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# China's green intentions

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China's growth story 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 | Aim/ Progress |
|---|---|
| Accelerating the establishment of a green financial standard system | Progress has been made in the formulation of a number of green finance standards. The comparative study of China-Europe green finance standards is about to be completed. |
| Continuous strengthening of information disclosure requirements and financial institution supervision | 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. |
| Gradually improving the incentive and restraint mechanism | This will guide financial institutions to increase green asset allocation and strengthen environmental risk management thus helping to improve the financial industry's ability to support green development. |
| Enriching green financial products and market system | For example, encouraging product innovation, improving the issuance system, standardizing transaction procedures, enhancing transparency. |
| Deepening of international cooperation in green finance | 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.

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