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International Dimensions of Industry Decarbonization: Elements for International Cooperative Approaches

Summary of the Workshop, 03rd March 2021

SNAPFI Project
EU Study 2020-21

The workshop took place as part of a DIW-IKEM led study to address the topic of industry decarbonization, mainly focusing on its transnational implications and on the possibilities that arise for international cooperation in the context of international climate finance (ICF). While there is increasing clarity on concepts for such partnerships and coordinated action, a few issues stand out as being unresolved till date: these are intertwined questions related to combinations of obligations and incentives to participate in such arrangements, necessary political conditions to partake, and the role of international climate finance (ICF).

The 90 min workshop which took place on March 9th 2021, aimed at taking a deeper look into those unresolved issues. It brought together 20 experts from various countries and institutions and was structured into two main discussion rounds. The first addressed the political conditions of a transnational partnership. The second focused on the role for international climate finance. The results of the two discussion session are presented at continuation. The input presentation by Heiner von Lüpke (DIW, IKEM) provided an overview on partnership approaches for industry decarbonization and is distributed with the present workshop summary.

First discussion session: Political Conditions for international partnerships to support industry decarbonization

First, with respect to political conditions of transnational partnerships, four aspects were concentrated on: 1. the conditions under which an agreement comprising incentives as well as obligations becomes politically acceptable, 2. the role of political situations in individual countries, 3. the motivations for countries to join such cooperative approaches and 4., the way in which those motivations are influenced by the emerging international norm of climate neutrality in industry.

A good starting point for policy design was argued to include creating momentum with a mix of incentives and attractive to comply with obligations . This could build on and support the further development of an existing long-term vision. Institutional development, research and industry roadmaps can create momentum and help build coalitions, which consequently give impulse for governmental action. An important driver for action is the focus on benefits, capacity and institutions, whereas concentration only on negative factors (e.g. carbon leakage) may become a disincentive.

A participant noted that for many developing and emerging economies there are still challenges to meet existing safety or environmental obligations. If climate policy is merely seen as the creation of additional decarbonisation obligations it may be very challenging. In regard to the choice of appropriate policy tools, it was referred to Iacobuta et al. (2018), stating that carbon pricing may not be the main instrument for "emerging economies". Starting with incentives that encourage innovation and small reduction steps would be better received and could provide big opportunities for SMEs. It was pointed out that negotiations with larger industry actors would presumably be tough for legislators.

In this regard, a participant pointed out with a view to the situation of emerging economies that some industries will be in favour of having such an international partnership involving governments and industries with a good mix of incentives and obligations (typically, companies that already operate internationally). However, according to the expert, the majority of companies might be very reluctant. Thus, discussion and consultation between industries and government have to be continuous so that both sides understand each other and can find common solutions. This is particularly relevant if also interactions with the international community are envisaged.

It was added, that the most sustainable political motivations for governments, producers and service providers arise when they are demand driven. Thus, the education side to influence policy should not be neglected.

Building on this dialogue topic, a participant brought up the idea of putting the industry actors in the "driver's seat" as they possess technical expertise and knowledge of the most effective channels for decarbonization. Otherwise, industry is left to merely react to external decisions. Apart from that, the participant commented on a sectoral approach for the study, encouraging to outline a clear rationale, which should take into account supplier substitutability on national and global scales, technological homogeneity and possibility of multiple jurisdictions for cross-border operations.

It was stated that buy-in of the industry to the objectives and participation in the process is important. However, for an initiative in a specific sector it is important not to forget that relevant actors may also be outside of the sector. In South Africa, for example, an agreement without labour unions would not be successful, which gives an example that societal structures of the individual partners really have to be taken into account.

Another issue that drew the attention of the experts were carbon border adjustments. In some emerging economies, the carbon border adjustment mechanism (CBAM)[1] is largely criticized. According to participants, this is, among others, due to the fact that companies are very different in their ambition level (even within one country). Thus, the EU needs to make sure that "good" companies are not grouped together with less ambitious companies. It was argued that rather than penalizing countries with a carbon border adjustment, it should be searched for ways to incentivize the companies and make sure that ambitious companies are not penalized. This becomes even more crucial as some voices in the US have now also indicated interests in carbon border adjustment mechanisms. It was recommended exploring the case of ArcelorMittal´s commitment to be carbon neutral by 2050 in Europe, but not in South Africa, in order to gain knowledge on the reasoning and possible implications.

Second discussion session: Role of International Climate Finance to support industry decarbonization

Regarding international climate finance, three aspects were addressed: 1. the suitability of finance instruments in the context of a transnational partnership approach, 2. the suitability of finance instruments in specific policy contexts and 3., the conceivable governance structures for transnational partnerships.

In the context of a transnational partnership, it is essential that an instrument be chosen considering both recipients' and financial institutions' interests. This raises the question of what instrument (mixes) may be best suited for such partnerships. A participant suggested the first step would be to gain an understanding of who the main actors would be, since financing needs would vary greatly depending on the type of actor. For example, it would be much easier for large multinationals to have access to financing from banks or international finance institutions than it would be for SMEs.

A participant argued that emission attribution is paramount to any partnership approach. Indeed, as financial actors are increasing their climate commitments, banks need to be able to attribute emissions to particular actors. In the context of partnerships it would then be of particular interest for the financial institutions to be able to attribute reductions in emissions to specific actors.

Those points were supplemented by two observations in relation to an existing international partnership. The participant first observed that, in addition to the diverging financial needs of industry players, the financial needs of individual countries were also quite different from each other. For developing countries for example, the cost of capital is very high, which means

[1] The CBAM is proposed by the EU as part of the Green Deal: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12228-Carbon-Border-Adjustment-Mechanism

financing is a bigger challenge there. Further, it was observed that there are a lot of countries who are looking for ways to come together and fund demonstration projects. However, it was also mentioned that some of the international finance institutions need to come onboard stronger as well.

Next to taking into account the different players, an instrument should also be chosen considering the political context of a specific country. In order for this to happen, a participant underlined the importance of creating an environment in which companies are willing to constructively engage in the design of a policy framework for low-carbon development. This will involve both initiatives to outline pathways, but could also be part of a broader political discourse for the structuring of fair transition opportunities.

More specific visions for finance instruments that could help operationalize an alignment with domestic policies were given: First, it was referred to the Green Growth Equity Fund, which has been launched in 2018 by the National Infrastructure Fund of India and the UK government. The fund provides investors with a vehicle to invest at scale into clean energy projects, taking care of the assessment and verification of projects. It was also argued that performance-based instruments could be particularly suited for this task - not only on a project level, but also for a broad industry approach. Policy-based lending was mentioned as an example. Such instruments have the additional benefit that they are easier to align with the financial institutions' interests.

Another crucial question is what the governance structure of such a partnership would look like and how finance could best be coordinated for harmonized contributions. The fact that governance structures are often an issue was outlined by a participant. It was specified that questions of design and the composition of the body - i.e., who pays for activities, who holds the secretariat, etc. - would need to be carefully addressed.

Next steps for the study subsequent to the workshop: The study report will be launched during a workshop during the second half of July 2021. Invitations will be distributed beforehand.