China Carbon Forum | 中国碳论坛

An independent platform to foster trust and cooperation among China's stakeholders for climate action

Scaling Up Climate Finance in China: How to unlock private investment?

Executive Summary

China's highly ambitious mitigation efforts require huge amounts of investment. With US 71 trillion globally under management of pension funds, insurance companies, and investment funds, there is much potential for growth in private investment for climate related activities. However, the fundamental political and financial risks are still seen as too high for large scale, low carbon investment. Insurance can play an enabling role in reducing the investment risk often associated with these investments. As climate finance in China is driven by policy, there is a significant policy opportunity to incentivize business to invest in climate based projects, with an emphasis on creating meaningful public private partnerships (PPPs) to reduce investment risk.

Record of Discussion

The following is an edited synthesis of discussion that took place at the event among panelists (around 1 hour) and open Q&A with participants (45mins). As per convention, individual's comments are not attributed.

- China has done a lot in the area of climate change policy, however, there is still a large gap between the policy targets and reality. Currently, it is very difficult to scale up any investment in climate finance. **China's carbon markets, for instance, are too immature to send strong pricing signals.** It is extremely risky for an investor to enter this type of environment. A strong pricing signal allows the investor to accurately calculate carbon costs, and to represent these in financial models.

- **How is the China CDM Fund using money?** Money is **used for both direct and indirect investments.** In 2012, China CDM Fund provided 200 million Yuan in grant money for more than 100 indirect investment projects which helped provinces develop low carbon development plans. In the same year, China CDM Fund provided around 3 billion Yuan in direct investments to support 47 projects on energy conservation, renewable energy and manufacturing. The beneficiaries use CDM money but also use different sources of funding, e.g. commercial banks. **China CDM Fund's 3 billion yuan investment leveraged 16 billion yuan of private investment. The potential for growth, in cooperation with international partners is, therefore, significant.**

- Climate finance can be analysed at three levels – global, national, and provincial. Firstly, at a global level, it is important to understand what climate finance means - **as long as the finance can generate any obvious mitigation and / or adaptation; it can be considered climate finance.** While in theory it is a simple concept, in practice it is complex because of the challenge in tracking the capital flows, and the impact. A lot of the private funding at present is going toward mitigation because adaptation projects are usually economic (i.e. infrastructure projects), rather than revenue generating. Secondly, at the national level in China, the key is to **understand institutions and capital flow** from source to project. China has been investing heavily in climate change, and particularly looking to mitigation – mostly driven by policy, but more must be done. The 13th five year plan is set to be even more ambitious than the current one. Lastly, for the local level in China, the national level must firstly more clearly establish the carbon / climate investment activities in policy, then, we can more effectively drive the local actions. **Climate finance in China is driven by policy.**

- **How can we deal with risky climate related investments from an insurance perspective?** For insurance, climate finance is often viewed as natural catastrophe risk, but investment risk for climate related projects also requires insurance. There are insurance solutions to reducing the investment risk in these projects. Insurance companies can be viewed as investors like any other. **But many low carbon investments are linked to new technology that is not always proven – this creates additional risk for investors. So what insurance and reinsurance can do is bridge that gap** and provide confidence to an investor to invest in this field.

- Climate financing requires cooperation from many different private and public stakeholders, often with divergent interests. At the policy level, there needs to be market signals for the market players to have confidence to work together. In China, **there is a significant policy opportunity to improve incentives for business to invest in climate projects.** This has already been successful at the project level through PPPs. If private investors and enterprises can have early understanding of government policy and incentives then this will provide the setting for early and effective private investment.

- **There is low insurance penetration (level of cover) in China, but the potential insurance loss from a large flood in china is enormous – possibly US35 Billion.** With a low insurance penetration, the **actual economic loss would be much higher** than this. In a climate changed world, many assets will become uninsurable, or at such a price no one is willing to pay. This provides incentive for insurance companies support low carbon projects. Allianz Insurance, for instance, just announced they would provide US 10 Billion in loans for infrastructure and low carbon investments across Europe and Americas. Loans for Asia and China would most likely follow.

- **How is the China CDM Fund positioning itself with regard to its future revenue streams?** The future of the CDM fund should involve more PPPs. Currently, loans are concessional, meaning the interest is lower than commercial rates. China CDM Fund is also looking to develop new instruments in cooperation with the IFC, local governments, and commercial banks to modernize the capital scheme and support more SMEs. We also provided our first active investment to the Shanghai environment and energy exchange. The aim is to provide a strong signal that the Chinese government not only uses policies for market control, but also uses public finance to support these practices. For instance, the China CDM Fund is helping enterprises to disclose the full emissions profiles and reduction potential so that enterprises can benchmark their emissions.

- **Market based instruments are only one tool** and cannot possibly mobilize all the investment required to address climate change. China is looking towards long-term carbon pricing but in the meantime needs international compensation to assist this development. Carbon markets are in China’s long-term policy and political plans, however, the journey won’t be easy and other initiatives will also be needed.