Greening finance for the low-carbon transition

Prof. Daniela Gabor (UWE Bristol)
Investments of 5-7% GDP per year to 2050

Carney-led finance coalition has up to $130tn funding committed to hitting net zero

Ex-BoE governor rallies capital to tackle climate change but fossil fuels remain a problem

Kate Aronoff @Ka... · Nov 3
Kerry on the $130tn Gfanz announcement today: "Blend the finance, de-risk the investment, and create the capacity to have bankable deals. That’s doable for water, it’s doable for electricity it’s doable for transportation."

On #ClimateFinance, BlackRock's Fink puts it plainly in @nytopinion: Investments in low-carbon projects in developing countries must total more than $1T/year—more than 6x the current rate—which must be catalyzed by $100B/yr in grants from rich countries.

COP26 @COP26 · Oct 25
NEWS: The #COP26 Presidency has released the $100bn Delivery Plan, led by 🇨🇦

The plan, endorsed by developed countries, states how and when they will deliver on the goal to mobilise $100bn per year in climate finance.

Read the plan:
ukcop26.org/wp-content/upl...
Institutional capital - portfolio glut

Pension fund assets and asset allocation, % of GDP

Data: OECD

Source: Braun & Gabor (2021)
The COVID-19 sell-off and the recent recovery
Emerging economies saw more than $100 billion of local currency portfolio outflows after the onset of the pandemic, but have recovered sharply lately.

Cumulative nonresident local portfolio flows to emerging markets, excluding China

Sources: Bloomberg, Haver Analytics, IIF.
Green macro-financial regimes: institutional modes of creation and access to green financial assets, including money

<table>
<thead>
<tr>
<th>Regime</th>
<th>Coordination mechanism of investment</th>
<th>Role of… financial regulation</th>
<th>fiscal policy</th>
<th>monetary policy</th>
<th>Degree of nationalization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carbon shock therapy</td>
<td>Prices + competition</td>
<td>Liberalize</td>
<td>Fiscal discipline &amp; monetary dominance</td>
<td>–</td>
<td></td>
</tr>
<tr>
<td>Small green derisking state</td>
<td>Prices + derisking</td>
<td>Private ESG taxonomy &amp; voluntary balance-sheet decarbonization</td>
<td>Dirty/green asset de-risking (soft credit guidance) Fiscal discipline &amp; monetary dominance</td>
<td>+ stranding assets</td>
<td></td>
</tr>
<tr>
<td>(Wall Street Consensus)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Big green state</td>
<td>Prices + indicative planning</td>
<td>Public ESG taxonomy &amp; mandatory balance-sheet decarbonization Capital controls</td>
<td>Green public investment Green monetary policy (quantitative allocation) Monetary-fiscal coordination</td>
<td>+ parts of the financial sector Re/nationalisation of green credit</td>
<td></td>
</tr>
</tbody>
</table>

Source: Braun & Gabor (2021)
Shock therapy in Washington Consensus

• Transition to market economy: structural transformation via subjecting state-owned companies to disciplining hand of price signals

• How: increase (liberalise) prices at which SOEs access imported/intermediary inputs & increase the price of credit via monetary austerity (Gabor 2011, Weber 2021)

• Politics: imposed via IFIs (WB/IMF) under BOP crises, in local coalitions with central bank and against political opposition/contestation (job losses)
Carbon shock therapy in Wall Street Consensus

• Transition to low-carbon economy: structural transformation via subjecting companies to disciplining hand of price signals

• How: increase (liberalise) prices at which companies pollute & increase the price of credit through risk-based monetary measures

• Politics: imposed via IFIs (WB/IMF), potential BOP crises in context of COVID19 debt pressures and SDR reallocation, in local coalitions with central bank and against political opposition/contestation (job losses)
Maximize public investment for low-carbon transition

State
  Invests in public services
  green public infrastructure
  green industries
  Taxes
  green industrial policies
  Private finance
    buys sovereign/green bonds
    Central bank-led mandatory decarbonisation
  Citizens

Creates green jobs

Maximize private finance for low-carbon transition (Wall Street Consensus): change risk/return profile for new asset classes

Derisking

State
  PPP infrastructure assets
  fiscal
  cash transfers/UBI
  user fees
  Central banks derisk green bonds and exchange rates
  institutional capital
    monetary
    cash flows
    invests in infrastructure assets & (SDG/ESG) bonds
    Citizens

Assumes demand risk and climate risks in PPP contracts (coding infrastructure capital)

Derisking State
Climate derisking (Ryan Collins et al. 2022)

• protect financial system from climate risks (single materiality) – both physical risks of extreme climate events and transition risks (fiscal decarbonization via carbon prices)

• correct the risk/return profile of dirty assets: tilt unconventional bond purchases or collateral frameworks without abandoning market neutrality (Dafermos et al 2022 for Bank of England)

• *soft credit guidance*: increase relative price of dirty credit without targeting any sector-specific prices/quantities of capital and without defining (or aligning with) any distinctive decarbonization pathway
  • delegate the pace and nature of decarbonisation to private finance, despite systemic (ESG based) greenwashing
  • no green (re)nationalization of credit possible under monetary dominance (see Monet 2014, Naqvi 2019)
Small green derisking state

1. Delegates the pace and nature of decarbonisation to private finance (but DSSI, energy and food security)

2. Global South as consumers but not producers of green tech – amplifies technological and financial dependency
   - Closing infrastructure gap is not enough for green structural transformation
   - Uganda’s Kiira Motors as example of green developmental state

3. De facto privatization of public goods: access and instability
Conclusion

• Can derisking state deliver on its low-carbon promises?
  • Without reforming market-based finance
  • Without challenging supremacy of USD
  • Without challenging (infra)structural power of finance

• Carbon shock therapies: learning from China

• Alternative green macrofinancial regimes: obstacles, actors, power and redistribution