Wilton Park

Interim summary report: Wilton Park virtual dialogue

BRI investment in the energy sector: framing sustainable policy solutions for the post-COVID world

The next 18 months are vital as countries decide on massive capital investments in infrastructure to restart the economy and create jobs in response to COVID. However, most energy sector spending in response to COVID thus far has not prioritised sustainable investment. The political economy and infrastructure framework in many countries favours traditional carbon-intensive infrastructure projects. Fortunately, global markets have acknowledged the inevitability of an energy transition, as financial institutions recognise that fossil fuel investments are a greater stranded asset risk and debt burden for governments.

A green shift in China's Belt and Road Initiative (BRI) investments is thus economically and financially prudent, sustainable and resilient and will be more attractive to investors for the coming decades. Green infrastructure investments can diversify economies, create more jobs, and be a centrepiece for stimulus packages. China's BRI will contribute a large share of the resources for future infrastructure. Governments can use BRI resources to invest in green projects, such as smaller-scale projects with jobs benefits across diverse geographies that support rural communities in electrifying across Asia. A green shift requires commitment from at least four key groups: Chinese institutions, host countries, global partner institutions, and diplomatic leaders.

Chinese institutions

At present, BRI deals between China and host governments are often led by State-Owned Enterprises (SOEs), with large projects requiring NDRC approval; these deals could benefit by having voices for greater sustainability involved. Participants in the Wilton Park dialogue noted that project recommendations may sometimes be driven more by China's domestic supply side considerations for SOEs (who are more experienced in fossil-fuel related infrastructure), and less motivated by what would be most sustainable for the host country.

China has already signalled high-level political commitment to green the BRI in principle, though implementation remains a challenge. There are already initiatives such as BRI Low Carbon Cities, tools like the China Green Finance Committee's calculator for environmental impacts, the Committee's innovative green finance products to lower the cost of renewables, and the green project investment database under the Green Investment Principles for the Belt and Road, which can help potential green BRI projects access global public sector and private sector capital.

Further measures that could have significant impact include the following.

- China could accelerate a shift for BRI by funding smaller south-south cooperation projects ($1-$5million) for green investment. Instead of investing in fossil fuel infrastructure, China can orient towards more investment in transmission and distribution upgrades that countries have put forward.
- China can share its expertise in innovative financial products: sustainable bonds, green/ESG bonds, crisis recovery facilities.

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- As government funds are limited, including for China, Chinese companies can increase their engagement with multilateral development banks and financial institutions such as EBRD, ADB and AIIB to crowd in more capital for green projects.
- China could promote and contribute to more integrated solutions for energy infrastructures in the host countries, including grid infrastructure and capacity building that are choke points for the broader deployment of renewable energies.
- And China can connect its own civil society organisations with those abroad through platforms for greater south-south cooperation.
- China can consider encouraging its companies, SOEs or private ones, to enhance environmental and climate considerations for project investments overseas, especially along the Belt and Road, e.g. through the “traffic light system” which is already under discussion.

Countries in the Belt and Road Initiative

To green BRI, host countries must first articulate demand for more green investments. With host countries in need of financial resources, there is a tendency to accept BRI projects as proposed, without sufficiently considering the long-term socioeconomic impacts – though there are exceptions. In some cases, host government leadership may opt for highly visible mega-projects for political benefit. But it cannot be assumed that the benefits of a mega-project will trickle down to most citizens, and in fact, some projects may lock in unnecessary government subsidies and sectoral inefficiencies.

Participants in the Wilton Park discussions noted that many countries are asking for disproportionately high levels of investment in coal. For example, in Bangladesh coal project power capacity will be 30 times higher than for planned renewables projects. Countries need to reassess energy demand needs in light of COVID and plan for a “net-zero” emissions future, then develop enabling conditions for the full suite of policy, regulatory, technical and institutional measures to scale up green investment. Designing post COVID infrastructure requires integrated planning, such as new roads with electric vehicle infrastructure built in and railways and water systems using clean energy. Countries should increase collaboration on green investment with Chinese BRI-affiliated SOEs and private companies that are contractors, project developers, and financiers. A lesson from China’s own industrial development is that having green standards from the outset would have reduced severe water and air pollution.

Further measures that could have significant impact include the following.

- As suggested by several Wilton Park expert participants, their countries must address the conservatism in behaviour of relevant ministries and procurement officers. These stakeholders can benefit from learning about the rapidly changing energy landscape so they are less likely to prefer outdated fossil fuel infrastructure technologies that could pose long-term stranded asset risks or burdens for government budgets.
- More government guarantees for green, sustainable projects can put them on a more level playing field.
- A growing market for green investments and bonds can attract more private sector capital.
- One potential idea is to develop a green coalition of BRI nations, with a shared investment framework and higher environmental, climate and health standards. A green coalition could link regulators, utilities, financiers, project developers and others, standardising procurement policies. Many resources exist, but countries should improve information sharing via existing channels (ASEAN, Southeast Asia Energy Transition Partnership). Having Green BRI “pilot countries” will allow learning on scaling green investment.
- Governments can support civil society organisations working with counterparts in China to discuss the benefits of a sustainable transition.

Partner institutions and regional cooperation

Global institutions and partners can support sustainable recovery through these measures.

- Global institutions such as development banks, intergovernmental institutions and coalitions can encourage the formulation of stronger environmental and social governance standards around BRI projects – articulating the need for these policies with Chinese institutions such as NDRC, MOFCOM and SASAC, and with ministries in each BRI country.

- Institutions should encourage China to implement green investments with clear targets and timelines.
- Countries and partner institutions can support more rapid deployment of green projects by establishing a Green Guarantee Fund to reduce project risk costs, such as through participation in the Green Investment Principles for the Belt and Road, which has already brought together 37 global institutions with total assets of over 41 trillion USD.
- Institutions can support the development of green BRI pilot countries, facilitate dialogues and exchanges on standardisation of project development and procurement, help crowd in private finance, provide blended financing and other options.
- Institutions can accelerate South-South peer-to-peer awareness raising and learning, investment, and development by promoting regional hubs of excellence.
- The private sector and multilateral financial institutions can engage more with Chinese companies that are leaders in renewable energy.
- Multilateral Development Banks could help bring initial capital support to finance higher risk clean project pilots, as well as financing development missions such as education, capacity building and awareness enhancement.

Diplomacy

Sustainable infrastructure discussions should focus on the jobs and economic benefits of green stimulus. Any framing must be led by stakeholders from within the country and their understanding of how to drive green stimulus forward. Further measures that could have significant impact include the following.

- Diplomatic efforts should address basic information asymmetries, as not all BRI countries know the benefits from green investment, and diplomacy should encourage such discussion on sustainable investment.
- Institutions must identify the right public sector and private sector partners within China and link them to partners and capital elsewhere to push past existing barriers to renewables uptake in BRI countries.
- Diplomatic efforts should support the development of a Green BRI coalition among host countries and expand communication channels to high-level actors, but also to regional and local policymakers versed in local political complexities.

Conclusion

In a time of great economic disruption from COVID, countries will benefit by finding means of social and economic recovery that also address the profound long-term threat of climate change. BRI countries can create conditions to attract more public and private investment in clean energy and sustainable infrastructure. Outreach to Chinese institutions should highlight the imperative to enhance environmental and climate considerations for all BRI investments. Global institutions and diplomats should facilitate this virtuous circle of increasing demand for clean energy, leading to a crowding-in of resources for these projects, and thereby attracting more BRI institutions and global investors to accelerate the energy transition.

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