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Did COP26 discussions deliver on incentivizing sustainable investment?

A few months ago, UN Secretary General Antonio Guterres offered a frank assessment of COP26: the success of these climate discussions, he said, rests on finance.

Research shows that achieving net-zero emissions for the global energy system will require at least US$50 trillion of investment by 2050 and possibly more than US$130 trillion. Increasing government funding will be necessary—but not sufficient. In addition, we must look to private finance, as one of the COP26 goals states, "to turn the billions of public money into trillions of total climate investment."

In financial markets, money gravitates toward investments that balance risk and higher returns. However, financial benefits alone are no longer enough for making investment decisions. Factoring in the cost of inaction rapidly increases the potential economic returns on climate action investment. Deloitte research shows that accelerating the decarbonization agenda could add US$843 billion annually in Europe and US$9 trillion annually in Asia Pacific to the gross domestic product (GDP) by 2070. Governments need to play a key role in ensuring markets are set up to catalyze this new growth.

In recent years, asset owners and managers controlling over US$88 trillion have joined the Glasgow Financial Alliance for Net-zero (GFANZ), a global coalition of leading financial institutions committed to accelerating the decarbonization of the economy. Yet progress is still not fast enough. Already, developed nations have failed in their goal of mobilizing US$100 billion in annual investment in climate action in developing nations. To have any hope of preventing the worst climate damage, capital will need to move much faster — now.

So, at COP26's "Finance Day" on Wednesday, leaders across government, business, and civil society discussed how to drive additional financial commitments and more importantly, how to deliver that capital to where it's needed most. The day brought promising developments on several fronts.

ESG reporting: More transparent and meaningful reporting

To incentivize necessary industry-wide transitions, strong performance on sustainability must be rewarded in the market. The first step is to ensure that measures of sustainability performance are prepared and disclosed to the same level of consistency and comparability as measures of financial performance. Deloitte welcomes a major stride toward that goal with the establishment of an International Sustainability Standards Board (ISSB), to set global standards for sustainability reporting.

The establishment of the ISSB, and the successful adoption of global sustainability standards, will bring clear benefits:

- Global standards respond to global issues and reflect the fact that companies operate and source through global value chains. ISSB's global sustainability reporting standards should reflect the way business operates by encouraging companies to embed sustainability into their operations and enhancing integrated thinking and reporting.
- Global standards help increase the efficiency of capital markets, which are inherently global, by enabling consistent and comparable information needed by capital market participants in making investment decisions.
- ESG investing is growing fast; from 2018-2020, in the U.S. alone, assets managed using sustainable investing strategies grew from US$12 trillion to over $17 trillion—a 42 percent increase. Global standards help enable the deployment of capital to long-term sustainable ventures that support the transition to a low-carbon economy.

Global sustainability standards are an essential part of a systemic change that will be required to create a global baseline of sustainability information addressing the needs of global capital markets. To be effective, the standards will need to be incorporated into regulation around the world, together with associated enforcement, monitoring, governance and controls, assurance, and training. Worldwide adoption of the ISSB standards is needed to achieve true harmonization and to replace the alphabet soup of voluntary standards and frameworks. This would emulate the success of International Financial Reporting Standards (IFRS) that are adopted in 144 jurisdictions.

Mobilizing and accelerating growth of markets to support the race to zero

While globally consistent and detailed reporting is a vital step in the right direction, reporting alone is clearly not enough to transform markets to support the race to zero.

UN Special Envoy on Climate Action and Finance Mark Carney laid out three priorities in addition to reporting for accelerating private finance on climate action: mobilizing capital by connecting ready funding with pressing needs; ensuring the financial sector can manage the risk of the transition to net-zero; and helping to create and identify investible opportunities with solid returns. While acknowledging the criticality of these priorities, the global net-zero transformation must happen at the intersection of public and private finance and requires tactical and strategic policy considerations.

1. Connecting key players

Markets are built on connections—between investors, suppliers, distributors, and customers. So, one way for leaders to accelerate the growth of greener markets is to serve as conveners.

Increasingly, partnerships are emerging to stimulate industry and system-wide changes. For instance, the World Economic Forum's Climate Action Platform has launched 31 projects bringing together leaders across business, government, and civil society to take on a broad range of sustainability challenges, from greening the world's shipping systems to rethinking the future of protein.

Or take the Goal 13 Impact Platform, a project Deloitte initiated in partnership with the CBI, Chapter Zero, A4S, Dell and the Met Office. This platform is a free repository of information on impactful global climate initiatives, designed to highlight significant gaps in progress and encourage more ambitious action. Deloitte expects to see more initiatives like this that help connect the right resources to the right needs.

As more climate financing flows to populations in developing economies and environments experiencing disproportional climate impacts, these collaborative efforts will be particularly important to help ensure local communities have a seat at the table and can help design solutions that truly address their key challenges.

2. Mobilizing for increased climate investments

Finance Day discussions also centered on strategies for decreasing risk associated with new sustainable investments. Governments can seed funding for particularly risky investments, such as early-stage research and the development of green technologies.

Leveraging public-private partnerships, too, can help draw in new private sector investors by introducing mechanisms that help reduce the risk of funding new approaches. Central banks and multilateral development banks can help de-risk investments in sustainable innovation and infrastructure by deploying guarantees, equity, and low-interest or interest-free loans. This could be vital in vulnerable communities, as well as in developing countries and small island developing states.

3. Enabling markets for climate action

Finally, government and regulatory authorities can influence markets in favor of a positive response to climate change through incentives for sustainable activities and disincentives for carbon-generating activities. Such incentives and disincentives typically come through the tax system and are thus generally implemented at a local rather than global level although in some areas such as a global carbon tax coordinated action is likely to be required.

Additional policy levers available to governments are explored in Deloitte's Negative Emissions Systems paper. One option is advancing carbon markets and other innovative market mechanisms that unlock finance for climate solutions. For example, expanded coverage of the European Emissions Trading System will continue to make projects more attractive to private finance and prompt supply chain transformation.

Ultimately, new markets and investments will be necessary. Governments will need to move now to nurture new sectors, lest they be left with nothing to replace old carbon-intensive industries.

Conclusion: What does this mean for business?

In the past, business leaders have often viewed the move to net-zero as a costly and risky challenge. But the Finance Day discussions showed how powerful an opportunity this transformation can be for businesses that get it right.

Stakeholder demands of corporate transparency have changed. So, too, have their expectations for how a company is run—not for profit alone, but with purpose employing sustainable and equitable processes. Global sustainability reporting standards will help businesses meet these expectations and win the trust and loyalty of their stakeholders through transparency and accountability.

Meanwhile, the global push to mobilize green finance can open lucrative opportunities for businesses to collaborate with government and take decisive steps that will make the Paris Agreement goals a reality.

Deloitte research shows the economic growth potential of decarbonization and not just the costs. The sooner the world accelerates this transformation, the sooner it will realize the benefits; thus reducing the adverse impacts on vulnerable communities from extreme events such as droughts, floods and cyclones which destroy livelihoods. Check back next week for an analysis of the progress made at COP26 toward advancing equity and enabling a just transition to a low-carbon future.

Right now, the world is looking for strong leadership to combat this climate crisis. Business has the chance to take up that mantle.

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Find out more:

- Deloitte COP26 Climate Exchange
- Leading in a Low Carbon Future
- Will COP26 incentivize the scale of investment needed and deliver an equitable transition?
- Did COP26 discussions deliver on incentivizing sustainable investment?
- Did COP26 lay the groundwork for a just transition to net zero?
- COP26 has wrapped. What’s next for finance and climate equity?

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