Financing the Energy Transition

The Paris Agreement was signed in 2015 by 196 countries, including Trinidad and Tobago. In the landmark document, countries pledged to reduce their greenhouse gas (GHG) emissions to limit global warming to below 2º Celsius relative to pre-industrial levels.

The Paris Agreement acknowledges three key elements that are critical to ensuring a just transition that supports less-resourced and vulnerable countries – finance, technology, and capacity building. Finance is needed immediately to enable mitigation, to reduce GHG emissions; and adaptation, to reduce the impacts of climate change. Finance underpins technology and capacity building as all aspects of the energy transition come at a cost.

Countries, corporations, financial institutions, intermediaries as well as non-profit organisations in the public and private spheres, are responding to the increasing requirement for green financing. This response is driven by consumer demands in tandem with organisations' thrust towards sustainability.

Green and sustainable financing options

Non-profit and community-based organisations in Trinidad and Tobago can access financing for green projects from the country's Green Fund. Organisations can also access grant support from international organisations such as the Inter-American Development Bank (IDB). From 2015 to 2020, the IDB's Infrastructure and Climate Change and Sustainable Development Sectors invested US$813.23 million in green and green-grey infrastructure projects. Green-grey infrastructure development is a hybrid approach that employs traditional engineering methods such as revetment walls and dams, as well as green methods including mangroves and forests. At COP 26, the IDB announced its target of US$24 billion of green financing including biodiversity financing. In the United States, most government departments offer funding for green projects, such as the Environmental Protection Agency (EPA) which has provided a wide range of grants for green infrastructure projects. The UK government has made over £5 billion available to help businesses become greener.

Green bonds, social bonds, sustainability bonds and sustainability-linked bonds (SLBs) are rapidly emerging as popular forms of sustainable financing. Green bonds are fixed income securities used to fund environmental and climate projects. Green bonds usually have long maturity periods and offer tax incentives to investors. Similarly, blue bonds are debt instruments which are issued to support investments in healthy oceans and blue economies.

Social bonds are similar to green bonds but are geared toward development of social projects. Sustainability bonds seek to raise funds for both social and environmental initiatives. Regarding SLBs however, funding is usually linked to specific sustainability targets established by the issuer that can impact the entire organisation. There are usually premiums or penalties to be paid if the issuer does not meet its sustainability targets.

Funding can also be accessed through commercial banks and other international and regional funding agencies such as the World Bank and the Caribbean Development Bank.

Risks associated with sustainable finance

The sustainable financing industry is not without risks, not least of which is the threat of 'greenwashing'. This happens when bond issuers mislead investors by overstating the environmental benefits of their activities. There is also a risk related to a reliance on ESG ratings in which companies are ranked based on their ESG performance. These scores are widely inconsistent since performance can be measured based on the potential impacts of ESG factors on the issuer, rather than the impact the issuing company can have on the environment and people.

Sustainable financing comes with inherent investment risks that projected returns may not be realised. These risks are exacerbated by the fact that sustainable financing is a relatively new field and investment periods are generally long. Targets are set with imperfect information and in some cases, may prove to be unrealistic and unachievable.

One of the most serious risk elements associated with sustainable financing is that the industry is essentially unregulated. The International Capital Market Association (ICMA) has issued guidelines for green, social, sustainability, and SLBs. The guidelines are built on four principles:

- **Use of proceeds** – It is imperative that the proceeds of green bonds be used for green projects that provide clear and quantifiable environmental benefits. Projects can involve renewable energy, energy efficiency, prevention of pollution, biodiversity on land and in the water, clean transportation, wastewater management, climate change adaptation, circular economy products, technology and processes, or green buildings.
- **Process for project evaluation and selection** – The issuer should clearly state the objectives of the project and the processes by which projects will be identified as well as the selection and exclusion criteria.
- **Management of proceeds** – As long as the green bond is outstanding, the issuer should disclose periodically, how the green account is being reconciled against project expenditures. Unallocated balances should also be disclosed.
- **Reporting** – Issuers are to report annually on the amounts allocated and the performance of eligible projects using both qualitative and quantitative metrics.

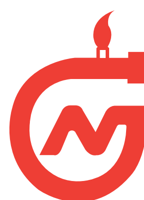
The World Bank has issued similar guidelines. However, these guidelines are voluntary and not legally binding.

Is sustainable financing worth the risk?

At NGC, we believe that the opportunities far outweigh the risks. Within sustainable financing there is the opportunity for introducing standards to govern sustainable financing, eliminating the practice of greenwashing, making a real impact on the economy, society, and the environment, and of course, doing it all profitably.

In 2021, NGC made its first venture into the sustainable financing arena with the introduction of our Sustainable Investment Initiative. Under the initiative, the Company is diversifying its investment portfolio to include investment in green funds. The Company is currently assessing opportunities to expand the initiative through direct investments in environmental projects. In the absence of industry standards, NGC analyses potential sustainability investments with the same degree of rigour with which the Company evaluates all its investments. Relevant best practices are applied.

The energy transition is no longer approaching. It is here. While NGC continues to grow its core business built on the transition fuel of natural gas, the Company is investing in its own future and that of Trinidad and Tobago. We acknowledge the challenges that the energy transition will bring, and we are pivoting and positioning ourselves to overcome those challenges.



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