Financing Ambition for Climate in the Time of COVID-19

Summary

Virtual Session, April 29, 2020

The Petersberg Climate Dialogue was launched by Germany ten years ago to bring together ministers and heads-of-state and be a bridge between implementation and negotiation to address the climate crisis. These annual convenings have been critical for driving ambition, in particular to increase financial commitments for climate action. The recently concluded 11th edition was historic – not just because it was convened virtually for the first time, but because the attendees were unequivocal in their acknowledgement that rescuing the world from the Covid crisis was consistent with ensuring that the recovery continued to address the needs of the world to combat the climate crisis.

Much of how a green recovery could and should be effected was discussed at a high-level side session of the Dialogue, "Financing Ambition for Climate in the Time of COVID," organized by Germany[1], the UK COP26 Presidency, and the Climate Policy Initiative who were honored to bring together key decision makers, thought leaders, and experts from the worlds of diplomacy, regulation and policy, as well as public and private finance.

The event came at a critical point to help bridge economic action with the key need for a green, resilient recovery globally. Speakers stressed that we must continue ambitious action on climate change as the world convalesces from the pandemic, particularly as trillions are spent on economic stimulus. And they identified specific strategies to get the (re)allocation of capital right; for public policy to help address the risks so that public finance can harness and co-opt private finance to seize the opportunities to deliver an inclusive, sustainable future; and to measure and communicate transformation as we decarbonize the economy. Three specific themes emerged from the discussions:

Theme 1: A Truly Green, Resilient Recovery

Panelists stressed the need for green, resilient economic stimulus packages, combined with a strategy to enable structural changes. As central banks and finance ministries roll out the much-needed economic stimulus packages, they agreed that the

[1] Through the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety.

macroeconomic impetus should lead to building resilience against future systemic shocks to society and the financial markets, particularly those likely to be triggered by the climate crisis – from stranded assets to massive uninsured losses.

Initial estimates indicate that USD 10-20 trillion will likely be invested during the next six to eighteen months to stimulate economies in the wake of the coronavirus crisis, and Jochen Flasbarth, State Secretary at the German Federal Ministry for the Environment, Nature Conservation and Nuclear Safety emphasized that "we are really at an essential point of time where we can choose the way forward or the way backward." He pointed to the emerging question how to gain fiscal space for developing countries and to address the question of debt relief.

Lord Callanan, Parliamentary Under Secretary of State at UK's Department for Business, Energy and Industrial Strategy, emphasized that while leaders are rightly prioritizing the COVID-19 threat, "climate risks are escalating … the steps we take now to stabilize and rebuild our economies will have a profound consequence on our future well-being". He committed the UK Presidency's intention to champion support for those who need it whilst accelerating a shift in global financial flows to a low emission, resilient future.

This theme of using the current stimulus to crisis-proof the world for future challenges was the headline for all speakers. Kristalina Georgieva, Managing Director of the International Monetary Fund, noted: "In the minds of some, the health crisis and the 'great lockdown' needed to address it mean that we can push the pause button in the fight against the other existential crisis we face—our changing climate. Nothing is further from the truth. We are about to deploy a massive fiscal stimulus which can help us address both crises at the same time." She called for utilizing all available levers to enable a green recovery, and highlighted the importance of using public finance wisely, to promote green private finance, to introduce carbon pricing and secure long-term commitments to lower carbon alternatives.

Frank Elderson, Executive Board Member, De Nederlandsche Bank N.V. [2] and Chair, Network for Greening of the Financial System pointed out the need to tie public investment closely to climate and SDG goals, emphasizing that state aid measures to industries, like aviation, should be made conditional on moving toward a more sustainable future to avoid a historic error; citing what Ms. Georgieva also said, the aid provided to the

[2] The Dutch Central Bank.

US auto industry in the wake of the great financial crisis of 2008 that required accelerated efficiency improvements.

Pekka Mor□, Senior Ministerial Adviser and Special Representative of the Finnish Finance Minister to the international Coalition of Finance Ministers for Climate Action, stressed the role finance ministers can have, and the importance of strategic partnerships and a cross-sectorial approach; amongst others, by influencing climate-related priorities in MDBs and enforcing regulations and rules related to transparency.

Several panelists including those from the private sector stressed the need to implement much higher levels of carbon pricing and use the opportunity of historically low oil prices to eliminate fossil fuel subsidies. As Ms. Georgieva stressed, "When governments provide financial lifelines to carbon-intensive companies, they should mandate commitments to reduce carbon emissions. […] With oil prices at record-low levels, now is the time to phase out harmful subsidies."

Additional work is needed to understand more granularly how to ensure that recovery packages are green, how to get the proper scale of investments for the packages, and how to accompany them with proper enabling policies.

Theme 2: An Enhanced Role for Development Finance

Development finance is key to both amplifying and deploying the investments needed for a green recovery in developing countries, and as Minister Nigel Clarke of Jamaica said, ensuring that climate finance is accessible and fit for purpose is fundamental, particularly for the more vulnerable countries. Speakers noted that development banks and international finance institutions can help build strategy and support policy development; deploy a wider range of instruments to manage, share, and reduce risk; convene relevant stakeholders and decision makers across the public and private sectors; and through these activities greatly enhance what the private sector can do.

Lord Nicholas Stern, Chair of the Grantham Research Institute on Climate Change and the Environment at the London School of Economics and Political Science, and adviser to the UK COP26 Presidency noted the need to expand the ability of multilateral development banks and international financial institutions, saying "it is by far the cheapest and least risky way of enhancing low-cost finance." Given the dimension of the upcoming global recession, he explicitly warned against the temptation of backtracking on green programs and environmental regulations, which would undercut sustainable, inclusive growth.

Patrick Dlamini, CEO, Development Bank of Southern Africa highlighted the impact of Covid on economic development pathways in Africa and the need for a just transition with responsible financing. He captured the need for strong leadership from public institutions and strong relationships throughout the international community when he said: "I really strongly count on networks of development banks and DFIs, foresighted governments, and institutions like the Green Climate Fund for us to forge ahead and build to the future of sustainable development goals where we can say we are leaving no one behind."

Building on that, Alzbeta Klein, Director and Global Head of Climate Business, International Finance Corporation, recommended a focus on investing in sectors with strong labor benefits – both that can preserve jobs, but also those that can add the much-needed millions of jobs. She noted that much of this could be achieved by designing lending policies and regulatory frameworks that are tilted to green.

Yannick Glemarec, Executive Director, Green Climate Fund underscored the role of job creation from shovel-ready green projects like energy-efficient buildings and renewable energy storage that could catalyze massive private investments, as well as the benefits of water and sanitation, and agriculture projects that preserve livelihoods and address environmental challenges. He did warn that most of these investments were unlikely to see the light of the day as they face a range of financial and policy barriers, requiring urgent policy interventions to make them bankable.

A deeper conversation is needed on how to mobilize development finance, and how to ensure that the crisis toolbox of instruments and the ability of such institutions to take higher levels of risk is in fact sticky so that development and climate action go hand in hand.

Theme 3: The Coming Shift in the Financial System

The COVID-19 crisis is a wake-up call for our social and financial systems to be better prepared for the climate crisis that will be bigger in every way and stay with us over a much longer period of time. To achieve this, all financial institutions need to ultimately align their portfolios with a better future – strong, inclusive, sustainable, and resilient. Panelists across the public, development, and private finance spectrum were in agreement about the need to shift the entire financial system to better respond to and help reduce and manage both physical and transition risks triggered by climate change, as well as to standardize related disclosures.

Mark Carney, United Nations Special Envoy for Climate Action and Finance, UK Prime Minister's Finance Adviser for COP26, and former Governor, Bank of England, pointed out that the economics of the post-COVID world will be fundamentally changed, saying "we are experiencing decades of change within weeks," and that the resulting reallocation of capital will require difficult debt restructuring that nonetheless presents some opportunities for improving the sustainability of the financial system. He highlighted that his work in relation to COP26 would seek to ensure that climate is taken into account in every financial decision. He noted that at the heart of this this work is reporting on climate risk and moving towards standardized, mandatory disclosure; improved risk management; and increasing returns in the transition to net zero. Reporting rules and climate risk management have to become mandatory.

Brian Deese, Global Head of Sustainable Investing at Blackrock, pointed to the fact that more than 80% of sustainability-linked indices had outperformed their benchmarks during the Covid crisis as evidence that managing ESG risks including climate was financially smart to do. Investors and managers will be looking to companies to deliver on this and deploying better tools to measure and analyze it. He asked for analytical tools for companies to be able to assess alignment of their businesses with the goals of the Paris Agreement.

Günther Thallinger, Member of the Board of Management of Allianz Investment Management and member of Net-Zero Asset Owner Alliance, said that the upcoming recovery is just the starting point for investors to get onto the pathway for sustainability. ESG standards are fine but have to include the requirement of reaching net-zero. Also state-owned assets have to be managed towards a net-zero impact. And while this will require companies and markets to actively transform, the time is right given the need to re-assess investor portfolios anyway.

Both representatives of the broader private finance community strongly endorsed active policy support to ensure that investments were climate smart, whether they focused on actively avoiding stranded assets or facilitated job creation by upgrading energy efficiency for the commercial built environment that currently stands vacant.

Conclusion

Throughout the discussions, it became crystal clear that there are three cross-cutting prerequisites to financing climate ambition in the time of COVID-19, in keeping with the themes discussed:

- First, to focus on concrete policies and solutions that enable investments for a green recovery. Critical for this is the mainstreaming of climate change across the financial system, with Mark Carney's framework of risk management, recovery, and return providing a clear framework for doing so.
- Second, the need to better bridge between the various conversations and initiatives, improve collaboration to address risks, and seize opportunities. It will require a better way to stress-test economic stimulus packages to ensure they don't create or sustain assets that the climate crisis will strand; measure and communicate progress across the economy in relation to the decarbonization we need to see in all sectors of the real economy; and to ensure that the transformation happens at the scale and speed needed for a better world.
- Third, that cooperation - in particular between the public and private sectors - would be critical for maximizing the positive impact of the recovery on mitigating the climate crisis and building resilience. It will be important to overcome siloed thinking and ensure that the range of complex tools needed, particularly in developing and emerging countries where financing needs are greatest, are used together to be as efficient and effective as possible. This point was further stressed by Tosca Barucco, Special Envoy for COP26, Ministry for Foreign Affairs, Italy and other panelists.

We have a window to rebuild our world for a more inclusive, more resilient, more sustainable future. An opportunity to act responsibly and mainstream climate change considerations into the entire finance ecosystem, targeting both short-term economic recovery and long-term structural changes aligned with sustainable, inclusive growth and strengthening society's resilience. Not doing so would pose a significant threat to a sustainable recovery and risk propagating future systemic shocks brought about by the impacts of the climate crisis.

This event demonstrated that finance is the cornerstone for making this happen, providing some indications on the how. Now it's time to translate the guiding messages into a concrete set of actions.