WHITE PAPER

From Catwalk to Carbon Neutral: Mobilising Funding for a Net Zero Fashion Industry

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The views and opinions expressed in this paper are those of the authors and researchers and do not necessarily reflect the views or positions of the entities commissioning or supporting this work.

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MANUFACTURER FOREWORD

To our peers and fellow climate activists across fashion value chains and beyond,

The catalyst for co-commissioning this paper is our shared conviction that if we fail to devise new ways of funding decarbonisation, we will also fail to realise our climate goals. We wanted to inspire more expansive, creative and imaginative thinking about how the sector might go about collectively funding decarbonisation in such a way that goes beyond business-as-usual, and primarily debt-based, solutions.

Although the intention and objectives of this paper have been fairly narrowly defined, it's worth emphasising the broader context within which this paper sits. Currently, the sector's approach to climate action places the burden for action on factories in predominantly global South nations. Although this is to a certain extent rational, given that this is where the vast majority of fashion's emissions are currently concentrated, a just transition requires shared risk and responsibility.

Second, this paper's focus reflects the fact that the sector's approach to climate action more generally is overwhelmingly focused on decarbonisation—with less emphasis on adaptation and resilience. However, as the direct employers of some of the individuals most vulnerable to climate change globally, it is our shared conviction that the sector must expand the framing of the current climate action conversation to also include adaptation and resilience. Both adaptation and resilience have their own funding requirements and a just transition demands a collective approach to all three.

Third, the specific challenge of how to fund decarbonisation is an opportunity to re-imagine cost-driven supply chain structures to ensure that they are fit for the future and capable of driving sustainability more generally. Currently, funding for decarbonisation must compete with many other manufacturer investment needs such as improved wastewater management systems, worker wellbeing programmes, and more general growth and infrastructural improvement investments.

Finally, the need for this paper originated in private discussions between producers hosted by the Asia Garment Hub , which led to the realisation that many of our decarbonisation funding challenges are shared. However, we also want to emphasise that our perspectives are not monolithic and we do not align on everything. Indeed, some of us are direct commercial competitors. **Nonetheless, we came together to commission this paper because of our shared belief that manufacturer perspectives on this topic—in all their breadth and complexity—must be better understood if we are serious about driving meaningful impact.**

The contents of this paper represent the outcomes of independently conducted research and not a singular point of view. We hope it inspires more producers to come together to amplify their perspectives.

Sincerely,

Artistic Milliners, Epic Group, MAS Holdings, NITEX, TAL Apparel, Pactics Group, Simple Approach

EXECUTIVE SUMMARY

Cutting roughly 50% of emissions by 2030 and achieving net zero by 2050 in the fashion sector requires significant investment. The Apparel Impact Institute (Aii) estimates fashion industry decarbonisation will cost USD1 trillion up to 2050.

The vast majority—by some estimates up to 80%—of fashion's emissions are in the supply chain. Much of the work needed to deliver on the sector's net zero goals must thus happen in production.

Yet, brands and retailers hold the largest share of revenues and margins. Upstream actors also usually have smaller turnovers and steeper debt-to-revenue ratios. **The misalignment of margins, contrasted against the concentration of emissions, poses a real challenge to funding sector decarbonisation.**

Compounding this structural inequity are the variety of decarbonisation funding needs manufacturers have, ranging from projects with payback within three years to those with payback of over ten years. Even within a single class of projects, nuances based on geography, age of the in-use infrastructure and its design, local policies and energy costs as well as relationships between the manufacturer and its brand and retail customers will change approaches to financing. Payback periods, too, are highly contextual.

It is within this complex environment that manufacturers interviewed for this report described a number of hindrances to their decarbonisation efforts. They include financing challenges; policy barriers tied to geographical location and national agendas; condition of facility infrastructures; challenges in the brand-manufacturer relationship associated with purchasing practices; and a lack of a collective approach to decarbonisation.

↓ Specifically:

Business and Financing Bottlenecks Faced by Manufacturers:

Capital expenditure (CapEx) risk not shared	Manufacturers said that, on the one hand, the full burden and risk of capital investments tended to fall on them whilst, on the other, they struggled to raise the requisite funding.
Lack of solutions beyond debt	Many manufacturers, especially in the small and medium enterprise (SME) sector, said their high leverage and limited company size placed debt out of reach. Without other (non-traditional) funding options, and the sharing of climate action risk-reward, industry-wide decarbonisation will lag and falter.
Burden of increased operating expenses (OpEx) not shared	When decarbonisation projects add to their operating costs (short-term or otherwise) without the option of sharing these among value chain participants, including consumers, manufacturers worry they cannot invest without making unworkable margin cuts.
Business cycle risk	Interviewees said they typically do not have much visibility into the order pipelines beyond a season. The fashion industry's cyclical nature thus reduces the span during which investment practically occurs.
Debt affordability	Lack of access to lower-cost US dollar or euro funds keep domestic financial markets in manufacturer countries from supporting decarbonisation. Other obstacles were high double-digit interest rates applicable in local currencies and, to a degree, the absence of financial system transparency and depth resulting in poor local capacity and resources.
Lack of tools to derisk investment and debt	An estimated 45% of Tier-1 entities and nearly 30% of Tier-2 entities are in developing countries where adverse macroeconomic conditions have led to elevated country and equity risk premiums, making them riskier to potential lenders (Appendix 2). Some manufacturers cannot raise funds because of the risk profile of their organisation or of a given project.
Lack of local policies for renewable energy and energy transition	Some respondents in certain jurisdictions lamented the lack of reliable legal frameworks, the adverse impact of certain domestic energy policies and the absence of physical infrastructure to support specific decarbonisation strategies.

Available solutions for decarbonisation projects are grossly inadequate compared with the requirement and are only accessible to a narrow group of manufacturers. Consequently, manufacturers are overwhelmingly likely to implement short-payback, smaller-scale projects. Medium, long-term and no-payback initiatives call for larger investment as well as innovative solutions that extend beyond debt and address the issues of accessibility, affordability and availability of funding.

Innovative funding solutions that could meet these challenges are:

Establishing a Fair Climate Fund	Built on the principle of equity, adopting the Fairtrade model. Each value chain partner diverts to it a portion of revenue, which is then disbursed as grants to finance supply chain decarbonisation projects.
Brand-supplied debt repaid via product discounts	The larger, more profitable brands and retailers provide funding for which repayments are through discounts on future product orders.
Cost-sharing with consumers—green tag for decarbonisation	A clothing line priced slightly over the conventional range, with clear information to consumers that the premium—displayed as a “green tag” at the point of sale—will exclusively fund decarbonisation of the product’s supply chain.
Green bonds and equity	Capitalises on growing interest for green bonds and equity in an environment where investors are increasingly focused on economic, social and governance (ESG) factors.
Islamic finance	A project funding tool—particularly for countries with a majority of followers in the Islamic faith—that differs from regular bonds in that it is not speculative and derives revenue through direct asset ownership rather than interest-bearing debt.
Mitigating business cycle risk	Business cycle insurance for investment policies to cover disruptions or downturns that impact loan repayment ability.
Credit guarantees	Credit guarantees from governments, multilateral development banks (MDBs), development financial institutions (DFIs) or export credit agencies (ECAs).
A Just Transition Fund	Created through regulatory levies, it will be accessible to manufacturers in developing countries to support value chain decarbonisation.