COP27: TIME FOR PRETTY WORDS?

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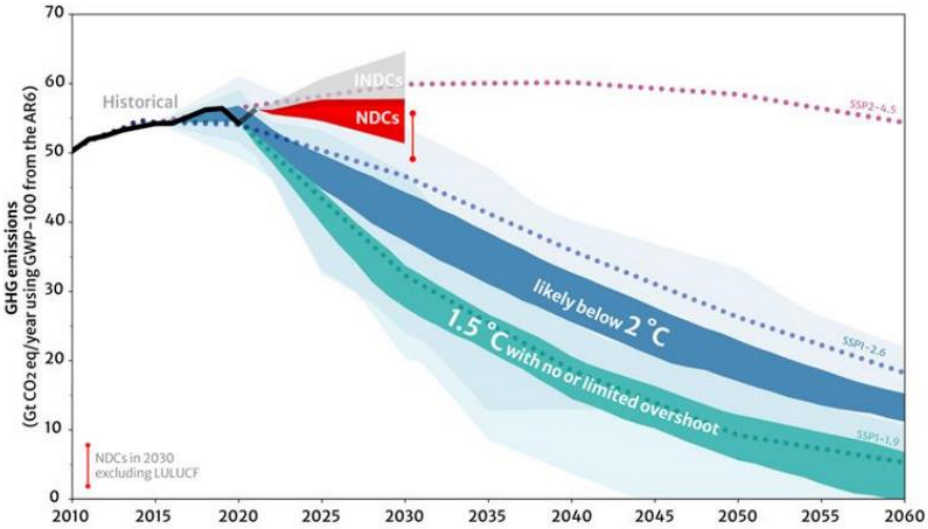
Last year COP26 concluded with ambitions nowhere near the requirements for a 1.5°C global warming scenario. The UK's COP ambition to 'keep 1.5°C alive' was not reached, but as usual (unfortunately), promises were made for the year after. Hence, all eyes on the next one. What has COP27 to offer, apart from a controversial sponsorship?

4 GRAPHS TO KEEP IN MIND DURING COP27

Bridging the gap: are the renewed pledges in line with Paris or still completely off track?

On the eve of COP27, the UN's Climate Change division published another worrying report: we are nowhere near the scale and pace of the required emissions reductions to limit global warming to 1.5°C by the end of the century. Rather, based on the combined climate pledges (Nationally Determined Contributions or NDCs), we could put the **world on track for around 2.5°C of warming by the end of the century**. It looks like the Glasgow Climate Pact got lost somewhere in the mail. One positive note however: according to the analysis, emissions are no longer increasing after 2030, although the downward trend is far from what is needed.

The emissions gap: a worrying sign



Source: UN Framework Convention on Climate Change (UNFCCC), 2021

Hence, **more ambitious NDCs are required**. Since last year several countries made some promises to step up their ambitions, so that's an easy task, right? Well, think twice: since COP26, only 24 new or updated plans were submitted. Moreover, to date, only three G20 nations submitted 1.5°C aligned targets and the EU announced a delay linked to the finalization of the Fit for 55 package. Furthermore, rumour goes this COP will not focus on new ambitions, but rather deal with all financing worries.

Can we at least put our hopes up from **latest news coming from major nations** like the US, with its historical Inflation Reduction Act (USD 369bn for climate-related action), or Brazil, with the election of Lula da Silva (with promises to protect the Amazon rainforest and restore Brazil's climate leadership)? And what about China, the lead renewables investor (more investment in wind, solar and EV capacity in 2021 than the rest of the world combined)? Will they announce more at the COP? We cannot be too optimistic, but global leadership

is and has always been an important trigger.

Unfortunately (or luckily?) this **COP will be overshadowed by yet another crisis, or worse, multiple crises**. The covid19 aftermath and war in Ukraine triggered global inflationary shocks, food worries, energy shortages as well as deglobalization. Recent spikes in O&G prices (and issuers' valuation) and a revamped coal focus are triggering significant concerns for climate ambitions across all regions. Will this hamper the expression of more ambitious pledges and negatively impact emissions trajectories? Let's hope this is not rhetorical. Recent events showed environmental goals could and should go hand in hand with energy security ambitions.

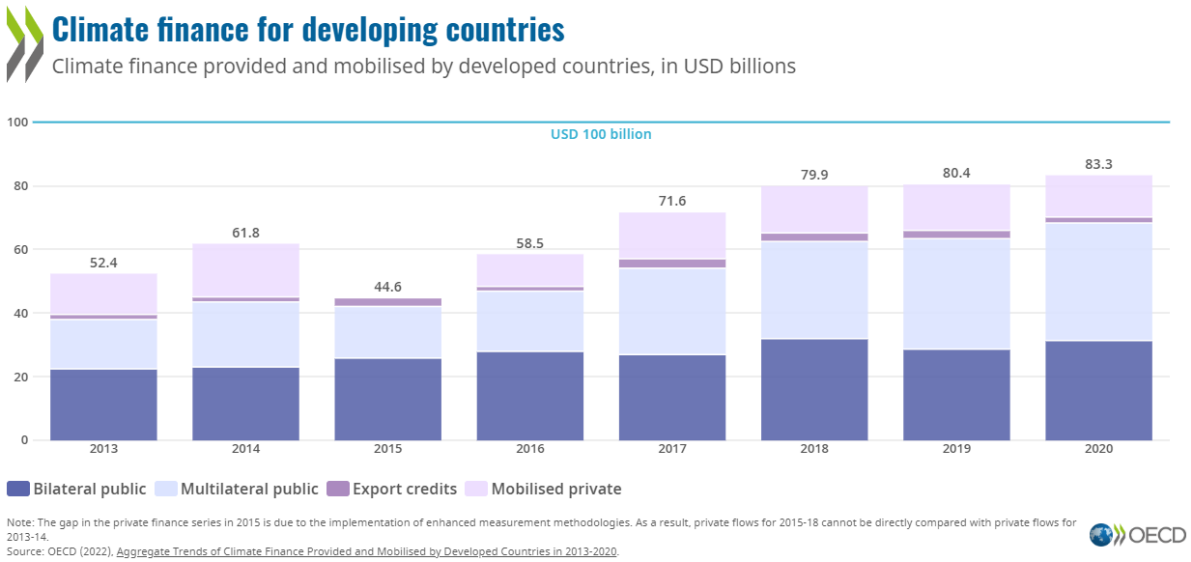
But these crises not only trigger worries around emissions reduction efforts but also, the highly required transition financing streams as well as the loss & damage financing requirements are at risk. Let's have a closer look at the state of affairs of climate financing:

An ever-increasing bill: is it finally time to bridge the transition financing gap?

The risk perception on climate change is becoming increasingly negative, as clearly showed in WEF's Global Risk Report and now also in AXA's Future Risks Report 2022, the latter published only last week: **climate change is becoming the number one concern around the world** and, as recent years have shown, is clearly interlinked with other major risks. The cost of inaction will be extremely high, and the world is currently unprepared to tackle what's coming. The 2021 Adaptation Gap Report shows worrying signs of gap widening, while developing nations are calling for long-awaited transition financing. So, what is the current state of play?

It seems that the transition financing promise of USD 100 billion per year, from developed to developing nations which was scheduled to start in 2020, was more of a marketing stunt than an actual resolution. References to the financing needs remained part of the final Glasgow text, stressing 'effort doubling' by 2025, but omitting the setup of a 'fund' as it only focuses on 'technical support'. The EU nonetheless expressed already some ambition to scale up and target 2023 instead of the initial 2020 starting date. However, until proven, the transition financing gap remains in place**, especially considering the vast majority of funding comes in the form of expensive loans, not grants**. Luckily, Europe's regulation against greenwashing is only targeting corporates and financials, and not sovereigns. Or can we expect some tangible action in Egypt?

Transition financing: the broken 100bn promise



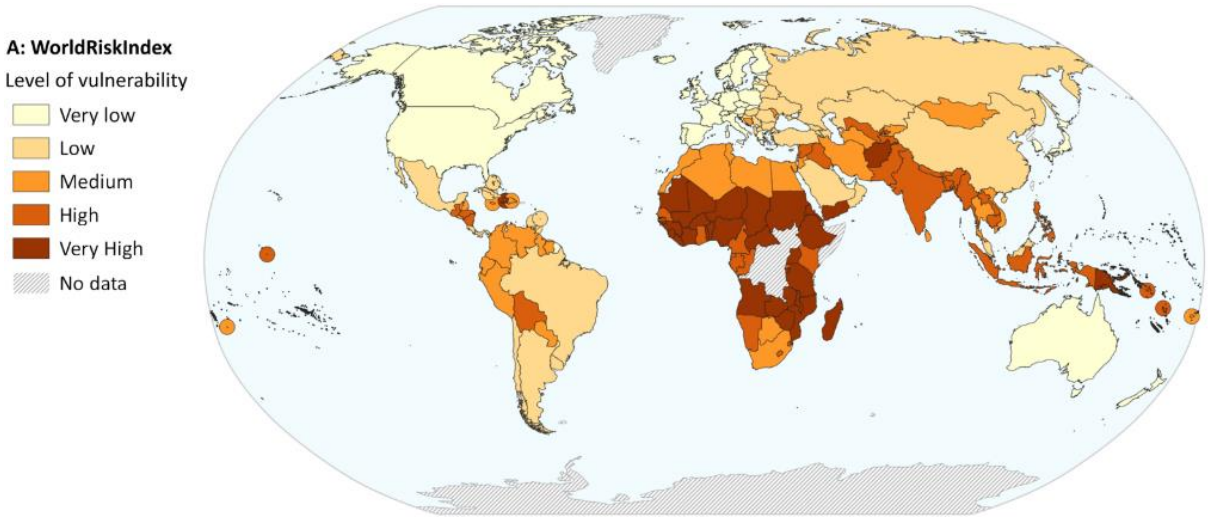
Source: OECD, 2021

Apart from transition financing gaps, **fossil fuel financing is on the loose** and will hopefully, and yet again, trigger some debate. With G20 companies providing approximately USD 693bn of fossil fuel financing in 2021 and coal phase out committers of the Glasgow Pact boosting their reliance on coal, last year's COP ambitions

have already been flawed. Watering down the wording at the end of the conference clearly offered some leeway. Will we finally turn the page on coal? And what about the record profits made by Big Oil as a result of the Ukraine war? Is this something to be tackled at international level?

Next to transition financing and current fossil fuel spending, also **loss & damage compensation will likely be heavily debated** as the most vulnerable countries continue to be significantly more impacted by the effects of global warming. IPCC estimates state 3.3 to 3.6 billion people (nearly half the world's population!) live in contexts that are highly vulnerable to climate change. Sadly, the most vulnerable people are largely living in countries with the lowest historic GHG emissions. However, in terms of compensation, no promises were made yet by 'historic' emitters and EU countries already remained more cautious, reiterating 'readiness to engage constructively with partner countries'. In other words, no bold commitments or action to be expected just like the 'Glasgow Dialogue'? Or will the long-awaited dedicated loss and damage finance facility be finally created? All eyes on the 2022 Bridgetown Agenda for the Reform of the Global Financial Architecture**.**

Why loss & damage compensation matters



Source: World Resources Institute

Lastly, what can be expected from that other financing mechanism, Article 6 of the Paris Agreement aiming to establish an **international carbon market**? At COP26, some of the loopholes in the system were closed in terms of accounting via uniform reporting standards. Finalization of Article 6 guidance is however still expected in order to increase the integrity of the market. Are the recent developments in Canada, Indonesia or Australia hopeful signs to also trigger nations like India and Turkey?

Innovation, innovation, innovation

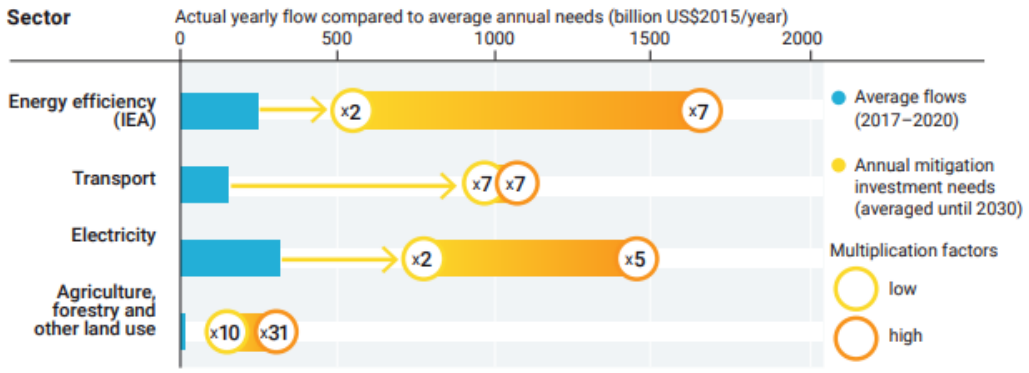
Apart from direct investments, we need innovation to tackle the climate crisis. Estimates from the International Energy Agency state **46% of decarbonisation targets currently rely on technologies yet to be developed, or that are only at the early stage of commercialisation**. So, what can we expect from COP27?

At the COP, interesting innovation news for investors can be found at the **Innovation Zone**. As such, an update on the First Movers Coalition (see previous COP26 article) is something to look forward to. Did the initiative already showcase tangible action or result in change? Next to that, also the Hydrogen Transition Summit will be an interesting side event to monitor more closely.

Another promising thought is the fact that **renewables economics become more favourable year on year**, so energy security ambitions and climate action should indeed go hand in hand moving forward.

Cleantech ambitions in the US, amongst other with the **Inflation Reduction Act**, and renewables investments in Europe via **RePowerEU** are hopeful signs for the future. Also further strengthening of initiatives like zero-emission vehicles or the Global Methane Pledge would be hopeful signs. Furthermore, we should note that most recent climate financing and risk regulation, including the link with financial stability, are promising evolutions which will hopefully be transposed among nations at COP27. According to the IEA, under a Net Zero scenario, we need to drastically scale up investments in low-carbon power, energy efficiency, low carbon fuels and carbon capture as well as EVs, grids and battery storage.

Investments and innovation need to increase if we want to reach Net Zero by 2050



Source : International Energy Agency, 2021

Innovation and financing bring us also to the importance and **role of financial institutions**. Will the Glasgow Financial Alliance for Net Zero (GFANZ) hold ground? Will the initiative be able to maintain its credibility amidst criticism and external pressure? Ahead of the start of COP27, Mark Carney confirmed GFANZ received over 250 science-based interim targets. And will the first movers on taxonomies, capital requirements and mandatory disclosure rules spark other nations or regions to push investors towards more disclosures and integration? Compared to last year, 2022 definitely speeded up actions, so maybe, we can be moderately hopeful?

This brings us to one of the more hopeful aspects of the COP meetings: **collaboration on climate action through the Climate Action/Climate Champions Program**. These events often trigger or advance initiatives between governments or the private sector to accelerate real-world progress on climate mitigation and adaptation. Recent announcements like the Just Energy Transition Partnership or the Debt Suspension and Relief initiatives are good examples of such a collaboration.

Overall conclusion: wait and see, yet again.

All in all, we don't want to get our hopes up for the 27th conference. We can yet again expect some formal and informal announcements. If, by some miracle, COP27 would turn out to be successful, this would mean emissions reductions efforts are strengthened across signatories to close the emissions gap, climate transition financing towards developing countries reaches (at least) USD 100bn per year and an agreement (or financing facility) on loss and damages compensation would be attained.

Apart from this, we do look forward to additional corporate climate announcements, although we do have the feeling companies don't wait for the COP anymore to make bold announcements. Knowing recent years have shown the impact of administration changes to sovereign pledges and commitments, corporate commitments and tangible actions during the year are often more hopeful and worth focusing on in order to keep our hopes up.

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