

# Observations on the financial system as it relates to the Paris Agreement

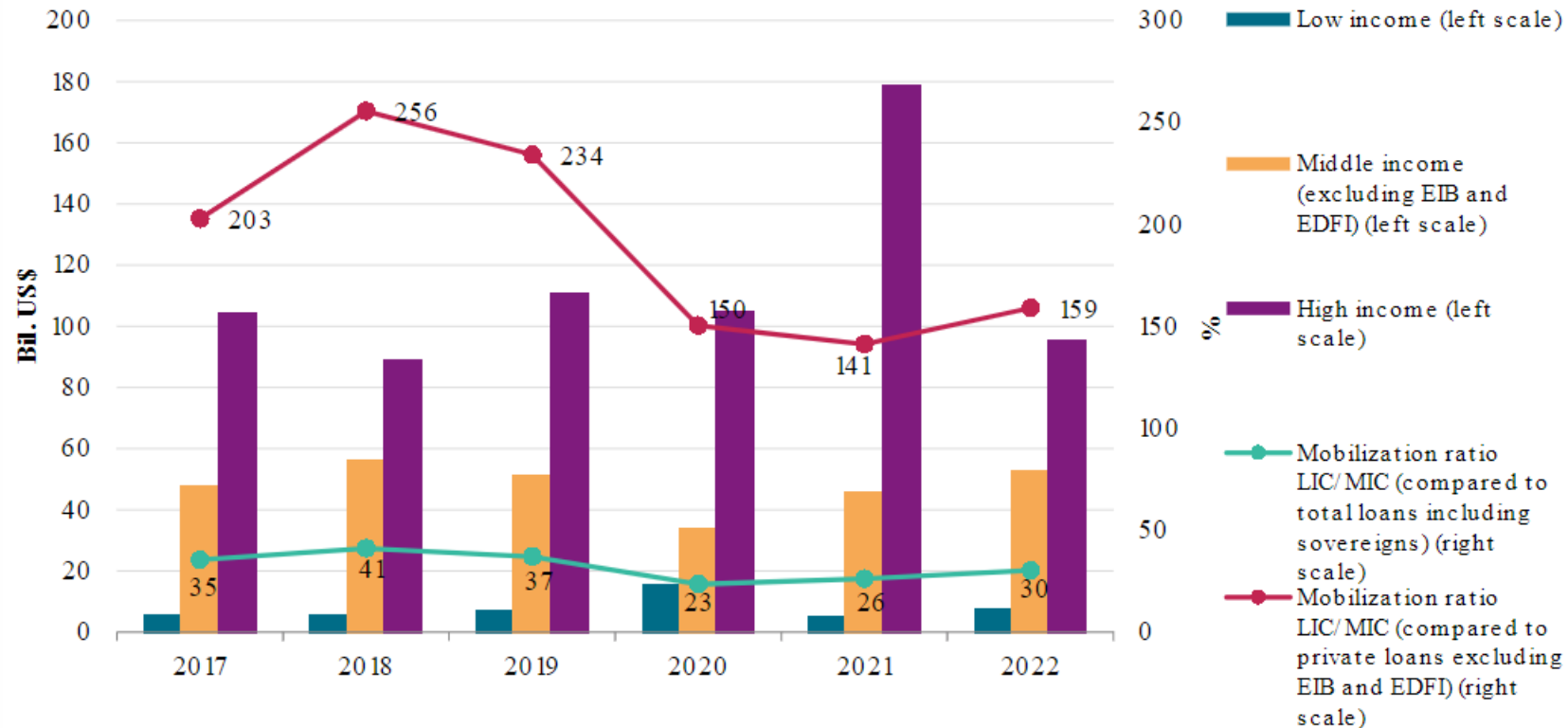
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# Private Capital Mobilization is not Happening at Scale, in particular in Low and Middle Income Countries

Mobilization of private sector by country income level



EIB--European Investment Bank. EDFI--European Development Finance Institution. LIC--Low-income countries.

MIC--Middle-income countries.

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Source: S&P Ratings 2024.

# International System Roadblocks Are Well Established

## Bankable Projects

There are opportunities, what is needed is more technical assistance at all levels and capacity building (including on institutional frameworks).

## Asset and Liability Mismatch

This mismatch is limiting access to finance and generating risks that are difficult to mitigate:

Domestic Capital

Foreign Currency

Transfer and Convertibility Risks

Small Scale Loans

## Catalyst Capital & De-Risking

More First Loss, would allow a greater mobilization multiplier effect

## Standardization

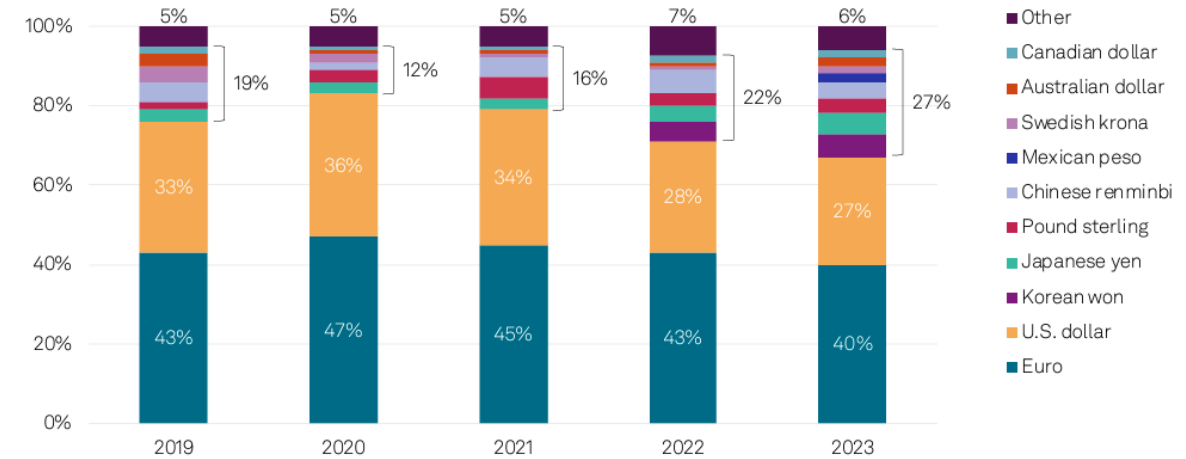
Lack of individual project standardization that would allow for scaling.

Lack of structures pooling assets to deliver size & diversification, to comply with large investors investment needs.

# Other Developing Opportunities For Capital Mobilization

- More effective cooperation across stakeholders, the cultural gap between MDBs and private sector is among the roadblocks to unlock blended finance potential
- Label debt market is gradually expanding across EMDEs, allowing to broaden investor base and channel capital towards projects which support climate transition and adaptation.
- Development of local and international taxonomies is supporting enhance transparency and standardization

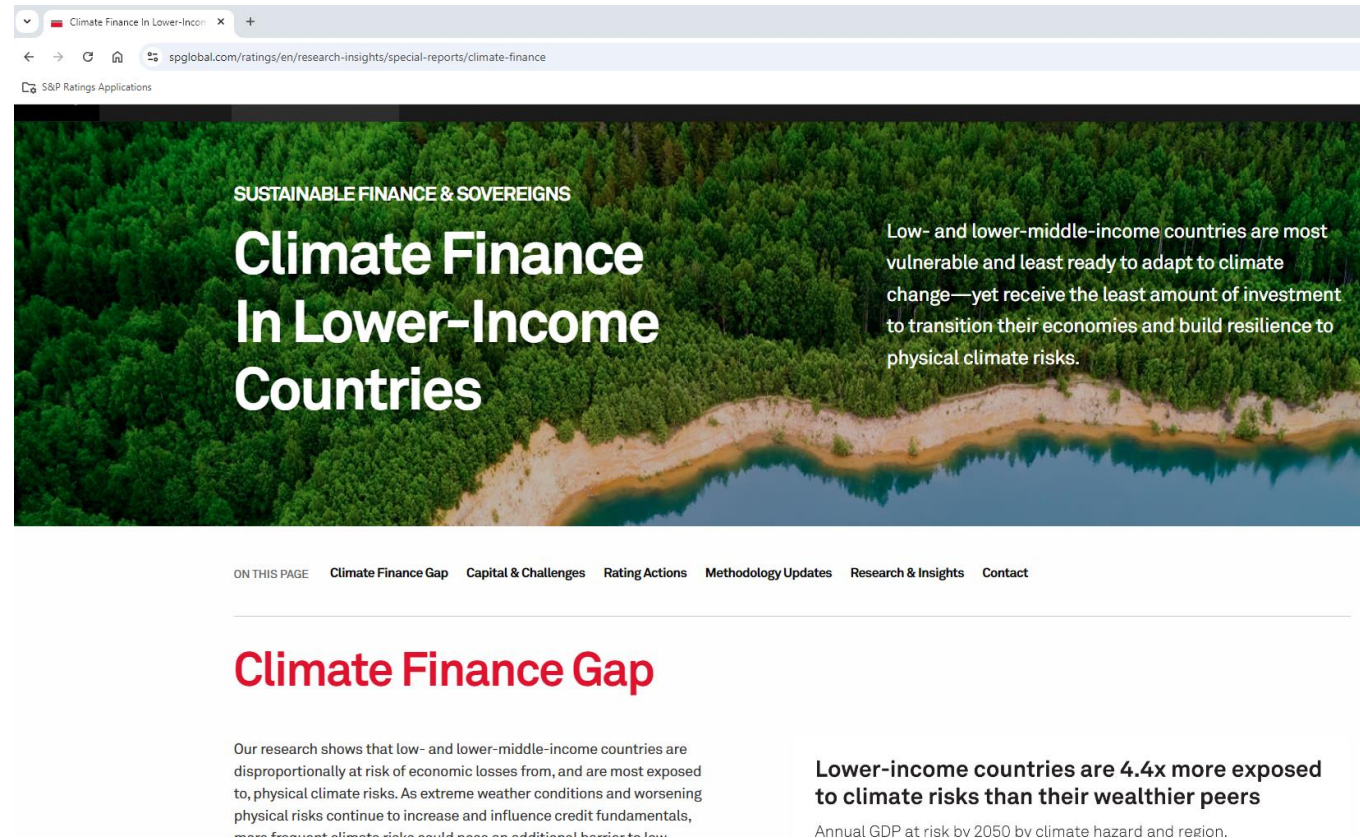
Sustainability Labelled issuances are denominated in an increasingly diverse set of currencies



\*Other\* represents all currencies in which GSSSB issuance is less than 1% of global annual volume. Excludes structured finance. GSSSB--Green, social, sustainability, and sustainability-linked bonds. Sources: Environmental Finance Bond Database. S&P Global Ratings. Copyright © 2024 by Standard and Poor's Financial Services LLC. All rights reserved.

# S&P Global Ratings wants to be a stakeholder, while keeping in line with our Mandate to Provide Independent High-quality Ratings

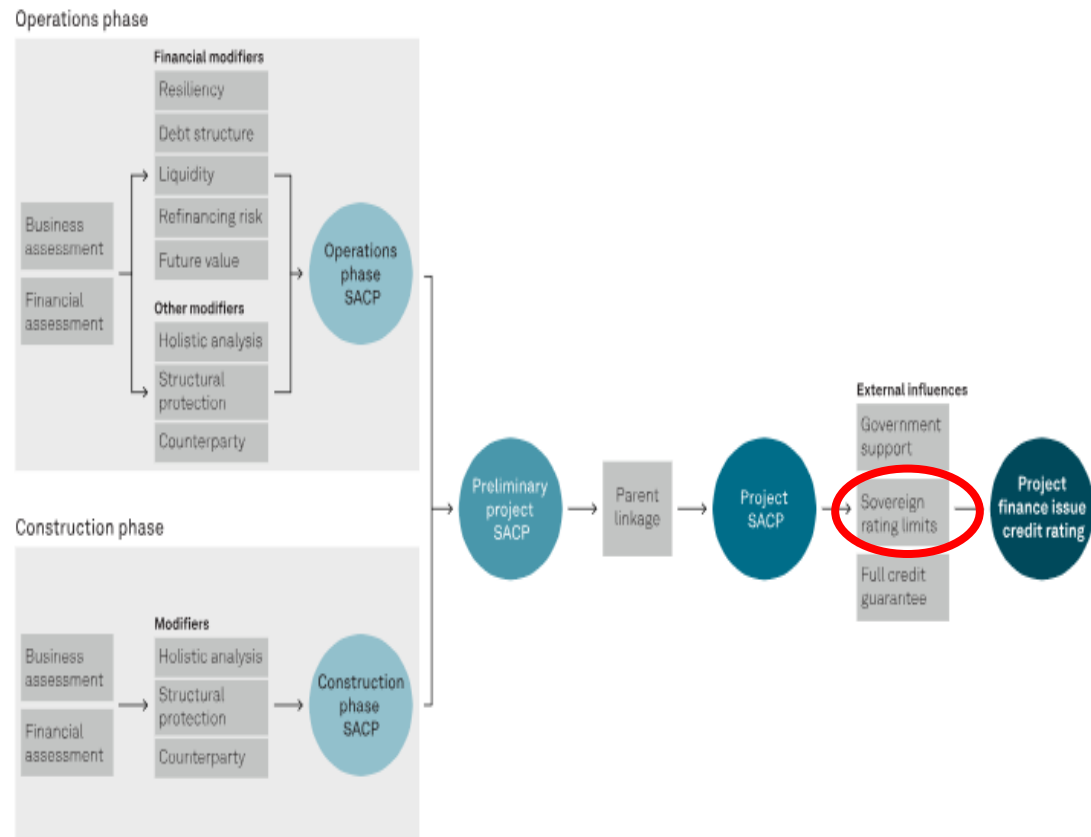
- From a credit rating agency perspective, we have set up **a dedicated task force** on the Climate & SDG Financing gap topic to engage with Stakeholders with a view to.
- Identify roadblocks, produce research, enhance rating transparency, provide our rating perspective where valuable, ensure that our ratings methodologies are on top of recent developments.
- We are looking for more data on default and recoveries of project finance and corporate lending in developing economies
- We have also changed our organization to be able to rate in a timelier way innovative transactions, including blended finance ones.



The screenshot shows a web browser window with the URL [spglobal.com/ratings/en/research-insights/special-reports/climate-finance](https://spglobal.com/ratings/en/research-insights/special-reports/climate-finance). The page features a large green forest background with a river. The main heading is "Climate Finance In Lower-Income Countries" under the sub-heading "SUSTAINABLE FINANCE & SOVEREIGNS". A text box on the right states: "Low- and lower-middle-income countries are most vulnerable and least ready to adapt to climate change—yet receive the least amount of investment to transition their economies and build resilience to physical climate risks." Below the image is a navigation menu with links: "ON THIS PAGE", "Climate Finance Gap", "Capital & Challenges", "Rating Actions", "Methodology Updates", "Research & Insights", and "Contact". The "Climate Finance Gap" link is highlighted in red. Below the menu, the "Climate Finance Gap" section is visible, starting with the text: "Our research shows that low- and lower-middle-income countries are disproportionately at risk of economic losses from, and are most exposed to, physical climate risks. As extreme weather conditions and worsening physical risks continue to increase and influence credit fundamentals, more frequent climate risks could pose an additional barrier to low-". To the right of this text, a bold statement reads: "Lower-income countries are 4.4x more exposed to climate risks than their wealthier peers", followed by the sub-text: "Annual GDP at risk by 2050 by climate hazard and region."

# Project Finance Rating & Country Risk– We first analyze the project standalone characteristics and simulate a Sovereign Stress to assess if a Project can be rated above its Sovereign

## Project Finance Criteria Framework

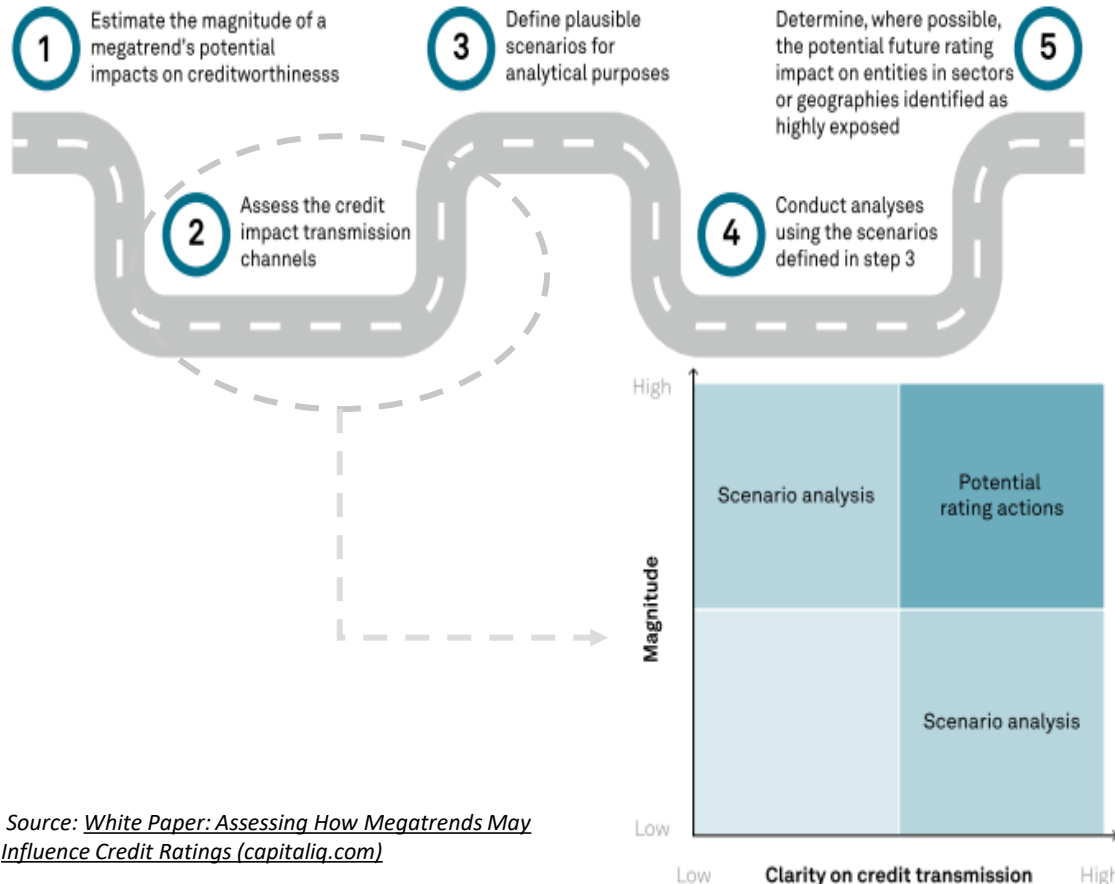


SACP--Stand-alone credit profile.  
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- **Historical evidence show that economic stress** that has accompanied sovereign defaults is severe, and has typically led to a significant increase in non sovereign defaults
- **We can rate a Project above the Sovereign rating if**, in our view, there is an appreciable likelihood that the transaction would not default if the sovereign were to default.
- To evaluate that likelihood, **we simulate a Sovereign stress scenario** and if relevant, assess Transfer and convertibility risk
- **Rating above the Sovereign can be achieved either based on standalone characteristics** of the project **or through external support factors** like a guarantee
- **Example of Rating above the Sovereign without a guarantee:** MV24 Capital B.V Rated BBB-, versus Brazil Sovereign BB+ stable. A Vessel which is doing oil and gaz exploration in the Tupi Field and is seen as important for Brazil energy matrix. Predictable cashflows and Strong incentive to avoid payment interruption.
- **Example of Rating above the Sovereign thanks to a guarantee:** Sociedad Concesionaria Vial Montes de María S.A.S, a toll road in Columbia. “AA” rating reflecting an irrevocable guarantee received from Development Finance Corp (DFC)

# Climate Change is integrated into our Credit Ratings methodologies, it is however only one factor among others, influencing default likelihood

## The road to credit materiality: Five steps from megatrend to credit impact



Source: *White Paper: Assessing How Megatrends May Influence Credit Ratings (capitaliq.com)*

- As a provider of ratings on long term debt, Climate change is a major area of research and is integrated into our credit rating methodologies
- **The Climate Finance Gap in developing economies is an area of specific focus** for us. Our research shows that lower income countries GDPs are **4.4 time more exposed** to climate physical risk than their wealthier peers. Failure to address the climate finance gap, **could undermine global climate transition and heighten long term environmental and social risks to financial stability**
- Climate risk influence on credit ratings is often mitigated by a number of factors
- 1) **The inherent uncertainty in climate science**, including the precise exposures of companies or countries, when/where events may crystallize and any associated economic losses
  - 2) **The existence of multiple other ratings factors which in many instances have more influence on likelihood of default** (negative or positive)
  - 3) Climate change risk is very long term, it **is difficult to project financial impacts beyond 5 to 10 years** as many rating factors can change significantly.
- **In order to address the lack of sufficient visibility and certainty** on how climate change will impact creditworthiness, **we do scenario analysis** (We typically look at three energy transition scenarios (Green rules, Inflection, Discord) **to assess the potential effect they could have on credit transmission channels if they were to materialize**