital markets, is the largest issuer of Green bonds; in development cooperation, has made important announcements of contribution to South-South Cooperation funds with a focus on climate projects and in initiatives that contribute to the Agenda 2030 targets.

(1) Agenda 2030: https://sustainabledevelopment.un.org/?menu=1300

This Quarterly Brief aims to provide an overview of what is the current state of the debate on climate finance and SDGs finance as key policy spaces under the umbrella of sustainable finance. It also maps what China has been doing in practice that is somehow shaping this landscape. The critical questions it aims to answer are: **(1) What is the current state of the debate on climate finance and Sustainable finance? (2) What announcements and initiatives China has announced recently and how is it shaping this landscape?**

This policy brief is divided in three parts. **First**, it provides an overview of conceptual debates and provides an overview of the amount of resources involved. **Secondly**, it analyses how China and Chinese related institutions are shaping the discourse and action around climate and sustainable finance. **Thirdly** and finally, it concludes and provide some recommendations.

2. Sustainable Finance: Sustainable Development and Climate Landscape

Sustainable finance is a large and growing field, both in terms of theoretical debate and in volume of resources involved. Sustainable finance usually refers to any form of financial service integrating environmental, social and governance (ESG) criteria into the business or investment decisions.

Multiple knowledge areas – from banking to business management, from international development to environmental studies - have been working in further elaborating the concepts of “sustainable”, “green”, “clean”, “environmental” and “climate” finance. However, there is still no agreed global agreement of which specific criteria and transparency standards must be followed by financial institutions to allow them labeling the financial instruments under each of these categories.

Policymakers, civil society groups and in particular the media often use these categories are if they were synonyms, which create some confusion in the field to understand their underlying differences. In practice, sustainable financial instruments are used to fund many intersecting areas among these subcategories, such as energy, agriculture, sanitation and transport, but this does not make them necessarily the same thing.

2.1 Sustainable Finance Landscape

Since the recent adoption of the 2030 Agenda, sustainable finance instruments are being reframed and screened towards the implementation of the SDGs. The Goals cover many areas of development policy and in multiple levels (local, national, regional and global) with loose policy coordination. Thus, although virtually almost any resource could be framed as supporting the implementation of at least one of the goals, in practical terms, meeting the targets remain an open challenge.

It is quite likely that the 2030 Agenda shall drive the sustainable finance policy landscape from now on, specially in large infrastructure investments. However, this does not necessarily contribute to increasing the public understanding of the

The normative framework for the SDGs Means of implementation (MOI) comprises the SDG 17 (partnerships for the goals) and the Addis Ababa Action Agenda (AAAA) on financing for development (FfD). Together, they are meant to guide policy directions and indicators to quantitatively assess the mobilization of resources for SDG implementation. The funding gap to the Agenda 2030 implementation is still estimated in trillions of dollars per year.

differences among the different categories of sustainable finance instruments mentioned above. The sentence below, from a recently published OECD report[2], is a good example:

> "In addition to renewable energy, the term green infrastructure can cover a broad range of investments, including sustainable agriculture, foodplain levees and costal protection, waste management infrastructure and "green" water infrastructure. (…). This report focus on a subset of green infrastructure investments, namely LCR (Low-carbon and climate-resilient) investments made in companies, projects and financial instruments that operate primarily in the renewable energy, renewable technology, and environment technology markets, as well as those investments that are climate-change specific. (…)".

This brief focus on climate finance, as it encompasses a substantive part of the resources in this broader sustainability agenda. Having a better understanding of this field is important given the possible risk of other development resources being hijacked by the climate finance rhetoric. While incorporating climate concerns in all financial instruments design is positive and welcome, as climate change is a transversal topic that is influencing all aspects of our society, this may lead to an increasing dispute over resources among different development fields.

This risk would have at least two negative results: First, the tendency of pushing even more the 'additionality' argument further in a global development policy landscape. Apart from being politically sensitive, in times of public resources scarcity and the current trend in the North of shifting attention to inward looking demands, the difficulty of having OECD countries meeting their commitment to raising ODA flows to 0.7% of GDP shows that this line of argument is unlikely to succeed much. Second, it tends to open more space for the return of narratives that put the environmental, climate and traditional development agendas 'against' each other. This would be a strong step back to the idea of improving living standards to everyone.

2.2 Climate Finance Landscape

Under the UNFCCC and back in 1992, developed countries have committed to transfer[3] financial resources and technology to developing countries to allow the implementation of their actions to tackle climate change and pursue the transition to low carbon development models. Parties agreed to create financial entities such as the Global Environment Facility (GEF), the Green Climate Fund (GCF), the Adaptation Fund, among others, to manage and distribute the resources labeled as climate finance that would contribute to the implementation of the Convention's goals. Developed country Parties pledged and made commitments to transfer resources to these entities in order to fulfill their obligations under the Convention.

During all these years, the conceptual debate about climate finance became more complex and can be analyzed through multiple lens. In short, if one looks from a geopolitical and International Relations point of view, the Global North and Global South development debt argument would lead to a discussion on the critical role of public resources from developed countries in financing the

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(2) (OECD 2016) Green Investment Banks, Scaling up Private Investment in Low-carbon, Climate-resilient Infrastructure, Green Finance and Investment, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264245129-en
(3) UNFCCC, Article 4 - "The extent to which developing country Parties will effectively implement their commitments under the Convention will depend on the effective implementation by developed country Parties of their commitments under the Convention related to financial resources and transfer of technology and will take fully into account that economic and social development and poverty eradication are the first and overriding priorities of the developing country Parties".

adaptation to climate impacts and decarbonization of economies in the Global South[4].

If the debate is framed from an international development perspective, the theoretical dispute between development vs. climate priorities leads to a discussion on additionally of resources and the need of guaranteeing resources for poverty eradication, health and education demands, despite the urgency of tackling climate change[5].

Finally, from a political economy perspective[6], the critical issue relies on which are the most efficient financial instruments to promote economic structural change in a way that properly values pollution externalities and natural resources use and the role of private sector and business in financing the economic transformations and infrastructure demands that are needed to implement sustainable development models.

Fast-forward to 2009, at COP15, in Copenhagen, developed country Parties have committed to jointly mobilize $100 billion per year by 2020 for the needs of developing countries. Intense discussions have been taking place in many arenas since then to try to reach an agreement on how[7] to count the contributions to the accomplishment of this joint commitment.

In 2015, at COP21 when the Paris Agreement was adopted, there was a significant change in the language of the agreement. It brings in its Article 2 the command that **finance flows** should be "**consistent with** a pathway towards low greenhouse gas emissions and climate resilient development". The idea of consistency is conceptually difficult to define and opens a new large space for discussion on what elements constitute a financial flow that contributes or not to the Paris Agreement and the overall Convention implementation.

This language opens a window of possibilities on how to frame and design financial instruments in a way that contribute both to climate and development goals. Blended finance[8] is one example, DAC Official Development Finance Rio Marked[9] is another, among several instruments.

In fact, many years have passed and "there is as yet no agreed definition of "climate finance", and no centralized system for tracking all relevant climate flows. **Crucial questions remain regarding what can be accounted for both under "climate" and under "finance"**, i.e. which activities and which flows are eligible to be counted towards the $100 bn." (OECD, 2012, Ex. Sum)

In a cloudy landscape of conceptual discussions, the reality is that climate negotiations continue to face severe constraints when it comes to moving climate finance from pledges to effective financial contributions and means of implementation to developing countries. Despite developed countries efforts to publish a draft $ 100 billion Roadmap[10], there is still an overall very low confidence that the

(4) Barnett, J. (2007). The geopolitics of climate change. Geography Compass, 1(6), 1361-1375.
(5) Steele, P.,(2015). Development finance and climate finance: achieving zero poverty and zero. IIED, London, UK. https://www.iied.org/development-finance-climate-finance-achieving-zero-poverty-zero-emissions
(6) Nakhooda, S., Fransen, T. Caravani, A., Kuramochi, T., Prizzon, A., Shimizu, N., Halimanjaya, A., Tilley, H. and Welham, B. (2013). Mobilising International Climate Finance: Lessons from the Fast-Start Finance Period. Overseas Development Institute, London, UK World Resources Institute, Washington DC, US and Institute for Global Environmental Strategies, Japan.
(7) M.I. Westphal, P. Canfin, A. Ballesteros, and J. Morgan. 2015. "Getting to $100 Billion: Climate Finance Scenarios and Projections to 2020." Working Paper. Washington, DC: World Resources Institute. Available online at: www.wri.org/publication/getting-to-100-billion.
(8) OECD (2018) Making Blended Finance work for the Sustainable Development Goals, OECD Publishing, Paris. http://dx.doi.org/10.1787/9789264288768-en
(9) OECD DAC Rio Markers for Climate - Handbook. http://www.oecd.org/dac/environment-development/Revised%20climate%20marker%20handbook_FINAL.pdf
(10) https://dfat.gov.au/international-relations/themes/climate-change/Documents/climate-finance-roadmap-to-us100-billion.pdf

map would be followed, and the target met[11].

Finally, although the obligation of providing climate finance under the UNFCCC relies on developed country Parties (given their historical responsibilities for climate change and relative more capacity), the negotiations at COP21 also stressed the debate about the role of Emerging Economies in the climate finance landscape. The so-called POTODOSO[12] countries, in particular China, were under pressure to contribute more to finance the solutions, given their higher and increasing participation in total global GHG emissions. The approach followed by China in becoming a player in this landscape is strongly informed by this UNFCCC North and South dynamics.

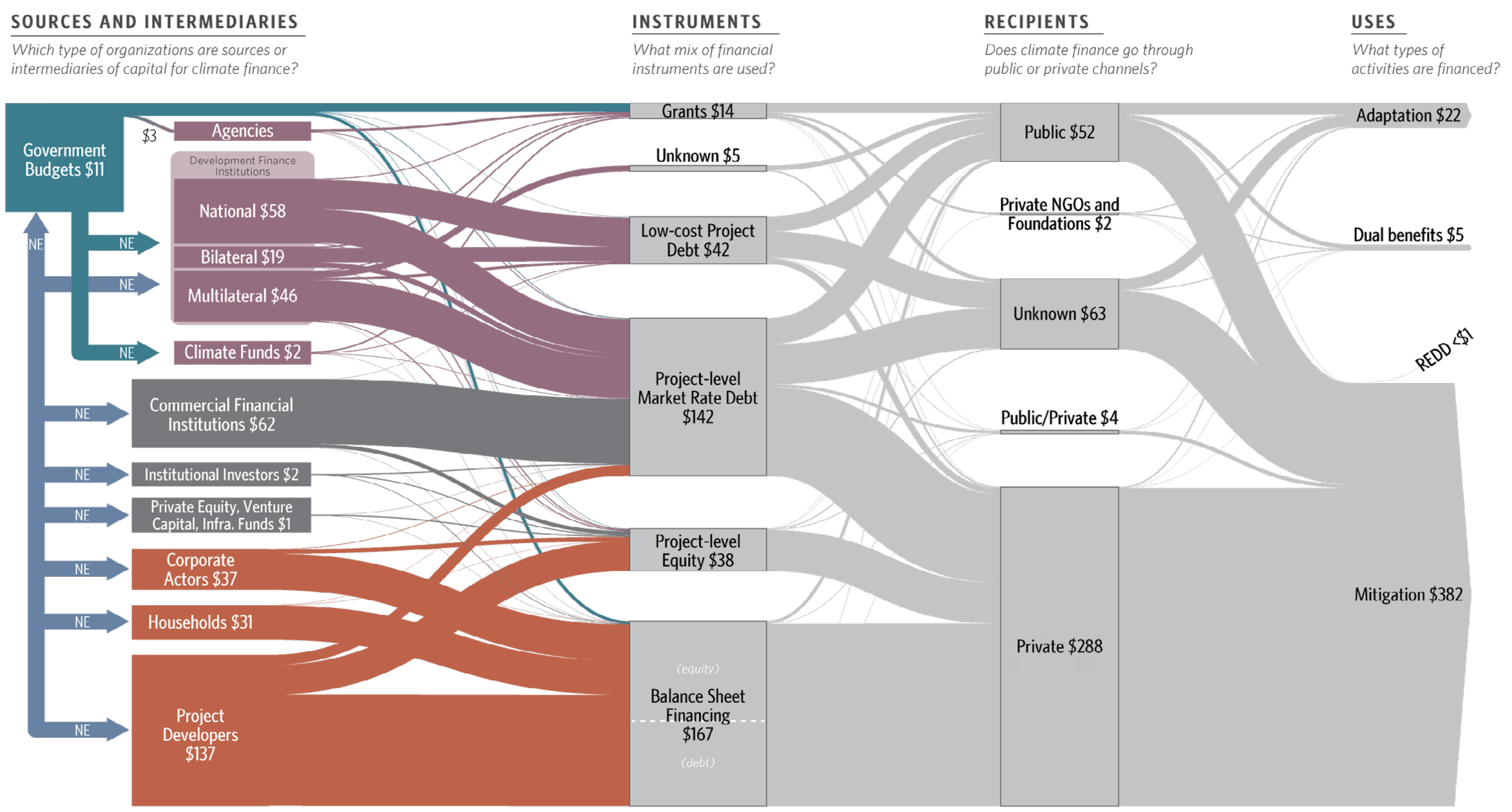
Climate finance is a mix of local, national and international resources – from public and private sources, flowing through a plethora of intermediaries, instruments and implementing agencies – intended to address the causes and consequences of climate change. It is commonly defined as mitigation and adaptation finance.

2.3 How much money is involved?

There are many initiatives trying to map and quantify sustainable and climate finance invested and available. On what concerns climate finance, the most notable effort is the Climate Policy Initiative's global landscape of climate finance report.[13] Their most recent figures show a record high of USD 437 billion in 2015 and a decrease to **USD 383 billion** in 2016. The box below shows the overall picture.

Landscape of climate finance in 2015/2016

Global climate finance flows along their life cycle in 2015 and 2016. Values are average of two yaers' data, in USD billions.



Source: *CPI Report 2017*

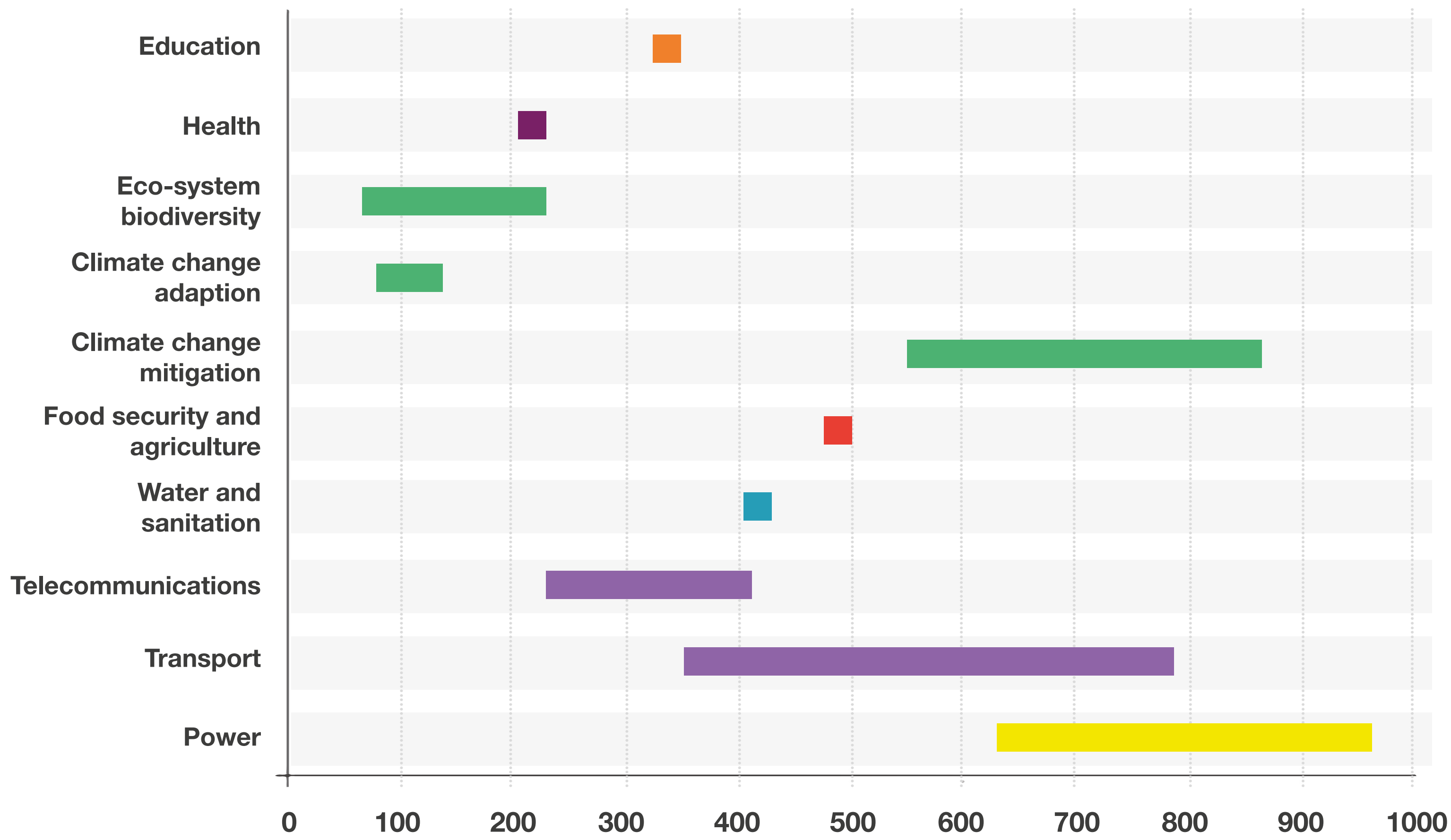
(11) Upon the USA withdrawal of the Paris Agreement, the confidence became even lower.
(12) The acronym stands for developing countries "in a Position To Do So", or with established financial and technical capacity to provide support to other developing nations in their mitigation and adaptation needs.
(13) Barbara Buchner, Padraig Oliver, Xueying Wang, Cameron Carswell, Chavi Meattle and Federico Mazza (2017) Global Landscape of Climate Finance 2017, Climate Policy Initiative. https://climatepolicyinitiative.org/publication/global-landscape-of-climate-finance-2017/

Among the many possible analysis of this chart, for the purpose of this brief, three aspects are noteworthy: (a) the concentration of flows in two instruments - “project-level market rate debt” and “balance sheet financing”; (b) the unbalance between public and private recipients and (c) the unbalance between mitigation and adaptation uses.

From a 2030 Agenda perspective, the latest figures from the UN Secretary General Report claim a peak in 2016 of OECD-DAC ODA resources, summing $142.6 billion[14]. The report brings data on remittances, but does not bring any data on private flows contribution to meet the targets. UNCTAD estimates the funding gap for the SDGs implementation in developing countries in **USD 2.5 trillion**[15]. It explicitly suggest that public funding will not be enough to meet the targets and recalls that while private investment is needed, it require countries facing “policy dilemmas” and challenges like the “lack of transparency on environmental, social and governance performance” and the need of “building or improving pricing mechanisms for externalities” to name just two.

The figure below shows the estimates of the annual required investments per field. Interestingly, the energy sector (both electricity and fuels) is precisely the area that captured more private investments from climate finance, according to CPI’s report[16].

Estimated Annual Investment Requirements, Core SDG Sectors (US$ billions)



Source: *UNDP calculations based on UNCTAD, World Investment Report 2014*

(14) http://www.un.org/ga/search/view_doc.asp?symbol=E/2017/66&Lang=E, pp.18-19
(15) UNCTAD (2014) World Investment Report 2014, http://unctad.org/en/PublicationsLibrary/wir2014_en.pdf
(16) CPI(2017), pp. 9. Data gaps in financial flows to other sectors are noteworthy, though.

The global sustainable and climate finance is complex and there are many shadow areas between them and SDGs Means of Implementation. It is difficult to track and monitor all these resources in a decentralized and non-mandatory reporting system as we have nowadays.

Let alone the methodological difficulties, new players in the field, such as China and other developing countries, have been setting new institutions and frameworks that fall short in providing public data on what they are funding, the amount of resources and where it goes. Instead of strengthening existing structures, such as the United Nations Fund for South South Cooperation (UNFSSC), there has been a proliferation of announcements of new investment structures and channels. The next section looks at China in this field.

3. China as a crucial player in sustainable and climate finance

The increasing volumes flowing from China to the implementation of the sustainable development agenda – both for climate and SDGs initiatives - are noteworthy. The country has been showing a strong political will in leading both agendas, by making many public announcements[17] and pledges of financial contributions in the past two years. Under the Chinese presidency of the G-20, one of the critical topics of the summit was precisely the "development of Green Finance". The box below shows some of the key announcements.

Date / Act	Value
2015-Jun: China-LAC Cooperation Fund is initiated with an initial Chinese investment. (See more)	**US$ 5 billion**
2015-Sep: China South-South Climate Cooperation Fund announcement. (See more)	**US$3.1 billion**
2015-Sep: Chinese pledge to LDCs implement the Post-2015 Agenda. (See more)	**US$ 2 billion**
2016-Nov: At COP22, China announces the UNDP-China programme to assist countries in SDGs and climate targets implementation. (See more)	**N/A**
2017-May: Joint communiqué of leaders roundtable of Belt and Road forum. (See more)	**N/A**

In addition, recent data from UNOSSC, the financial flows from China increased more than twenty times in fifteen years[18].

(17) https://www.twn.my/title2/finance/2015/fi151101.htm
(18) https://www.unsouthsouth.org/2018/01/24/the-unstoppable-strength-of-the-south/

The Chinese recently published an assessment of its own implementation of the 2030 Agenda[19], and their analysis of the SDG17 implementation provides interesting insights. It recalls the commitments to replenishment USD 1 billion to the South-South Cooperation Assistance Fund, its contributions to a range of Development banks to pursue sustainable development projects. But, most importantly, it frames the **One Belt One Road** initiative as a “highly compatible with the 2030 Agenda”. The framing of this massive Chinese-led infrastructure investment package, that promises to change the whole dynamics of Asia trade and logistics infrastructure, as a 2030 Agenda investment contribution may boost the numbers of sustainable finance but opens a lot of questions on to what extent and under which criteria, the investments made are actually “sustainable”.

From a sustainable finance supply side, it is interesting to note the green narrative adopted by Chinese-led development institutions such as the Chinese Development Bank (CDB), the AIIB and the NDB.

The CDB includes Green Growth in its Core Values, as “an important aspect of our social responsibilities. As one of the members of the United Nations Global Compact, CDB places great emphasis on energy and resource conservation and environmental protection. We support green, circular and low-carbon development, incorporating the notion of “green credit” into all aspects of its business operations. (…) CDB will adhere to the green development principle, reduce waste of resources in business operations, and prioritize green finance in line with our commitment to combating pollution in China. (…)”. According to its website, by the end of June 2015, the balance of the banks outstanding green loans totaled RMB 1.5 trillion (approximately USD 235 billion).

The AIIB has as founding principles to be “Lean, Clean and Green[20]”. Among its thematic priorities is to foster sustainable infrastructure, in particular “Promoting green infrastructure and supporting countries to meet their environmental and development goals”. The NDB’s Articles of Agreement, Article 1, suggests that its purpose is to ”mobilize resources for infrastructure and sustainable development projects in BRICS and other emerging economies and developing countries (…).

In addition, it is interesting to note that the results-based/carbon metric approach for finance adopted by the climate constituencies to quantify the resources under the UNFCCC seem to have left a legacy in the way new players, in particular development banks, frame the climate finance investments and impacts. Both AIIB and the NDB, their approved project description presents not only the usual data on number of potential beneficiaries or jobs created, but also the volume of CO_2 emissions avoided[21]. The marker for correlation with the investment and the SDGs agenda is unclear, as there is no explicit mention on the target SDG, but the institutional narrative also address them.

Whereas China is becoming a global leader in both climate and sustainable finance in the Global South, it is from a sustainable finance demand side that we see where most of the resources are flowing. China is also capturing for its domestic purposes a substantive part of the available sustainable investments. According to recent International Development Finance Club (IDFC) data[22], in 2016, IDFC members contributed $173 billion in green finance commitments, $159 billion of which was climate finance. Under this category, $153 billion commitments (88%), represent investments in decarbonization of urban transportation in China.

(19) (2017) China’s Progress Report on Implementation of the 2030 Agenda for Sustainable Development. http://www.cikd.org/cikd/English_Version/E_DocView_CIKD.aspx?docid=2894207&leafid=1326

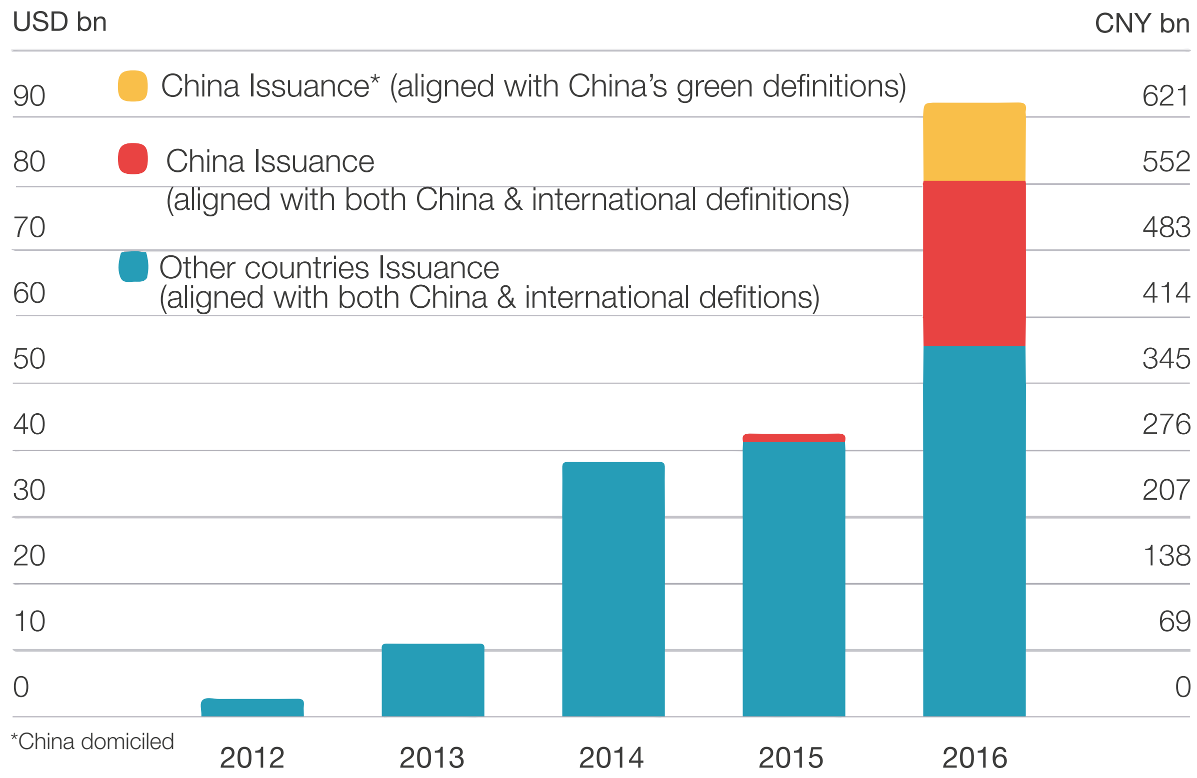
(20) Their definition of Green is “Demonstrating a keen sense of awareness and respect for the environment, and actively promoting sustainability are key guiding principles which underpin AIIB operations. The Bank is committed to financing infrastructure that is environmentally friendly and socially sustainable, and it will support members in their transition towards a low-carbon energy mix”.

(21) https://www.ndb.int/projects/list-of-all-projects/ and https://www.aiib.org/en/projects/approved/2017/_download/beijing/beijing-air-quality.pdf

(22) http://www.idfc.org/Downloads/Publications/01_green_finance_mappings/IDFC_Green_Finance_Mapping_Report_2017_12_11.pdf

According to a recent study, China would need annual green investment amounting to at least USD$ 315 million US dollars over the period of the 13th five-year plan (2016 to 2020) to be able to effectively combat its environmental problems[23]. These figures also explain why China is becoming the largest global Green Bond issuer, surpassing the USA in 2017[24]. See figure below.

Global Growth in green bound issuance was driven by China in 2016



Source: *China Green Bonds Market 2016*

4. Conclusions and Recommendations

The policy brief presented an overview of the sustainable and climate finance landscape, its key conceptual debates, resources and starts exploring the role of China as a key player in this field. It was framed under the UNFCCC/climate finance and Agenda 2030/SDGs agenda, as the leading international policy spaces that are setting this agenda[25]. As said before, it does not intent, by any means, to exhaust the topic, but rather bring some updated data and help to present the issue for a non-expert audience.

Both the Agenda 2030 and the Paris Agreement are in their initial stages of implementation, but the magnitude of resources involved, and the multitude of financial instruments being used to implement them already show the trend of the substantive (and growing) importance of this agenda.

(23) KAS (2017) Climate Report 2017. http://www.kas.de/wf/doc/kas_49481-544-2-30.pdf?170711095417
(24) https://www.cnbc.com/2017/12/26/climate-change-china-is-the-worlds-biggest-green-bond-issuer.html
(25) It does not cover other international fora where there are many overlaps and synergies such as the Convention on Biological Diversity (CDB), the Montreal Protocol among others.

Despite their positive contribution to push the incorporation of a sustainable development framework by financial institutions in developing financial instruments, the sustainable finance field still lacks methodological, conceptual and on the ground assessments and analysis to guarantee that sustainable investments have indeed positive environmental, social and governance impacts on the ground. In other words, nowadays is somehow easy to frame almost anything as sustainable, but there is little accountability to guarantee that the projects are indeed addressing the society's environmental, social and governance demands.

The standards are improving, but so far there is no official global consensus on what resources are accounted as climate finance, green finance or sustainable finance. Having more non-state actors' players from the Global South, in particular the academia and civil society, trained to participate and dispute the underlying assumptions and practices of sustainable finance is crucial.

China and other Chinese led institutions are becoming strong players from the Global South, both in setting this agenda and capturing the resources. New multilateral development banks such as the AIIB and NDB are already starting to publish more information on environmental and climate implications of the funded projects, but still in a superficial level, in particular if one moves away from a solely GHG mitigation point of view. This will improve only if players from the Global South become watchdogs of their practices and hold them accountable.

Last but not least, there is a risk of the 2030 Agenda and resources being hijacked by the pressure and market forces involved in the implementation of the climate targets set by Parties to the Paris Agreement. This may lead to developing countries insisting on the 'additionality argument' putting pressure on developed country Parties to contribute with more resources to finance their climate and SDGs targets. While the financial commitments assumed by developed countries must be honored and followed, there is a whole new set of investments and instruments being made that should also be screened according to these global objectives. The sustainable infrastructure projects financed by China are one example.

Recommendations

1. Initiatives like the IDFC should be strengthen by more Development Banks, in particular the AIIB and the NDB, to push all major development banks in aligning and broadly communicating their transparency and accountability practices and standards. Through participatory processes, the banks should aim to refine and make it public a common criteria for distinguishing "green", "clean", "sustainable" and "climate" finance;

2. There should be more capacity building efforts funded by and led by Global Southern institutions to help policymakers, NGO and international relations students reaching a better understanding of these financial instruments;

3. Development Banks, in particular from China and other Southern countries, should provide resources to fund academic and/or think-tanks, NGOs evidence-based assessments to better understand the social and environmental impacts on the ground of their sustainable projects.

4. Public finance and Tax policy makers working at national level should start screening and testing, by default, any new policy or financial instruments towards their contribution to the implementation of both the 2030 Agenda and the Paris Agreement.

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