

The UK's Green Industrial Revolution and Key Takeaways for Energy Sector from the Recent UN Climate Conference

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** co-authored by Trainee Solicitor Christopher Orford*

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On 7 December, the UK announced over £116 million in new government funding to boost green innovation across the country – this includes supporting projects to develop new technologies that (a) increase energy efficiency in homes and buildings, (b) reduce carbon emission, (c) boost the UK's energy security and (d) provide cleaner ways to generate power and heat. Following the two-week UN climate conference (“**COP26**”) which concluded last month, this announcement is likely one of the first of many to come as the UK is under increasing pressure to set up net-zero initiatives across the governments. Framed as the world's last chance to limit global warming to 1.5oC as per the 2015 Paris Agreement, participating countries including the UK signed up to a raft of commitments and pledges to address the pressing need to tackle climate change. The outcomes of COP26 at both an international and national level will have wide-ranging implications on businesses across the entire upstream to downstream spectrum of operations, and will help to support a just transition to net-zero.

We summarise below some of the key takeaways for the energy sector from COP26:

1. Phase-Down of Coal

The transition away from coal was an important theme of COP26, where a large number of countries agreed to redirect investment to clean energy. Major economies committed to transition away from unabated coal power generation by the 2030s, with transition for the rest of the world to occur within the 2040s. In particular, certain countries, including the UK, agreed to cease the issuance of new permits and direct government support for unabated coal-fired power generation while also ceasing the construction of unabated coal-fired power generation projects. Alongside this, countries committed to ensure that those impacted by this transition are properly supported to ensure that the transition is inclusive and just.

Notably though, there are two major limitations in relation to these commitments. Firstly, any projects which have reached financial close are excluded which mean that a number of projects will continue to be built in the next decade. Secondly, only around 40 countries have pledged to end the use of coal power, with four of the major coal producing and burning countries, being the US, Australia, China and India, all absent from the accord.

Despite the setbacks, the explicit reference to reducing coal use marked a significant first for the UN climate process, after nearly 30 years of summits, calling for a “phasedown of

unabated coal” and a “phase-out” of “inefficient” fossil-fuel subsidies.

2. Beyond Oil and Gas Alliance (“BOGA”)

BOGA launched at COP26 is the first international coalition of countries committed to phasing out the production of oil and gas, beginning with the ending of new licensing rounds for oil and gas. However, given that the alliance only has the support of 8 members, being Costa Rica, Denmark, France, Greenland, Ireland, Sweden, Wales and the province of Quebec, its impacts will likely be muted.

Moving beyond oil and gas, which currently still make up a large percentage of the energy mix of most countries, will require a sustainable and financially viable energy transition route. It therefore remains to be seen whether the phasing out of oil and gas will gain increased traction at the next round of the UN climate negotiations.

3. Glasgow Financial Alliance for Net-Zero (“GFANZ”)

Some 450 firms across 45 countries have committed US\$130tn towards the net-zero transition (and to align their portfolios to net-zero by 2030). The GFANZ announced that it is working on defining net zero pathways for carbon-intensive sectors, agreeing a unified approach to robust transition plans for corporates and financial institutions, and developing an industry-wide plan to mobilise the capital needed for decarbonisation in emerging markets. There has already been some short-term progress with 29 asset owners within the alliance committing to reducing their portfolio emissions by 25-30% by 2025. This new alliance makes clear that banks, asset managers and asset owners fully recognize the business case for climate action and the significant risks of investing in the high-carbon, polluting economy of the past.

In addition, lenders from both the public and private sectors are attaching conditions to proposed lending, such as seeking formal environmental commitments at the outset and for the duration of the loan from new borrowers – this includes increased prominence of sustainability and ESG considerations in term sheets and loan agreements, and the scaling up of climate-related reporting, climate risk management and climate-related investment returns.

4. Breakthrough Agenda

One key item to come out of COP26 was the Breakthrough Agenda which aims to make clean technologies the most affordable and reliable option globally by 2030. For instance, UK Prime Minister Boris Johnson set out the first five “Glasgow Breakthroughs” that cover more than 50% of global emission, and these include: (a) making clean power the prominent option globally, (b) making zero-emission vehicles the new normal, (c) creating markets and support for “near-zero” steel and ensuring it is used in infrastructure projects globally, (d) creating low-carbon hydrogen globally, and (e) delivering climate-resilient and sustainable agriculture across the world by 2030.

Countries have committed to discussing and strengthening international progress on breakthroughs on a yearly basis. With increased coordination and cooperation globally to accelerate the growth of the relevant markets, together with the competition to supply those markets, it is estimated for instance that the costs of clean energy technologies such as batteries and hydrogen electrolysis may fall by 45% by 2030 and 75% by 2050.

5. Global Methane Pledge

More than 100 countries representing 70% of the global economy and nearly half of man-made methane emissions have signed up to collectively reduce global methane emissions by at least 30% from 2020 levels by 2030. This is a significant step to achieving net zero by 2050 as methane is one of the most potent greenhouse gases and its reduction is expected to help the world avoid 0.3C of warming by 2040.

One of the biggest sources of methane emission is from the production, transport and use of natural gas. Researchers have also linked a spike in methane emissions since 2008 to the boom in fracking for gas in parts of the US. The pledge therefore entails tackling issues relating to the leakage of methane from oil and gas wells, pipelines and other fossil fuel infrastructure.

Looking ahead

The commitments and pledges made at COP26 have the potential to have real and lasting impacts on the global effort to achieve net-zero by 2050. With the UK's promise to provide a report on the state of transition by the second quarter of next year and an agreement to have an annual global checkpoint process from 2022, countries and organisations will come under increasing pressure to demonstrate their actions and commitments to achieving climate related targets going forward.

Having a sustainable and financially viable energy transition route is critically important, and this will require funding and support from governments as well as private capital to accelerate the growth and adoption of green energy globally.