Background Paper

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The Role of Sub-state and Non-state Actors in International Climate Processes: Financial Institutions

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Summary

- The trillions of dollars needed to secure the sustainable, climate-compatible pathway outlined in the 2015 Paris Agreement have focused attention on private finance and investment, and on the role of the financial sector as a potentially powerful non-state actor in the international climate debate.

- Leading individual financial institutions reacted to the Paris Agreement by framing it in terms of what it would mean for markets – i.e. risks and opportunities – and by underlining the importance of national implementation of climate change commitments.

- Key recent developments signal that the financial sector actively supports Paris-compatible government action on climate change, as well as company-level action to understand the physical and 'transition' risks and opportunities associated with climate change and policy responses. Financial sector engagement is taking place through well-organized and well-supported international initiatives and platforms. A critical part of this process entails robust activity by financial institutions to embed climate change and broader sustainability factors into strategies and operations.

- At country level, attention to implementation of Nationally Determined Contributions (NDCs) and associated sector-level policy development has been largely separate from the broader 'sustainable finance' dynamic. National-level action has not benefited from the same level of organized financial sector involvement evident in international action. One of the reasons for this is that, with some notable exceptions, international financial initiatives lack the capacity and resources to participate in the granular detail of national policy processes. Policymakers in turn often lack the internal capacity to consult or engage with the financial sector domestically.

- This paper includes some thoughts on further international and national climate actions. Ensuring that messages from successful international financial sector initiatives are heard in regional and non-climate forums offers one avenue for building a stronger foundation for greater climate ambition. Building the resource base for stronger national climate policy engagement, as a counter-voice to incumbent interests and to ensure that the quality of policy is 'investment grade', is another. This will be critical to the delivery of policy outcomes. Other key elements include the need to pool knowledge across relevant parts of the finance sector, build alliances, and shift action towards joint problem-solving with policymakers. A 'Talanoa 2.020'-type initiative offers one potentially promising approach to advancing dialogue in this respect.

Introduction

The investment – estimated in the trillions of dollars – required to secure a sustainable, climate-compatible pathway has focused attention on private finance and investment since the 2015 Paris Agreement.

This background paper examines the financial sector as a potentially powerful non-state actor at the international levels of the climate debate. It opens with a brief history of the sector's engagement around the United Nations Framework Convention on Climate Change (UNFCCC), illustrating some of the differences in approach between financial institutions and the broader business and industry lobbies. It examines the substantial evolution in strategies that occurred in the lead-up to the 21st Conference of the Parties (COP 21) and Paris Agreement in late 2015. The paper reviews the elements that made financial sector engagement particularly effective in respect of COP 21. It also identifies gaps in current financial sector engagement and strategy, as the world responds to the Intergovernmental Panel on Climate Change (IPCC) special report on *Global Warming of 1.5°C*.[1] A concluding section offers observations on approaches the financial sector could pursue in the lead-up to 2020, when there will be both an expectation and a pressing need to deliver high-ambition national climate plans.

The need to generate stronger international momentum for increased climate ambition and action in the short term is the main starting point of this paper. However, the development of strategies focused on national and subnational implementation will also be critical to the successful delivery of climate solutions (both in terms of mitigation and resilience), and to the effective mobilization of capital on the scale illustrated in technical models.

The primary inputs to this paper consisted of two workshops, held under the Chatham House Rule, and a number of interviews with leading actors from international finance and investment initiatives, as well as the direct experience of the author. The paper has an inevitable bias towards English-speaking, and London-based, perspectives. Still, as the actors concerned are participating in international networks and working directly with investors, this approach offers a practical (albeit not comprehensive) means of anchoring preliminary observations.

As a final preliminary note, it is important to state that finance is a topic of central political importance for securing outcomes in the UNFCCC negotiation process. It is not, however, within the scope of this paper to examine finance-specific parts of the UNFCCC agreements.

The financial services sector as a non-state actor or observer

The financial services sector's engagement with the UNFCCC process has been historically distinct from that of the corporate sector (i.e. business and industry), as outlined below.

[1] Intergovernmental Panel on Climate Change (IPCC) (2018), 'Global Warming of 1.5 °C', http://www.ipcc.ch/report/sr15/ (accessed 20 Nov. 2018).

Pre-Kyoto: insurance sector

The impact of climate change on the insurance and reinsurance sector was one of the early drivers of engagement between financial institutions and the international climate process in the first half of the 1990s. Major insurers and reinsurers, such as MunichRe, SwissRe, and Tokio Marine & Nichido Fire Insurance Company, were already beginning to make the link between climate change and rising losses from 'catastrophe' weather events such as windstorms. An influential report in 1993 – the year after Hurricane Andrew, which caused $16.5 billion worth of insured losses – set out the then landscape of climate science, weather-related risk, losses and insurance, and the role of the financial sector in the climate change debate.[2] This report provided an important stimulus for the early participation of a small number of representatives from both the insurance industry and the wider financial services sector at the UNFCCC negotiations.

Having coordinated a banking sector voice for the Rio Earth Summit in 1992, the United Nations Environment Programme (UNEP) spearheaded the development of a statement by the insurance industry on climate change in 1995, for the UNFCCC's first Conference of the Parties (COP 1) in Berlin. The UNEP Insurance Industry Initiative (III)[3] became a primary vehicle for insurer engagement with the UNFCCC process (as well as for wider financial sector engagement with it),[4] and later evolved into the UNEP Finance Initiative (UNEP FI). This direct link to UNEP gave the III and its successor, UNEP FI, 'intergovernmental organization' status at the negotiations, meaning that the financial industry was one step removed from the lobbying ranks of observers.[5] In the 1990s and early 2000s, there was little cross-fertilization between them.

Few individual financial institutions were otherwise involved with mainstream observer business organizations, as the aims of the latter tended to be oriented around short-term interests linked to corporate emissions. A split in the business lobby, however, occurred in the mid-1990s, with the emergence of a 'progressive' cohort in favour of binding climate action (led by organizations such as the Business Council for Sustainable Energy, in the US; and e5, a European equivalent). However, at that time only isolated financial institutions were involved.

Some environmental NGO observers articulated the idea that the insurance industry would be a counterforce to the fossil fuel lobby.[6] In reality, this was more of a hope at that point, notwithstanding the important messages that the UNEP initiative conveyed. Nevertheless, the early involvement of the insurance industry in the UNFCCC process laid important groundwork for the development of financial institutions as non-state actors in the climate debate today.

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[2] Leggett, J. (1993), *Climate Change and the Insurance Industry: Solidarity among the Risk Community?*, Amsterdam: Greenpeace International, https://solar-aid.org/wp-content/uploads/2018/02/leggett-insurance-climate.pdf (accessed 5 Nov. 2018).
[3] In 2003, the UNEP Insurance Industry Initiative (III) merged with the UNEP Financial Institutions Initiative (FII) to form the UNEP Finance Initiative (UNEP FI). United Nations Environment Programme (UNEP) (2018), 'History of Statement', http://www.unepfi.org/about/unep-fi-statement/history-of-the-statement/ (accessed 5 Nov. 2018).
[4] UNEP III held an awareness-raising conference in Tokyo to build engagement and share analysis between leading European and Japanese actors in the insurance sector; there was also a side-event at the COP 3 negotiations.
[5] All companies or organizations attend via UN-accredited NGOs, which have 'observer' status, whether from business and industry NGOs (so-called 'BINGOs'), environmental NGOs, unions or other categories.
[6] For example, Leggett (1993), *Climate Change and the Insurance Industry*.

From Kyoto to Copenhagen

A defining feature of the period following the 1997 Kyoto Protocol was the development of emissions trading through the protocol's flexibility mechanisms, which involved commodities desks within financial institutions. This prompted the rise of instrument-specific lobbying groups (e.g. the International Emissions Trading Association) and, coupled with the start of the EU Emissions Trading Scheme, resulted in the creation of 'compliance-linked' markets. These developments arguably kick-started a more serious consideration of climate change within financial institutions – albeit not in a fundamental sense of giving the industry a vested interest in overarching climate policy (in terms of individual financial companies being winners or losers). Rather, action on climate change was seen as another new market that needed to be understood or shaped.

In addition to UNEP FI on the intergovernmental side, organizations such as the Institutional Investor Group on Climate Change (IIGCC) emerged in the early 2000s. In the middle of that decade, pioneering specialist firms started operating. These included players such as Climate Change Capital, which – critically – had climate-dedicated policy capacity and could follow the detail of the UNFCCC process with an investment interest in broader climate solutions than emissions trading. The rise of these politically savvy, even if small, financial companies brought a financier-framed, risk-based view of climate change and climate policy to the negotiations – with the potential for this to influence investment decisions and capital flows for the first time. This shift also aligned with emerging external trends, such as the rise in mainstream investor interest in renewable energy. (New Energy Finance, later bought by Bloomberg, was founded during this 2004–05 period.)

At the UNFCCC negotiations, this era was characterized by formal statements from all observer organizations to the negotiating plenary, outlining priorities (including two statements from the business lobby, reflecting its differing interests); and by specialized briefings (direct and written), dinners and meetings with lead negotiators, as well as side-events. The IIGCC had its first dinner with the UNFCCC executive secretary, Yvo de Boer, in 2008.[7]

UNEP FI produced short 'CEO briefings' on climate-related topics, which sought to communicate market developments, key issues and the climate change-related perspectives of financial institutions to negotiators. However, these documents were somewhat removed from the 'daily grind' of detailed text. An inevitable 'language gap' arose as UNEP FI sought to communicate in a way that was relevant to both businesses and governments. While this worked at a general level, it meant that the sharper focus needed for the negotiations at that time was lost, which was not helped by the fact that negotiators increasingly became too busy to attend side-events or do additional reading.

[7] In the history of the UNFCCC negotiations it is useful to note that Yvo de Boer, as executive secretary, was at the helm of the first comprehensive assessment of 'Investment and Financial Flows to Address Climate Change' in October 2007. This was mandated by parties at COP 12 in December 2006. The full report is available at unfccc.int/resource/docs/publications/financial_flows.pdf. In his introduction, de Boer described the intent: 'In recognition of the relevance and importance of the financing and investment dimension, the Parties to the United Nations Framework Convention on Climate Change (UNFCCC), requested the Secretariat to analyse and assess investment flows that will be necessary to address climate change mitigation and adaptation in an effective and meaningful way, with a special focus on developing countries' needs.'

In the lead-up to COP 15 in Copenhagen in 2009, there was a determined effort to build on alliances between the progressive business lobby and the financial sector. The former had grown during the 2000s and brought in some major companies, reflecting the investment maturity of the renewable-energy, efficiency-related and low-carbon technology sectors. The companies involved included, among others, Johnson Controls, Enel, Vestas, EnerNOC, RES and some of the big UK utilities. The financial sector had also matured, with larger institutions and banks – for example HSBC,[8] APG Asset Management[9] and Deutsche Bank – taking a more active public role in the climate debate.

However, the full potential for financial institutions to impact the UNFCCC process was not achieved, due in large part to the relative lack of resources and capacity for following the twists and turns of policy and politics at different tiers of the debate (important for working out sharper inputs into the process with a view to shaping outcomes). Financial sector organizations also suffered, in particular, from a lack of capacity for working more consistently at national level and in a politically relevant way (also important for international policy, as governments developed their negotiating mandates at home). Notwithstanding the above, this period saw steadily growing leadership and the organization of an impressive number of financial institutions (with large aggregate volumes of capital under management) to back statements in support of climate action from governments.

It is important to note that the scale of financing needed to tackle climate change was already on the agenda of international negotiators by COP 15. The summit itself produced the Copenhagen Accord, which called for developed countries collectively to mobilize $100 billion annually by 2020 for developing countries, with the funds to be raised from both public and private sources. Agreement on establishing the Green Climate Fund (GCF) followed a year later at COP 16 in Cancún, with a subsequent consultation process that actively sought input from the private finance sector. The sector has remained active in the GCF in both advisory and operational roles.[10]

Post-Copenhagen and the lead-up to Paris

Political engagement by the financial services sector fundamentally changed in the lead-up to and during the Paris negotiations. Those involved have highlighted the 18- to 24-month programme of initiatives set up by the UNFCCC secretariat and the Peruvian and French COP presidencies, in collaboration with other entities, to involve non-state actors. A key part of this process was enabling financial institutions to play to their strengths rather than having to become climate negotiation

[8] HSBC's Climate Change Centre of Excellence started in 2007.
[9] The Earth Negotiations Bulletin (ENB) reported on a COP 15 side-event in Copenhagen at which HSBC, APG Asset Management and Climate Change Capital, alongside UNEP, discussed challenges and opportunities. See IISD Reporting Services (2009), 'ENB on the Side - A Special Report on Selected Side Events at the Fifteenth Conference of the Parties to the UN Framework Convention on Climate Change (UNFCCC) and Fifth Meeting of the Parties to the Kyoto Protocol (COP 15 and COP/MOP 5)', http://enb.iisd.org/climate/cop15/enbots/11dece.html (accessed 5 Nov. 2018).
[10] For useful overview briefings with access to source documents and other references, see London School of Economics and Political Science (2018), 'What is Climate Finance?', http://www.lse.ac.uk/GranthamInstitute/faqs/what-is-climate-finance-and-where-will-it-come-from/ (accessed 5 Nov. 2018); and Climate Focus (2018), 'COP21 Paris 2015 – Loss and Damage in the Paris Agreement and the Green Climate Fund and the Paris Agreement', https://climatefocus.com/news/cop21-paris-2015-loss-and-damage-paris-agreement-and-green-climate-fund-and-paris-agreement (accessed 5 Nov. 2018).

experts. Non-state actors were thus 'beaten into a more influential shape',[11] so to speak, by this new style of engagement, and the right platforms created to maximize their contribution.

Bigger themes were also starting to emerge on the ground that would increasingly have a galvanizing impact on the wider climate debate. One important development was the emergence of so-called 'green' or climate bonds – in which mainstream debt instruments are used to raise money for investment in low-carbon/climate solutions. The resonance of this approach went beyond the specific focus on bonds, with lead organizations in the area described as 'unbelievably influential in unleashing an idea'.[12] At the same time, on the fossil fuel side, there was a growing emphasis on the threat posed by 'stranded assets', on the need for divestment from high-carbon companies, and on the implications of climate change for valuations of those companies.

While these trends were not about climate politics *per se*, they provided an idea that policymakers could readily grasp. Through the actions of finance professionals, the sector showed that it was starting to take climate change seriously. For policymakers, this reinforced the narrative both that meeting climate goals was possible and that a 'business as usual' course of action presented risks for financial institutions. The narrative was augmented by the ever-strengthening track record of climate solutions, such as those around renewable energy. It was supported by the in-depth work of investor organizations to help financial institutions understand climate change and structure their internal responses to it.

Some particular features of this period:

- Specific high-level intergovernmental meetings gave investors a stronger voice, allowing financial actors to gain greater prominence in the lead-up to Paris. The Global Investor Statement on Climate Change, presented at the UN secretary-general's Climate Summit in September 2014, provided important momentum and was described by the IIGCC as 'a landmark event that brought down barriers between government and the private sector'.[13]
- National and regional efforts to shape the climate policy positions of key negotiating blocks (albeit still largely OECD countries at the time) gained traction. In Europe, a 'Green Growth' group of ministers provided another platform for engagement. It was noted in one interview that input (when it occurred) from reinsurers and financial institutions into specific ministerial forums was influential.
- In and around the Paris process itself, official infrastructure and parallel forums provided a much greater public platform and opportunities to give prominence to investor-themed actions. This enabled the CEOs of financial institutions to participate in the process and interact with top-level counterparts on the policy side, without themselves having to be experts in the machinations of the negotiations (indeed, several forums in Paris were hosted by financial sector firms).

[11] Financial institutions and corporations project consultation workshop, held on 21 September 2018 under the Chatham House Rule.
[12] Ibid.
[13] Institutional Investor Group on Climate Change (IIGCC) (2015), *How the investor voice shaped COP21 into the post-Paris climate era*, http://www.iigcc.org/files/publication-files/IIGCC_Post-Paris_COP21_report_final.pdf (accessed 5 Nov. 2018).

This bolstered the perception that there was an upside for financial institutions in engaging on climate change, in terms of providing a more public and high-level platform for demonstrating leadership. After Paris, there was a sense that there had been a discernible 'tectonic' shift for the financial sector on climate change – and that the growing momentum around the issue and increased internal attention to climate change within financial institutions were not going to be reversed. Notwithstanding recognition that much remained to be done to render climate change and its consequences a mainstream issue for the financial sector, a leading group of financial institutions had become visible in the international climate debate.

The Carney/Bloomberg route to market

The impact and influence of Mark Carney, the governor of the Bank of England and chair of the Financial Stability Board, together with Michael Bloomberg, the former mayor of New York, in launching the Task Force on Climate-related Financial Disclosures (TCFD) in Paris have been highlighted by financial sector organizations. The impetus for the creation of the TCFD included a ground-breaking speech by Carney, two months before the Paris conference, which redefined financial stability in the context of climate change.[14] At COP 21 itself, other leading events – including a 'mayors' summit' (the Global Summit for Local Leaders) and an official Paris Finance Summit – created a direct 'line in' enabling Carney and Bloomberg (at the time also the UN Special Envoy for Cities) to bring financial sector arguments to the top tier of leaders at the negotiations. This provided powerful additional visibility for the financial sector, giving investors access to government in a way that they could not necessarily have secured by themselves. Dialogue was aided by the presence, in effect, of independent interlocutors trusted by both sides.

In summary, a fundamental shift took place – from Copenhagen-era demands on government to an approach that was much more 'we are with you' and 'here's what we are doing as well'. Multiple finance-orientated initiatives were launched,[15] along with reports, analyses and individual action pledges from financial institutions. This provided a strong *ongoing* agenda, in many cases backed by CEOs, which contrasted with the idea of Paris being a culmination of activities to influence government decisions.

In that sense, non-state actor involvement around Paris was very successful as a tool of communication and mobilization. It created the right 'atmospherics' for governments to reach the framework agreement, and included some key elements for investors seeking to understand its consequences. In particular, the Paris Agreement's global temperature ceiling and trajectory[16] will determine carbon budgets and national plans, both of which have investment implications in terms of the volumes of fossil fuels that can be burned and how national policies might evolve at sector level to deliver decarbonization. In addition, the 'ratchet' mechanism for Nationally Determined Contributions (NDCs) means that these pledges can only be amended upwards against a timetable

[14] Bank of England (2015), 'Breaking the tragedy of the horizon – climate change and financial stability – speech by Mark Carney', 29 September 2015, https://www.bankofengland.co.uk/speech/2015/breaking-the-tragedy-of-the-horizon-climate-change-and-financial-stability (accessed 5 Nov. 2018).
[15] Hamilton, K. (2015), 'Paris Climate Briefing for Investors', https://www.slideshare.net/slideshow/embed_code/key/KLUc7uXudrQcjN (accessed 5 Nov. 2018). This includes an outline of the various initiatives launched and the reaction from financial institutions to the Paris Agreement.
[16] Consisting of a long-term goal of keeping the global temperature rise to 'well below' 2°C, and of 'pursuing efforts' to limit the increase to 1.5°C.

set out in the agreement. This provides some level of visibility to investors on the direction of policy, even if not on the detail.

Post-Paris: What happened next and outlook to 2020

The immediate reaction of leading financial institutions to the Paris Agreement gave a good indication of the important factors for the agenda ahead from an investment perspective. This included framing the agreement's significance for markets in terms of risks and opportunities,[17] and underlining the importance of national implementation (see Box 1).

Financial institutions could not ignore the launch of the TCFD, given its Carney/Bloomberg pedigree, the presence of financial sector participants on the task force, and the consequences of its disclosure agenda. This, alongside the 'ratchet' mechanism within the Paris Agreement, created a sense that financial institutions could not risk betting that actions consistent with the temperature ceilings in the Paris Agreement were *not* going to happen. This point is key to understanding the importance of implementation to the strength of the Paris Agreement: financial institutions still had to see how markets were going to develop (via climate policy), as they had to meet standard internal risk criteria for investments when deciding where to deploy capital.

Box 1: Selected financial sector reactions to the Paris Agreement

BAML (Bank of America Merrill Lynch)

'The global market for low carbon goods and services is already worth $5.5 trillion a year and this deal **will turbo charge the amount of capital chasing new low carbon investment** opportunities.'[18]

Barclays

'… we think that the wording that all parties have in the end signed up to represents a very significant breakthrough in the history of international climate negotiations. Most crucially of all, in our view, **the provision for a ratcheting-up mechanism** means that the possibility of a 2°C trajectory is kept alive.'

'[A] 2°C world would put $33.1trn of revenues at risk to 2040 for the fossil-fuel industry, of which $21.2trn for the oil industry, $6.1trn for the gas industry, and $5.8trn for the coal industry.'[19]

Goldman Sachs

'In its post-Paris Investment Research report, GS agrees with other FIs that **regulation will remain "country-by-country and sector-by-sector" and will continue to be fragmented**. It described key markets – China, EU and select US states –as "regulatory pressure points" with "disproportionate global influence".'[20] On the Paris Agreement itself, in addition to the 'ratchet' mechanism for increasing national actions, Goldman Sachs positively highlighted the 'relatively comprehensive' measurement and reporting framework.

Emphasis added. More reaction is outlined in Hamilton (2015), 'Paris Climate Briefing for Investors' (accessed 20 Nov. 2018).

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[17] Hamilton (2015), 'Paris Climate Briefing for Investors'. This includes an outline of the various initiatives launched and the reaction from financial institutions to the Paris Agreement.
[18] Stothard, M. and Stacey, K. (2015), 'COP21: Big polluters see no short-term change', *Financial Times*, 13 December 2015, https://www.ft.com/content/441249f2-a19e-11e5-8d70-42b68cfae6e4 (accessed 20 Nov. 2018).
[19] Wilkins, M. (2016), *The Paris Agreement: A New Dawn For Tackling Climate Change, Or More Of The Same?*, London: Standard & Poor's, https://www.ipfa.org/wp-content/uploads/2016/01/View-the-full-report.pdf (accessed 20 Nov. 2018).
[20] Kooroshy, J. (2015), *The Low Carbon Economy, Key Takeaways from the Paris Agreement*, London: Goldman Sachs, https://www.goldmansachs.com/insights/pages/new-energy-landscape-folder/report-the-low-carbon-economy/paris-agreement-takeaways.pdf (accessed 20 Nov. 2018).

Galvanizing themes

Some argue that the success of Paris rested on pushing for an achievable goal – an opt-in approach for national sign-up through national climate plans. However, the fact that the latter are not firmly secured means that attention and pressure on securing strong national implementation will be critical to success, not least for creating investment opportunities at the scale implied by the Paris Agreement's overarching goals.

There has been positive change: the big-picture narratives around climate risk disclosure and the TCFD; and the positive growth story of 'green' bonds and broader sustainable finance initiatives being picked up by policymakers, such as through the G20 (under Chinese and UK leadership) and the EU. These all reinforce the message that the financial sector is committed to actively advancing the climate and broader sustainability agenda, but that it is also looking for government leadership.

Some further detail:

- The 18-month TCFD agenda created a platform for climate change disclosure, with an industry-determined set of influential recommendations for voluntary uptake by companies and financial institutions. This has been influential in mainstreaming climate change as an issue within the financial sector. The TCFD recommendations created a strong adoption and implementation agenda, around which various actions have been taken and subsequent update reports have been produced.

- The growth of the 'green' and climate bond markets (both in terms of issuance and buyer appetite), as referred to above, has enabled initiative leaders to position these market developments as advancing an agenda aligned with the interests of national treasuries responsible for sovereign capital raising. Specific schemes such as the Climate Bonds Initiative have engaged with a broader range of middle-income developing countries at senior government treasury level, often alongside the multilateral development banks (MDBs) that have led much of the first phase of activity in this area.

- Public–private crossover initiatives have been influential. The G20 Green Finance Study Group (established under the Chinese presidency of the G20, co-chaired with the UK, and subsequently renamed the Sustainable Finance Study Group) and the two-year 'UNEP Inquiry into a Sustainable Financial System' created an effective bridge between the Paris work by financial sector organizations and the post-Paris governmental agenda. This has helped to expand government engagement beyond environmental ministries and emissions reduction policy into the area of financial regulation.

These examples illustrate the powerful, well-marketed themes that resonate among senior-level political, policy and 'green' finance leaders. Indeed 'green'/sustainable finance is variously described as the new soft power, and as the compelling new post-Paris idea that is creating dynamism between finance and politics.

Set-piece occasions – illustrating momentum and progress

Other prominent events and processes show that mobilization has moved beyond the UNFCCC framework, supporting other international initiatives that in turn assist developments at the national level.

The Global Climate Action Summit (GCAS) in 2018, spearheaded by Jerry Brown, the governor of California, provided a high-profile opportunity for informal engagement between the top tier of government and financial institutions. It also created a key platform around which to organize coalition-building and CEO-level announcements.

Other initiatives of note have included the 2018 Investor Agenda (involving 400 institutions, with $32 trillion in assets under management); and Climate Action 100+ (bringing private financial institutions and corporates together). These have illustrated an ability (and the hard work needed) to align organizations and interests with different characteristics and histories, including the UN Principles for Responsible Investment (PRI), UNEP FI, CDP (formerly the Carbon Disclosure Project) and the Global Investor Coalition.

The influence of such 'top-down' mobilization, both on the 'green' investment side and the stranded asset/high-carbon investment side, is indisputable. It has spurred several government initiatives: not only under the G20, as mentioned above, but also the EU's High-Level Expert Group on Sustainable Finance (HLEG) and a subsequent Action Plan;[21] France's Finance for Tomorrow initiative;[22] the UK's Green Finance Initiative and 2017/2018 Green Finance Taskforce;[23] and the Brazil Green Finance Initiative.[24] At central bank level, there is also the Central Banks and Supervisors Network for Greening the Financial System, chaired by Frank Elderson from the Dutch central bank's governing board, which brings together a range of developed- and developing-country institutions.

Box 2: Factors coming into alignment that have stimulated investment in climate solutions

Prevailing market, industry and technological conditions have reinforced international initiatives for realizing the Paris goals, leading some observers to claim that an economic tipping point has been reached. These conditions include:

- Cost reductions in renewable energy, and anticipated cost reductions for new technologies.
- Stronger investor interest in infrastructure (often described as translating into 'more capital than projects' – there is no shortage of capital *per se* for the right assets).

[21] European Commission (2018), 'Sustainable Finance', https://ec.europa.eu/info/business-economy-euro/banking-and-finance/sustainable-finance_en (accessed 5 Nov. 2018).
[22] Finance for Tomorrow by Paris Europlace (2018), 'The Sustainable Future Begins in Paris', https://financefortomorrow.com/en/ (accessed 5 Nov. 2018).
[23] Green Finance Initiative (2018), 'Green Finance Initiative', www.greenfinanceinitiative.org (accessed 5 Nov. 2018); and Gov.uk (2018), 'Accelerating green finance: Green Finance Taskforce report', 28 March 2018, https://www.gov.uk/government/publications/accelerating-green-finance-green-finance-taskforce-report (accessed 5 Nov. 2018).
[24] Patzdorf, L. (2018), 'Brazil Green Finance Initiative (BGFI) holds first meeting for 2018', Climate Bonds Initiative, 26 April 2018, https://www.climatebonds.net/2018/04/brazil-green-finance-initiative-bgfi-holds-first-meeting-2018 (accessed 5 Nov. 2018).

- Rising energy demand in emerging markets alongside technology cost reductions, as mentioned above, plus growing interest in investment opportunities more generally in emerging markets and infrastructure.
- The rise of technology-led disruption as a compelling investment theme, as ‘transitions’ in the energy and transport sectors are increasingly driven by new technologies and digitalization. This is fundamentally changing business models and creating new opportunities that are attracting much greater attention from traditional infrastructure investors. With 30- to 50-year time horizons, such investors must assess scenarios of how sectors might evolve.
- Greater investor interest in sustainable infrastructure finance, as well as a stronger focus on so-called ‘ESG’ (environment, social and governance) reporting.
- A growing pool of ‘impact investors’ looking for investments that are consistent not only with tackling climate change but with the broader UN Sustainable Development Goals.
- Increasing mainstream debate and pressure in relation to divestment from fossil fuels. This is evident, for example, in the fact that a growing number of stock market indices now offer climate-aligned or non-fossil fuel indices.

Mind the gap: NDC implementation

The important momentum outlined above has still largely occurred in parallel to the debates influencing delivery of near-term national climate policies (whether through formal NDCs or the various sectoral energy/transport/infrastructure or adaptation policies at national level). The clear investor voice seen at the international level has not been visible or sustained

Many of the ‘green’ or sustainable finance initiatives have focused on the ‘top-down’ supply of capital for climate solutions, hoping to deliver the trillions of dollars that technical models indicate are required. However, the ability to attract investment for delivering the near-term NDC-linked climate goals is strongly influenced by national or local conditions on the ground, and by the risk profiles of different investment opportunities. Policies, regulations, procurement processes and public finance interventions remain centrally important to that investment case, very often with challenging politics at sector or even sub-sector level (which in turn can impact the perception of risk). This means that it is essential to work on both tiers simultaneously. A sequential strategy – ‘sort the trillions and then get to the detail on the ground’ – will not be adequate.

The implementation environment post-Paris is complex. Fossil fuel-based sectors have pushed back against the existential threats of climate policies. Such policies are increasing pressure to reduce fossil fuel use, and fostering technology-driven disruption that is having a serious impact on conventional energy and transport businesses in many countries. National politics have also become more difficult as result of the rise of populism, which has often coincided with shrinking support for market intervention, including in respect of climate change. One view is that the ‘Paris wave’ of momentum on climate policy has not had a long-lasting positive impact on national policies when confronted by the complexities of domestic politics.

This matters as the 2020 timeframe is fundamentally about the achievement and ‘ratcheting up’ of national emissions reduction goals, and about the conditions needed to bring about increased national ambition.[25] Yet national policy development is still thinly served across countries by identifiable, sector-level finance voices at the right level of detail on policy issues, notwithstanding the positive drivers of transition within certain sectors.

Contributing to this challenging situation is the fact that the notion of 'policy' itself has become somewhat unfashionable as attention has increasingly focused on mobilizing capital at scale – with the implication that difficult debates and slow governments can be side-stepped.

Yet a failure by governments to appear serious in their policy responses to the IPCC's *Global Warming of 1.5°C* report will undermine the very market drivers that investors saw in the Paris Agreement in the first place.

National policy and sector-level endeavours also face a kind of asymmetry of scale, in the sense of a massive global issue being addressed via actions aimed at small sub-sectors. More practically, this also means that financial organizations seeking to build climate strategies face inherent resource constraints. Sector-level policy debates often remain largely influenced by corporate incumbents, dominant trade associations or direct sectoral interests. Even where climate-aligned sectoral trade associations are active (e.g. in renewable energy), their relative power may not be sufficient to influence sceptical governments (or key parts of government), even where evidence-based arguments, persuasive strategies and large member companies are involved. This is one area where stronger alliances can be built.

What's happening: a range of national action-related activities

At the international level, NDC investment initiatives include the Climate Finance Accelerator[26] and the MDB-led NDC Invest.[27] Such initiatives can work at the level of detail relevant to unblocking barriers faced by businesses and investors.

Sector-relevant endeavours that bring different actors together are also occurring. These include: corporate commitments to buy renewable energy as part of RE100+ (an initiative that intersects with finance interests as a route to market for power-generation investments); capacity-building; and efforts by MDBs to align infrastructure, climate action and 'access to energy' (in line with Sustainable Development Goal 7) in their investment strategies. Additionally, some government initiatives launched in Paris have the potential to create wider-scale investment platforms, for example initiatives for scaling up the use of solar power in India and Africa. However, even where efforts to accelerate deployment of renewables or enhance energy access are in place, relevant energy regulations will still need to be aligned with objectives. Depending on the actors involved, these sorts of ventures may not be in a position to negotiate difficult local politics, or to provide a counter-voice to incumbent interests that are holding back national policy development.

[25] Financial institutions and corporations project consultation workshop, held on 21 September 2018 under the Chatham House Rule.
[26] Ricardo (2017), 'Climate Finance Accelerator - London 2017 summary report', https://ee.ricardo.com/downloads/climate-change/climate-finance-accelerator-london-2017-summary (accessed 5 Nov. 2018).
[27] NDC Invest (2018), 'NDC Invest', https://www.ndcinvest.org/ (accessed 5 Nov. 2018).

There have also been examples in the past decade of effective, specialized, sector-level national initiatives that have aimed to leverage financier participation. These include the Partnership for Renewable Energy Finance in the US and the Low Carbon Finance Group in the UK. The latter, which has worked largely on an electricity market reform process, was founded by senior-level mainstream finance practitioners aiming to engage with governments and help governments understand the conditions and policy design to attract capital at greater scale.

What is *not* happening

Another observation is that, at national level, far fewer of the mainstream financial trade associations are focusing on the climate agenda relative to the (much greater) attention accorded to the issue by corporate trade associations. For the latter, bottom-line commercial considerations have been a powerful factor informing the detail of climate strategies and lobbying positions. In contrast, financial trade associations continue to focus on the detail of financial *regulatory* developments. The intersection between financial regulation and climate change at national level is a newer area,[28] and warrants greater attention than it has received to date. The new Central Banks and Supervisors Network for Greening the Financial System, launched in late 2017, has a potentially important leadership role to play in this area. Its stated aims are 'to strengthen the global response required to meet the goals of the Paris agreement and to enhance the role of the financial system to manage risks and to mobilize capital for 'green' and low-carbon investments in the broader context of environmentally sustainable development'.[29]

There is no question that the big financial non-state actors do engage and seek to influence governments on national and regional policies, but a distinct lack of resourcing for the daily grind of national policy is highlighted.

There is a final point about trust: engagement by financial institutions on policy detail is not, by definition, always seen as a positive by policymakers. Nor is such engagement straightforward. There can be concern that financial institutions are profiteering in terms of what they are advocating to policymakers, or that governments will be seen as responding to pressure to meet private financial interests when their policies should be about the public good. Financial organizations need to take care to understand any such concerns and if this is a barrier to policy engagement, with possible approaches in that situation being to collaborate with other stakeholders and to ensure that governments set overarching objectives and engage with investors to test assumptions about how policy will drive investment.[30]

[28] UNEP/World Bank (2017), *Roadmap for a sustainable financial system*, November 2017, http://unepinquiry.org/wp-content/uploads/2017/11/Roadmap_for_a_Sustainable_Financial_System.pdf.
[29] Bank of England (2017), 'Joint statement by the Founding Members of the Central Banks and Supervisors Network for Greening the Financial System', 12 December 2017, https://www.bankofengland.co.uk/-/media/boe/files/research/greening-the-financial-system-statement.pdf (accessed 5 Dec. 2018).
[30] The author is working on an initiative to embed investment assessment more effectively into government institutions and decision-making.

Discussion: five areas to drive ambition

National level: countering high-carbon investor narratives and securing 'investment-grade' policy for solutions

1. Finance initiatives to counter lobbying by incumbents are already becoming active as a strategy. Such initiatives have the capacity to create a counter-voice to those seeking to undermine government ambition on climate change, including on specific policies.

Financial institutions are uniquely well placed, as shareholders, to pressure companies to provide full climate-related disclosure, put climate action at the heart of their strategic planning, and ensure that company lobbying is consistent with that objective. The form and weight of that pressure are still set by individual investors, according to their engagement strategy or style, and there is an ongoing debate over the relative merits of 'engagement' (i.e. investor pressure as shareholders) versus divestment or more overt public pressure. A number of notable organizations lead coordination of shareholder pressure on companies.

Interviewees for this paper emphasized the potential influence of a politically well-delivered counter-voice from investors to offset lobbying by incumbents in high-carbon industries. This was seen as a key element for challenging the financial sector's role in so-called 'brown' (i.e. high-carbon) growth, as well as in promoting a stronger role for the sector in supporting low-carbon 'green' growth.

2. Strategies are needed to build clear input and engagement to shift the politics and outcomes of sector-relevant climate policy. Alliance-building is essential across sector-expert groups and specialist finance associations, where those exist. Depending on the national (or subnational) starting point, this can be done in collaboration with policymakers. It is 'two-way' investment confidence that matters – meaning not only that investors need to be confident in their understanding of policy drivers and design, but also that governments need to be confident that policy frameworks will attract the capital assumed (or that funding gaps can be tackled through targeted use of public finance).

There are extensive pools of investment knowledge and commercial expertise at the national sector policy level in many countries. Renewable-energy trade associations and networks are one example of this.

It is worth noting that financiers involved in top-down 'green' and sustainable finance developments across financial institutions and governments may not be directly connected with the project-level financiers involved in sector- or technology-level investment, even within the same firm.

Developing strategies to tap into the right ecosystem of financiers for a particular outcome or policy debate is key to reaching an investment-relevant outcome faster.

The most important thing is to connect top-down efforts to 'green' the financial sector with existing investment expertise relevant to securing national implementation.

Infrastructure and project-level investors frequently emphasize that 'the devil is in the detail' of government plans in terms of assessing investment opportunities. This simply reinforces the importance of building engagement on national and local policy and politics in parallel to work on ensuring overall capital flows are consistent with climate response. Implementation must work at a practical level for finance practitioners making the decisions. Discussion about solving the project pipeline question post-Paris must also be connected with those factors that drive project and business development at a range of different scales, including national policy and planning conditions.[31]

Convergence or **sharing between knowledge pools** (top-down and bottom-up) to accelerate this agenda is **one of the greatest achievable opportunities**, particularly when combined with shareholder pressure.

One avenue for building networks of engagement is through **flexible, nationally focused, time-specific alliances**. These need to work at the right level of granularity for investors (i.e. evidence-based), where decisions need to be delivered and where interests that drive markets align. There is a clear opportunity to work with other types of organization or non-state actors – an obvious example is at city or community level, through linked specific infrastructure projects, or through other leverage points or groupings, e.g. associated with air pollution or job creation.

International and regional level: from 'you and us' to 'solving it with you': a further shift towards joint problem-solving

3. The UN secretary-general's forthcoming Climate Summit in 2019 will provide an important platform for generating further momentum. Care may be needed to avoid a sense of 'AUM fatigue' – i.e. if international initiatives get updated to show ever larger numbers of firms and the volumes of capital that they manage (although not necessarily a commitment to invest) yet are not then visible in policy or implementation debates on the ground. The key will be how to target this growing intent of financial institutions in a way that also builds momentum at a national level; otherwise there is a risk of diminishing returns.

A greater focus on solving the real-world issues facing countries also means tackling the pressing need to stimulate capital flows to, or within, emerging markets and least-developed economies: to support investment in energy access, for example. These areas are already on the agenda of investor initiatives, with some sector-relevant regional investor initiatives now under way.

4. Regional, sector-relevant ministerial forums represent another opportunity for financial sector stakeholders to have an active strategy of introducing investor messages on climate change to wider constituencies. Such efforts could encompass ministerial-level regional forums on economic or sectoral issues. Setting up investor engagement in these settings is one option, with a format

[31] See also OECD (2018), *Developing Robust Project Pipelines for Low-Carbon Infrastructure*, Paris: OECD Publishing, 12 November 2018, http://www.oecd.org/investment/developing-robust-project-pipelines-for-low-carbon-infrastructure-9789264307827-en.htm. The author of this paper was involved in coordinating initial investor input for the OECD research for this report.

guided by aims and outcomes. It may also involve having a prominent advocate of climate finance 'following the money', so to speak, by engaging with leading regional forums for investors.

One figure who could perhaps be deployed in this context is Michael Bloomberg, in his role as UN Special Envoy for Climate Action. Other regionally influential people from among Bloomberg's peer group could also fulfil such a role.

5. Talanoa 2.020?

Though not discussed above, another potential opportunity to boost climate change cooperation between the investor community and other stakeholders is to continue to use the 'Talanoa Dialogue'.[32] This process, initiated by the Fijian COP presidency and starting in 2018, is based on bringing people together in a more informal, participatory meeting format that aims to build trust and shared understanding.

The style of the Talanoa process has attracted generally positive feedback and could be one avenue for ongoing finance practitioner–policymaker sessions around specific questions, or indeed between specific parts of the financial sector and other stakeholders.

Adopting such a meeting style or process would break away from the 'high-level panel plus audience' format, and potentially support a shift towards a more participatory approach focused on problem-solving. However, it would raise the question over whether its effectiveness was partly a result of its formal link to the UNFCCC, and whether that link or a national equivalent is needed to ensure outputs are used to good effect.

[32] Talanoa Dialogue Platform (2018), 'Talanoa Dialogue for Climate Ambition', https://talanoadialogue.com/ (accessed 21 Dec. 2018).

About the author

Kirsty Hamilton has been an observer at the UNFCCC process since 1991, working in various capacities. She was an adviser to UNEP FI's Climate Change Working Group from 2004 to 2011. As an associate fellow at Chatham House, she set up and led an initiative to close the gap between policy and finance in 2004, working with leading clean-energy and infrastructure finance practitioners (international, developing country/emerging market and European focus). Following the 2008–09 global financial crisis, she was involved in the establishment of the Low Carbon Finance Group in the UK, leading its policy and strategy work. This first-of-a-kind group was founded by senior financiers to help policymakers and ministers understand the conditions required to attract capital at greater scale, predominantly focusing on electricity market reform policy in 2010–15. Following a stint as a specialist adviser for a parliamentary inquiry into investor confidence, Kirsty is now focused on embedding investment-related themes into government decision-making. She also does advisory work. She has had invitational roles, with the World Economic Forum and REN21 among others, and is an expert reviewer and contributing author to the IPCC.

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