CLIMATE AND FINANCE - ALSO A LOST DECADE?

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AALBORG UNIVERSITY
COPENHAGEN

How has the changing regulation of finance in the wake of the financial crisis influenced the contribution of finance to facing climate change?

Frederik Lasserre, Analyst, Cevea

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AAU Copenhagen, 01.03.2019

What is the role of finance?

- At its core, finance is a ***means*** to an end.
- Financial activities are ***means*** that exist to support ends that originate from society – households, companies and governments.
- Savings, reallocating capital for productive purposes, distributing risks = serving the real economy

A proliferation of new initiatives

- Green Finance
- Sustainable Finance
- Prompted by the SDGs and the Paris Agreement and the new market opportunities they represent

UN environment

WORLD BANK GROUP

A UN ENVIRONMENT – WORLD BANK GROUP INITIATIVE

ROADMAP FOR A
SUSTAINABLE FINANCIAL SYSTEM

UNEP FINANCE INITIATIVE
CHANGING FINANCE, FINANCING CHANGE

European Commission

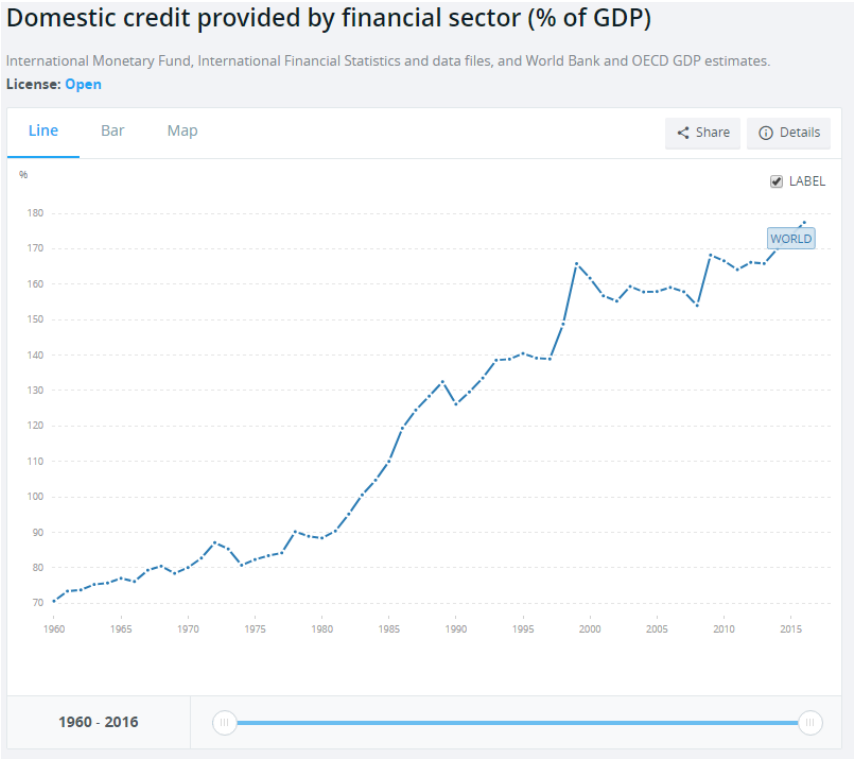
Finans Danmark lancerer nyt Forum for Bæredygtig Finans

Sustainability has a double meaning in relation to finance

- The financial sector should be sustainable in and of itself - it shouldn’t provoke crises or destabilise the real economy
- The financial sector has to manage and steer economic acitivity so that it unfolds within the boundaries set by the environment, the climate and the scarce resources of the Earth

What is the problem?

- **Financialization:** A process through which financial markets, financial institutions and financial elites gain greater influence over political and economic outcomes.
- **Decoupling since the 1980'ies:** The financial sector has outpaced the real economy, credit fueled expansions



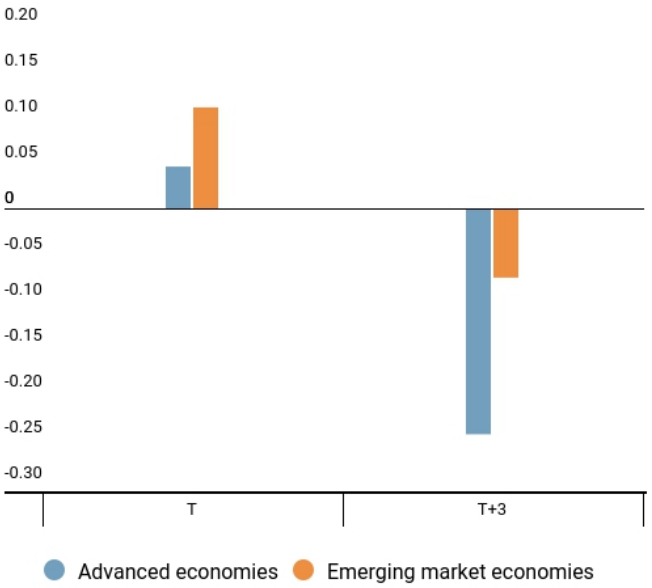
Private debt have long-term negative impacts on real GDP

- The bloated financial sector and the excessive amount of credit can be a drag on the real economy
- Gradual blowing up of asset bubles
- Financially driven upswings are followed by deeper recessions

Economic impact

Gains in household debt have a positive impact on the economy in the short term.Three years later, the impact is negative.

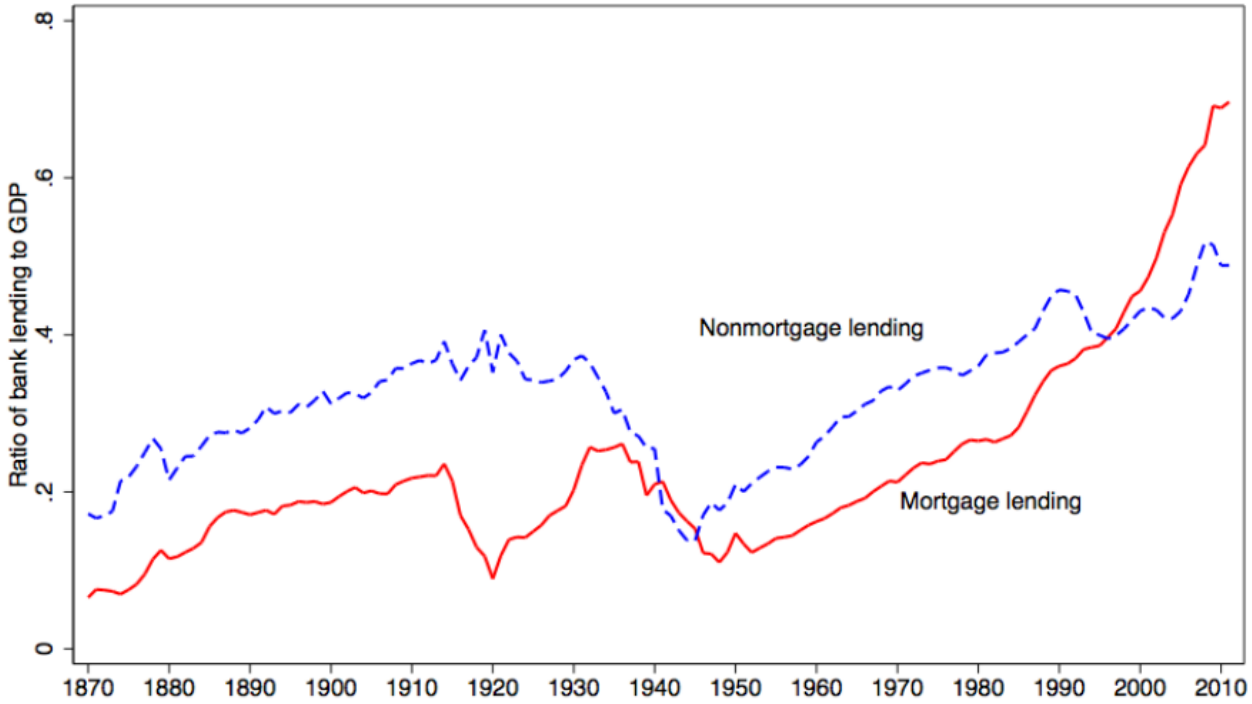
(impact on real GDP growth of a 1 percentage point change in household debt-to-GDP, in advanced and emerging economies, percent).



Source: IMF staff calculations.

Credit has shifted away from the real economy

Figure 2: *Bank mortgage and non-mortgage lending to GDP, 1870–2011: Average ratio to GDP by year for 17 countries*



Post-crisis regulation has not addressed this challenge

- Narrow institutional reforms – capital and liquidity
- The Basel-framework and structural disincentives to lend to the real economy
- Internal risk weights, tax incentives for debt financing
- Systemic risks neglected, if not increased – bigger banks, less diversity

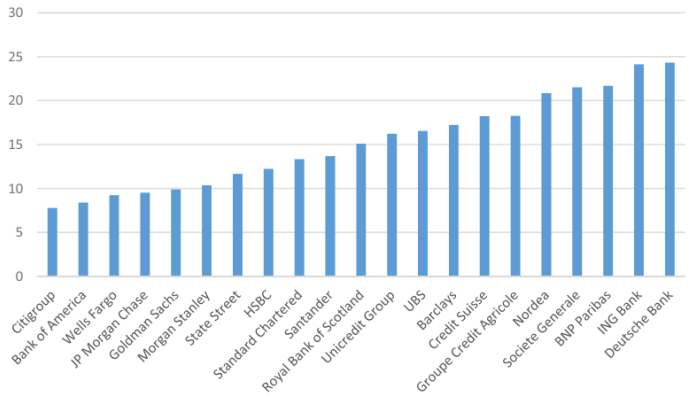


Figure 2. Leverage in 2015 (ratio of total assets to total equity).

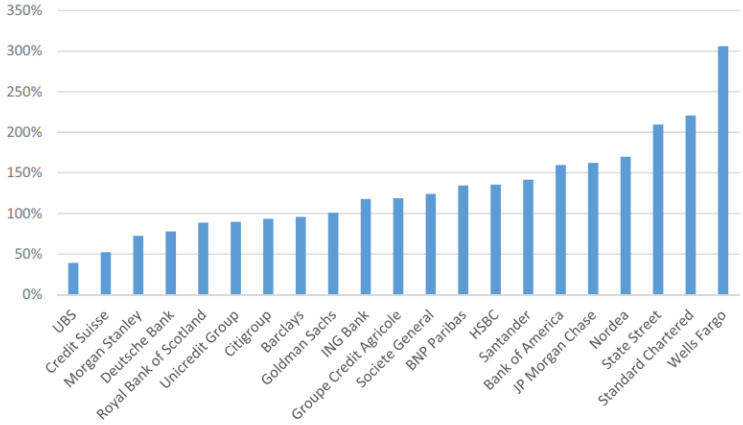


Figure 7. 2015 assets as a % of 2005 assets.

Sustainable finance risks becoming a dangerous stepping stone

- The need for long-term investment and additional funding in the real economy has been tied to expanding the shadow banking sector – casting hedge funds and private equity funds to play the role of banks

Completion of the first measures is essential for the CMU to have a tangible impact on the ground. The European Council of 28 June 2016 called for an agreement by the end of 2016 on the proposals for Simple, Transparent and Standardised (STS) securitisations[4], to free up capacity on banks' balance sheets and provide investment opportunities for long-term investors, and on the proposal for the simplification of prospectus rules making it easier for companies to seek investment from the capital markets.

Rapid implementation of the securitisation package has the potential to quickly generate additional funding in the real economy. Establishing more risk sensitive capital charges for STS securitisations, will help to build confidence in the market and free up the balance sheets

In being af vehicle for economic insecurity and growing inequality, finance has negatively affected the politics of sustainable transition

Tak for jeres tid

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Climate and Finance
- also a lost decade?

What are the key challenges ahead for climate finance

The Lost Decade
Planning the Future

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available at:
.nasa.gov/apod/ap020811.html

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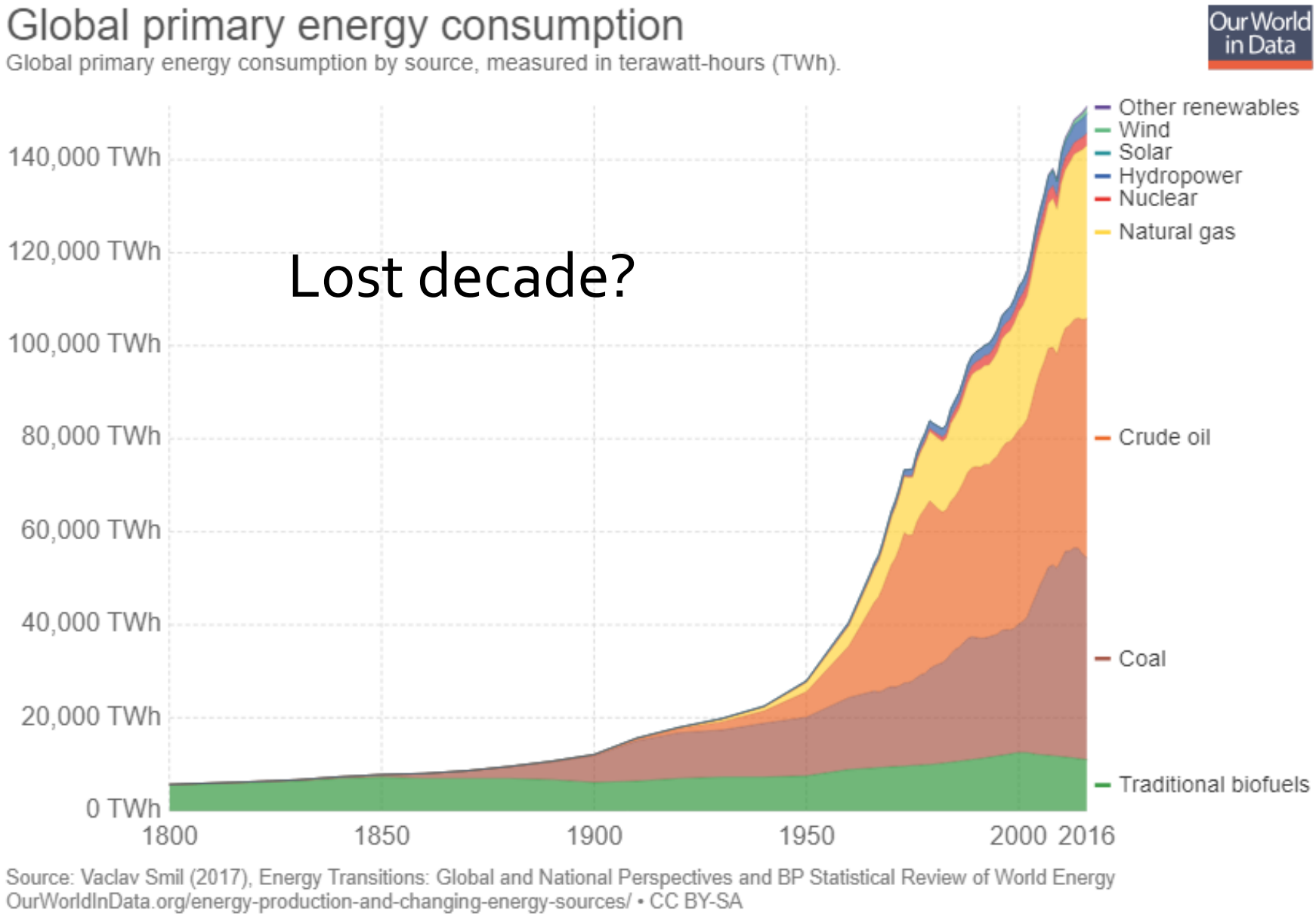

Our world in data, 2017

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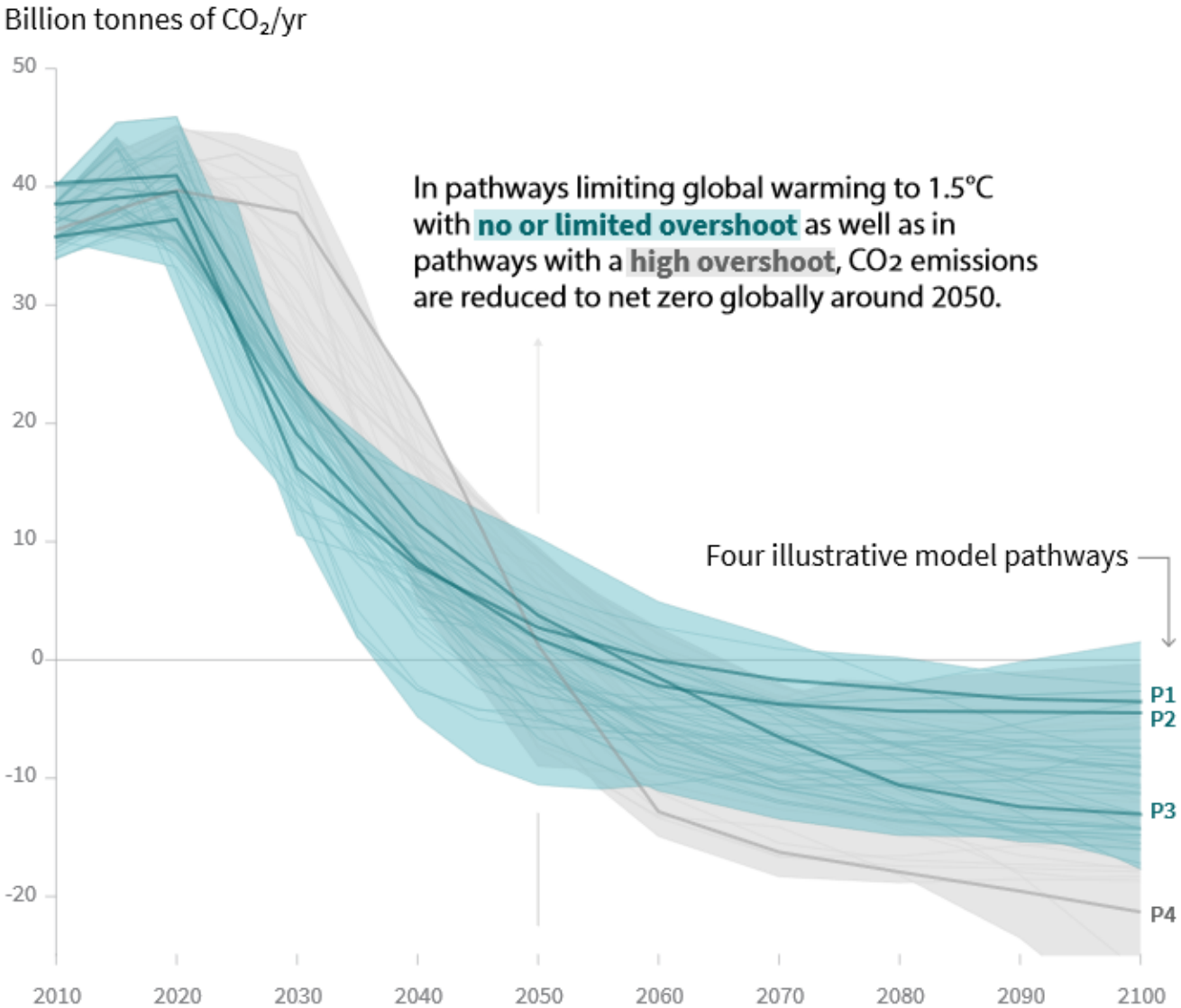
Global total net CO_2 emissions



'Overshoot' will make everything much more expensive

Need to "shift to the trillions" asap

Source: IPCC, IR 1.5, 2018

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- Around US$90 trillion in infrastructure investment is needed by 2030 to achieve global growth expectations (NCE, 2015).

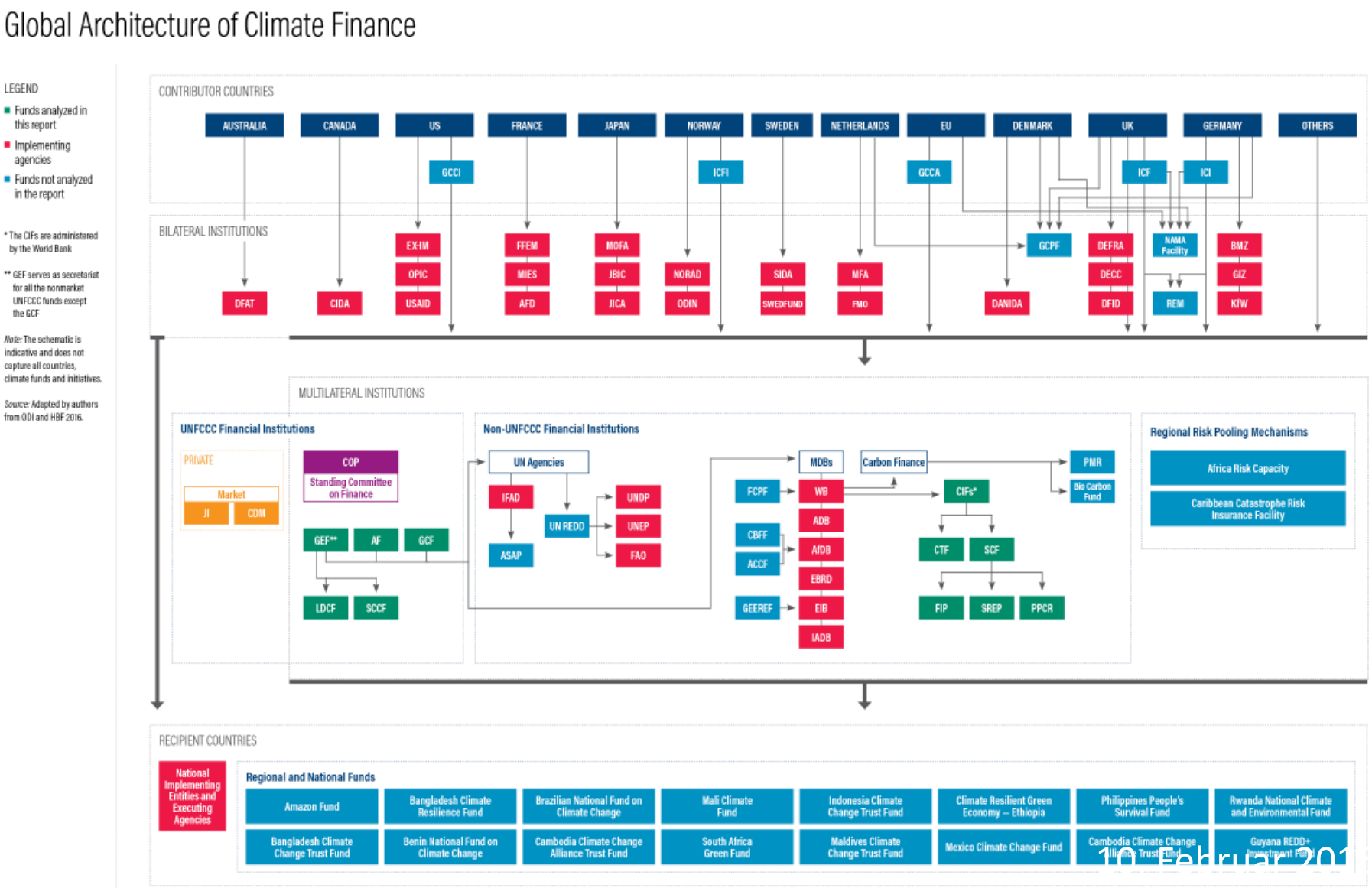
- That is equivalent to around US$6 trillion per year, but current annual global investment is estimated at only around US$1.7 trillion.

- The NDCs of 21 emerging market economies alone represent $23 trillion by 2030 in **investment opportunities** (IFC).

- Overall, a shift to low-carbon, resilient economies could translate into $26 trillion in **global economic benefits** through to 2030 (IFC)

- Leveraging and gearing private capital at **SCALE AND SPEED** is critical – color of money is less important

Proliferation of public climate finance



www.wri.org/publication/future-of-the-funds

Source: WRI 2017, Future of the Funds: Exploring the Architecture of Multilateral Climate Finance

Public Climate Finance is up, but not enough

	2013	2014	2015	2016	2017
1. Bilateral public climate finance from developed countries	22.5	23.1	25.9	28.0	27.0
2. Multilateral public climate finance attributed to developed countries	15.5	20.4	16.2	18.9	27.5
Subtotal (1+2)	**37.9**	**43.5**	**42.1**	**46.9**	**54.5**
3. Officially-supported export credits (climate-related) from developed countries	1.6	1.6	2.5	1.5	2.1
Subtotal (1+2+3)	**39.5**	**45.1**	**44.6**	**48.5**	**56.7**
4. Private climate finance mobilised by developed countries	12.8	16.7	Forthcoming		
Total (1+2+3+4)	**52.2**	**61.8**			

Note: The sum of individual components may not add up to sub- and grand totals due to rounding.

Source: OECD analysis based on OECD DAC (2018 and forthcoming), OECD TAD (2018), UNFCCC (2018, 2016), supplementary country reporting to the OECD.

Source: OECD 2018

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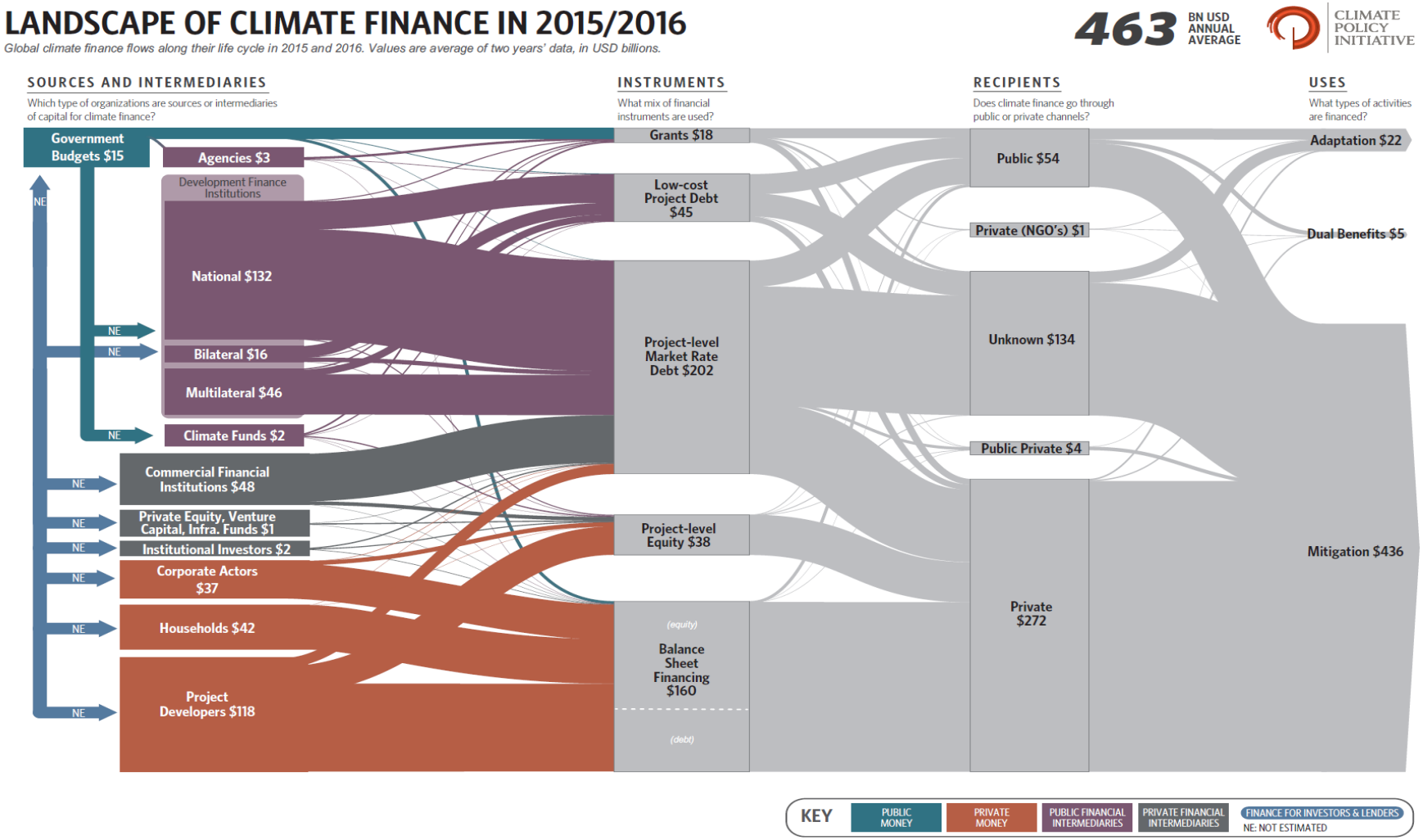
”Its complicated…”



Source: CPI, Global Climate Finance Landscape 2017

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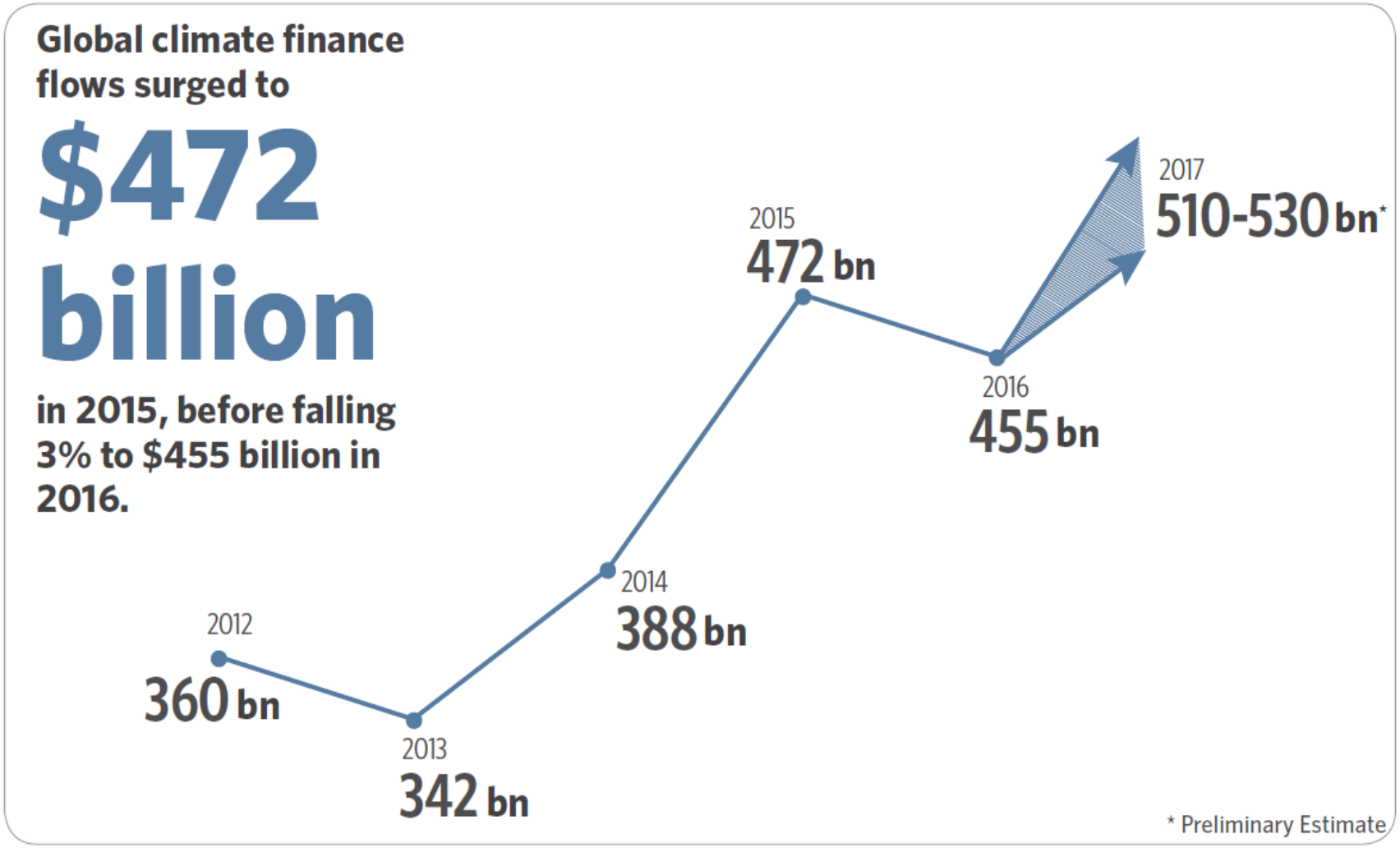
But increasing…

Figure 1: Amount of global climate finance 2015-2017* (*estimate)



Source: CPI, Global Climate Finance Landscape 2017

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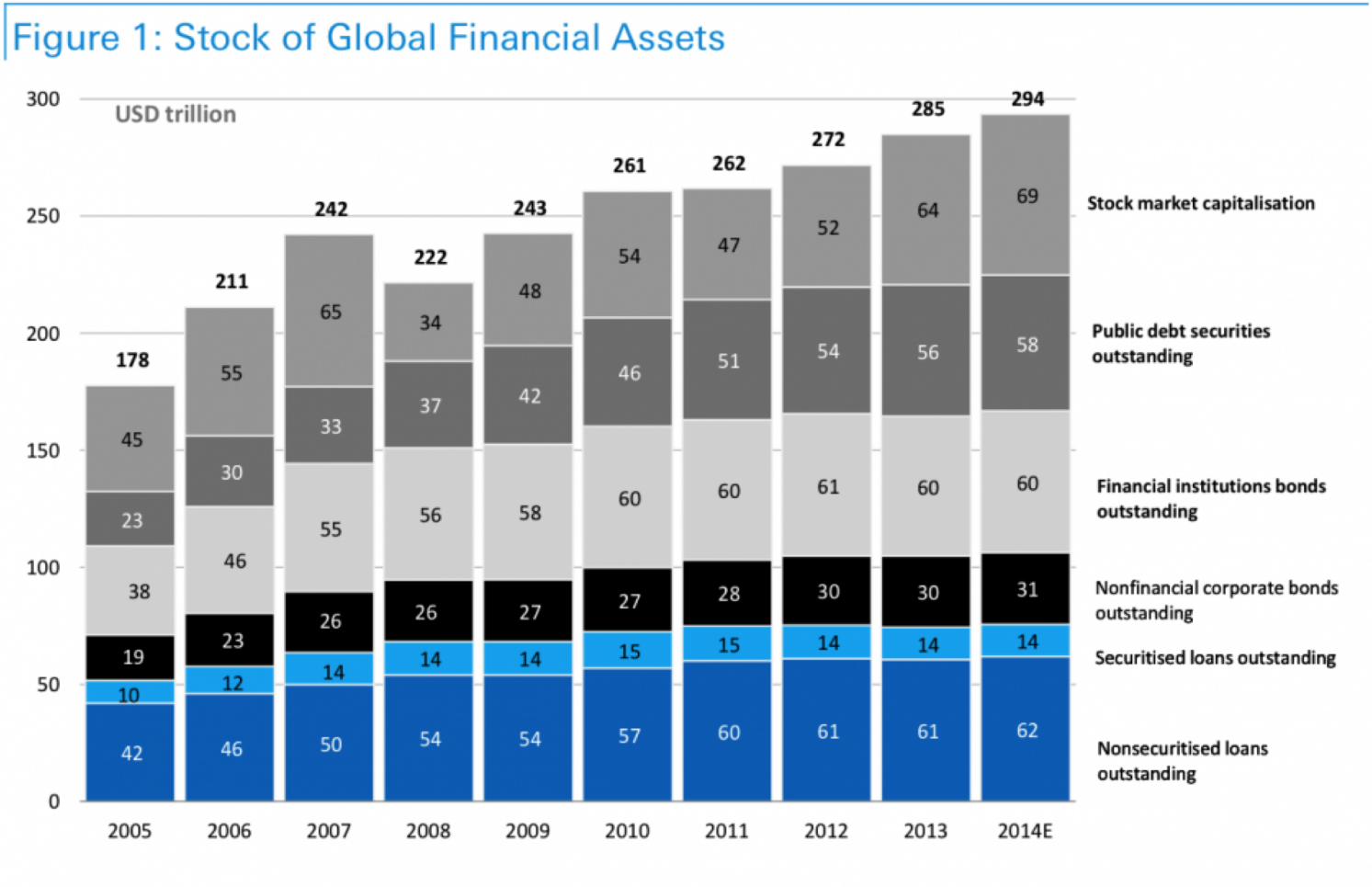
We have more capital than ever before



Source: McKinsey Global Institute, Haver, BIS, Deutsche Bank estimates

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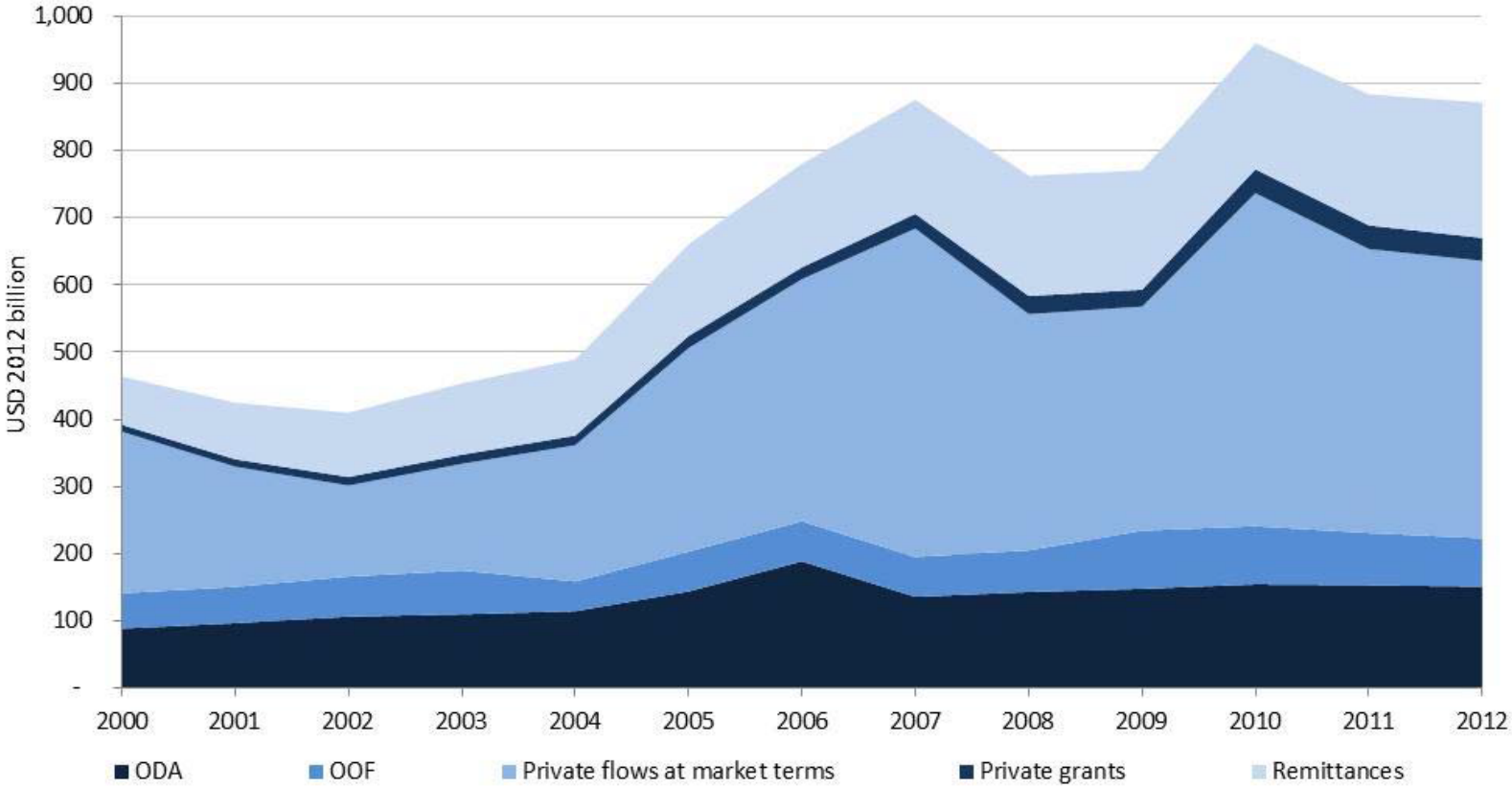
…also in developing countries



Source: World Bank Group, 2012

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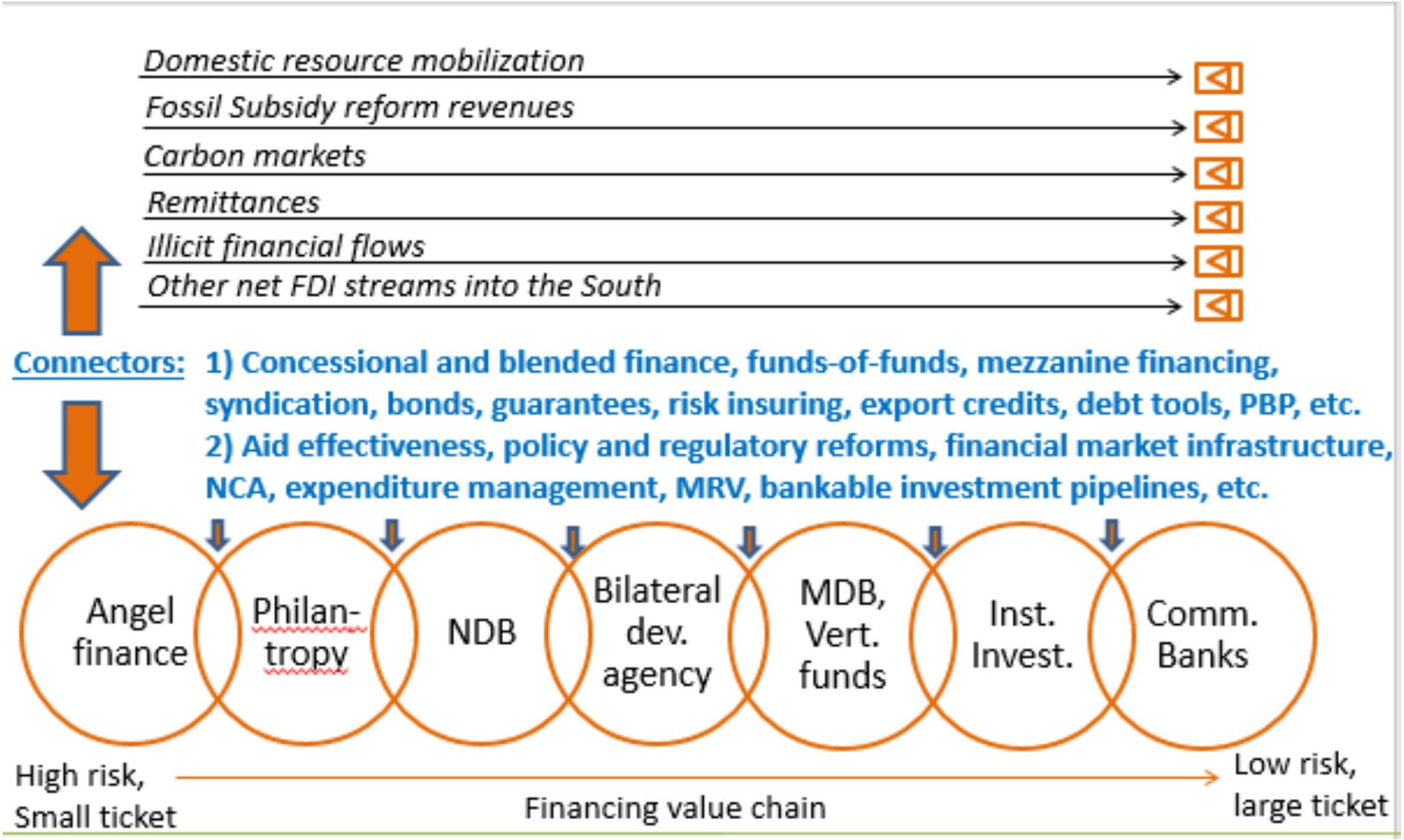
Some of the challenges

- Moving from lab-finance to serious modus operandi: Unlocking the big envelopes
- Alignment with other policy domains / paradigms and integrating delivery of finance and public goods
- Risk aversion among investors / understanding opportunities
- Lack of investment grade project pipelines (competencies)
- Lack of concessional / blended finance
- Enabling returns in adaptation
- Optimizing the climate finance value chain

Understanding role of financial actors



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