Standard Chartered

Opportunities and Challenges for Sustainable Finance in the UAE

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In November 2019, the Abu Dhabi Global Market and Standard Chartered co-hosted a roundtable at the ADGM on the *Challenges and Opportunities for Sustainable Finance in the UAE.* The roundtable brought together over 25 participants from the finance, government, industry and legal sectors at a timely juncture when dialogue around sustainability is garnering increasing attention. This White Paper draws upon those discussions to provide recommendations for financers and investors looking to enter the market or increase their involvement, by providing an insight into current best practices and guidance on how to tackle several key challenges facing market participants.

The roundtable included representatives from the following institutions: ADGM, Citibank, Dubai Carbon Centre of Excellence, First Abu Dhabi Bank, the Federal Competitiveness and Statistics Authority, ING, Masdar, McGuireWoods LLP, Meraas Leisure & Entertainment, PwC Middle East, Standard Chartered, and White & Case LLP.

"As an international bank that is deeply rooted in the UAE, we are committed to playing a leading role in sustainable finance, through initiatives such as this White Paper, to help our clients as they overcome climate change issues. There is a potential opportunity] for countries with resources, reach and capabilities, such as the UAE, to become a regional and global hub for sustainable finance."

Rola Abu Manneh, Chief Executive Officer, Standard Chartered UAE

"We are not on track to meet the Paris Agreement or the UN SDGs by 2030. It is therefore critical that we accelerate the flow of funds to tackle this, especially to areas of the world where it matters most – emerging markets. Initiatives such as the Abu Dhabi Sustainability Week are key to catalysing this activity and we hope that this Sustainable Finance White Paper can play a small but helpful role in building momentum as we enter the UN's decade of delivery."

Daniel Hanna, Global Head of Sustainable Finance, Standard Chartered

"As a global company at the forefront of investment into renewable energy, clean technologies, and sustainable real estate, Masdar was a proud signatory of the Abu Dhabi Sustainable Finance Declaration announced at the Abu Dhabi Sustainability Week 2019. We publicly endorse the creation of a robust and sustainable finance hub in the United Arab Emirates and hope that this White Paper provides further insight on the requirements for the continued growth of sustainable finance in the UAE and the wider region."

Mohamed Jameel Al Ramahi, Chief Executive Officer, Masdar

Standard Chartered is pleased to play a leading role in sustainable finance worldwide and to facilitate the growth of the market in the Middle East. For media enquiries, please contact Wasim Benkhadra at Wasim.Benkhadra@sc.com. For questions about sustainable finance at Standard Chartered, please contact the author, Oliver Phillips at Oliver.Phillips@sc.com.

Executive Summary

In November 2019, the Abu Dhabi Global Market and Standard Chartered co-hosted a roundtable at the ADGM on the *Challenges and Opportunities for Sustainable Finance in the UAE*, bringing together over 25 participants from the finance, government, industry and legal sectors. Discussions concerned the evolution of the market in the UAE over the last decade and what needs to be done to ensure the continued market growth required to achieve the Sustainable Development Goals (SDGs) and to restrict the pace and adverse effects of climate change. This White Paper draws on the roundtable to provide recommendations to financers and investors who are looking to be further involved in sustainable finance by sharing best practices and suggestions for tackling key challenges, in the hope that this will increase market activity and encourage further collaboration.

The last few years have seen significant growth in the sustainable finance market globally, with several notable deals in the UAE, such as First Abu Dhabi Bank's 2017 green bond issuance, and the DP World green conventional and *Murabaha* revolving credit facility, for which Standard Chartered was the Green Loan Coordinator. This White Paper looks at lessons from those issuances, and others across the world, to provide guidance to market participants. Key takeaways include the importance of appropriate nomenclature for an issue and establishing quality frameworks to prevent accusations of greenwashing. While there is no doubt that there must be continued efforts to expand the green economy if there is to be any hope of limiting global warming to well below two degrees Celsius, it is critical that efforts to meet all the SDGs are also stepped up sooner rather than later, since we are not currently on track to achieve either goal by 2030.

The clear potential for the UAE's renewable energy sector makes it an appealing area of focus for financial institutions. Solar energy has continued to grow in the region since Masdar inaugurated what was the world's largest concentrated solar power (CSP) plant at the time – Shams Solar Power Plant – in 2013. The plant, which remains one of the world's biggest CSP projects, has paved the way for additional renewable energy capacity in the UAE, most notably with the recent development of the Mohammed bin Rashid Al Maktoum Solar Park in Dubai and the completion of the Noor Abu Dhabi solar power project, and the country's climate lends itself well to the technology. Islamic finance is a particularly useful mechanism for the UAE. Given the intrinsic layers of governance that already exist in Islamic structures and the inclusion of social principles in determining what funds can be used for, there is an evident harmony with sustainable finance.

There is also an important role for regulators in this market. By providing guiding principles and the appropriate support, they can provide a framework for the market to continue to grow. There are four key areas that regulators should consider: creating certainty; encouraging collaboration; facilitating awareness; and fostering innovation. Supporting the provision of these should be a focus for market participants so that they can be confident in the long-term health of the market.

There is no one right path for sustainable finance as long as the underlying principles of doing less harm and striving to do more good are respected and incorporated. This White Paper does not seek to be prescriptive but to share important lessons and, through conveying the state of current dialogue and providing guidance, to ensure continued growth by offering advice to existing and new market participants.

Background

Sustainable development and the finance required to achieve the SDGs are increasingly at the centre of attention. The energy transition and the threat of climate change and rising sea levels are no longer niche topics but have become key issues. Across the globe, the call to action on these most pressing of issues is now impossible to ignore. The impact of climate change and other pressures on the UAE will not be negligible. The global cost of rising sea levels alone is estimated to be USD 14 trillion per year by 2100 and the cost for the UAE would amount to 9% of GDP.[1] According to a 2010 report, as much as 85% of the UAE's population will be affected by rising sea levels, alongside 90% of infrastructure.[2]

Although these potential impacts may appear daunting, there is still a window of opportunity to tackle and reverse these issues. In 2018, 40% of the primary energy consumption in the country was oil, while 59% was from natural gas, a significantly cleaner fuel source. While it is notable that less than 1% of primary energy consumption was coal, a yet smaller portion was from renewable energy.[3] With natural gas playing an important role as a bridge fuel, there is clearly room for significant growth of renewable energy as a percentage of energy consumption, as will be discussed later in the White Paper. By continuing to adopt low carbon energy and improve energy efficiency, the UAE can reduce greenhouse gas emissions and prevent the worst impacts of climate change. To overcome these challenges and make the most of the opportunities that will be presented, it is essential to promote sustainable finance and accelerate its implementation in the UAE.

The UAE took an early leadership position on sustainability and climate change, evidenced by the establishment of Abu Dhabi's Future Energy Company (Masdar) in 2006 and the Ministry of Climate Change and Environment in 2016. As an indication of the country's leadership position in sustainability, the International Renewable Energy Agency (IRENA) established its offices in Abu Dhabi in 2009 and celebrated the official inauguration of its permanent headquarters in Masdar City in 2015. The country has set bold renewable energy targets, which are outlined in the UAE Energy Strategy 2050, with 50% of energy to come from clean sources by 2050.

The UAE leadership's efforts in economic and energy diversification have also bolstered the country's knowledge development efforts. Through the Abu Dhabi Sustainability Week (ADSW) managed by Masdar, knowledge platforms and events such as the World Future Energy Summit, the Zayed Sustainability Prize (ZSP), Women in Sustainability, Environment and Renewable Energy (WiSER) and Youth 4 Sustainability, Masdar is developing the knowledge and skills needed to increase awareness of climate change, shape global future energy leaders, provide sustainability solutions to challenges in areas that need it most and catalyse action globally on sustainable development. ADSW 2019 also saw the inaugural edition of the Abu Dhabi Sustainable Finance Forum led by ADGM, another indication of the commitment of the UAE and the Abu Dhabi leadership to sustainability.

[1] https://noc.ac.uk/news/rising-sea-levels-could-cost-world-14-trillion-year-2100
[2] https://government.ae/en/information-and-services/environment-and-energy/climate-change/climate-change
[3] https://www.bp.com/en/global/corporate/energy-economics/statistical-review-of-world-energy.html

From ‘Green’ to ‘Sustainable’

The development of the green finance market, since the World Bank issued the first green bond in 2008, during a time when sustainability was often viewed as a ‘*nice to have*’, has provided a grounding that has helped to support the recent growth of the entire sustainable finance market. **With over USD 200 billion of green bonds and loans issued in 2019, the green debt market is clearly well established and has recently started to gather momentum in the UAE.** In 2017, First Abu Dhabi Bank, at the time known as the National Bank of Abu Dhabi, issued the first green bond in the region for a total of USD 587 million. Companies such as Masdar and DP World have also tapped the loan markets for green financing.

This increased activity has been supported through the actions of governments and regulators. All countries that are signatories to the Paris Agreement should be cognizant that these targets will only be achieved by enabling the private sector. As such, authorities in the UAE have been collaborating on Sustainable Finance Guiding Principles for the whole country, building on the momentum generated through the UAE Vision 2021, the UAE Green Agenda 2015–30, the 2016 Dubai Declaration and the 2019 Abu Dhabi Sustainable Finance Declaration. Regulators, such as ADGM, have built on these initiatives by further supporting the markets under their purview, for example through the ADGM Sustainable Finance Agenda, and ensuring a programme of ongoing work to support these initiatives, such as the hosting of the roundtable.[4]

This increased support has helped to drive a paradigm shift from ‘green’ to ‘sustainable’ to encompass the entirety of the ‘sustainable’ agenda, with the setting of the SDGs by the United Nations in 2015 also acting as a decisive catalyst. **During the roundtable discussion it was acknowledged that one of the most powerful methods of implementation is by adding a sustainable layer to green financing activities. This can be achieved if financers and investors identify which particular SDGs are most achievable for them** and include targets addressing them, for example by integrating female employment targets in a wind farm project, which would meet SDG 5 (Gender Equality). This reflects the recognition at the roundtable that increasing the quality of sustainable finance activities is more important than simply increasing the quantity.

There are several notable recent efforts in the UAE that have sought to tackle the wider range of SDGs, for example Etihad’s recent EUR 100 million loan to fund a project linked to the SDGs.[5] The Ma’an Authority for Social Contribution recently announced its intention to launch Social Impact Bonds in 2020, which will be outcome-based and therefore will only return capital to investors if successful.[6] The sustainability agenda is not only achieved through financing, as is the case with ADGM’s Gender Equality Initiative, which seeks to foster gender equality through leading by example, working collaboratively and championing effective change.[7] It is essential that market participants capitalise on these by incorporating features that have worked well in the past.

[4] https://www.adgm.com/-/media/project/adgm/adgm-fsra/adgm-abu-dhabi-sustainable-finance-agenda-16-jan-2019-all.pdf
[5] https://www.etihad.com/en/about-us/etihad-news/archive/2019/etihad-becomes-the-first-airline-to-raise-funds-tied-to-united-nations-sustainable-development-goals/
[6] https://www.crowdfundinsider.com/2019/11/154203-abu-dhabi-plans-gccs-first-social-impact-bond/
[7] https://www.adgm.com/media/announcements/adgm-launches-programme-to-foster-gender-equality-in-the-workplace

One method of ensuring that financing activities reflect the full range of sustainable activities is by combining the underlying principles of doing less harm and striving to do more good. As an example of the former, the Equator Principles which are adopted by over 100 international financial institutions and chaired by Standard Chartered, require the implementation of a broad range of environmental and social criteria. These are often specialised towards the specific environmental and social risks, such as climate change, conservation of biodiversity, protection of indigenous people's rights, that may be impacted by a project financing activity.[8] By ensuring that appropriate standards are incorporated into loan documents and bond covenants, not only will investors have greater confidence that the projects are financing what they are supposed to, but there will also be reduced risk of unwanted side effects.

An issue surrounding green finance to date, and which was raised at the roundtable by various institutions, has been that companies may face additional costs, such as for reporting on metrics. Although one solution is to incentivise through pricing, this is not a sustainable long-term solution, with financial institutions already facing increased margin pressure due to the new norm of low interest rates. **Financers and investors must therefore consider the possibility that there are intangible benefits to these investments, such as future-proofing business models and client bases.** This may become more relevant as regulators begin to consider scenario analysis around climate risk.

Another recommendation mentioned at the roundtable is the importance of cooperation between public and private sectors to consider best practice and knowledge exchange in the implementation of the SDGs, such as the Private Sector Advisory Council run by the Federal Competitiveness and Statistics Authority, as the secretariat of the UAE's national committee on the SDGs, which works to identify how public-private alliances can be used to achieve the SDGs at scale.[9] In this spirit, blended finance offers a readily accessible solution. Blended finance is the use of development capital from donor governments, development banks or philanthropy, to mobilise commercial capital towards the SDGs by mitigating investor risks, for example through subordinate capital or technical assistance for project preparation. In the UAE, so far, sustainable finance has frequently been through public projects, and this positions blended finance well to be a bridging tool that crowds in the private sector.

It is also important that the pace of innovation continues and there is an increasing number of nuanced offerings that provide the framework to match the supply and demand of sustainable financing. Notable recent innovations around the world include the world's first blue bond from the Republic of Seychelles, which raised USD 15 million to support the development of a sustainable marine economy;[10] the IFC Forests Bond, raising USD 152 million to support the Kasigau Corridor project in Kenya; and Standard Chartered's Sustainable Deposit, a money market instrument for corporate and retail clients wanting access to sustainable financing that supports the SDGs.[12] These examples all show that there is a burgeoning space in the sustainable finance universe that bespoke thematic financing can fill. Most importantly, the fundamental principles of each of the above were rooted in existing products, making them more accessible and ensuring that future innovations can continue to build on the progress made so far.

[8] https://equator-principles.com/
[9] https://www.sdgfund.org/sdg-fund-private-sector-advisory-group
[10] https://www.worldbank.org/en/news/press-release/2018/10/29/seychelles-launches-worlds-first-sovereign-blue-bond
[11] https://www.ifc.org/wps/wcm/connect/982eb7ef-1daa-49ca-b9c0-e6f3a2ddcd88/FINAL+Forests+Bond+Factsheet+10-5.pdf?MOD=AJPERES&CVID=lxS1w0E
[12] https://www.sc.com/en/media/press-release/weve-launched-the-worlds-first-sustainable-deposit/

Moving beyond ‘greenwashing’

A key challenge for the entire sustainable finance market is credibility. Since the inception of the green bond market, there have been several cases of ‘greenwashing’, where funds designated for green activities have not been used as expected. Accusations of greenwashing can also be levied at the use of Environmental, Social and Governance (ESG) metrics that are deemed to be insufficient. Detractors of sustainable finance have, unsurprisingly, used this as an angle to discredit the market. Roundtable participants also raised concerns about clarifying definitions and use of terms such as ‘sustainable’ or ‘green’, and how market awareness and consensus is critical to ensuring adoption while avoiding greenwashing.

Non-governmental organisations and journalists continue to be at the forefront of uncovering greenwashing and achieving accountability through reputational damage. However, recently the momentum behind climate litigation has increased, both for deal-level greenwashing and over corporate climate disclosures. Although there is not yet a significant volume of case law to be used as a precedence for litigation, existing examples from other fields can be applied to provide a pathway towards litigation. This creates a risk for transition products that bridge the gap between brown and clean but which are not pure green, and clearly shows the importance of the appropriate labelling.

Part of the difficulty in labelling sustainable finance properly stems from there being different ‘shades of green’. It is very easy to label a solar farm as green, but an energy efficiency project for a steel manufacturer might be more contentious if fossil fuels are still used. The relative benefit of solar over steel is not necessarily as clear-cut as might be expected, given that the technology for completely clean steel manufacturing does not yet exist, so incremental improvements are still a worthwhile investment. **Describing projects such as this as sustainable, or indeed even transitional, rather than green will help to reduce the appearance of greenwashing and ensure continued movement towards a more sustainable future.** This a critical consideration for an economy like the UAE, which has been traditionally dependent on hydrocarbons and where there is an opportunity to ‘green the brown’.

The use of frameworks to clearly define what an organisation views as credible sustainable finance activities is an important tool for avoiding greenwashing and tackling the SDGs. Good frameworks will clearly identify which underlying assets are eligible as well as factors which preclude inclusion. Matching these activities to the relevant SDGs will help other parties to understand how this relates to their own frameworks. To help establish credibility, organisations should look to certify their framework with a second-party opinion from a reputable sustainability consultancy or rating agency, and should engage them, or a party with experience in writing frameworks, in the creation process.

Another method of instilling confidence is through the use of covenants specifically related to sustainability. This is certainly part of the solution and should act as a deterrent but does still require a means of monitoring and assessing whether funds are used properly. **Financers and investors should insist on the inclusion of covenants that will reduce the likelihood of funds being used in unexpected ways,** for example through clauses that render such an event as a default, and seek to standardise this as industry best practice.

The underlying assurance that funds are being used as intended must also come from quantifiable reporting practices. For project financing, this can be less of a challenge. It is straightforward to prove that a wind farm has been built and any sceptical backer could even visit the site in question if required. When considering whether ESG metrics have been reached, there are greater questions to be considered. While CO2 reduction targets are simple to grasp conceptually, the underlying measurement, reporting and verification process that substantiates such targets is much more complex. For continued growth of the market, it will be essential that robust data collection processes are put in place when targets are set and are communicated transparently to the market, such as those espoused by the Task Force on Climate-related Financial Disclosures.[13]

Measurements should be made using the most current science-based methodologies, which should be made available where possible to ensure confidence in the process. Third-party verification should also be used to provide an additional layer of quality control that can certify that the data collection is carried out appropriately and that accurate performance is presented. As more companies vie to participate in the sustainability verification space, institutions looking to partner with one should ensure that they choose a credible institution that has the experience required to assess against the required metrics.

One particularly interesting area of uncertainty may arise as new principles and regulations are introduced that make previously acceptable standards appear redundant. It is important that such developments are treated appropriately. **Regulators and market participants should be cognizant of the fact that standards do evolve so should not allow this to become an opportunity to retrospectively litigate but to continue to make progress going forward.** To do so, in part, requires initial criteria to be stringent enough that they do not warrant undermining but also that regulation is not retrospective.

Islamic Finance

During the roundtable connections were drawn between the growth of the sustainable finance market and the growth of the Islamic finance market several years previously. It was noted that the market took several years to take off, with smaller transactions allowing the various stakeholders to learn what worked. Market standards formed due to landmark deals which reflected the potential that Islamic structures could bring. Not only does the evolution of the Islamic finance market offer valuable lessons to those attempting to understand how the sustainable finance market might grow, and potentially avoid any common pitfalls, but the combination of the two can be a powerful driver of the market.

Islamic finance can help to provide a solution to the need to offer further assurance to financers and investors that funds are used as expected. Islamic instruments already have a layer of embedded governance in the form of a Sharia board, consisting of qualified scholars, that must approve the product before issuance and must ensure that all products conform to Sharia principles at all points during their life cycle. In particular, there are Sharia requirements that financings relate to ethical objectives and are backed by tangible or intangible assets, creating a direct link between funds and their intended use of proceeds. This extra layer of assurance can play an instrumental role in ensuring investor confidence and reducing the risk of greenwashing.

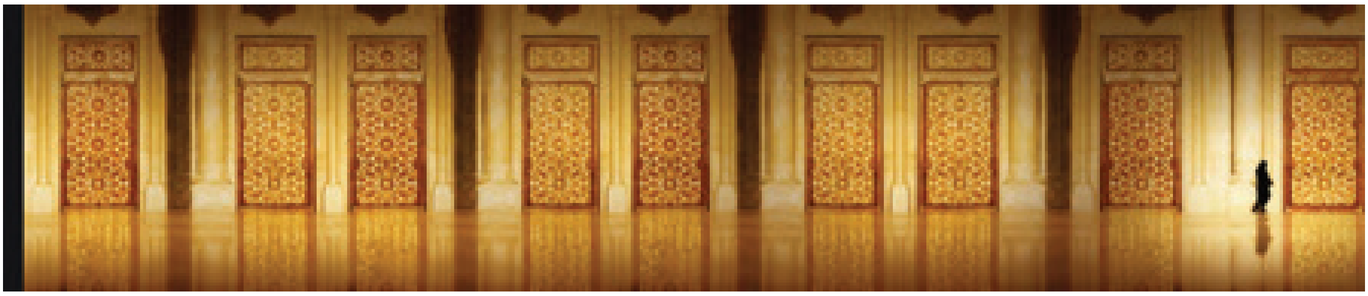
[13] https://www.fsb-tcfd.org/

Another benefit of using Islamic finance is that there are already provisions that consider social responsibility, which was earlier identified as part of the growing umbrella of sustainable finance beyond green. Alongside prohibiting *Riba* (usury or interest) and *Gharar* (speculation), there are restrictions against financing non-Sharia-compliant sectors, such as weapons production, many of which do not align with the SDGs. More broadly, Sharia encourages responsible and ethical behaviour, with the intention of creating a financial system that is sustainable in the long term and which is focused on stakeholders and social responsibility.

The market for sustainable Islamic products has seen some development alongside the growth of the broader sustainable market, but the volumes so far have been significantly smaller. There have already been notable issuances in the UAE. In July 2018, DP World launched the market in the Middle East with an amendment and extension of a USD 2 billion conventional and *Murabaha* revolving credit facility, for which Standard Chartered was the Green Loan Coordinator, linking the pricing to the company's carbon intensity ratio.[14] More recently, in 2019, Majid Al Futtaim issued two USD 600 million green sukuk, with the proceeds of each going towards green buildings, renewable energy, energy efficiency and improved water management.[15] These issuances were well received by the market, showcasing the potential that the combination of sustainable and Islamic finance can have.

In order to continue to drive the market forward, there should be industry standardisation of Sharia interpretation of sustainability concerns, as well as harmonisation of legal documentation and increased sustainability metric awareness. This process would combine the perspectives of all relevant parties to help to shape the future direction of the market and boost the volume of issuance while reducing the risk for investors. **Financers and investors should encourage supervisory guidance on this matter and should take every chance to explore whether Islamic finance can be incorporated into a sustainable finance transaction, particularly since the product is especially relevant in the UAE and the wider region.**

[14] https://uk.reuters.com/article/dp-wrld-loan/dubais-dp-world-amends-terms-of-2-billion-green-loan-idUKD5N1QN01V
[15] https://www.majidalfuttaim.com/en/media-centre/press-releases/2019/05/majid-al-futtaim-lists-world-s-first-benchmark-corporate-green-sukuk--on-nasdaq-dubai



The Energy Transition in the UAE

As discussed at the outset of this White Paper, the energy transition from fossil fuels to renewable energy presents an enormous opportunity for the UAE, and one which is also critical for the future. **It is estimated that at least 19 GtCO2e of annual greenhouse gas emission reductions are required in order to limit global warming to within two degrees** Celsius.[16] This is the equivalent of 44 billion barrels of oil, 125% of current annual oil consumption, which would have a market value in excess USD 2.5 trillion. This is a clear economic opportunity for the country, since emissions and energy consumption in the UAE have both grown by 11% since 2013.[17] In 2018, renewable energy accounted for less than 1% of the energy mix, therefore growth of renewables is crucial for restricting increases in emissions while allowing continued growth of energy consumption.

There have been several notable developments in the country in recent years, since Masdar's Shams Solar Power Plant came online in 2013. Between 2017 and 2018, the equivalent of approximately 100,000 tonnes of oil equivalent in additional consumption has been provided by renewable energy.[18] One of the most notable projects is the Mohammed bin Rashid Al Maktoum Solar Park, which will be the largest single-site solar project in existence upon completion, with a planned capacity of 5,000 MW by 2030. Another is the 1,177 MW solar plant Noor Abu Dhabi that was completed mid-2019 as the world's largest single-site operational solar plant. Finally, Masdar is also developing the first waste-to-energy project in the Middle East in partnership with Sharjah-based environmental management company Bee'ah. The Sharjah Waste-to-Energy project has been recognised internationally and received Project Finance International's Clean Energy Deal of the Year award for the Middle East and Africa region in 2019.

[16] https://www.imf.org/en/Publications/FM/Issues/2019/09/12/fiscal-monitor-october-2019
[17] https://www.bp.com/en/global/corporate/energy-economics/statistical-review-of-world-energy.html
[18] https://www.bp.com/en/global/corporate/energy-economics/statistical-review-of-world-energy.html
[19] https://www.dewa.gov.ae/en/about-us/strategic-initiatives/mbr-solar-park

Declining tariffs have been a key trend in recent years, making renewable energy costs competitive, if not even cheaper, than conventional fossil fuels. However, this has also reduced returns for developers, not least given the reduction of government subsidies that has accompanied falling costs. In addition, developers need to consider the availability of space when developing projects. While there are many large open areas in the UAE, the country is geographically smaller than its neighbours, therefore it is important to consider this as a factor now, to ensure that projects are built in a way that leaves room for growth as technology advances and becomes more efficient.

For developers there is a clear reason for continuing to pursue renewable energy despite falling returns given the global shift towards clean energy.[20] Masdar is one of the standout companies in the UAE and the wider region involved in the development of renewable energy. Masdar has invested in renewable energy projects with a total capacity of over 5 GW including technologies such as wind, solar and waste-to-energy. However, a key risk facing even successful developers such as Masdar is from off-takers looking to move risk onto developers as the technology improves and the market matures. This can result in projects being harder to finance and the pool of liquidity that can be accessed to fund them being reduced, which will be reflected in the financing terms.

The investment case is both clear and complex for financers and investors. While financial institutions should not abandon solid project finance principles, there is a clear argument for exploring ways to incorporate a sensible degree of leniency in choosing to finance renewable energy. When considering long-term returns, the energy sector faces potentially significant stranded asset risk for legacy fuel sources, but this is much less likely to be the case for renewable energy. Developing relationships with renewable energy companies now will ensure that the financial sector is prepared for a future where pure-play fossil fuel companies may no longer be the obvious sector leaders. The financial sector should also engage in a supportive dialogue with energy sector clients to help them to capitalise on the opportunity presented by the energy transition.

There is one factor that could decisively shift the economics in favour of renewables and away from fossil fuels. **A global carbon price is recognised in many corners of the world as being a decisive factor in tackling climate change; however, a regional carbon price is a key initial requirement for this and can bring significant local benefits.** A sufficiently high carbon price would deter investment in high-emitting projects and can also make low carbon activities more attractive if a carbon offset can be monetised as a carbon credit.

There are two primary mechanisms for carbon pricing, taxation and markets, both of which have their own advantages. A carbon tax allows for a high price to be set at the inception of the tax, causing a potentially radical shift in investment flows, and revenues can easily be invested in the sustainable economy. However, the immediate transition to a higher price has the potential downside of an uneven transmission of wealth, since there is little time for transition in the economy, meaning that workers can find themselves unemployed and with minimal time to retrain.

[20] https://masdar.ae/

A cap-and-trade carbon market, on the other hand, should bring about a gradual change in price, reducing the effects described above. There are also greater incentives to transition, since companies which take ambitious steps to reduce emissions can actually profit in the long term. Furthermore, laggards are not put out of business rapidly, although may be eventually, so they will be able to catch up if they choose to do so. The longest-standing carbon market, the European Union Emissions Trading Scheme (EU ETS), which has been in operation since 2005, provides a useful framework that can be applied worldwide.[21]

The merits of both these mechanisms warrant greater attention, especially since the lack of agreement to date on Article 6 of the Paris Agreement creates a role for regional markets, formed by clubs of countries with shared ambitions. In the UAE, the Dubai Carbon Centre of Excellence has over a decade of experience managing projects that produce carbon credits in the region, demonstrating that there is a significant opportunity if a market does emerge.[22] The financial industry should actively engage in discussions on the subject and seek to encourage the establishment of a regional market.

In order to continue to promote the growth of the renewable energy market in the UAE, market participants must continue to weigh the tangible benefits, such as financial returns, against more intangible considerations, such as the need to pivot towards the industry of the future to protect their future returns. They should also be open to new mechanisms that may accelerate the energy transition, such as carbon pricing, and take every opportunity to engage in dialogue that will shape the sector for years to come. Market participants should also explore ways to expand financing for projects that contribute to sustainability more generally. A case in point is the sustainable Real Estate Investment Trust launched by Masdar at ADSW 2020, the first 'green' REIT to be introduced in the UAE. The REIT will be established at ADGM and will offer an attractive option to invest in four commercial income-generating real estate assets in Masdar City. These assets were designed and built with strict energy and water efficiency criteria in order to reduce their overall carbon footprint, in line with Masdar City's mandate to be a showcase for sustainable urban development.

The Role of Regulation

A common theme underpinning many solutions to the challenges that the market faces is the requirement for a clear set of best practices and guiding principles that can be readily applied. It was agreed by the roundtable participants that establishing these is a key facet of the role of a regulator in supporting the sustainable finance market. **Through early involvement in the development of new markets, by promoting transparency and ensuring continued support as markets mature, regulators can provide the conditions and ecosystem to support and scale up sustainable development.**

Guiding principles, such as the UAE Guiding Principles on Sustainable Finance,[23] can help to bring additional participants into the market and therefore put the country firmly on the right path. Regulators should look to establish frameworks that point a broad range of industries towards an appropriate transition pathway. To establish what the direction of travel should be, they should work in unison with the private sector and other government bodies to ensure that standards are appropriate and can be translated into achievable targets. Furthermore, regulators should consider whether setting reporting standards for companies to disclose performance on sustainability issues can be a significant market driver.

[21] https://ec.europa.eu/clima/policies/ets_en
[22] https://dcce.ae/#welcome
[23] https://www.adgm.com/media/announcements/working-group-formed-to-advance-sustainable-finance-practices-and-investments

As already discussed, **the only way to achieve the SDGs and to limit global warming to less than two degrees Celsius is through collaboration between all parties.** Market participants will be able to have a greater impact if efforts are aligned and experiences shared, since this will make it more likely that mistakes are not repeated, and a broad range of sectors are comprehensively tackled. Regulators should therefore take the opportunity to bring people together, both formally, for example through initiatives such as the Abu Dhabi Sustainable Finance Declaration,[24] and informally, such as the roundtable that led to this White Paper.

Alongside efforts to encourage collaboration, regulators should help to build awareness. Capacity building programmes are an essential part of facilitating the growth of the emerging sustainable finance market, ensuring that individuals have the base knowledge required to make decisions that reflect the previous decade of evolution and learning. Programmes such as the Abu Dhabi Sustainable Finance Certificate,[25] developed by the ADGM Academy in conjunction with the London Institute of Banking and Finance, are an excellent starting point. As the number of new entrants to the market increases, it is important that they have adequate opportunities to understand the required fundamentals. Regulators should also think to the future and encourage schemes that seek to raise awareness among younger generations, for example Meraas's Green Planet in Dubai,[26] which has the power to instil in children the importance of protecting the natural environment in a fun and enjoyable way.

Finally, regulators should look to foster innovation. Innovations that can help to support the entire finance industry have a role to play in the development of sustainable finance, not just those with a focus on sustainability. An example of fostering innovation is the ADGM FinTech Digital Lab,[27] a virtual environment hosted by ADGM where financial technology companies, institutions and regulators can interact and collaborate on the technological innovation required to address pressing concerns, thereby solving issues such as those previously addressed around data collection. An example of one such innovation is that of the Monetary Authority of Singapore, which has put in place a process that provides assistance towards the additional costs of certifying a transaction as green, reducing one of the potential hurdles that might dissuade an issuer from choosing to look beyond conventional financing.[28]

It is evident that regulators have a decisive role to play in encouraging the sustainable finance market in the UAE. **By helping to create the dialogue that will lead to the development of the market and continuing to promote transparency and consistency, regulators can create an environment for institutions to comprehensively address some of the most pressing issues facing the country and encourage inward investment into sustainable developments.** Financers and investors should engage openly with regulators to facilitate this.

[24] https://www.adgm.com/media/announcements/25-key-uae-public-and-private-entities-committed-for-abu-dhabi-sustainable-finance-declaration-at-abu-dhabi-sustainability-week
[25] https://www.libf.ac.uk/study/professional-qualifications/certificate-in-sustainable-finance-registration
[26] https://www.thegreenplanetdubai.com/en
[27] https://www.adgm.com/setting-up/fintech-digital-lab/overview
[28] https://www.mas.gov.sg/schemes-and-initiatives/sustainable-bond-grant-scheme

Conclusion

It is evident that there is ample opportunity for sustainable finance in the UAE and for the UAE to become a leader in the wider region. A great deal of work has already gone in to establishing the infrastructure required for the market to develop, but clearly there is more to be done. The challenges facing the UAE are not insignificant and it will be critical for the future that global warming is limited to two degrees Celsius, and that the SDGs are achieved by 2030. **At the current rate of investment, the world is not on track to meet either objective. While this may appear daunting, there is still undoubtedly an opportunity for institutions that embrace the challenge and seek to establish themselves as market leaders.**

Incorporating the recommendations given in this White Paper and continuing to build on them, in keeping with the spirit and principles alluded to throughout, will ensure that the market grows healthily. It is also important that work continues into the understanding of how to create the right balance of incentives for private investors and other market participants, to ensure that there is increased investment in sustainable products. Furthermore, it is essential that all opportunities are taken to drive incremental changes. **Even a reduction of one-tenth of a degree in global warming will have a dramatic improvement on the environmental outlook. An extra household receiving greater opportunities can bring change to an entire community.**

To achieve this, financers and investors who are looking to be further involved in sustainable finance must actively share best practices and make suggestions for tackling key challenges, to increase market activity and encourage further collaboration. Those with experience of the market should be open to sharing past experiences and challenges with newcomers, who should not be reticent to seek guidance. Only through increased engagement from all sectors, public and private, will we achieve these goals.

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Established in 2006, Masdar, or Abu Dhabi Future Energy Company, is a global leader in renewable energy and sustainable urban development. Masdar means 'source' in Arabic.

Masdar's mandate is to help maintain the leadership of the United Arab Emirates (UAE) in the global energy sector, while supporting the diversification of both its economy and energy sources for the benefit of future generations.

At Masdar, we develop commercially viable renewable energy projects in the Middle East & North Africa (MENA) and international markets. We advance innovation in clean technologies. We are building the world's most sustainable city. We also deliver knowledge and industry platforms to stimulate further growth in the wider renewable energy and clean-tech industry, creating new revenue streams for the UAE over the long term.

Wholly owned by the Abu Dhabi government's Mubadala Investment Company, Masdar is supporting the UAE's transition towards a knowledge-based economy. A catalyst for renewable energy development in the Arab world over the last decade, Masdar is demonstrating how the business community can deliver on the global sustainability agenda.

About Abu Dhabi Sustainability Week

Since 2008, Abu Dhabi has provided a sustainability platform for the global community which has grown through its initiatives and events, to become a global catalyst for accelerating the world's sustainable development.

Abu Dhabi Sustainability Week (ADSW) is committed to the sharing of knowledge, implementation of strategies and to the delivery of real-world solutions that drive human progress.