# 9 Sustainable finance definitions and taxonomies in China

China issued several legislative frameworks in relation to sustainable finance. The green bond catalogue issued by the People's Bank of China in 2015 is often referred to as China's taxonomy. China also issued a "Guiding catalogue for the green industry", updated in 2019. For lending, the China Banking Regulatory Commission issued green credit guidelines, performance indicators and reporting forms.

## 9.1. History and present status of sustainable finance definitions and taxonomies in China

### 9.1.1. Introduction

In the case of China, no legislative definition falls into the strict category of a “taxonomy” comparable to that of the EU. China has not issued a sovereign green bond. The green credit regulations in China provide some metrics but no thresholds, and the green bond regulations do not contain metrics or thresholds. The legislative frameworks are reviewed below. It is worth noting that the green bond catalogue issued in 2015 by the People’s Bank of China (PBOC) is usually referred to as “a taxonomy”.

China is a pioneer on green and sustainable finance. As the largest economy in the world, its efforts to develop and apply sustainable finance definitions, build sustainable finance markets, and shift investment from environmentally unsustainable to sustainable activities will be essential to meeting global environmental objectives.

China is the largest coal consumer and emitter of greenhouse gases in the world. High levels of local air pollution have become a significant concern. In 2006, the Chinese government decided to promote environmental insurance strongly. In 2007, the 17th national congress of the Communist Party of China proposed in 2007 the construction of an “eco-civilization”. In 2008, the government started national trial applications of pollution insurance in several cities and provinces (Feng et al., 2013[1]). Since then, environmental issues have received even more attention.

China is actively engaged in international cooperation regarding climate change and climate finance. China approved the Paris Agreement and set up its Nationally Determined Contribution on June 30, 2015 (UNFCCC, 2015[2]), in which it committed that its carbon dioxide emissions would peak around 2030 and carbon dioxide emissions per unit of GDP in 2030 would be 60% to 65% lower than in 2005. At the One Planet Summit in December 2017, China joined the Central Banks Network for Greening the Financial System (NGFS). China also started to implement its 2013 Belt and Road Initiative (BRI) strategy (Wikipedia, 2020[3]). The BRI focuses mainly on mobilising capital for infrastructure investments and improvement of the connectivity of nations, most of which are still relatively low income (Vivid Economics, 2019, p. 4[4]). The BRI involves 126 countries representing about 28% of global carbon emissions in 2015. “China is proposing a holistic implementation of the BRI, covering a number of broad aspects that will be important for achieving the 2030 sustainable development goals” ” (OECD, 2018, p. 13[5]). Aspects of this much broader approach include ecology and the environment including green and low carbon development, and water conservation.

### 9.1.2. The development of sustainable finance definitions in China

China’s has multiple policies and programmes in the area of green and climate finance, not limited to financial regulation. For instance, five pilot zones for green finance innovation were set up in 2017 in Guangdong, Huizhou, Jiangxi, Zhejiang and Xinjiang. In other regions, seven regional carbon market pilots also were launched in 2013 and 2014, and a national carbon market in 2017[1]. In terms of financial regulation, China has three main frameworks for green finance definitions. The core framework is the “Guiding catalogue for the green industry”. Originally established in 2016 and updated in 2019, this framework is the joint production of seven ministries and related commissions. These include the NDRC (planning ministry), the Ministry of Finance, the Ministry of Environmental Protection, the People’s Bank of China (PBOC, the central bank) and the financial regulators of respectively the banking sector (China Banking Regulatory Commission, CBRC), the securities sector (China Securities Regulatory Commission, CSRC) and the insurance sector (China Insurance Regulatory Commission, CIRC). For lending, the CBRC issued in 2012 and subsequent years green credit guidelines, key performance indicators for green credit and green credit statistics forms. For green bonds, the PBOC issued a “green bond endorsed project catalogue” in 2015, which is often referred to as “the Chinese green bond taxonomy”. Those frameworks are reviewed below.

## 9.2. Objectives and scope

### *9.2.1. The Guiding catalogue for the green industry*

There is no official translation of the catalogue into English as yet. An unofficial summary translation was consulted. The summary consists of a list of eligible sectors and contains no metrics or thresholds. The catalogue is based on both industrial policies and environmental considerations. For instance, based on the summary, the catalogue indicates a list of “high priority” hydropower projects but does not use quantitative, technology-agnostic thresholds like the EU taxonomy does. The six categories of green industries listed in the catalogue are:

1. Manufacture of energy efficient equipment
2. Clean production industry
3. Clean energy industry
4. Industry of ecology and environment
5. Green upgrade of infrastructure
6. Green services

### *9.2.2. Green lending*

Banks are the main providers of green finance in China. At the end of 2017, total green lending from 21 major Chinese banks was RMB 8.3 trillion (USD 1.1 trillion), or about 9% of their total lending. The five major green lenders were China Development Bank, Industrial and Commercial Bank of China, Construction Bank of China, Agricultural Bank of China and Bank of China.

The banking regulator CBRC regulates green lending by commercial banks. Between 2012 and 2014, the CBRC issued green credit guidelines, Key Performance Indicators (KPIs) for implementing green credit, and green credit statistics forms. The green credit guidelines provide a full set of recommendations for banks to embed climate, environmental and social risks and opportunities in their governance, strategy, policy, and disclosures. All policy banks, state owned commercial banks, joint-stock commercial banks, and postal savings banks are required to report data to the CBRC (half-year frequency) using a template. The data reporting is declarative and it appears that no external verification is required.  Annex IV of the KPIs for implementing green credit provides a “brown list” of four categories of non-compliant loans that must be reported:  amounts of loans to enterprises in violation of environmental protection or safety regulation, enterprises with obsolete capacity to be eliminated or those presenting worker safety concerns.

A “green taxonomy” is provided in another template to be similarly filled by banks: the form on “statistics on credit to projects and services of environmental protection and emission reduction”. The form does not request that the reporting bank has adopted a broader sustainability agenda. However, it includes a list of green sectors and requests associated emission reductions.

It is worth noting that the CBRC green lending criteria exclude fossil fuel lending, which is the not the case for the green bond regulation as outlined below.

### *9.2.3. Green bonds*

#### *The green bond market in China*

China is one of the largest issuers of green bonds in the world. Taking into account bonds issued in China that comply with international green bond standards, according to the Climate Bonds Initiative (CBI), China was the second largest green bond issuer ~~in~~ 2019 with USD 31.3 billion issued, after the USA (USD 51.3 billion issued) (CBI, 2019[6]). USD 24.2bn of Chinese issuances of labelled green bonds were excluded from these figures because they were not in line with international green bond definitions. Chinese entities issue green bonds not just on the domestic market, but also in overseas markets. According to CBI, about USD 6.6 billion of offshore green bonds were issued by Chinese entities in 2017, representing one fifth of total green bond issuance by Chinese entities in that year. Conversely, China also has established a green "panda bond" market, where RMB denominated green bonds may be issued in China by a foreign entity. Commercial banks make up the largest portion of issuance, representing 60% of new issuance in 2018. Bond maturity is relatively short, with 59% of total 2018 issuance with maturity below 5 years. Most proceeds are allocated to low carbon transportation (33% of the use of proceeds of bonds issued in 2018) and renewable energy projects (28%). The PBOC allows green bonds issued by financial institutions to be used as collateral for low interest central bank loans, which gives financial institutions a strong incentive to issue green bonds. It must be noted that 50% of bond proceeds are allowed to be directed to repaying bank loans and investing in working capital, while the CBI standard sets a maximum of 5% for those uses of green bond proceeds. CBI excludes from its count of green bonds those where more than 5% of proceeds are used for general corporate working capital or general funding purposes. In 2019 such bonds represented 75% of all excluded deals, the majority of which were from Chinese issuers.

#### *Green bond regulation*

China's green bonds legislation consists of two main components: the 2016 Green Bond Catalogue regulating corporate bonds, provided by the NDRC, and the Green Bond Endorsed Project Catalogue issued by the Green Finance Committee of China Society of Finance and Banking (under PBOC), which regulates green bonds issued by financial institutions. As noted, the latter is generally referred to as the Chinese green bond taxonomy.

More relevant information is available for the PBOC Catalogue, and information is added below about the NDRC Catalogue where available.

The PBOC's China Green Bond Endorsed Project Catalogue (2015 Edition) (Green Finance Committee, 2015[7]) for green bonds issued by banks and other financial institutions is available online in an English translation provided by ICMA. It provides a taxonomy of eligible activities, divided into six categories (Level 1 Category) and 31 sub-categories (Level 2 Category), with detailed explanations and defining criteria. Criteria include references to National Industry Classification Codes. The approach to eligibility is multidimensional across several environmental objectives, in a similar vein as the EU Taxonomy which it pre-dated. The Catalogue states that it "must take multi-dimensional environmental benefits as the defining standard. Project definition should take special consideration of environmental benefits in GHG emission reduction, pollution reduction, resource conservation, ecological protection."

The following text from the Catalogue describes the basic principles to which it adheres:

- Conforming to national conditions: focusing on improving the ecological environment and easing resource pressure, and following the lead of national industrial policy at the current stage.
- Highlighting environmental benefits: supporting projects with marked environmental benefits and positive spill over effects.

- Being simple and clear: taking into account the fact that most of the capital market practitioners are non-environmental professionals, and thus employing definition and classification method that is easy to follow and operate.
- Making continuous adjustment: timely updating the Catalogue according to technological advancement, policy adjustment, standard updates and changes in resource and environmental conditions.
- In line with international practice: taking international standards and practices as reference to develop domestic definition and classification method, in order to facilitate international cooperation in green finance."

Level 1 and 2 Categories in this taxonomy are shown below:

## Table 9.1. China – financial institutions green bond taxonomy (PBOC/ICMA 2015)

| Level 1 Category | Level 2 Category |
|---|---|
| Energy savings | Industrial Energy Savings |
| | Energy Savings – Technology Improvement |
| | Sustainable buildings |
| | Energy Management Centre |
| | Urban and rural infrastructure Construction with energy saving efficiency |
| Pollution prevention and control | Pollution prevention and control |
| | Environmental Restoration Project |
| | Clean Utilization of coal |
| Resource conservation and recycling | Water saving and unconventional water use |
| | Redevelopment and integrated utilization of tailings and associated mine |
| | Recycling and utilization of industrial solid wastes, exhaust gas and effluent |
| | Recycling, processing and utilization of renewable resource |
| | Remanufacturing of electromechanical products |
| | Recycling and utilization of biomass resource |
| Clean Transportation | Railway transportation |
| | Urban rail transportation (light rail) |
| | Public urban and rural transportation (bus) |
| | Waterway transportation |
| | Clean fuel |
| | New energy automobile |
| | Internet application on transportation |
| Clean energy | Wind power generation |
| | Solar Photovoltaic Power Generation |
| | Smart Grid and energy internet |
| | Distributed energy resource |
| | Social Thermal application |
| | Hydropower generation |
| | Other new energy application |
| Ecological protection and climate change adaptation | Natural ecological protection and protective development of tourism resource |
| | Ecological agriculture, husbandry and fishery |
| | Forestry development |
| | Emergency Prevention and Control of disaster |

Both the PBOC and NDRC green definitions include some project types that would not necessarily be considered green under some other international definitions (e.g. the EU Taxonomy). These include:

- Nuclear power generation
- Gas power production with criteria related to storage and shipping
- “Clean production of oil” is eligible as well as flaring
- Retrofits to fossil fuel power stations and infrastructure used for transporting fossil fuels
- “Clean” coal , although there have been announcements by Chinese officials that clean coal would be taken off the list of projects eligible for green bond financing. What is referred to as “clean coal” by Chinese authorities is otherwise known as supercritical coal (EDF, 2020[8]), i.e. a modern coal fired power generation process that is more efficient than traditional coal-fired generation, emits 20% less carbon dioxide and divides by 7 and 10 respectively nitrogen and sulphur oxide emissions.
- Large-scale (>50 MW) hydropower electricity generation

## 9.3. Metrics and thresholds

Metrics (in terms of emission reductions), but not thresholds, are available for green lending. Neither metrics nor thresholds are readily available in English language for the PBOC green bond taxonomy, nor the guiding catalogue for green industry.

## 9.4. Outlook and next steps

The sustainable finance definitions and taxonomies in China are not fully aligned amongst themselves. A case in point is the inclusion of fossil fuel related projects for the PBOC green bond standard but not for green lending. According to one prominent professor of green finance in China, “…various departments have standards for green agriculture, green buildings, and green manufacturing and technology, but there is no coordination between them” (Yao, 2018[9]). The Chinese authorities are working on harmonizing definitions, taking the 2019 guiding catalogue for the green industry as a main point of reference. China is also supports efforts to harmonise sustainable finance definitions at the international level. China became a member of the International Platform on Sustainable Finance (IPSF) launched by the EC in September 2019 to encourage international coordination on the various sustainable finance definitions. One of the future possible topics for a specific working group of the IPSF would be to work on a closer alignment of the Chinese definitions and the EU taxonomy, including where possible metrics and thresholds. The European Investment Bank (EIB), together with China’s Green Finance Committee (GFC), issued two “white papers” (EIB, 2017[10]) (EIB, 2018[11]) on mapping and comparing China’s Green Bond Endorsed Project Catalogue and the Common Principles for Climate Mitigation Finance Tracking.

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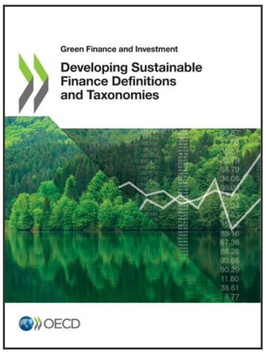
## Notes

[1] The national trading programme is still in the implementation phase and as of 2019, the first trade was anticipated to take place in 2020.

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