The Climate Finance Landscape and the Green Climate Fund

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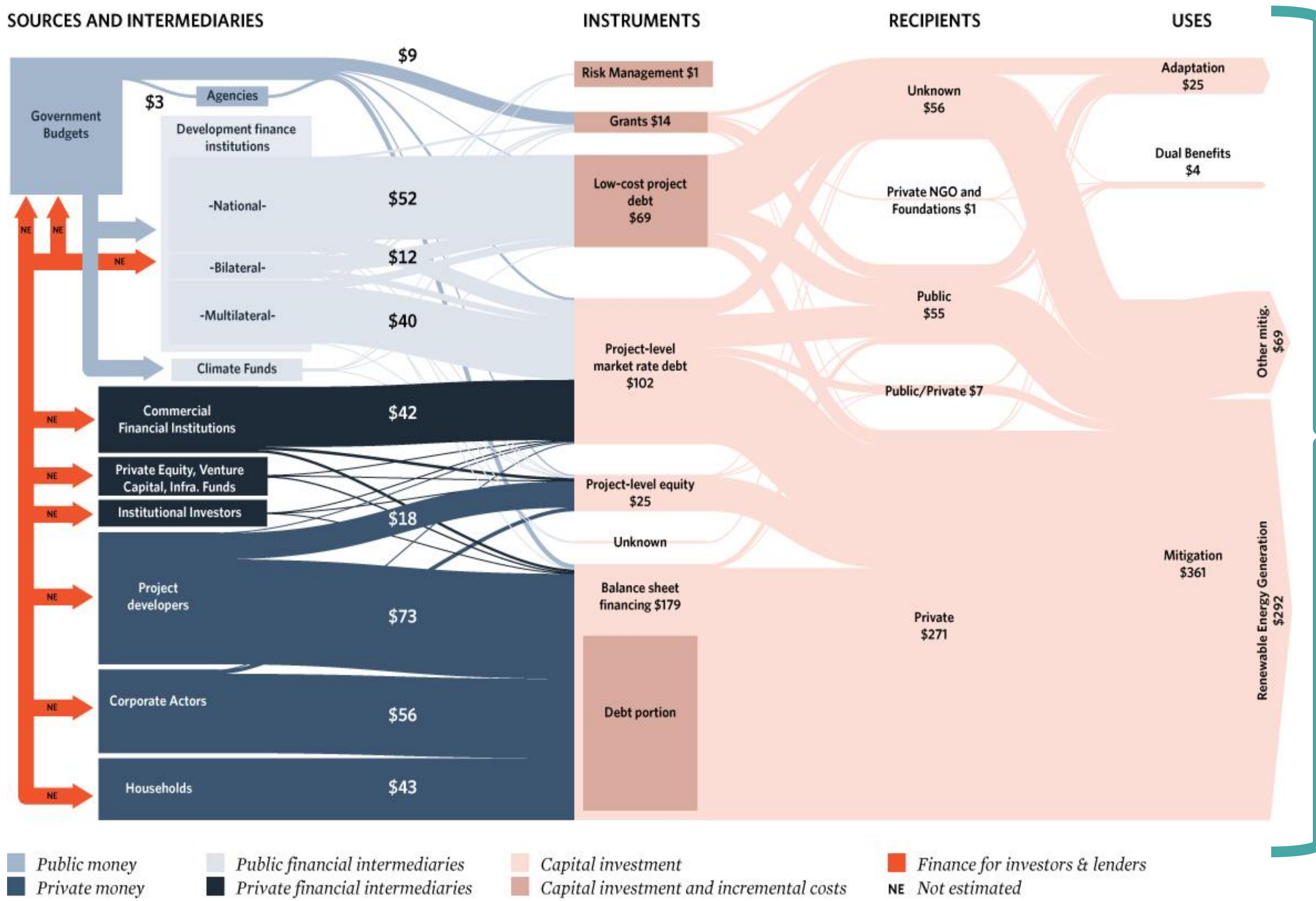
I. Climate Finance

Climate finance flows, 2015



Total needs = $700 billion

Total flows = $391 billion

- 93% to mitigation
- 87% to developed countries
- 71% from the private sector

Source: Climate Policy Initiative

Developing countries – our best guess of the climate finance gap

DEVELOPING COUNTRIES Climate finance gap 2010 - 2029			
($ billion per year)	**Mitigation**	**Adaptation**	**Total**
Current annual flows	35 - 50	..	35 – 50
Annual financing gap	350	70 - 100	430 - 450

Why don't climate projects get financed in developing countries?

The issues seem to be:

- Very little private financing, due to excessive risk for investors
- Market failure (lack of suppliers or adequate finance, information gaps)

Source: Green Climate Fund

How best to finance climate investments

GHG emissions are **global externalities**

- Costs not borne by the polluters
- Leads to sub-optimal investment decisions *(e.g. coal-fired power plants rather than gas or renewables)*
- To realign investment decisions, "externalities need to internalized"

First best

- **Externalities internalized** by assigning tradeable property rights
  e.g. cap and trade (SO_2, NOx)

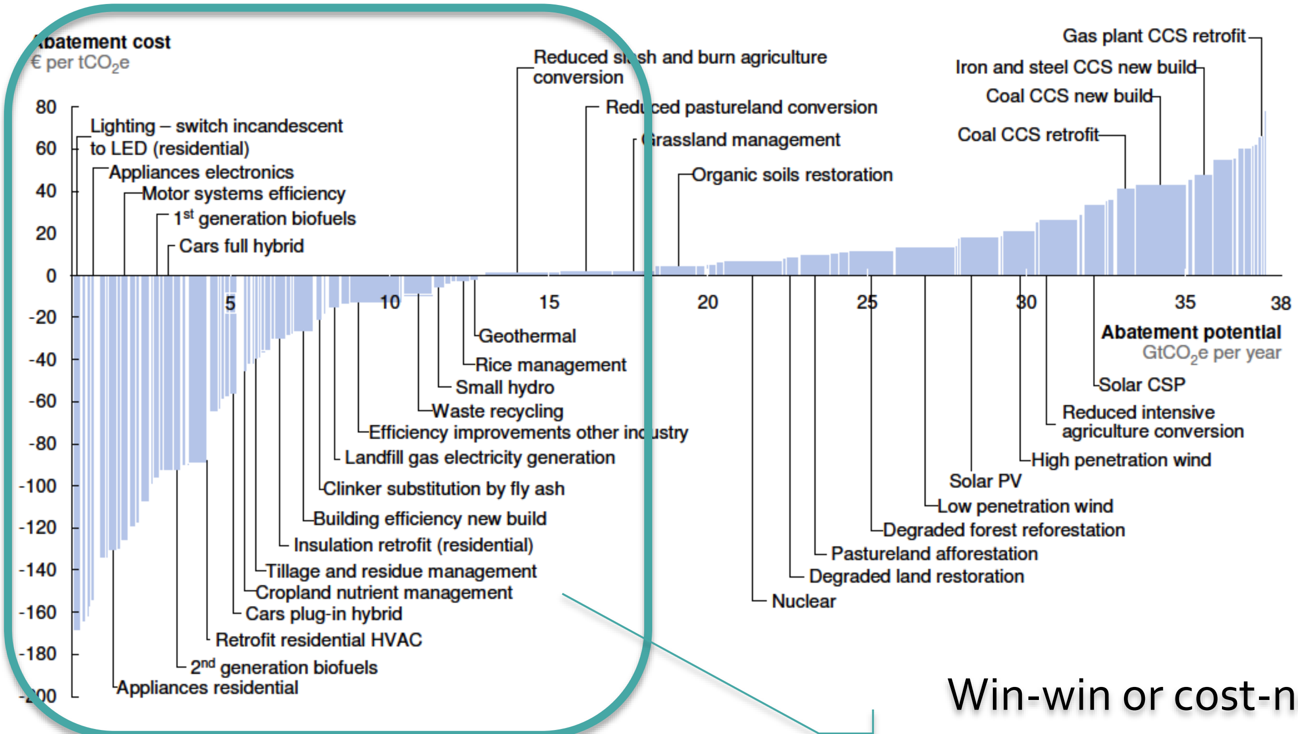
Second best

- Costs realigned through **fiscal policy**
  e.g. carbon tax

Third best

- **Direct financing** covers incremental costs of "doing the right thing"
  e.g. GCF

It gets more complicated – some investments incur no incremental cost



Source: McKinsey

Win-win or cost-neutral

(not financed because of market failure)

II. International Climate Architecture

International climate change architecture

UNITED NATIONS FRAMEWORK CONVENTION ON CLIMATE CHANGE (UNFCCC)

- Adopted at the Earth Summit in Rio de Janeiro in 1992
- Became effective on March 21, 1994
- Signed by 196 countries
- Governance structure = Conference of the Parties (COP)

The UNFCCC was the first attempt to address climate change on a global scale

International Panel on Climate Change (IPCC)

Green Climate Fund (GCF)

Every country has one equal vote
Decisions are largely taken by consensus
UNFCCC architecture is not conducive to taking incisive decisions

COP21: some important outcomes
(positive and negative)

195 INDCs

- First **global** agreement to limit GHG emissions
    - *But not enough to limit temperature change to 2 degrees Celsius*

COP text is not binding

- Text provides an important ***market signal*** to investors at the national level
    - *But no cap-and-trade or carbon tax*
    - *Agreement is creating new markets in low-carbon technologies*

Text does not provide for a carbon price*

- Alternative climate finance vehicles are needed
    - *The GCF fulfils an important need*
    - *One of many funds*

*e.g. through cap-and-trade, or the imposition of a global carbon tax

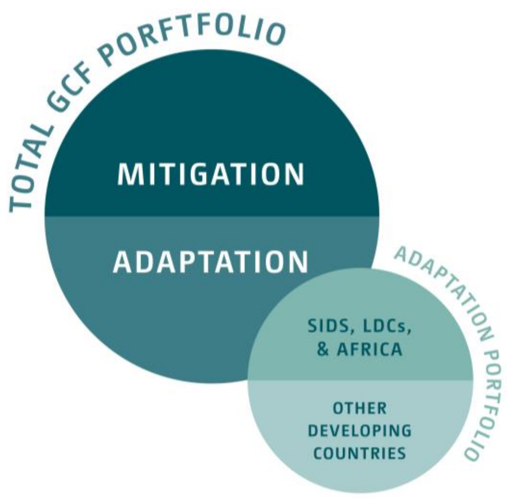

GREEN
CLIMATE
FUND

What is the Green Climate Fund?

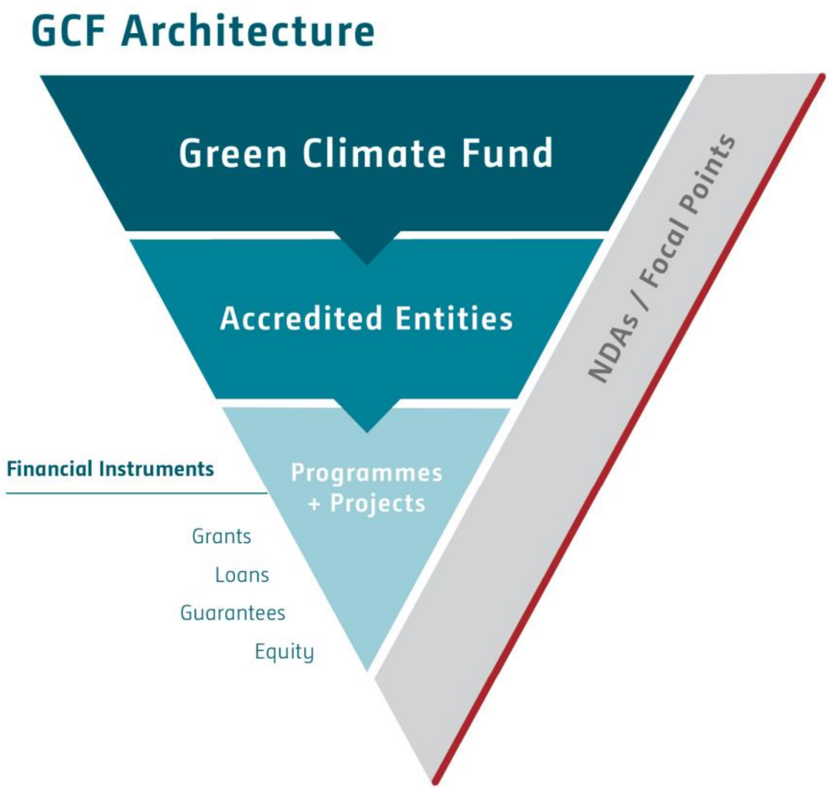
- Main operating entity under the financial mechanism of the UNFCCC
- Established at COP16 (Cancun)
- MGCF's mandate is to promote a "paradigm shift" in climate investments
- Funds currently pledged (2016-2018): $10.3 billion
- First investments approved November 2015
- March 2017: $1.5 billion committed to 35 projects, generating $4.7 billion in investments

How does GCF differ from existing development finance institutions?

- GCF is a *fund of funds*, working through accredited partners
- Its purpose is to "de-risk" climate investment projects in developing countries
- Full range of financial instruments
  - equity, senior debt, sub-debt, guarantees, grants
- 50/50 mitigation/adaptation
- Geographic balance
  - Focus on SIDS, LDC, SSA
- Significant allocation to private sector projects



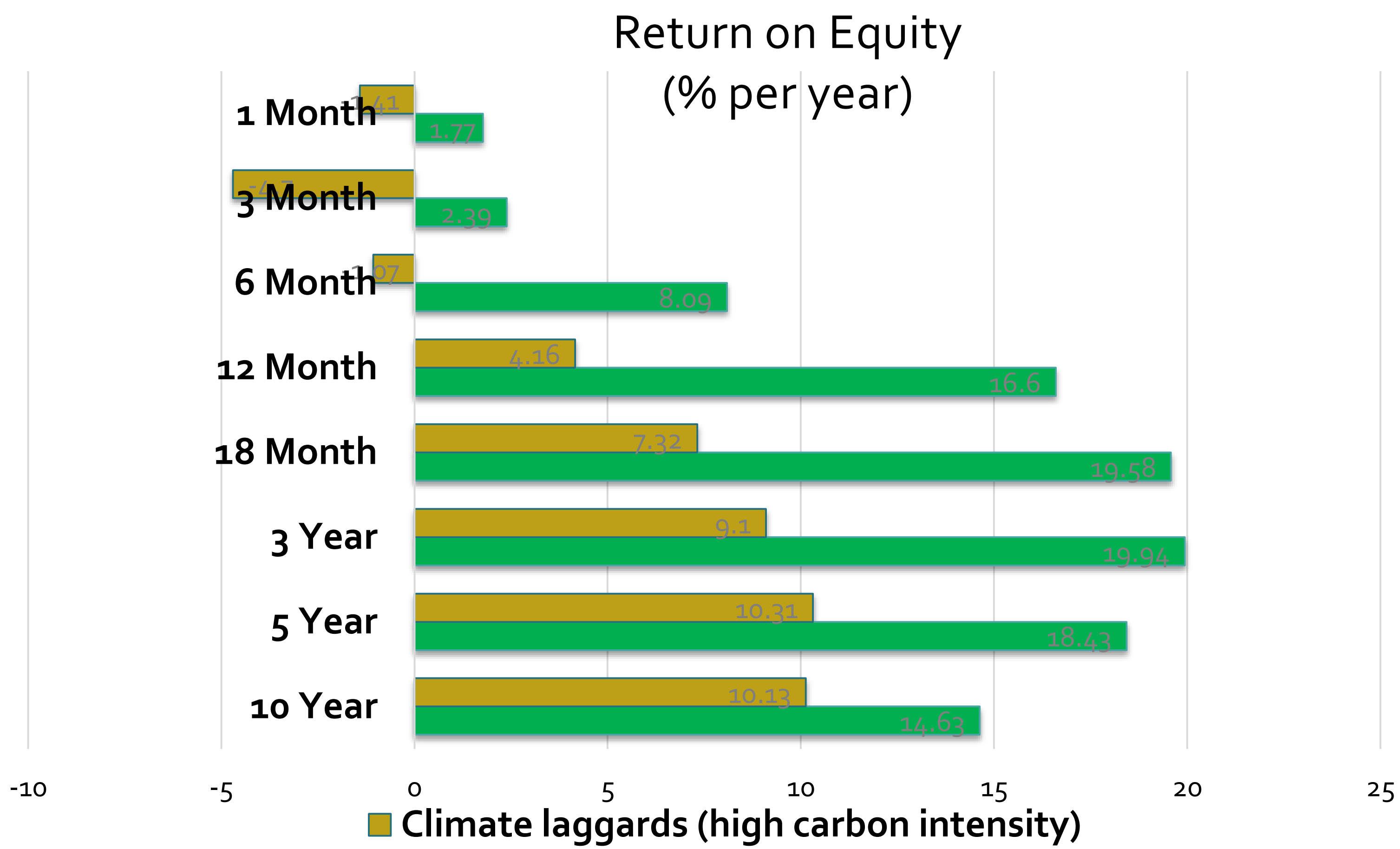
The GCF and its Partners



How are projects judged? Investment Framework

Impact Potential	• Potential to the achieve the Fund's objectives and result areas
Paradigm Shift Potential	• Potential to catalyse impact beyond a one-off project or programme investment
Sustainable Development Potential	• Potential to provide wider benefits and priorities
Needs of Recipient	• Vulnerability and financing needs in recipient country
Country Ownership	• Beneficiary country ownership of and capacity to implement funded activities
Efficiency & Effectiveness	• Economic and, if appropriate, financial soundness of the programme/project

Climate sensitive firms provide better investment returns



Source: Etho Capital
(Based on 5000 US and international equities)

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