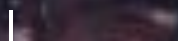
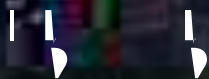


An aerial night view of a city with colorful digital glitch effects. The text is centered in the middle of the image.

**DELIVERING ON THE \$100 BILLION
CLIMATE FINANCE COMMITMENT
AND TRANSFORMING CLIMATE FINANCE**



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**The views expressed are those of the expert group in their individual capacities, not of the institutions or organizations they represent and nor of the United Nations. Leonardo Martinez Diaz contributed to the report until 9 November 2020, after which he recused himself from further engagement given new official responsibilities.*

INDEPENDENT EXPERT GROUP ON CLIMATE FINANCE

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AF	Adaptation Fund
AfDF	African Development Fund
AsDF	Asian Development Fund
AUM	Assets Under Management
BAs	Biennial Assessments and Overviews of Climate Finance Flows
BRs	

SYNOPSIS

As implementation of the Paris Agreement moves into its first five-year cycle, the focus must immediately pivot to ensuring that there is a major collective boost of climate finance to support strong and green recovery packages and enhanced ambition of Nationally Determined Contributions (NDCs).

The next five years are crucial, starting with 2021.

The collective goal must be to more than surpass the \$100 billion per year target in 2021 and to scale up international public finance in the period thereafter to accelerate the drive to net zero carbon and climate-resilient growth.

The \$100 billion target therefore needs to be seen as a floor and not as a ceiling.

2021 will, thus, be a critical year – to sustain trust between developed and developing countries, maintain momentum in the run-up to COP26, and to forge a new consensus about the necessary climate action and ambition to achieve global carbon neutrality by mid-Century.

The immediate and urgent need for ambition in 2021 so as to recover lost ground does not end in 2021. It only starts then. There is a need for a significant ramping up of climate finance from here on in, *and it will have to be mobilized from all sources.*

These steps will also lay the foundation for a more robust climate finance architecture in the period leading up to 2025 when an ambitious new collective target must be set.

To mobilize resources commensurate with the quantum of needs will effectively require a coordinated effort to make all financial flows, public and private, “consistent with a pathway towards low greenhouse gas emissions and climate-resilient development”, as stipulated in Article 2.1c of the Paris Agreement.

The Climate Finance Framework as illustrated by *Figure 1*

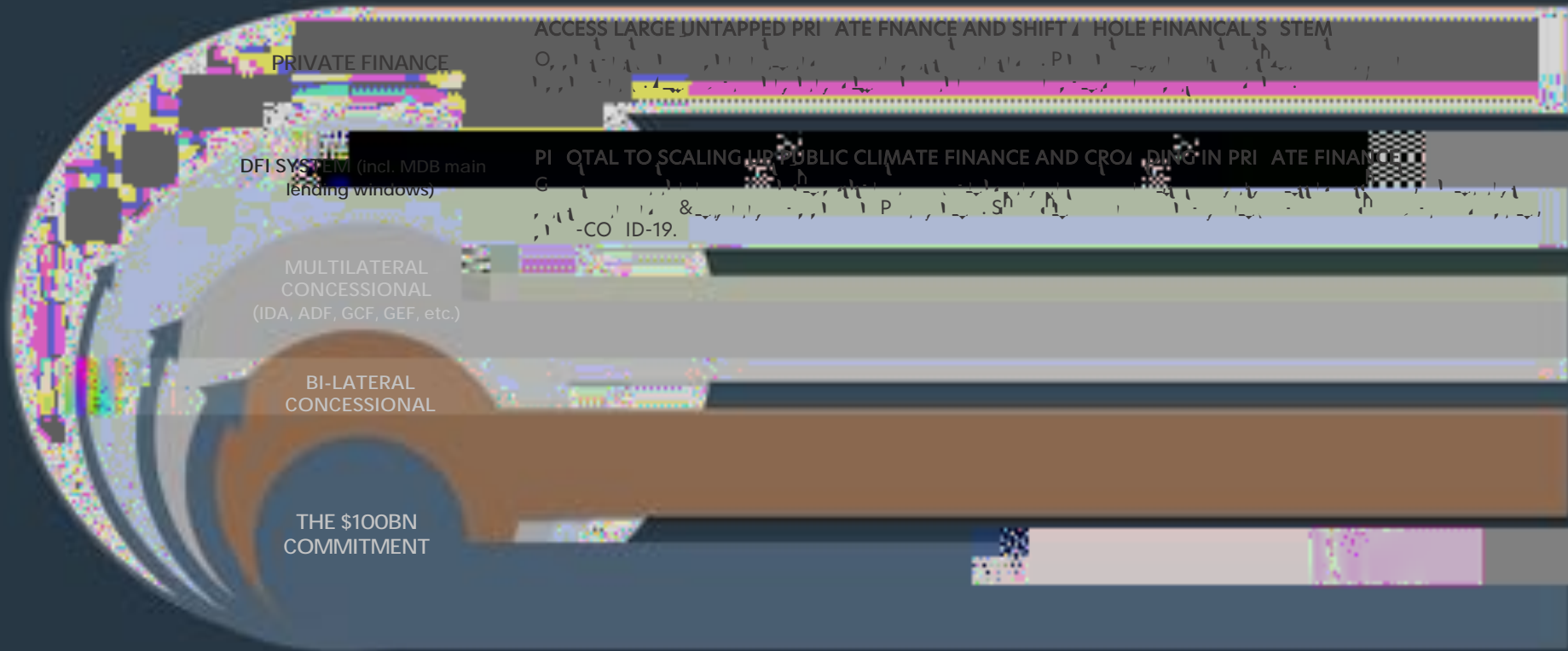
to developing countries. Ambitious replenishments for these funds will be critical over the coming five years given their importance for boosting mitigation and adaptation finance and enabling the MDBs and Development Finance Institutions (DFI) system more broadly to mobilize private investment.

- The DFI system, including the MDBs and the IDFC (International Development Finance Club), are the most effective international means to support enhanced climate action in developing countries and mobilizing and leveraging climate finance at scale. The DFI system is also the principal interface between the public and the private sectors. It will be essential for DFIs to align their operations with the goals of the Paris Accord, to work better as a system, seek to better leverage their balance sheets, and enhance their private sector multipliers through strategic partnerships and better instruments.
- Given the volume of emergency rescue and stabilization finance that MDBs will be providing, and the magnitude of finance that will be needed for recovery and transformation, it is critical for shareholders to consider additional and substantial infusions of capital with urgency, taking individual MDBs' circumstances into account. There is also a strong case for an extraordinary replenishment of IDA in 2021, and possibly the African Development Fund, given the 'front-loading' of resources that has occurred in response to COVID-19.

The international community under the leadership of the UN should explore all options to enhance the envelope of international public finance including through innovative and alternative sources of finance. One promising option would be large additional SDR (Special Drawing Right) allocations and revised allocation mechanisms to enable poor and vulnerable countries to access low cost finance.

It will also be critical to tackle debt distress and excessive debt overhang especially in poor and climate vulnerable countries. COVID-19 has greatly exacerbated debt vulnerabilities in both low and middle-income countries at a time when they urgently need to scale up investment. The DSSI program and its extension have provided temporary relief to a targeted set of countries. But a more comprehensive approach is needed and must be a priority for multilateral discussions in 2021. A promising systemic approach, with

There can be only one way forward: to fully integrate climate-aligned structural change – in particular by accelerating the transition to low-carbon and climate resilient infrastructure – with a strong post-COVID economic recovery. This will require a fundamental shift in the whole finance system and a massive increase in private finance to get the world from the billions to the trillions that are urgently needed – as set



1. THE CHANGING CONTEXT: THE IMPACT OF THE COVID-19 PANDEMIC AND THE TRANSFORMATIVE IMPERATIVE OF CLIMATE FINANCE

In addition, as ILO analysis shows,¹⁴ the rate of relative poverty, which is defined as the proportion of workers with monthly earnings that fall below 50 per cent of the median earnings in the popula-

The macro-fiscal context has worsened substantially in the past year, especially in the developing

Hence, economic recovery programs that necessarily seek to rescue and stabilize economies must also pave the way for accelerated and sustained transformation to low-carbon climate-resilient growth.

Sustainable investments to boost recovery and long-term transformation have good short and long-term features. In the short run, they should be labor intensive but not import intensive, and have strong economic multipliers. In the long run, they can boost productivity and generate powerful co-benefits such as protection of ecosystems and biodiversity. There is overwhelming evidence of how investment in sustaina-

2. PROGRESS TOWARDS THE \$100 BILLION TARGET - WHAT IS THE CURRENT STATE OF CLIMATE FINANCE

SUMMARY OF KEY MESSAGES & RECOMMENDATIONS

The nature of the target:

- The commitment by developed countries to mobilize jointly \$100 billion per year in climate finance by 2020 has been central to the climate accords since 2009. As such, delivering on this commitment

agencies. In this regard, it is important that MDBs continue to provide disaggregated data to the DAC Creditor Reporting System (CRS).

- Private finance mobilized by public interventions is a core component of the \$100 billion that must be accounted for in a clear, transparent, and credible way. The approach taken by the OECD in its 2019 report is a step forward towards greater transparency and a more robust estimation of mobilized private finance. Further progress on assessing mobilized private finance will require working out appropriate modalities for sharing commercially sensitive data, which can be tackled.
- The OECD's DAC system for reporting on climate-related finance can complement countries' reporting of climate finance to the UNFCCC. In particular, it is important to increase transparency by Parties at project level on how they go from climate-related (under the DAC) to climate-specific

2.1 UNDERSTANDING THE NATURE OF THE \$100 BILLION COMMITMENT

The recovery pathway must avoid structural damage while fostering structural change.

The \$100 billion commitment is a central part of the “grand bargain” at the heart of the Paris Agreement. As such, delivering on this commitment is an important symbol of trust. The commitment came out

funds provided through bilateral, regional and other channels, multilateral channels and mobilized through public interventions, and include reporting by financial instrument, e.g. grant, concessional loan, non-concessional loan, equity, guarantee, insurance, other.

What is not specified in the agreements are the proportions of financing from these different sources

Table 1: Comparison of the key data sources that track and assess progress towards \$100 billion target

Assessment	Bilateral public climate finance from developed countries		Multilateral public climate finance attributed to developed countries		Officially supported export credits from developed countries	Private climate finance mobilized by developed countries
	Grant-equivalent	Concessional lending	Grant-equivalent	Concessional lending		
BRs 2020	Climate-specific, status, funding source (ODA, OOF, other), financial instrument (including grants and concessional loans), type of support, sector and additional information		Core/general, climate-specific, status, funding source (ODA, OOF, other), financial instrument (including grants and concessional loans), type of support and sector		Parties can include under Other Official Flows (OOF)	Parties have reported in narrative form, increasingly including information on public investments and estimates in the resulting private sector leveraged
BA 2018	BRs to the UNFCCC		Fund financial reports, CFU; MDB joint report		Included under bilateral	MDB joint report; OECD for bilateral & regional
OECD 2020	BRs to the UNFCCC and complementary data submissions		OECD DAC statistics on development finance (activity-level data)		OECD export credit statistics	OECD DAC statistics (activity-level data)
CPI 2019	OECD DAC		Surveys of DFIs; OECD DAC; Climate Funds Update; ODI/HBF; BNEF; IEA		n/a	Primary capital flows: BNEF; Climate Bonds Initiative; IEA; REN-21; IJ Global
Oxfam 2020 (Climate specific net assistance)	BRs, Climate-related finance OECD DAC	n/a	BRs, Climate-related finance OECD DAC	n/a		
MoF India (2015)	Disbursed; 'new and additional'	n/a	Disbursed; 'new and additional'	n/a	n/a	n/a

2.3 CRITIQUES OF ASSESSMENTS OF PROGRESS TOWARDS MEETING THE \$100 BILLION GOAL

Efforts to measure and report on progress towards the \$100 billion have been subjected to a wide variety of critiques that can be consolidated in four types:

- Counting private and non-grant finance, which some have argued should not be counted;
- Counting finance that is not climate-relevant;
- Applying non-transparent and inconsistent methodologies to count mobilized private finance, resulting in overstating finance volumes; and
- Shortfalls in the quality and composition of finance from what is suggested by the accords.

a. Counting private and non-grant finance

Some critics have argued that only public finance should be counted towards the \$100 billion, and that private finance mobilized through public finance and export credits should be excluded because of their commercial orientation. Other critiques argue that only grant finance should be counted as part of the \$100 billion commitment. Oxfam, for example, in its 2020 report has argued that: “only [the loans, guarantees and other non-grant instruments’] grant equivalent counts, [since] anything outside of this does not constitute assistance (in terms of a net transfer of resources) to developing countries.”⁵³ The Indian Ministry of Finance has made a similar argument.⁵⁴

These critiques respond to the diverging interpretations of the legal and political considerations underlying the climate accords. As cited above, Parties agreed that: “funds provided to developing country Parties may come from a wide variety of sources, public and private.” Moreover, excluding non-grant finance would understate the value that non-grant instruments, such as loans and equity, contribute to making climate investments possible. The fact that these instruments involve an expectation that a portion of the value generated by the investment will flow back to the investor does not render the instrument’s contribution valueless. Counting only grant finance runs contrary to the collective understanding of the \$100 billion under COP decisions. Parties decided that private sector finance that is mobilized by public finance provided by developed countries is to be included as a valid source, and since the private sector does not typically provide finance on concessional terms, excluding non-concessional finance necessarily entails excluding private sector finance from the calculation.

However, analysis of the composition of climate finance provided and mobilized is important for assessing progress. Reporting of detailed information by developed countries as specified in the modalities on the transparency framework for support (discussed earlier) - including voluntary reporting on grant-equivalent finance - is central for generating comprehensive and consistent data in this context.

b. Counting finance that is not climate-relevant

Another critique is that some finance is inaccurately reported as climate finance, which inflates the numbers. As noted above, the OECD DAC has set out the so-called “Rio markers” to monitor the mainstreaming of climate into development finance. The markers help determine the climate relevance of the official development assistance by identifying projects where the “principal” objective is climate-related,

(including for example the UK and the United States) currently undertake ad-hoc assessments for each project, whereas a number of countries use a range of fixed coefficients (e.g., 30%, 40%, 100%) that apply by default depending on whether climate change was the only, primary, or secondary objective pursued by the project. According to the OECD, based on responses received by 19 out of 30 DAC members, the results of the 2020 survey (forthcoming) show that in most cases, countries apply fixed coefficients to any activity marked principal or significant with the Rio markers on climate change.

The MDBs typically also conduct activity-by-activity analysis and make judgements about what to count as climate finance based on their own methodology, which is more detailed than the Rio markers, although the underlying activity data is usually not disclosed. Going forward, greater transparency in how the data they report to the UNFCCC is linked to the data they report to the DAC can help address this issue.

Given the approach taken, Oxfam has asserted that bilateral climate finance specifically targeting climate

As several stakeholders have noted, however, there are a number of problems with the current system of accounting for mobilized private finance:

- Counting public money provided on commercial terms. In the past, money provided in the context of a commercial transaction by public entities from developing countries, such as government-owned development or investment banks, has been reported and counted as mobilized private investment. This is not accurate, as the money is coming directly from public sources from a developing country, and it therefore should not be counted toward the \$100 billion. Clearer guidelines are needed on

d.

administrative, systemic and process deficiencies on the donor side.

Another issue relates to calls that the \$100 billion in climate finance should be “new and additional.

Although legally the concept of “new and additional” is not directly linked to the \$100 billion commitment, past COP decisions have referred to the need for new and additional finance to be provided to developing countries. This notion refers to the need for climate finance to be added on top of existing development aid flows and ensure that development finance does not decline as climate finance increases. Analysis by the OECD⁶⁹ for 2014-2017 did not find evidence for causality between the changes in the sectoral composition of development finance and climate-related allocations: aggregate ODA trends in climate sensitive sectors (e.g. energy, transport) and social sectors (e.g. education and health) displayed similar patterns.

The share of climate-related ODA reported to the DAC between 2014 and 2017, remained stable at around 20-21%, while the share of multilateral climate finance in total multilateral outflows to ODA-eligible countries grew from 18% in 2013 to 28% in 2017. Over time the overlap between climate and development finance has increased given that climate investments serve both climate and development needs and the other way around. In particular, the efforts to scale up support for sustainable infrastructure by multilateral development banks and many providers of bilateral finance mean that a growing proportion of finance serves both climate and development objectives. On the other hand, the compilation and synthesis report of the BR4s points to a trend of donors channeling more climate finance towards climate-dedicated initiatives rather than to other type of broader environmental and development funds.⁷⁰

Further clarity on what counts towards the climate finance goal in the UNFCCC and increased transpar-

Secretariat to provide an overview of the self-reported figures by Annex II Parties of the Convention. The OECD estimates for public finance track those of the BA assessments (based on the BRs and data reported by climate funds and the MDBs) and are a little lower because of the adjustments made discussed above.⁷¹

The CPI estimates of climate finance are much larger because they encompass all capital flows directed toward low-carbon and climate-resilient development interventions with direct or indirect greenhouse gas mitigation or adaptation benefits beyond the scope of \$100 target and hence not included. The Oxfam and Ministry of Finance, India estimates exclude concessional, mobilized private finance and other types of finance (as per Table 1) resulting in much lower ranges. For example, Oxfam (2020) assesses climate specific net public assistance provided to be in the range of \$15-19.5 billion in 2015-2016, and \$22.5 billion in 2017-2018.

The overall trajectory of climate finance has been in an ascending direction. Total climate finance mobilized by developed countries increased by 51 percent between 2013 and 2018 (*Table 2*). This push upward

Table 2: Assessments on finance provided and mobilized by developed countries for climate action in developing countries (USD billion)

	2013	2014	2015	2016	2017	2018
Climate finance provided						
2013-2014 ¹	23.1	23.9	29.9	33.6	n/a	
2013-2014, 2015-2016, 2017-2018 ²	23.1	23.9	29.9	33.6	32.3	32.3
2020 ³ (Excluding export credits, including finance by bilateral providers via multilateral channels)	22.5	23.1	25.9	28	27	32.7
Climate finance mobilized						
2013-2014	Not reported separately				n/a	
2020	1.6	1.6	2.5	1.5	2.1	2.1
Multilateral climate finance						
2013-2014	1.9	2.5	1.4	2.4	/	
MDB climate finance ⁴	14.9	16.6	17.4	19.7		
2013-2014, 2015-2016, 2017-2018 ⁵	14.3	16.4	12.8	13.1	16.4	16.4
2020 (MDBs climate finance and multilateral climate funds)	15.5	20.4	16.2	18.9	27.5	29.6

1 Sources: Table 2.6 page 64 of the 2018 BA Technical report for the whole period 2013-2016. The same data is reported in Figure 1, page 5 of the 2016 BA's Summary and Recommendations for 2013-2014, and Figure 1, page 6 in the 2018 BA's Summary and Recommendations for 2015-2016. These figures include climate-specific finance provided by Annex II Parties to developing countries, as reported in their BRs via bilateral, regional and other channels.

2 Sources: Figure 21, page 66 of the compilation and synthesis report of BR2s for 2013 and 2014; Figure 29, page 57 of the compilation and synthesis report of BR3s for 2015 and 2016; and paragraph 222, page 71 of the compilation and synthesis report of BR4s for 2017 and 2018, of Parties included in Annex I to the Convention. October 2016, November 2018 and November 2020. The compilation and synthesis report of BR4s gives an average for 2017 and 2018. Annex II Parties reported figures including climate specific and core/general support.

3 Source: Figure 1, page 5 of the 2016 BA's Summary and Recommendations for 2013-2014, and Figure 1, page 6 in the 2018 BA's Summary and Recommendations for 2015-2016.

4 This includes climate finance commitments by MDBs from their own resources attributed to the members of the OECD DAC, minus the Republic of Korea, to OECD-DAC recipients eligible for official development assistance. Table 2.9 page 67 of the 2018 BA Technical report presents figures for the whole period 2013-2016, providing an upper and lower range due the variation in the assessed share attributable to the Annex II Parties. The lower ranges use the approach based on the ownership shares held by developed countries and suggests about 65 per cent in 2013 and 2014, 74 and 77 per cent of the finance to developing countries in 2015 and 2016 respectively can be attributed to OECD member countries. The upper range is calculated based on the developed and published in OECD (2015d) that captures the mobilization effect through MDBs. Given that both the 2016 and 2018 BA's Summary and recommendations reports only present the upper range based on the OECD methodology, the same figures are presented here.

5 Source: Table 11, page 65 of the compilation and synthesis report of BR2s for 2013 and 2014; Figure 28 and table 6, page 56 of the compilation and synthesis report of BR3s for 2015 and 2016; and table 4, page 70 of the compilation and synthesis report of BR4s for 2017 and 2018, of Parties included in Annex I to the Convention. October 2016, November 2018 and November 2020. Annex II Parties reported contributions through multilateral channels, including climate specific and core/general support to MDBs.



3. TURNING THE BILLIONS INTO TRILLIONS: HOW CAN WE GET MORE MONEY TO FLOW TOWARDS CLIMATE-RELATED INVESTMENTS IN DEVELOPING COUNTRIES?

SUMMARY OF KEY FINDINGS & MESSAGES

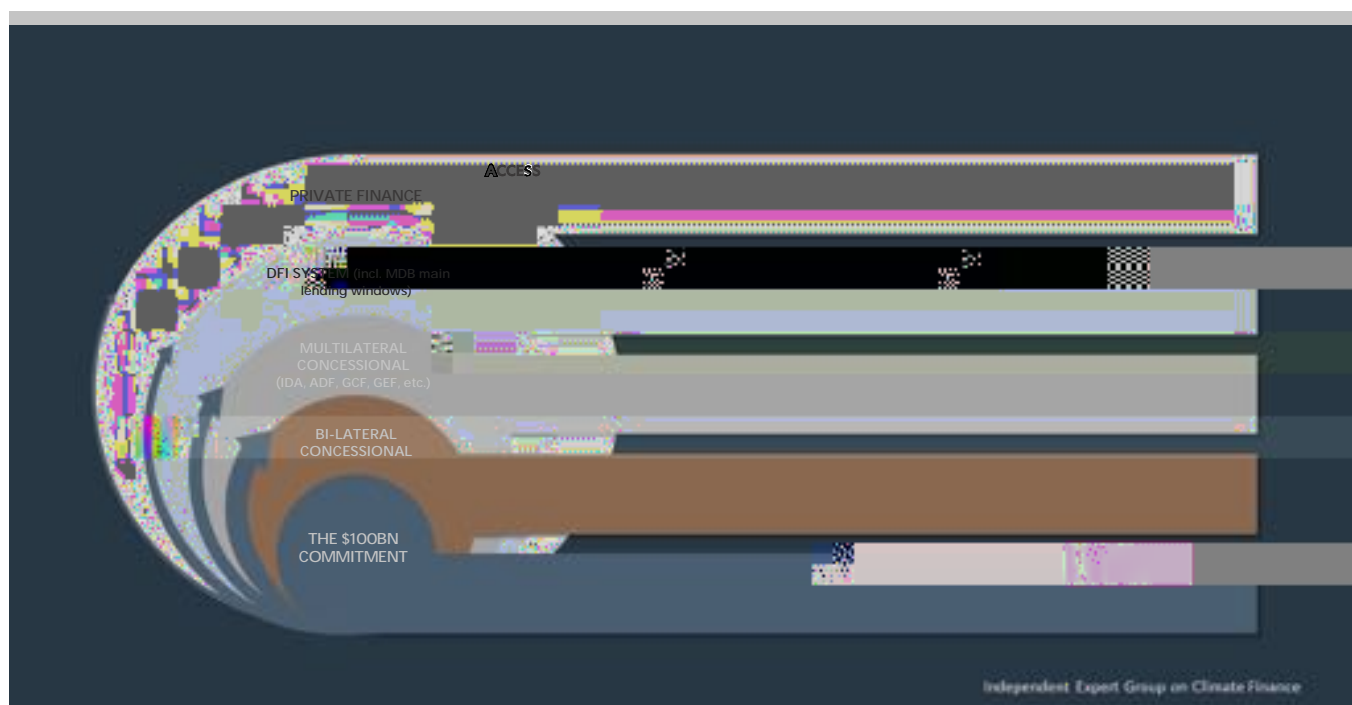
- Even prior to the COVID-19 pandemic, it was clear that a major scaling up of international climate finance would be needed to enable developing countries to adopt more ambitious NDCs and the sustainable development goals.
- The COVID-19 pandemic has made the delivery of international climate finance even more urgent. Developing countries need to put in place ambitious and sustainable recovery packages that can enable them to respond simultaneously to the COVID-19 and climate crises. But they must do so against a much more difficult debt and financing context. Beyond the recovery phase, a sustained scaling up of investments in green and resilient infrastructure will be required to enable them to transform their economies to meet their climate and development goals.
- The \$100 billion commitment should play a key role in enabling developing countries secure a strong and sustainable recovery and can be a foundation for the scaling up of climate finance in the 2021-25 period needed for sustained transformation. Although the \$100 billion commitment constitutes the dominant part of international public climate finance, given the scale of the needs, all pools of international finance will have to be bolstered and used more effectively - individually and collectively: bilateral and multilateral, concessional and non-concessional, and especially private finance.
- All countries will need to unlock opportunities for low carbon climate resilient infrastructure and other climate-related investments to support recovery and transformation. Domestic policy must play its part and should include a decisive phasing out of fossil fuel subsidies and the equitable pricing of carbon. This will also help boost progress on the SDGs.
- All bilateral donors must live up to their climate finance commitments and set more ambitious targets. The need for the grant component of climate finance is even greater than before; given its critical role in the climate finance architecture, grant finance should be at least doubled from its very low level of around \$12 billion in 2018.
- Multilateral climate funds, while modest in overall volumes, can play an important catalytic role in scaling up investments and leveraging other sources of finance including the MDBs. The international community under the leadership of the UN must seek to bolster and make more coherent the concessional climate finance architecture encompassing the Green Climate Fund, the Global Environment Facility, the Climate Investment Funds, the Adaptation Fund as well as the concessional windows of the multilateral development banks and the Global Infrastructure Facility.
- The MDBs occupy a key position within the international climate finance delivery system. Because

just transition. Carbon pricing, including subsidy reform, can be a critical component in the package of climate policies needed to restore growth and decarbonize the economic system. At last count, 78 countries, states, provinces, and cities worldwide have adopted carbon-pricing policies, but these initiatives

surpassed, given the urgent need to support a climate-aligned recovery from the COVID-19 crisis. But we must also anticipate the substantial scaling up of sustainable investments that will be needed beyond recovery to enable developing countries implement more ambitious NDCs consistent with the drive to net zero and climate-resilient growth.

Hence, the \$100 billion target by 2020 should be seen as a floor, and not a ceiling. Developed countries must continue to lead the mobilization of substantial financial resources that will be needed by developing countries for mitigation and adaptation. While the \$100 billion commitment is the foundation and the dominant part of international public finance, it will be necessary to scale up all pools of finance if we are to go from the “billions to trillions” if developing countries are able to deliver on climate action at the pace and scale that is needed. Moving into the full implementation of the Paris Agreement, as established in its Article 9, paragraph 2, the voluntary contributions of other countries must be encouraged too. Given the critical need to accelerate action and investment in adaptation, especially in poor and vulnerable countries, the scale of finance for adaptation needs to be urgently bolstered.

\$ To mobilize resources commensurate with the quantum of needs will effectively require a coordinated effort to make all financial flows, public and private, “consistent with a pathway towards low greenhouse gas emissions and climate-resilient development”, as stipulated in Article 2.1c of the Paris Agreement. Ensuring flows from all public financial institutions become so aligned will be especially important.



The Climate Finance Framework above represents the key channels through which the \$100bn commitment by 2020 can help transform the climate finance system – underlining in particular the relative scarcity of public concessional resources, and hence the need to deploy these for maximum impact:

- The \$100bn per annum by 2020 commitment is the foundation of the entire international climate finance system. It not only represents the climate finance mobilized by developed countries for climate action in developing countries, but also constitutes the bulk of international public finance.

- Bi-lateral donors are the original source of almost all concessional climate finance, whether deployed via bi-lateral or multilateral vehicles. Concessional resources are necessary not only to support activities that cannot generate cashflows with which to repay debt including for investments in low-income and vulnerable countries, but also critical for mobilizing other much larger pools of non-concessional finance. Bi-lateral vehicles consist predominantly of developed country national official developed agencies.
- Multilateral concessional vehicles can target climate finance to high priority needs especially for

IDA and the African Development Fund are very important sources of concessional finance for poor and vulnerable countries.

The first replenishment of the GCF will enable it to increase its annual programming by more than 70 percent. The successful replenishment of the GCF hosted by the Government of France, in October 2019, mobilised \$9.78 billion from 27 countries. Eight contributors have made additional pledges since then with the total now in excess of \$10 billion.¹⁰⁵ Together with the replenishment, the Board of the GCF adopted important measures to improve governance arrangements.

Since the replenishment in October 2019, the GCF has made significant strides in strengthening its operational strategy and delivery of climate finance.¹⁰⁶ At its last meeting, the Board of the Green Climate Fund approved an Updated Strategic Plan for the Green Climate Fund 2020-2023, hopefully setting an ambitious direction for the GCF during its first replenishment period. Over USD 2 billion in new commitments was approved by the Board in 2020 despite the constraints imposed by the COVID19 pandemic, making it a record year for GCF programming.

The improved track record of the GCF provides a strong basis to expand its role with commensurate ambition on the scale of resources. The GCF has not only successfully expanded its own role in financing climate mitigation and adaptation, but has emerged as an important platform for cooperation on scaling up climate action with both the public and private sector.¹⁰⁷ Buttressing the resources of the GCF within this replenishment cycle and beyond can greatly contribute to enabling it to become a powerful driver of strong climate action in developing countries supported by a strong international network of public and private entities. In the immediate term, a commitment by the United States to honor its past commitments and join the new replenishment and additional contributions from others could provide a welcome boost to the resources needed by the GCF. There is also a need to anticipate and prepare for a much more ambitious second replenishment.

In addition, the GCF's Private Sector Facility is well placed to engage proactively with the private sector to achieve results at scale. It has achieved good results so far but will need substantial reforms to live up to its original expectations.¹⁰⁸ The GCF's Board should permit the PSF to directly finance projects¹⁰⁹ by making specific changes to the Fund's business model and by ring-fencing a specific amount for the PSF to pilot direct investment. This would allow the PSF to invest in opportunities other than those that accredited entities are putting forward to develop a better project pipeline, and invest with private sector entities that are not interested in going through the accreditation process. The GCF can then take a more proactive role in facilitating investments in lagging sectors such as urban¹¹⁰, disaster risk, and private sector adaptation investments, as well as contribute to paradigm shifting projects and programs in partner countries.¹¹¹

The Global Environment Facility (GEF), which serves as a financial mechanism to five conventions, including to the UN Framework Convention on Climate Change as well as Convention on Biological Diversity and UN Convention to Combat Desertification, has secured US\$ 4.1 billion for the 2018 - 2022 investment cycle. Since GEF resources are provided as grants, they play an important role in providing upstream support for capacity building and policy support and in leveraging other pools of finance. The GEF has been developing multi-stakeholder platforms such as a Food and Land use coalition, and one for sustainable cities, which are joined by national and local governments, business and finance, CSOs and academia. This has enabled it to enhance its scale and impact. The GEF is well positioned to play a direct and catalytic role in specialized areas of climate action and in non-climate aspects of the global commons. This will likely require a significant augmentation of its resources in the next replenishment cycle.

Building on its successful track record over the past 12 years, the Climate Investment Funds (CIF) can play an important role as a scaling up instrument for mitigation action and resilience through the MDBs.

The COVID19 pandemic has required an extraordinary response from the MDBs, with implications for their future support for climate action. Altogether MDBs have committed in excess of \$230 billion in sup-

step up their support to enable developing countries to accelerate the phase out of coal and tackle the related challenges of managing the social transition.

MDBs will need to achieve higher mobilization ratios going forward, whilst taking into account developing country concerns relating to increased private sector investment. There are a number of new initiatives to bolster mobilization of private finance.¹²⁴ Pending the outcome of these, we would like to draw attention to instruments important to the private sector that MDBs already employ, but which could be further developed and more extensively deployed.

- *Guarantees*: Despite guarantees having generated almost 45% of the private finance mobilized by MDBs (whilst represent only 5% of their commitments), both MDBs and their donors have had limited incentives to scale up their use. Guarantees require the same amount of capital set-asides as loans and are more complex to originate. An additional factor for donors is that guarantees are not counted as ODA unless actually called.¹²⁵
- *Local currency lending*: Exposure to exchange rate fluctuations constitutes a very substantial risk associated with foreign or 'hard' currency borrowing, as evidenced by major swings in foreign exchange markets caused by events such as the 2008 financial crisis and coronavirus pandemic. This represents a significant barrier to enhancing private sector investment in many developing countries¹²⁶, and a more diversified currency offering would facilitate access to climate finance by a range of private sector entities, domestic and international alike. The ability to borrow in domestic currencies would also be critical to many sub-national government entities.

Moreover, as mentioned above, since public borrowing by a number of countries via international bond markets in 'hard' currencies has been rising, MDBs being able to offer them refinancing options in domestic currency can help reduce their debt risk profile. MDBs' business model has traditionally involved providing the bulk of loans in the 'hard' currencies of the largest 'core' capital markets where they are able to readily place large bond issues. Such matching minimises their exposure to exchange rates, and means that they have limited incentive to actively stimulate demand for local currency borrowing. Whilst MDBs have been working to diversifying the currencies in which they issue bonds, continued effort will be required.

- *Equity investments*: Equity investments are another potentially impactful means of de-risking activities to attract private capital. MDBs can leverage their research units and databases as well as their on-the-ground presence and long-standing relationship with key in-country actors to support equity operations.¹²⁷ Existing disincentives (such as reluctance to tie up capital for extended periods before returns can be realised, lack of ready exit opportunities to limit losses, and the fact that equity investments are rated lower for transfer and convertibility risk compared to loans¹²⁸) would need to be addressed.

Greater scale of action can be achieved by growing the capacities of cities as well as domestic private sector and non-profit entities in developing countries, and for this to happen new mechanisms that significantly increase the flow of funds to them must be developed. A good starting point would be to target capacity building support towards urban adaptation planning, and thereby highlight risks associ-

disasters strike. A timely and effective response can save lives and livelihoods, but many countries don't have access to disaster risk finance and must rely exclusively on the humanitarian community for aid post-disaster. The MDBs' regional risk insurance pools, and other entities now provide financial tools including sovereign parametric insurance and contingent credit lines. But few countries have well-developed strategies that deploy multiple instruments to cover the full range of risks they face since only a few have been able to do so.

Donors and other entities must find new ways to channel concessional finance for disaster risk finance, including by expanding the roles of regional MDBs, IDA, including through the potential creation of new financial vehicles that incentivize collaboration among disaster risk finance providers.¹²⁹ Additional voluntary contributions to other funds are also needed; for example, the Adaptation Fund, serving to the Paris Agreement and its goals.

3.7 The Broader Development Finance System

In addition to the MDBs, the broader development finance system, and in particular the International Development Finance Club, can play an important role in both scaling up and better aligning its support to the Paris Agreement. A concerted effort from all major International Financial Institutions will be required to help meet increasing needs for climate-aligned development finance during the post-pandem-

The IDFC recently convened the Finance in Common Summit, an inaugural meeting of all public development banks. As stated in the preamble of their joint declaration, this new coalition has the potential to make a major contribution to ramping up climate finance through enhanced public-private partnership and greater collaboration between international and national development banks:

IDFC members have great scope for expanding their role in climate finance, both directly and in partnership with the private sector and national development banks. In addition:

- **IDFC members should take the lead in providing climate finance to non-sovereign actors within their circumscriptions** - including to state/provincial and municipal governments.
- **IDFC members should also assume a larger role in the provision of guarantees to diversify away from their present reliance almost exclusively on loans, particularly for infrastructure.** As national development banks, along with some other members of IDFC, benefit from the backing of their national treasuries and thus have a lender of last resort (unlike MDBs), these institutions are already well placed to do this if mandated to.¹³⁴
- **IDFC members should accelerate the alignment of their finance with the Paris Agreement based on the framework that they have been developing, including through coal/fossil fuel divestment.**

3.9 Export Credit Agencies (ECAs)

Whilst MDBs, along with a number of DFIs, have established climate finance targets and are working towards phasing out support to fossil fuel investments, the Export Credit Agencies (ECAs) of G20 countries continue providing billions of dollars in finance for fossil fuel projects. Given that ECAs provide almost twice as much international public finance as MDBs, it is critical for policymakers to engage with this issue.¹³⁵ A report by Oil Change International¹³⁶ identifies ECAs as the least Paris Agreement-aligned public finance actors analysed; in 2016-2018 they provided \$40.1 billion a year support for fossil fuel (roughly equivalent to the volume of climate finance provided by MDBs) and just \$2.9 billion for clean energy. Shift-

and that the methodologies used to track progress draw on the best available information and continually improve in coverage and technical sophistication.

- International and national carbon markets should be promoted more actively. Progress in the negotiations over Article 6 of the Paris Agreement has renewed hopes that international carbon markets can be brought into operation. Parties should resolve outstanding technical and political issues and ensure the integrity and credibility of international carbon markets. At the same time, progress in domestic carbon market development should be encouraged and accelerated.

4.1 THE IMPERATIVE TO HARNESS PRIVATE FINANCE

In addition to public finance and public policy action, meeting the commitments in the Paris Agreement will require mobilizing private capital at scale. This is the outer 'layer' of the climate finance system, representing the largest pool of available capital that can be deployed to scale up climate-related investments especially in sustainable infrastructure. Without a fundamental and vast shift in private finance and in the financial system as a whole, the climate goals of net zero carbon by 2050 and those of the Paris Agreement cannot be met.

Private finance is pivotal to the future. According to the Climate Policy Initiative, while public actors accounted for 44% of the \$579 billion in total climate finance in 2017-18, private actors provided the other 56%, and that calculation likely underestimates significantly the share of private finance because of data gaps.¹³⁸ However, the bulk of private climate finance is in advanced economies. At present, in emerging markets and developing countries, 80 percent of infrastructure investment is public and mostly publicly financed; private investment in infrastructure has stagnated over the past decade and amounts to less than \$100 billion annually.¹³⁹

A central challenge for international public climate finance going forward will thus be to mobilize increasing volumes of private investment into sustainable infrastructure in EMDEs. The role of private capital in climate finance will be even more important during and after the COVID pandemic, as the economic crisis is causing significant declines in fiscal revenue in almost every country while also multiplying public expenditure needs.

More broadly, meeting these commitments will require financial systems that promote the flow of finance toward net zero carbon and resilient development.

operationalized. Currently, no global mechanism or platform exists to systematically track progress toward the operationalization of Article 2.1c. The UNFCCC includes provisions related to the tracking of public finance provided and private finance mobilized for climate action in developing countries, but currently there are no requirements to track broader financial flows. Several frameworks have emerged to help stakeholders “unpack” the article’s complexities.¹⁴²

“Making finance flows consistent” with a pathway towards low greenhouse gas emissions and climate-resilient development implies several things: (1) identifying appropriate, science-informed pathways based on temperature goals set by Paris; (2) identifying the characteristics that investment portfolios, balance sheets, and investment decisions should have if they are to be consistent with those pathways; (3) benchmarking the current state of portfolios, balance sheets, and decision-making, and setting targets and benchmarks at different time horizons; and (4) tracking and disclosing progress toward those targets and benchmarks.

New financial structures and business models will be needed, as well as more rigorous definitions, labels, and standards, to ensure that finance designated as “climate-aligned” or “green” really is what it purports to be. Paris Alignment of finance flows will require clear, comparable and transparent methods and metrics that are applied to all investment decisions. The MDB Building Block approach is one method MDBs are developing. Green Budgeting can help the public sector/finance ministries. Taxonomies can also help the public and private sector (but have limitations).

There will be a need to shift investment portfolios. This is where we link back into investment decisions (which would be expanded to include divestment, etc.), and also get into science-based pathways to Net Zero and other transition tools that can provide guidance on decarbonisation pathways; for example, the Paris Agreement Capital Transition Assessment (PACTA), which measures the alignment of portfolios with climate scenarios. This is the most challenging part of alignment. Going forward the world will be asking for transparent information that answers the question: is the financial sector doing what is sufficient to get to net zero? In other words, a portfolio may not be Paris-aligned until, say, 2050, but it needs to be able to give confidence that it is on a realistic path to get there.

With this context in mind, the COP26 *Private Finance Strategy to Drive Whole Economy Transition* that was

instruments include, for example, climate-risk stress testing for banks and insurance companies, risk-weighting of bank assets based on their climate-related characteristics and monitoring of transition risks in asset portfolios and across the financial system as a whole. Policies in this category are essential to ensure that financial institutions systematically incorporate climate considerations into their decision-making.

- *Returns.* Actions in this category are meant to enable investors to identify the opportunities in the transition to low-GHG emissions, resilient development and to report their own alignment with these pathways. Some financial institutions are pledging to boost the green portion of their portfolios, and others are going further, promising to decarbonize portfolios altogether by mid-century. These commitments can serve as important signals to the market about the long-term expectations of major capital providers.
- *Mobilization.* This dimension involves building new public-private partnerships, developing pipelines of “bankable” projects, and creating market structures to increase sustainable private financial flows, particularly to developing countries. Investment in clean power generation, clean transportation, and building efficiency has grown significantly in recent years, but low-carbon investment in other sectors is lagging and requires additional capital mobilization.

This approach can yield significant positive results and further propel a shift in capital deployment away from high-carbon destinations and if it can be scaled up across national financial systems, buttressed with appropriate policy frameworks and catalyzed by appropriate public finance, then the world will get much closer to reaching the aspirations of Article 2.1c.

However, more thought and attention must be given to how private finance trends will benefit emerg-

- Define the most fundamental and cross-cutting factors limiting private climate finance in emerging markets;
- Open new engagement channels with key decision-makers to identify policy improvements that will help stimulate private investment; and
- Catalyze essential collaboration between private finance, public finance, and policymakers to dramatically expand pipelines of sustainable infrastructure opportunities to drive investment in a sus-

INITIATIVE	INSTITUTIONS THAT ARE THE PRIMARY FOCUS OF THE INITIATIVE			
	BANKS	INVESTORS	INSURERS	NON-FINANCIAL CORPORATIONS (+ INVESTORS & BANKS)
MOBILIZATION				
<i>Developing new financial struc</i>				

- *Shareholder activism.* In several countries, shareholders are using or pledging to use their influence to push the companies in which they own stock to embrace more climate-friendly behavior. For example, of 429 shareholder resolutions on environmental, social and governance (ESG) issues filed for the 2020 proxy season in the United States, 15% concerned climate change – the second-largest category. The \$1 trillion Norwegian government pension fund adopted climate-related expectations for all companies in its portfolio, covering strategy, risk management, disclosure, and policy. And BlackRock, the world's largest asset manager, said it will increasingly likely to vote against company managers and board directors if companies don't make sufficient progress on sustainable business practices. Public rankings of financial institutional performance have also propelled some to act – for example, ShareAction's work in this regard.¹⁵²
- *Awakening of financial regulators t*

mentioned, the extent to which private finance can be mobilized for climate action has at times suffered from inflated expectations. In 2019, six of the seven MDBs mobilized less than \$1 from the private sector for every \$1 of MDB climate finance.¹⁵⁷ Additional efforts are needed to raise these mobilization ratios.

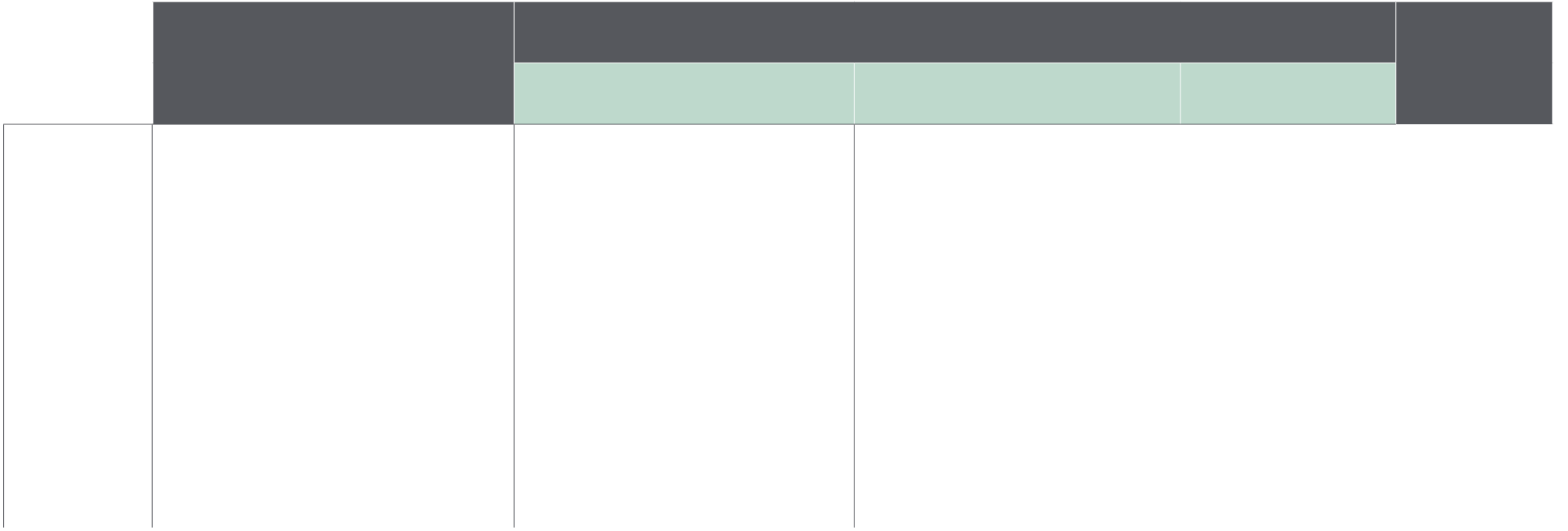
Despite many steps in the right direction, disclosure of climate risks is moving too slowly. Encouragingly, banks, insurers, pension funds, and investors with balance sheets totalling nearly \$150 trillion have expressed their support for disclosure following the recommendations of TCFD. But the TCFD's 2020 status report found that disclosure remains very much the exception rather than the rule. In eight of the eleven disclosures recommended by the TCFD, less than a third of the companies reviewed followed the recommendations. And in the other three disclosures, the share of firms complying did not break 50 percent. Notably, only 7 percent of companies are reporting on perhaps the most important disclosure—the resil-

For that reason, the OECD recently called on ESG funds to carry labels and engage in disclosure practices that enable investors can make informed choices.¹⁶⁶ The European Union's taxonomy for sustainable activities provides one example of how transparency can improve in the sustainable investing world.

4.5 RECOMMENDATIONS

- **National governments should take a more active role in the implementation of Article 2.1c through coordination, harmonization, and regulation.** While private-sector initiatives are very welcome, there is a risk that the unbounded proliferation of private sector-led standards, definitions, benchmarks, principles, methodologies and frameworks will become counter-productive. This could result in regulatory arbitrage, whereby companies choose the weakest set of standards

- **International and national carbon markets should be promoted. Progress in the negotiations**



ENDNOTES

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106 Despite difficulties, the GCF has built a substantial track record since its establishment. As of November 2020, the GCF had approved 159 projects in 117 developing countries with \$7.2 billion in approved funding. In its private sector portfolio, with \$1.9 billion of GCF funding, it has mobilized \$6.7 billion in co-financing.

107 Two important examples are its involvement in the Climate Investment Platform and partnership with the International Development Finance Club to support public development banks in financing the green transition.

108 Research to develop the PSF strategy showed that the private sector needs faster response/turn-around times, and that certain changes in the Fund's business model would allow the PSF to more effectively fulfill its mandate. The Forward-looking Performance Review conducted to inform the replenishment confirmed that "a significant part of the PSF portfolio is virtually indistinguishable from the (climate or energy) portfolios of (international) development banks", flagging that "the PSF has so far funded a considerable number of projects that development finance institutions also finance, in cases even on the same financial terms, despite the Fund's ability to provide highly concessional finance".

109 GCF Governing Instrument, paragraph 41

110 For example, although low-emission transport is one of the Fund's key impact areas, the FPR found that only three such projects had been approved to date – in contrast with needs expressed in the NDCs of 50 LDCs, SIDS and African nations for such investments. Such projects being overwhelmingly urban in nature may explain their limited representation.

111 The PSF could for instance issue targeted RFPs and filter out early on proposals in the GCF pipeline that could be financed directly by DFIs and MDBs (e.g. hard currency loans for mature energy technologies). For adaptation finance, the PSF could provide early-stage finance through incubators and accelerators that contribute to de-risk private adaptation investments to help grow the share of these in the GCF portfolio (currently only 2 percent).

112 Clean Technology Fund and the Strategic Climate Fund, which consists of three programs: Pilot Program for Climate Resilience, Forest Investment Program, and Scaling Up Renewable Energy Programs in Low Income Countries.

113 Climate Investment Funds <https://www.climateinvestmentfunds.org/country>

114 The GIF's current donor support includes Australia, Canada, China, Denmark, Germany, Japan, Singapore and the World Bank.

115 In line with this commitment, the World Bank announced on December 9, 2020 a new target of 35 percent of lending with climate co-benefits for the next five years compared with the previous target of 28 percent by 2020. It also set a target of 50 percent of its support for adaptation and resilience. <https://www.worldbank.org/en/news/press-release/2020/12/09/world-bank-group-announces-ambitious-35-finance-target-to-support-countries-climate-action>

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