

When is it green? Bridging the gap of green bond standards between China and the West

A difference of ideology between China and the West has existed since the dawn of green finance. But now, it has become an issue that we have to solve. Since the launch of the labeled green bond market in 2015, China has maintained a steady growth trend in issuance. However, due to the difference in green bond standards and issuance regulation rules, disputes have arisen between China and the West about what is required to earn the label of green. Based on the different perspectives on the concept of ecological civilization we will try to identify the major differences between China and the West, and make suggestions for a better coordinated development of the global green bond market.

I. Green bond standards under different ideologies: More similarities than differences

Green bonds are an effective way to internalize the environmental externalities. In comparing the Chinese and western green bonds standards, the first step should be to understand the ideology behind them. For a long time, the ecological criticism in the West attacked the importance of economic development on behalf of climate change. From the perspective of human development and the welfare of the citizenry, China improved the ecology with the dialectic thinking of development while emphasizing a harmonious coexistence of man and nature. Due to the differences in stages of development, China and the West have varying views on ecological civilization, governance methodology and development priorities. However, both the theories from China and from the West explore the relationship between human beings and nature, which should make it possible to get a coherent ideology to resonate between the two .

i. Ecocriticism theory and green bond standard in the West

At present, the western concept of ecology and environmental economy originates from ecocriticism. Ecocriticism derives from 1970s United States when "nature" was taken from the background of human development and put at the front. After half a century

of continuous discussion, ecocriticism today is based on realistic concerns, responsibility and ethical care. It includes literary criticism of unsustainable development concepts like "developmentalism" and "science and technology first", which has played an important role in the western idea of ecological civilization.

The construction of an ecological civilization in the West focuses on adjusting the relationship between human and nature. It emphasizes the concept of low carbon, environmental protection and sustainable development, but it fails to include the human economic activities where ecological benefits are not clear. The formulation of current western green bond standards also reflects such characteristics. In 2014, the *Green Bond Principles* issued by ICMA divided the principles into four parts, including Use of Proceeds, Process for Project Evaluation and Selection, Management of Proceeds, Reporting. The Climate Bond Initiative (CBI) has issued the *Climate Bond Standard*, which divides the projects based on climate effects from two aspects: climate change mitigation and adaptation. On some of the definition issues, such as coal-related projects and the proportion of proceeds used into green bond projects, western society and markets stand firmly on pursuing environmental benefits. In terms of the current level of economic development and environmental protection in western developed countries, such standards-setting not only conforms to the actual situation, but also maintains relative "political correctness" in the mainstream public opinion due to the criticism of "developmentalism".

ii. Standard setting of Chinese green bond: an assessment of China's national conditions

The concept of ecological civilization construction in China originates from the judgement of the contradictions in current society. In the report to the 19th National Congress of the Communist Party of China, it was pointed out that what the country now faces is the contradiction between unbalanced and inadequate development and the people's ever-growing needs for a better life. Economic development and ecological civilization are two important aspects that affect the welfare of the whole society. The relationship between them should be unified in order to build a modern harmonious coexistence between human and nature. We should not be partial to one aspect over the other.

By choosing the path of ecological civilization, China pays more attention to practical rationality. Considering the present level of development and the existing resources, China should adopt a progressive development mode, but not an aggressive one. As for the green bond market, China has focused on key areas of the economy for green transformation and green industry financing, and formulated China's green bond standard from a developmental and dialectical perspective. For example, the *Green Bond Endorsed Project Catalogue (2015 Edition)* include coal projects in its current form. The threshold proportion of proceeds invested in green projects are not unified among different types of bonds, but the minimum cannot be lower than 50%. For asset backed securities, either the asset pool or the use of proceeds is green can the ABS be verified green. Green bond standards in China have maintained a timely trend in the long term and appropriate revision based on national conditions. Such mechanisms may not be totally suitable for the western society. But, according to China's current conditions and its development stage, the country should strive for a more effective and a larger supply of green capital and increase the supply of innovation to promote the green development of the economy. Only in this way can China achieve the absolute green goal.

iii. Few differences between Chinese and western green standards, Chinese experience deserves more respect and understanding

The ideas of ecological civilization in China and the West are both based on its own economic structures and hypotheses of homo economicus, in order to correct the dislocated relationship between human and nature in the process of economic development. However, there are still differences between China and the west in the extension of ecological civilization construction. In the white paper, *The need for a common language in Green Finance* jointly issued by China Green Finance Committee and the European Investment Bank, the green classification in China is highly consistent with the standards of the European Investment Bank. The only difference is that the Chinese standard has a broader definition of "green", including projects with insignificant climate effects but significant environmental benefits, such as clean coal, ultra-high voltage power stations, underground pipelines and green plant construction.

China's definition of green bond comes from an understanding and the practical rationality of China's economic structure. In view of the resource endowment of China, "rich coal, meager oil and deficient gas" is the energy structure of China which is different from most western developed countries. Although with the development of renewable energy, the overall energy structure in China is evolving in an efficient, clean, diversified and intelligent way, it is still difficult to get rid of the dependence on fossil energy in the short term, and hard to realize the leap-forward adjustment of energy structure.

China's economic growth rate is at a high level, but there is still a gap between the level of development in China and that of the West. The switch to high-quality economic development with more attention on the value of ecology and environmental productivity is undoubtedly an important breakthrough in for China's economy transformation. However, green industry is at a natural disadvantage in the capital market due to its longer return cycle and lower profits. Therefore, China should not take the absolute and perfect "green" as the only measurement standard and apply it to all industries and enterprises, but guide the real economy to turn "green". Given the current development situation, China's experience in green bond deserves respect and more understanding.

II. How to evaluate China's green bond market

Practical and realistic should we be to evaluate any green bonds market. In this case, a full consideration of the market's development and transition is needed. After three-years development, the Chinese green bond market has a large volume and covers a wide range of industries. Besides, China has offered a lot of supports and helps for renewable energy development and infrastructure construction in countries along the Belt and Road.

i. An overview on China's green bonds market: big, wide and advantageous

China is one of the earliest countries that set up a green finance policy framework. Through top-down policy transmission and market incentives, China's green finance market developed rapidly. Today it covers a wide range of sustainable development

finance areas. Assessing the practice, China began to issue green credit focused on energy efficiency in 2006. Up to now the total scale of green loans held by 21 major commercial banks in China has exceeded RMB 10 trillion, accounting for nearly 10% of total scale of loans.

China's green bonds aligns with international practice on the management of proceeds, information disclosure and external authentication. Since the labelled green bonds market was started at the end of 2015, China has maintained a yearly issue scale of more than RMB 250 billion and a grand accumulated issuance of nearly RMB 800 billion. China is the second largest green bonds issuer in the world with rapid growth, while supporting projects covers 6 categories and 31 sub-categories in the green bond catalogue. Additionally, China issues cumulatively billions of dollars of green bonds in foreign markets to support infrastructure construction and renewable energy development in countries along the Belt and Road. Moreover, it is worth pointing out that China's green corporate bonds has an advantage on issuing coupon rate, which reflects China's capital market's enthusiasm on green development.

ii. Divergence on China's green bonds practice

When evaluating China's green bonds practice, there are two issues that are mainly criticized by western countries. One is the usage of green funds on coal, the other is allowing part of green proceeds into general usages. As mentioned before, these divergences are essentially caused by the differences in the development path and stage between China and the West.

a. Clean coal: 3% of green proceeds lever 40% of emission reduction per unit of GDP

Whether green proceeds should be invested into fossil fuels is the quintessential disagreement between Chinese standards and international ones, taking GBP and CBS for instance. It is also the focus of the argument about 'absolute green' and 'relative green' between China and the West. Indeed, fossil fuel will never become the best solution to China's energy issue, but it is a necessary element in optimization of people's welfare under the current energy structure. Since it is infeasible to give up fossil fuel for a short time, it is undisputedly beneficial for the environment to upgrade the energy efficiency of traditional heat-engine plant

and to transform traditional coal into clean coal.

In fact, there are few green bonds used to support clean coal in China. Among 230 labelled green bonds issued in China since 2018, a total of 9 green bonds were issued for clean coal mining, washing, desulfurization projects, with a total amount of RMB 11.92 billion; this accounts for a mere 2.96% of the total issuance. Despite the rising trend in China's carbon emission, it is proved that China's carbon emission reduction is obviously effective with a lower emission growth rate aligned with the goals of World Climate Conference in Copenhagen.

At the conference, China has promised to reduce its unit GDP emission intensity by 40% to 45% by 2020. Finally, China finished the goal ahead of schedule by promoting the usage of clean energy.

b. Green proportion of proceeds: diversified issuing system in China and indistinctive evaluation framework in the West

The proportion of proceeds used in green projects is the argument between the 'absolute green' in the west and 'relative green' in China. CBI requires that 95% of the proceeds raised by a climate bond must be used to support climate projects. In China, different regulations are used for different types of issuers. For the green financial bonds issued by financial institutions the proportion should be 100%. For green corporate bonds, the proportion should be at least 70%. While for green enterprise bonds, the proportion should be at least 50%. Behind this balancing act is the dilemma between protecting the environment and developing real economy. Green bonds should not only be green, but have a supportive function of the sustainable development of the real economy as well. Under the framework of pure green proceeds, green bonds issued by entities can only support existing projects with no benefits on its survival and sustainable operation.

The criticism under the 'absolute green' would cause serious distortions to the Chinese green bond market. Since 2018, 230 labelled green bonds (excluding green ABSs) have issued in China, with a cumulative amount of RMB 402.972 billion raised. If we were to exclude all bonds with a proportion lower than 95% or supporting projects including coal-related industry and large hydropower station, only 142 bonds would be aligned with those conditions among the 230

bonds, of whom only 61.74%. While the truth is, there are RMB 364.093 billion, 90.35% of the amount raised by all the domestic labelled green bonds in China, that is used for green projects rather than general usages such as working capital or repaying non-green loans.

iii. Look at the Chinese contributions in the right context

The high-quality development of China's green bonds market needs a global platform, while growth-timid global capital market needs Chinese opportunities. Differentiated tolerance and strictness should be the cornerstone in this age of sustainable development. Whether seeking common ground in ideology or finding compatibility in developing capital market, China should be encouraged and advocated for, as a new player in the global green bonds market.

The chasing of high-quality assets is becoming harder in a time of negative interest rate policy. Green industries are going to become a new economic growth engine. They could also become a quality asset favored by capital markets owing to its internalization of externalities of environmental risks and benefits. Moreover, the development of green assets demands the support of cross-border capital flows and financing assurances from highly developed green bonds markets in both China and the West. Therefore, China and the West should be mutually respectful and trustworthy in the construction of an international green debt market, seek common development on the base of the common needs.

III. How to explore the similarities of green finance between China and the West

At present, the global ecological problems are serious and the need for sustainable development is urgent. The global market has gradually developed and matured, and the relationship between development and ecology has been straightened out rapidly as well to pursue the harmony between man and nature. However, there are divergences in the pursuit of harmony. Reaching a consensus of "joint harmony under different perspectives" is the way to develop green industrials and seek out common ground. A quick, four-step guide to that goal:

(1) Establish a platform-based leadership mechanism

At present, there are various participants in the global green bond market with sovereign governments and international institutions coexisting. The consensus among the parties is a difficulty to form an overall market consensus. Therefore, a unified leadership mechanism should be established to guide international institutions, issuers and other green debt market participants through platforms. For example, according to Network for Greening the Financial System, we could seek out a common language of global green finance. Undoubtedly, the platform-based leadership mechanism should be built on a consensus of harmony and diversity, allowing to pursue equal results in different ways.

(2) Enrich application of instrumental translation

Currently, there are multiple sets of classification and implementation standards around the world for the definitions of green bonds, which are constantly revised with the development of the market. China's green bond standards are also developing and constantly optimized with the evolution of the market. We should establish a translation mechanism under the existing standards, as well as a contingency mechanism to adapt to the changes of standards. In order to ensure the effective adaption of standards and the rapid transformation of standards during their evolution, we should pave the way for cross-border capital flows and high-quality opening. It is worth mentioning that the Green Finance Committee of China and the European Investment Bank have proposed to build a "Rosetta Stone". They also recommend deploying the transformation and translation means to achieve the consistency of standards through the release the white paper *The need for a common language in Green Finance*. Similar means should be mainly used by China and the West to explore a common language of green finance.

(3) Strengthen the practice of market-oriented cross-border issuance

We should further encourage high-quality opening of capital markets and promote cross-border capital flows. In cross-border capital financing, green bonds play a leading role in both ways, attracting global investors' attention to China's green industry as well as guiding domestic financial institutions to invest in green areas in countries along the Belt and Road Initiative. The flow of capital is an effective way to achieve mutual recognition of standards through practice. At present,

Moody's and other international institutions have expressed their preference for China's green bond market. The opening of China's capital market, it is expected to attract more international institutions to invest in China's green bond market and issue green bonds in China.

(4) Clearing the confusion of standardization

There is a wide range of differences in the concept of environmental benefits and climate effects between Chinese and western green standards. It is more difficult to distinguish the industrial boundaries contained in each concept. In this context, it is significant to clarify the confusion of concepts. It is also significant to promote the common concept of green finance based on harmony and diversity, and seek the consensus of capital market for standardization.