

June 2, 2021

# China's green intentions





Fredrik Skoglund BIL Group Chief Investment Officer



Hanzhi Ding CEO BIL Hong Kong

<u>China's growth story</u> and environmental sustainability are two prominent themes that are set to shape the investment landscape in the coming years. But these themes are not always mutually exclusive; junctions are emerging at which these two megatrends intersect.

Recently, Beijing made serious commitments to achieve peak carbon emissions by 2030, and

"carbon neutrality" by 2060 (sometimes referred to as its 30/60 goal). It is difficult to overemphasize how transformational China's carbon neutrality pledge is for international efforts to limit climate change. Indeed, Niklas Hagelberg, coordinator of the Climate Change Program at the UN Environment Program commented that "It's like steroids in the move to decarbonization." [1] China's move also had a halo effect in the region, with Japan subsequently committing to net-zero greenhouse gas emissions and South Korea to carbon neutrality, both by 2050. But the positive impact reverberated not just regionally, but globally, bringing an exciting boost of morale.

Combatting climate change is one area where the US and China appear to see eye to eye and where there is great potential for the G2 to collaborate. This year, their respective climate envoys, John Kerry and Xie Zhenhua, vowed to make "concrete actions in the 2020s" to reduce emissions in line with the aims of the 2015 Paris climate accord. In a statement, the countries committed to co-operating in multilateral processes, including at the COP26 UN climate conference in Glasgow this November. While previous summits in Kyoto and Paris were staging posts towards reaching international consensus, this year's summit will focus on setting out a road map for achieving the goals of the Paris agreement.

With China currently the world's largest carbon emitter, the task at hand is a colossal one, and will require a whole array of policies and targeted support for specific industries and technologies. What is certain is that when the Chinese government sets targets, it doesn't do so in vain.

## **GOVERNMENT POLICY**

The Chinese government has already started to incorporate environmental factors into policy making and policy action. China's 14th Five-Year Plan (2021-25) aims to advance the quality and sustainability of the country's development while its "new infrastructure" encapsulating 5G, the internet of things, cloud computing, blockchain, and smart transportation will clearly be instrumental in ushering in a greener economy, powered by clean technology.

At the same time, under the Made in China 2025 [2] strategy, some of the strategic, cutting-edge industries that China wants to become globally competitive in by 2025 and globally dominant in before the close of the century, are also industries deemed essential for the energy transition and sustainable growth in the future. For example, electric power equipment, new materials (e.g. for building solar cells), biotechnology (breakthroughs in this space can increase food production, provide cleaner energy and make manufacturing more efficient and environmentally friendly) and electric vehicles (EV).

With the government honing in on and investing substantially in such areas, China has already recorded success in scaling up solar power, improving efficiency in wind energy [3] and increasing economies of scale in the production of batteries for electric cars. It has also

emerged as a key competitor to the EU in the race to produce scalable, green hydrogen technologies. [4]

The electric car industry stands out as an area where Beijing's efforts are already bearing fruit. With the aim of ensuring that a fifth of vehicles sold in China are electric by 2025, Government support has flooded into the industry (e.g. R&D funding, direct investments in EV companies and charging infrastructure...), propelling China to become a global leader in the space in a very short space of time.

On the demand-side, direct subsidies, preferential access to license plates (which are restricted in many big cities to control traffic) and other measures have led to a rapid expansion of the domestic EV market: In 2016, 336,000 EVs were sold in China; four years later in 2020, 1.3 million EVs were sold. That's 41% of global EV sales, just behind Europe with 42%. In the US, EV sales represented just 2.4% of sales. [5]

This example highlights the efficacy of Beijing's targeted policymaking.



Shanghai

#### **GREEN MONETARY POLICY**

Alongside government policy, the People's Bank of China (PBC) will also contribute to China's objectives with the development of green finance. It recently outlined its plans in this area, which can be broken down into five pillars, summarized below. [6]

## **Target**

Accelerating the financial standard system

Continuous strengthening of information disclosure requirements and financial institution supervision

incentive and restraint mechanism

products and market system

Deepening of international cooperation in green finance

## Aim/ Progress

Progress has been made in the formulation of a establishment of a green number of green finance standards. The comparative study of China-Europe green finance standards is about to be completed.

> Refers to continual efforts to promote the classification of financial institutions, securities issuers, and public departments with goal of improving the mandates for, and standardization of, environmental information disclosure. Pilot work on disclosure by Chinese and British financial institutions continues to advance.

This will guide financial institutions to increase Gradually improving the green asset allocation and strengthen environmental risk management thus helping to improve the financial industry's ability to support green development.

Enriching green financial For example, encouraging product innovation, improving the issuance system, standardizing transaction procedures, enhancing transparency.

> Use multilateral platforms and cooperation mechanisms to promote international exchanges on green finance. Enhance the international community's recognition and participation in green finance policies, standards, products, and markets of China. The PBC is working with international counterparts to harmonize taxonomies.

The central bank also said that it is working towards creating a long-term mechanism for providing financial support towards the green transition and the low-carbon transformation, as well as supporting innovation in the area of green financial products.

Already, China's capital markets are beginning to have a green tinge to them. By the end of 2020, China's market for green loans and green bonds in China totalled \$1.8 trillion and \$125 billion respectively, ranking as the world's largest and second largest. More than 40 carbon neutral bonds have been issued, with a total volume of over \$10 billion. [7] The plans outlined by the PBC will likely give further impetus to China's green assets; directly, by guiding financial institutions to upsize their allocations, and indirectly by empowering investors through improved access to information (to avoid greenwashing).

#### **INVESTMENT OPPORTUNITIES**

For China to meet the emissions targets, there is a lot left to be tackled. It will require no less than a comprehensive economic transition, touching almost every industry. This will entail

investment in areas from energy storage, the power grid to renewable energy technologies. It will also involve reducing demand for industrial products (steel, cement, plastics...) and the development of alternatives to these. Upgrades to China's steel mills - which produce half of all the world's steel - will be of particular importance, given that this activity alone accounts for about one-third of the country's overall emissions. [8] Already, China's top steel producer, Baowu Group, is exploring green steel and has vowed to achieve carbon neutrality by 2050. [9] Beyond reducing emissions, China will also have to invest in carbon capture technologies and in the development of its natural carbon sinks.

As China gets to work on tackling its self-imposed 30/60 goal from various angles, innovation and investment will be crucial to support the green transition. It is expected that policy support will be strong and multi-faceted but there is ample room for this to be complimented with private capital: It is estimated that by 2030, China will need to invest 2.2 trillion yuan per year to reduce carbon emissions, and this amount will further grow to 3.9 trillion yuan from 2030 to 2060. [10]

Moving forward, we think this will present myriad opportunities for investors seeking exposure to China's growth story as well as the energy transition.

### References

- 1. https://www.dw.com/en/china-coal-emissions-climate-change/a-56644449
- 2. A blueprint for making China an advanced manufacturing economy, positioning it as a dominant player in the fourth industrial revolution by pursuing home-grown innovation.
- 3. https://www.evwind.es/2019/10/20/the-lcoe-of-onshore-wind-energy-in-china-has-fallen-by-over -40-in-the-past-decade/71416
- 4. https://www.cleanenergywire.org/news/europe-vies-china-clean-hydrogen-superpower-status
- 5. Canalys data quoted by Yahoo Finance https://finance.yahoo.com/news/canalys-china-electric-vehicle-sales-140000063.html
- 6. PBC Outlines Plans for Development of Green Finance in China,

  Moody's. https://www.moodysanalytics.com/regulatory-news/feb-09-21-pbc-outlines-plans-for-d
  evelopment-of-green-finance-in-china

- 7. Yi Gang: Green finance and climate policy. Bank for International Settlements https://www.bis.org/review/r210416a.htm
- 8. https://www.ft.com/content/46d4727c-761d-43ee-8084-ee46edba491a
- https://www.reuters.com/business/sustainable-business/chinas-top-steelmaker-baowu-group-vows-achieve-carbon-neutrality-by-2050-2021-01-21/
- 10. https://www.bis.org/review/r210416a.pdf

9.

Disclaimer

All financial data and/or economic information released by this Publication (the "Publication"); (the "Data" or the "Financial data and/or economic information"), are provided for information purposes only, without warranty of any kind, including without limitation the warranties of merchantability, fitness for a particular purpose or warranties and non-infringement of any patent, intellectual property or proprietary rights of any party, and are not intended for trading purposes. Banque Internationale à Luxembourg SA (the "Bank") does not guarantee expressly or impliedly, the sequence, accuracy, adequacy, legality, completeness, reliability, usefulness or timeless of any Data. All Financial data and/or economic information provided may be delayed or may contain errors or be incomplete. This disclaimer applies to both isolated and aggregate uses of the Data. All Data is provided on an "as is" basis. None of the Financial data and/or economic information contained on this Publication constitutes a solicitation, offer, opinion, or recommendation, a guarantee of results, nor a solicitation by the Bank of an offer to buy or sell any security, products and services mentioned into it or to make investments. Moreover, none of the Financial data and/or economic information contained on this Publication provides legal, tax accounting, financial or investment advice or services regarding the profitability or suitability of any security or investment. This Publication has not been prepared with the aim to take an investor's particular investment objectives, financial position or needs into account. It is up to the investor himself to consider whether the Data contained herein this Publication is appropriate to his needs, financial position and objectives or to seek professional independent advice before making an investment decision based upon the Data. No investment decision whatsoever may result from solely reading this document. In order to read and understand the Financial data and/or economic information included in this document, you will need to have knowledge and experience of financial markets. If this is not the case, please contact your relationship manager. This Publication is prepared by the Bank and is based on data available to the public and upon information from sources believed to be reliable and accurate, taken from stock exchanges and third parties. The Bank, including its parent,- subsidiary or affiliate entities, agents, directors, officers, employees, representatives or suppliers, shall not, directly or indirectly, be liable, in any way, for any: inaccuracies or errors in or omissions from the Financial data and/or economic information, including but not limited to financial data regardless of the cause of such or for any investment decision made, action taken, or action not taken of whatever nature in reliance upon any Data provided herein, nor for any loss or damage, direct or indirect, special or consequential, arising from any use of this Publication or of its content. This Publication is only valid at the moment of its editing, unless otherwise specified. All Financial data and/or economic information contained herein can also quickly become out-of- date. All Data is subject to change without notice and may not be incorporated in any new version of this Publication. The Bank has no obligation to update this Publication upon the availability of new data, the occurrence of new events and/or other evolutions. Before making an investment decision, the investor must read carefully the terms and conditions of the documentation relating to the specific products or services. Past performance is no guarantee of future performance. Products or services described in this Publication may not be available in all countries and may be subject to restrictions in some persons or in some countries. No part of this Publication may be reproduced, distributed, modified, linked to or used for any public or commercial purpose without the prior written consent of the Bank. In any case, all Financial data and/or economic information provided on this Publication are not intended for use by, or distribution to, any person or entity in any jurisdiction or country where such use or distribution would be contrary to law and/or regulation. If you have obtained this Publication from a source other than the Bank website, be aware that electronic documentation can be altered subsequent to original distribution.

As economic conditions are subject to change, the information and opinions presented in this outlook are current only as of the date indicated in the matrix or the publication date. This publication is based on data available to the public and upon information that is considered as reliable. Even if particular attention has been paid to its content, no guarantee, warranty or representation is given to the accuracy or completeness thereof.

Banque Internationale à Luxembourg cannot be held liable or responsible with respect to the information expressed herein. This document has been prepared only for information purposes and does not constitute an offer or invitation to make investments. It is up to investors themselves to consider whether the information contained herein is appropriate to their needs and objectives or to seek advice before making an investment decision based upon this information. Banque Internationale à Luxembourg accepts no liability whatsoever for any investment decisions of whatever nature by the user of this publication, which are in any way based on this publication, nor for any loss or damage arising from any use of this publication or its content. This publication, prepared by Banque Internationale à Luxembourg (BIL), may not be copied or duplicated in any form whatsoever or redistributed without the prior written consent of BIL 69, route d'Esch I L-2953 Luxembourg I RCS Luxembourg B-6307 I Tel. +352

