

THE CONVERSATION

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Australian investors want bankable projects that help us adapt to climate change

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Projects to adapt to climate change have come a long way since the 1960s when piles of cars were used to fight beach erosion. Griffith University, Author provided

Australia faces increasing costs of adapting to climate change over the coming years, but new research shows that, despite an appetite from investors to buy green bonds designed to deal with this, there are barriers that prevent this type of financing.

The Griffith University research involved interviews with 29 public and private sector stakeholders representing 25 organisations. These included all levels of government, institutional investors, bankers, insurers, consultants, advisors and legal experts.

In the past few years, the challenges of climate change have become increasingly apparent. The impacts and costs are evident, whether through record-breaking average temperatures, extreme events such as coastal erosion from East Coast Lows, droughts in north Queensland and Tasmania, or floods in Tasmania and Victoria. The need to adapt to climate change is essential, and will be expensive.

Globally, investment in adaptation amounts to US\$20-25 billion, leaving a \$60-\$100 billion investment

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gap. In Australia, the economic cost of natural disasters exceeded A\$9 billion last year alone. It is forecast to rise to A\$33 billion per year by 2050 – according to conservative calculations.

Government at all levels will not be able to pay for adaptation. Therefore, there is a need to think about how best to promote adaptation as an opportunity for the finance sector.

The research shows investors are looking for green bonds that support bankable and scalable projects helping Australia adapt to climate change and mitigate its effects, but that also generate a return on investment. However, there are no agreed ways to demonstrate when a city, infrastructure or coast has successfully adapted to climate change. So not only are there no standards around green bonds for adaptation, these bonds don't exist yet in Australia.

The bonds that governments and corporations use to raise capital for projects are different to bank loans. They are issued over a specific time and have a set face value when issued that is paid back upon maturation.

Most green bonds demonstrate green credentials through projects that reduce carbon emissions, which mitigates climate change. Green adaptation bonds would incorporate elements or projects that “climate-proof” investments or increase resilience to extreme events caused by climate change.

Green bonds have performed extraordinarily well in the market. For example, the global value of these bonds has tripled from to US\$11 billion in 2013 to over US\$36 billion in 2014 and almost US\$56 billion mid-2015. However, there is still a need for these bonds to support adaptation projects in Australia such as seawalls, beach restoration or stormwater upgrades.

A key problem in getting green adaption bonds financed is that the bulk of responsibility for adaptation falls on local governments, which typically do not have the means to negotiate directly with investors, let alone access private sector funds.

Another barrier is that many adaption projects aren't aggregated. The research shows that, to bring adaptation projects to the notice of investors, projects have to be substantial in size – at least A\$20-25 million.

At the moment several large adaptation projects would need to be aggregated to make up a green bond, which are usually issued at around A\$300-400 million. Suitable investments also must demonstrate a cash flow and return on investment, but the size of this is variable.

Yet the research findings still provide some hope that private sector financing for adaptation can become a reality. There is substantial interest and willingness to finance adaptation bonds in the private sector. As one research participant, Emma Herd, CEO of the Investor Group on Climate Change (IGCC), stated:

“Investors know that a certain level of climate change is now locked into the system and will increase the physical risks and costs for business, infrastructure and the economy. Investing today to increase resilience to the physical impacts of the future is critical for reducing the costs of climate change.”

In addition to this, private sector financiers in Australia already have some experience dealing with the risks posed by climate change, often as part of their environment, social and corporate governance requirements. Investors can build on this existing knowledge and protocols to seek out the opportunities represented by adaptation bonds.

All of this is backed up by Australia’s strong track record in climate finance. For example, the Victorian government and the National Australia Bank (NAB) are recognised leaders in the development of large-scale climate or green bond investment, along with the likes of the European Investment Bank. NAB issued Australia’s first climate (certified) bond in 2014, while the Victorian government recently **made headlines** as the first state or federal government in the world to issue a climate-certified green bond.

The research calls for rethinking and reforming partnerships between local and state government and private sector investors. An example is amending treasury standards to allow local governments to work with the private sector for investment. It also highlights the need for developing adaptation bond standards.

In some cases, a combination of public and private funding may be the only way forward. Still, any private sector investment is a way to stretch public money for adaptation further, something that will be increasingly important over time.

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