6 October 2017

Productivity Commission
By email: info@productivity.govt.nz

New Zealand Productivity Commission - Low-emissions economy: Issues Paper August 2017

NZX Limited ('**NZX'**) refers to the issues paper 'Low-emissions economy: Issues Paper' (the '**Issues Paper**') published by the New Zealand Productivity Commission ('**NZPC**').

We would like to thank the NZPC for the opportunity to make a submission. In respect of transitioning to a low-emissions economy, NZX has focused its comments on the opportunities and limitations for the capital markets and electricity market.

Our submission responds to the following questions in the Issues Paper (in the order they appear in this submission):

(1) What types of market-based instruments would best help New Zealand to transition to a low-emissions economy? (Q21)
(2) What type of alternative approaches (such as voluntary agreements or support for green infrastructure) would best help New Zealand transition to a low-emissions economy? (Q24)
(3) What changes will be required to New Zealand's regulatory, institutional and infrastructural arrangements for the electricity market to facilitate greater reliance on renewable sources of energy across the economy? (Q12)

We set out our response below.

(1) Types of market-based instruments that would best help New Zealand transition to a low-emissions economy

To meet the 2030 Paris Goals, NZX is committed to helping listed companies access economic opportunities in 'Green Finance' to help lower emissions. As investors globally are taking a greater interest in where their funds are invested, green financial products support sustainable and ethical investment. Generally, these market-based instruments must meet 'green' criteria (for example, either by being approved by the Climate Bond Initiative or meeting the Green Bond Principles set by International Capital Markets Association). While they are new in New Zealand, overseas 'Green' financial products are a well-established category of investment that offers significant opportunity for investors, companies and exchanges.

Locally, there is increasing demand for such products, and growing discussion about how transitioning to a low-emissions economy can be effected. Listed companies appreciate that this is a long-term challenge, which needs long-term vision. NZX notes that a number of companies who have submitted agree with the submission by Parliamentary Commissioner for the Environment that a long term plan for New Zealand, free from political changes, is necessary for meaningful progress long-term.

While NZX's efforts to support Green Finance becoming mainstream is currently at the policy development stage, we understand that green market-based instruments will provide rich opportunities to listed companies and act to set them apart as green finance leaders in the New Zealand capital markets. More broadly, Green finance offers an opportunity to trade on New Zealand's 'Clean Green' reputation internationally, attracting international investment.

NZX is currently considering options to promote listed green bonds[1] and whether NZX should have a role in the certification process. We note that one listed companies, Contact Energy, has already issued green bonds. Other future green exchange products may include Green Indices or Exchange Traded Funds (ETFS). NZX is currently undertaking targeted consultation with the market to ensure that any support NZX provides is fit for purpose. [2]

(2) What type of alternative approaches (such as voluntary agreements or support for green infrastructure) would best help New Zealand transition into a low-emissions economy?

As set out on the Issues Paper at page 47, Box 9, NZX agrees with 'nudging' as a behavioral strategy for the capital markets. We think that there is more value in presenting the positives of moving to a low carbon economy to listed companies and investors via voluntary regimes and guidance, as well as leading by example, than brandishing a stick of strict regulation.

In March 2017, NZX publically committed to the United Nations Sustainable Stock Exchange Initiative (SSEI) to promote sustainability performance and transparency in capital markets. Through this, we voluntarily committed to dialogue with investors, companies and regulators, to promote long-term sustainable investment and improved environmental, social and corporate governance disclosure and performance among companies listed on our exchange.

NZX is also a member of the Green Finance Advisory Group of the SSEI and we have been working closely with the Sustainable Stock Exchanges through the drafting on the SSE Guidance on Green Finance. This document acts as a voluntary took-kit for exchanges to assist in growing green finance. While it is still yet to be finalised and published, we hope to use this guidance note to assist NZX in educating the New Zealand market about green finance, investigating new opportunities and implementing change.

NZX also plans to shortly release its first Environmental, Social and Governance Guidance Note (**the Guidance Note**). The Guidance Note supplements the recommendation in the NZX Corporate Governance Code (the **Code**) which states that:

> '…*An issuer should provide non financial disclosure at least annually, including considering material exposure to environmental, economic and social sustainability risks and other key risks. It should explain how it plans to manage these risks and how operational or non financial targets are measured.*'

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[1] Green Bonds are an instrument where debt is issued to investors for a purpose that meets certain 'Green' criteria (i.e. building wind farms to produce energy).

[2] See our NZX Discussion Document which we recently released on the Main Board Rules that addresses this matter.

The Code is 'comply or explain' so if a company does not disclose the above information, they must explain why not, the same approach as the ASX Corporate Governance Principles and Recommendations. The Guidance Note supplements the recommendation, providing a framework for ESG reporting, suggesting internationally recognised frameworks, and explaining the value of ESG reporting to how a company tells its own story to investors.

A number of listed companies, such as Z Energy, have already taken steps to volunteer to report against the NZX Code. All listed companies must report against the code for reporting dates ending 1 December 2017 and beyond.

(3) What changes are required to New Zealand's regulatory, institutional and infrastructural arrangements for the electricity market to facilitate greater reliance on renewable sources of energy across the economy?

The electricity market facilitates the real time buying, selling and dispatch of physical power between market participants at the wholesale level. NZX is the Market Operator of these arrangements under contracts let by the market regulator; the Electricity Authority. Buyers in the market are typically the electricity retailers and major industrial users. The sellers are the electricity generators, with real time dispatch through the high voltage transmission network being centrally coordinated by the Transpower System Operator.

Around 80% of New Zealand's total generation is provided from renewable sources - primarily hydro, geothermal and wind. This is one of the highest concentration levels in the OECD and something we should be proud of. The government's Energy Strategy aims to lift this to 90% by 2025.[3]

It is important to recognise that achieving this target must not compromise security and reliability of the physical supply of electricity to the end user. Fossil fueled generation plays an important, and necessary, component in ensuring this secure and reliable supply. Since the establishment of the electricity market in 1996, investors and owners of generation assets have proven adept at adjusting their fleet to meet the underlying conditions in the sector driven by changes to demand, supply or fuel availability. NZX contends that investors and shareholders have efficiently developed and retired generation plant, or source alternative fuel supplies, without the need of government underwriting their security of supply decisions and thereby placing undue commercial risk onto the taxpayer. NZX therefore believes that direct government ownership (as referenced in the Issues Paper) or the provision of subsidies is not warranted in order to support standby fossil fueled capacity.

The electricity market has seen the steady increase in generation supply from renewable fuel sources; grid connected geothermal and wind developments. While these have been incorporated onto the market's existing trading arrangements (market rules), the rules were designed for an electricity system that was dominated by large scale hydro, gas and coal fired generation plants. Moving forward, the sector is seeing a proliferation of micro level hydro, wind, solar-PV and battery technologies that will have a profound impact on the current market's design and trading arrangements. NZX considers it timely for the market to review whether the current structures remain fit for purpose and/or can successfully enable these developments in fuel diversity and scale to flourish in a carbon constrained environment.

[3] http://www.mbie.govt.nz/info-services/sectors-industries/energy/documents-image-library/nz-energy-strategy-lr.pdf

Please do not hesitate to contact us should you have any questions.

Yours sincerely

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