

ESTABLISHING CHINA'S GREEN FINANCIAL SYSTEM

Detailed Recommendations 6: Create a Green IPO Channel



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Detailed recommendations 6: Create a Green IPO Channel

Green industries are the key to realizing the sustainable growth of China and represent three of the seven national strategic emerging industries (energy conservation and environmental protection, new energy, and new energy vehicles). According to the national goals for the development of green industry and estimates from experts, China's green industries have an annual investment demand of more than 2 trillion yuan (US\$320 billion). Characteristics of green industry, including large initial capital requirements, an asset-heavy capital structure and slow returns, have further magnified the shortage of financing. Aside from fiscal and credit support policies, broadening green financing channels through capital markets is vital to the development of China's green industries. China's current green financing structure is dominated by government funding and government loans across various administrative levels; the financing channels for green enterprises are rather limited in comparison to other countries. For instance, the equity market accounts for 18 percent of the total financing in sophisticated PV markets including the US and Canada, while this ratio is only 0.7 percent for Asia (mainly China and Japan). On the whole, China's green industries are not adept at financing from stock markets and the recently slow IPO process is a major bottleneck for Chinese green enterprises to enter into the stock market and stands in the way of further improving financing structure for China's green industries.

(I) IPOs for green companies are overly difficult and slow

As a key component of China's capital markets, the A-share market has contributed to the development of China's green industries. Nevertheless, given the pressing needs of developing China's green industries, the A-share market is yet to play a stronger role in supporting China's green industries.

First, most green enterprises have been unable to contact IPOs in China due to demanding thresholds of the A-share market. Given the uniqueness of green industries and their business models, together with the non-cyclicity of policy effects, many green enterprises cannot meet the standards for listing at the A-share market. Take the PV industry for instance, seven out of the global top ten PV companies by shipment volume in 2013 are Chinese companies, which are all listed on the US stock market; GCL-Poly Energy Holdings Limited, which is a leader of global polycrystalline industry, is listed on the Hong Kong stock exchange.

Emergence of the SME board and the GEM board provides some green enterprises with IPO opportunities but their market capitalization still accounts for a relatively small share. By August 18, 2014, a total of 147 green enterprises were listed on the A-share market, accounting for 5.8 percent of all listed companies. However, the combined market capitalization of these 147 green

enterprises only reached 1.28 trillion yuan, which represents 4.4 percent of the total capitalization of A-share market. Current market capitalization of listed green enterprises remains relatively low.

Second, the IPO process proves slow and green enterprises are particularly vulnerable. For instance, CECEP Wind-power Corporation (601016.SH) is the first company listed on the A-share market specializing in wind farm operation and used to be a leader of wind farm operation in China. Due to massive operation capital inputs and long cycles of investment return for wind farms, financing capabilities are a key factor of the company's development. Stagnation of IPOs in the A-share market led to a financial shortage of the company and thus affected the size of its newly installed wind capacity. As a result, the company's market share of cumulative installed capacity and newly installed capacity in the Chinese market has been on the decline since 2012. In contrast, Huaneng Renewables and Datang Renewable Power have maintained rapid growth of business revenues after the completion of capitalization in the Hong Kong stock market.

Under the restriction of IPO policy, the CECEP Wind-power Corporation only financed 390 million yuan (US\$60 million) from its IPO, which is far below the financing volume of similar companies in the Hong Kong stock market (Datang Renewable Power raised 4.77 billion Hong Kong dollars (US\$606 million) Huaneng Renewables raised 5.93 billion Hong Kong dollars (US\$760 million) and China Longyuan Power Group Limited raised 16.73 billion Hong Kong dollars US\$2 billion). Currently, the CECEP Wind-power Corporation only has a developable wind capacity of about 826MW, which requires an investment of six billion yuan (US\$1 billion) (Obviously, the IPO financing of mere 390 million yuan (US\$62 million) is far from sufficient for the company's short-term development.

By August 2014, among 98 companies under IPO review, only eight were green enterprises, which accounted for 8.2 percent. Among the 129 companies whose IPO reviews were terminated, 17 were green enterprises, representing a higher share of 13.2 percent.

Due to the slow IPO process, some green enterprises had no choice but to enter the A-share market through M&As by listed companies or backdoor listing, which led to a substantial increase in the M&As of green industry in the A-share market. In the first seven months of 2013, there were 41 M&As in the A-share market of environmental industry with a total transaction volume of 11.7 billion yuan; as well as 24 M&As in new energy sector with a total transaction volume of 1.95 billion yuan, which exceeded the level of 2013. Many companies involved in the M&As and backdoor listing of companies queuing for IPOs or companies listed on the New Third Board.

Hence, accelerating the IPO process of green enterprises should be one of the measures to expedite the development of China's green industry. By streamlining the IPO review procedure of green enterprises, the CSRC will be able to steer private equity investments towards green enterprises and enhance their financing capabilities.

(II) Recommendations on accelerating the IPOs of green companies

We would like to suggest streamlining the IPO review procedures for green enterprises in the following two aspects:

First, accelerate the IPO process for green enterprises by streamlining the IPO review procedure.

At present, green enterprises have no particular advantage in the IPO review process among the many other companies currently in the IPO queue. It is recommended that with reference to the special IPO policies offered to companies located in areas affected by the 2008 Sichuan earthquake and companies in China's western regions (including Tibet and Xinjiang) after 2012, a similar green channel for green enterprises be created in the form of a separate IPO queue for green enterprises in addition to the main board, the SME board and the GEM board. At least one day of each week should be dedicated to the review of IPO applications from green enterprises. And after receiving CSRC's approvals, green enterprises should receive the approval documents without further queuing. Qualified green enterprises should be entitled to simplified review process. With reference to the concept of separate review channel for M&As, a fast/exemption lane should be created for qualified green enterprises. After the IPO approval system is replaced by a record-filing system, if certain procedures of an approval nature are retained under the new system, it is still necessary to consider providing a special channel for green firms.

Second, increase the flexibility of supporting measures to adapt to the unique financing needs of green enterprises. There should be greater flexibility in the types of project that a green enterprise can invest in using the proceeds raised in the IPO process. Because most green enterprises are asset-heavy, they have strong demand for working capital. It is recommended that restrictions be eased to an appropriate extent to permit green enterprises to use a greater amount and proportion of IPO proceeds to replenish their working capital or repay bank loans. Efforts should be made to explore the mechanisms and conditions for green enterprises listed on the New Third Board to directly transfer to the main board, SME board or the GEM board. Although the New Third Board has already set out the principles supporting such a board transfer, the implementing rules and mechanisms are yet to take shape and currently board transfer still requires the completion of the normal IPO procedures. It is recommended that board transfer pilot programs be carried out first for green enterprises listed on the New Third Board.

THE GREEN FINANCE TASK FORCE

The Green Finance Task Force was initiated by People's Bank of China (PBC) Research Bureau and the UNEP Inquiry into the Design of a Sustainable Financial System in 2014. The Task Force brought together leading Chinese financial policy and regulation experts together with experts from the private sector, academia and think tanks, as well as international experts.

A number of organizations have lent great support to this Task Force, chief among them are Chongyang Institute for Financial Studies of Renmin University, the Ecological Finance Research Center at the Renmin University of China, the Eco Forum Global, the International Institute for Sustainable Development, the Green Credit Special Committee of China Banking Association, and China Finance 40 Forum.

Advisor: Pan Gongsheng, Deputy Governor, People's Bank of China

Domestic Convener: Ma Jun, Chief Economist, Research Bureau, People's Bank of China

International Convener: Simon Zadek, Co-Director, United Nations Environment Programme Inquiry into the Design of a Sustainable Financial System

TASK FORCE MEMBERS

An Guojun	Research Associate, Institute of Finance and Banking, Chinese Academy of Social Sciences
Chen Zheng	Research Associate, Shenzhen Stock Exchange
Chen Yaqin	Head of Marketing Division, Environment Finance Department, Industrial Bank
Guo Peiyuan	General Manager, SynTao (expert on corporate social responsibility)
Guo Sanye	Deputy Secretary General of China Banking Association
He Qiaonv	Chairman, Beijing Orient Landscape Industry Group
Huang Chaoni	Head of Business Development – Asia, Trucost
Huang Jianhui	President, Research Institute, China Minsheng Bank
Jiang Peixing	CEO, Zhong De Securities
Jin Hainian	Chief Research Officer, Noah Private Wealth Management
Lan Hong	Deputy Director, Ecological Finance Research Center, Renmin University of China
Li Donghui	Director and SVP, Beijing Orient Landscape Industry Group
Li Jianqiang	Research Associate, Research Bureau, People's Bank of China
Liang Pingrui	General Manager, Environment Finance Department, Industrial Bank
Lu Hanwen	Deputy Director-General, Project Appraisal Department II, China Development Bank
Qi Liang	CEO, China Securities
Sheng Hetai	Vice President, People's Insurance Company (Group) of China
Sang Qiang	Senior Manager, Strategic Planning Department, People's Insurance Company (Group) of China
Su Ting	International Sustainability Development Research Institute
Wang Guijuan	Research Associate, Research Institute for Fiscal Science, Ministry of Finance
Wang Lu	Deputy Director General, Credit Reference Center, People's Bank of China

Wang Wen	Executive Dean, Chongyang Institute for Financial Studies, Renmin University of China
Wang Yao	Director, Research Center for Climate and Energy Finance, Central University of Finance and Economics
Xie Hongxing	Secretary-General, Clean Air Alliance of China
Xin Benjian	Senior Research Associate, Chongyang Institute for Financial Studies, Renmin University of China
Xu Wen	Research Associate, Research Institute for Fiscal Science, Ministry of Finance
Yang Shuying	Research Associate, Policy Research Centre for Environment and Economy, Ministry of Environmental Protection
Yao Bin	Research Associate, Research Bureau, People's Bank of China
Ye Yanfei	Deputy Director-General, Statistics Department, China Banking Regulatory Commission
Yin Hong	Deputy Director, Urban Finance Research Institute, Industrial and Commercial Bank of China
Yin Lihai	Director, Tax Policy Department, Ministry of Finance
Yu Xiaowen	Director, IISD China Office
Yu Zhenli	Research Associate, Research Institute for Fiscal Science, Ministry of Finance
Zhao Lijian	Program Director, Environmental Management, Energy Foundation China
Zhang Hai	Director of the Secretariat, Eco Forum Global
Zhang Jialin	Chairman, Aron Capital Management
Zhang Yong	Executive Director, Eco Forum Global
Zheng Tingying	Executive Deputy Director, Ecological Finance Research Center, Renmin University of China
Zhou Yacheng	Partner, Zhong Lun Law Firm
Zhou Yueqiu	Director, Urban Finance Research Institute, Industrial and Commercial Bank of China
Zhu Shouqing	Senior Associate, Sustainable Finance Program, World Resources Institute

INTERNATIONAL EXPERTS

Mark Halle	Vice-President, International Institute for Sustainable Development
Sean Kidney	CEO, Climate Bonds Initiative
Alexander Barkawi	Founder and Director, Council on Economic Policies
Stanislas Dupré	Founder and Director, 2° Investing Initiative
Butch Bacani	Programme Leader, UNEP FI Principles for Sustainable Insurance Initiative
Sony Kapoor	Managing Director, Re-Define
Susan Burns	CEO and Co-founder, Global Footprint Network
Romulo Sampaio	Professor of Law and the Director of the Research and Policy Center for Law and the Environment (CDMA) at Getulio Vargas Foundation (FGV) School of Law in Rio de Janeiro.



The People's Bank of China

No.32 Chengfang street,
Xi Cheng district, 100800
Beijing, China
webbox@pbc.gov.cn
86-010-66194114
www.pbc.gov.cn/



Inquiry: Design of a Sustainable Financial System

United Nations Environment Programme International
Environment House
Chemin des Anémones 11-13
Geneva, Switzerland
inquiry@unep.org
+41 (0) 229178995
www.unep.org/inquiry