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Fitch: ESG-Labelled Debt Can Address Climate Funding Gap in Infrastructure

Fitch Ratings-Hong Kong/New York-02 August 2021: Issuance of green infrastructure and project finance bonds is expected to rise as more governments adopt a net-zero carbon emission target by 2050, says Fitch Ratings in a new report. This will be supported by strong investor demand for ESG-labelled bonds. We believe the bulk of financing required to address climate transition and adaptation will be allocated to sustainable infrastructure assets, such as renewable energy, and to upgrade existing assets to function in a 2°C temperature increase scenario.

The achievement of net-zero emissions by 2050 will require a plunge in fossil-fuel consumption. This will affect infrastructure associated in the production, transport and use of fossil fuels and could constrain medium- to long-term profitability and capital access for infrastructure asset owners. Fitch considers oil production and refining, liquids transportation, oilfield services and coal-fired power generation to be highly vulnerable to climate-related financial risk.

Climate change mitigation could require investment upwards of USD13 trillion by 2030, but the International Energy Agency estimates that current investment levels are one-third of that required. Infrastructure also faces adaptation costs for the physical risks caused by climate change. Changes in precipitation, temperature, sea levels and more extreme weather events can affect the operation and performance of infrastructure assets. Roads, railways, airports, seaports as well as coastal and urban infrastructure are among the most exposed sectors.

There has been consistent demand for high-quality green bonds in recent years. Green project finance bonds can limit an investor's exposure to non-green activities compared with green corporate bonds, where the issuer may have carbon-intensive operations outside of the bond's specific use of proceeds. As banks increasingly impose negative screening policies on fossil-fuel related activities, reallocation of capital towards sustainable investments can meet requirements under new climate-focused financial regulations.

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