International Development Finance Club

IDFC

IDFC's Contribution to the Climate Action Summit 2019



IDFC's Contribution
to the
United Nations Climate Action Summit 2019

Contents

International Development Finance Club (IDFC) Communiqué

Annex 1

Summary of IDFC Green and Climate Finance Mapping Report 2019
2018 data

Annex 2

Compilation of individual information and recent commitments by different IDFC members to promote the development of sustainable alternatives to fossil fuel

Annex 3

"Implementing Alignment with the Paris Agreement" - Study by CPI and I4CE
Executive Summary

Annex 4

Strategic Partnership between IDFC and the Green Climate Fund (GCF)
Short Summary

Annex 5

IDFC Climate Facility
Short Summary

International Development Finance Club (IDFC) Communiqué

United Nations Climate Action Summit

September 23, 2019 – New York

National and regional development banks have a huge potential to support the implementation of the Paris Agreement on climate, and to generate green and climate - public and private - finance at scale to address the specific needs of their national economies, societies and environments.

Over the period 2014-2018, the national and regional development banks of the IDFC reported on average close to USD 150bn yearly of climate finance, representing about 20% of their total financial commitments. The IDFC members have also shown they have the technical and financial capacities to deliver even higher amounts of climate finance, as the USD 200bn mark of yearly climate finance was reached during this period.

However, if this additional finance, as that being mobilized by other multilateral, international, regional and national development banks worldwide, remains "climate finance as usual", it will not be enough to be on track to fulfill our common climate objectives. The quality and redirection of all financial flows, beyond public and private climate finance, is essential. IDFC commits to contribute to this qualitative agenda by promoting the mainstreaming of climate considerations throughout the international and national financial communities and forcefully engaging, along with all interested partners, on the alignment of all financial flows with the Paris Agreement.

1. In light of the above and with a view to achieving the ambitious objectives of the Paris Agreement and foster sustainable, low carbon and resilient development, IDFC has the potential to mobilize **significant financing volumes** in order to help achieve these goals :
   - Provide more than USD 1 trillion of climate finance by 2025, including an increasing share for adaptation and resilience;
   - Leverage financing from the private sector and create the space for blending of public finance to accelerate the crowding in and reorientation of private finance for sustainable and climate-compatible development.

2. **Beyond volumes, IDFC commits to further contribute to the quality and impacts of finance to implement the climate and sustainable development agendas**. IDFC commissioned a study by think tanks I4CE and CPI on aligning finance with the Paris Agreement published on the occasion of the Climate Summit[i], which provides a robust framework usable by the financial community at large. It promotes (i) a comprehensive scope of action, i.e. screening all activities financed for positive or negative climate impacts; (ii) the contribution of near term actions to the achievement of long term goals of the Paris Agreement and the SDGs; and (iii) a do no harm approach while aiming for deep transformations of systems and value chains.

   Inspired by the recommendations of the study, **IDFC will further align financial flows with the Paris Agreement and the SDGs** by having Club members:

   - Work at country and sub-national level and engage with other actors to support national constituencies implement their commitments to the Paris Agreement and provide policy advice to devise development pathways consistent with long term resilience and carbon neutrality;
   - Further embed climate change considerations and alignment with the Paris Agreement within IDFC members' strategies;
   - Redirect financial flows in support of low-carbon and climate-resilient sustainable development.

3. **IDFC members play a key role to provide market signals and enable the reorientation of other financial flows, public and private, local and international, towards climate-compatible investment and development pathways**. Recalling its commitment taken at the 2017 One Planet Summit to promote the development of sustainable alternatives to fossil fuel, IDFC will work towards reinforcing collaboration to:

- Promote and contribute to long-term carbon neutrality;
- Support increased pace and coverage of renewable energy and energy efficiency investments as well as clean technologies;
- Consider the range of fossil fuel investments in portfolios, work towards applying more stringent investment criteria according to members' mandates, and consider ways and means to reducing it, taking into account national and regional circumstances and in line with NDCs and long term strategies, such as explicit policies to exit from or significantly reduce coal financing[ii].

  Several illustrations of contributions by individual IDFC members to such efforts are annexed to the present document.

4. To achieve these targets, and to operationalize alignment with the Paris agreement, the members of the IDFC are **implementing several concrete actions**, such as:
   - Launching a **USD10mn IDFC Climate Facility** to build collective capacities of all IDFC members to originate and finance climate activities, with effective operationalization before COP25, at the end of 2019, including the setting up of the Facility's Coordination Unit and related staffing arrangements as well as the implementation of initial knowledge sharing and analytical work;
   - Setting up a **strategic partnership with the Green Climate Fund** with a view to achieving together the Paris Agreement objectives and promoting direct access to national and regional development banks to provide, intermediate, implement and/or mobilize domestic and international climate finance[iii].

5. In addition, **IDFC members call for strong political support from governments and regulators** to consolidate this momentum and unleash the potential of public national and regional development banks to best (i) deploy, shift and facilitate increased investment towards low-carbon, resilient and sustainable development; (ii) lead the needed sectorial and national transitions; and (iii) make a systemic contribution to the achievement of the objectives of both the Paris Agreement and the Sustainable Development Agenda.

   This may include the **explicit mention of climate and sustainable development considerations in the mandates of development banks or in their business plans**. It may also entail **evolutions in the regulatory frameworks** of such institutions to further enhance climate and sustainable development investments (SDI). It also implies consolidating the international climate and sustainable development finance architecture, to make it more collaborative and coordinated, in particular by making the best use of the resources, capacities and added value of local financial systems, national and regional development banks, multilateral development banks and the United Nations Agencies and financial mechanisms.

   - In that perspective, **the IDFC would like to propose that, under UN sponsorship, a Summit of Development Banks be organized in 2020, ahead of COP 26**, to mobilize all development finance institutions worldwide as well as their broad stakeholders, with a view of further tapping their decisive potential to enable the implementation of the climate and SDGs agendas.

[i] Executive Summary presented in Annex.
Part 1 of the study: www.i4ce.org/download/framework-alignment-with-paris-agreement-why-what-and-how-for-financial-institutions
Part 2: www.climatepolicyinitiative.org/publication/implementing-alignment-recommendations-for-the-international-development-finance-club

[ii] JICA expressed its reservation on the ground that members are also subject to their countries' policies and long term strategies on climate change.

[iii] At the time of release of the present statement, 12 IDFC members are Accredited Entities to the GCF, making of IDFC the main group of financial institutions entrusted by the GCF to implement its resources. Accredited IDFC members include AFD, BNDES, BOAD, CABEI, CAF, CDG Capital, DBSA, KDB, KfW, JICA, SIDBI, and PTSMI that will officially join the Club in October 2019. Other members are in the process of gaining accreditation or are already channeling GCF resources. GCF and IDFC currently have a joint portfolio of 12 projects amounting to USD 838 million approved by the GCF and co-financed by accredited IDFC members.

Summary of IDFC Green and Climate Finance Mapping Report 2019
(2018 data)



$134 billion in green finance in 2018

$670 billion total green finance since 2015

78% in home country of IDFC members

79% to Green energy and Mitigation of Greenhouse Gases

x1.5 growth in adaptation finance from 2017

22% of total new commitments in 2018 were green finance commitments

25% of finance to non-OECD countries were international commitments

Introduction and Context

Since 2011, IDFC has conducted a periodic mapping of member institutions' contributions to green finance.

While 2015-2017 saw strong, sustained growth in green commitments from IDFC members, findings from 2018 indicate a decrease from the record levels of 2017, in particular in the areas of mitigation and other, non-climate-related, environmental projects. Among other factors, the fall is due to cyclical macroeconomic policy evolutions in some countries impacting development banks' overall financial commitments and hence green finance levels, in particular in the areas of urban development and (to a lesser extent) hydro-power generation, which benefited from considerable support in recent years. However, many IDFC institutions show stable or increasing green finance commitments.

2018 Key Findings

- IDFC members reported total green finance commitments of $134 billion. Although this represents a 39% decrease from commitments in 2017, cumulative green finance commitments by IDFC members are over $670 billion since 2015.
- Green finance commitments represented approximately 22% of total new commitments reported by members. Green commitments have consistently been above one fifth of total IDFC investments since 2016.
- Climate finance – consisting of all activities related to mitigation of GHG emissions and adaptation to climate change – accounted for 93.3% of total green finance.
- Finance for green energy and mitigation of greenhouse gases was the largest category, representing 85% of climate finance.
- Adaptation represents 12.3% of climate finance, and commitments for adaptation to climate change increased by 57% from 2017. Following a second consecutive year of growth, commitments to adaptation projects have more than tripled since 2016.
- Projects containing elements of both mitigation and adaptation, though still a small proportion of climate finance at 2.7%, doubled in absolute terms.
- The remaining 6.7% of green finance went to other environmental finance, which includes waste and water management, biodiversity, and controlling industrial pollution. Commitments in this category fell by 63% compared to 2017.

Figure 1: IDFC Green Finance 2018 by theme (rounded)

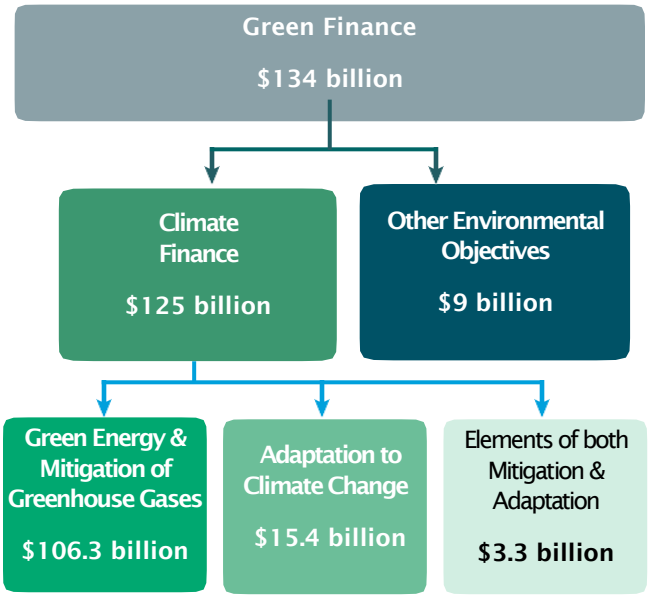


Figure 2: IDFC Green Finance 2015 -2018

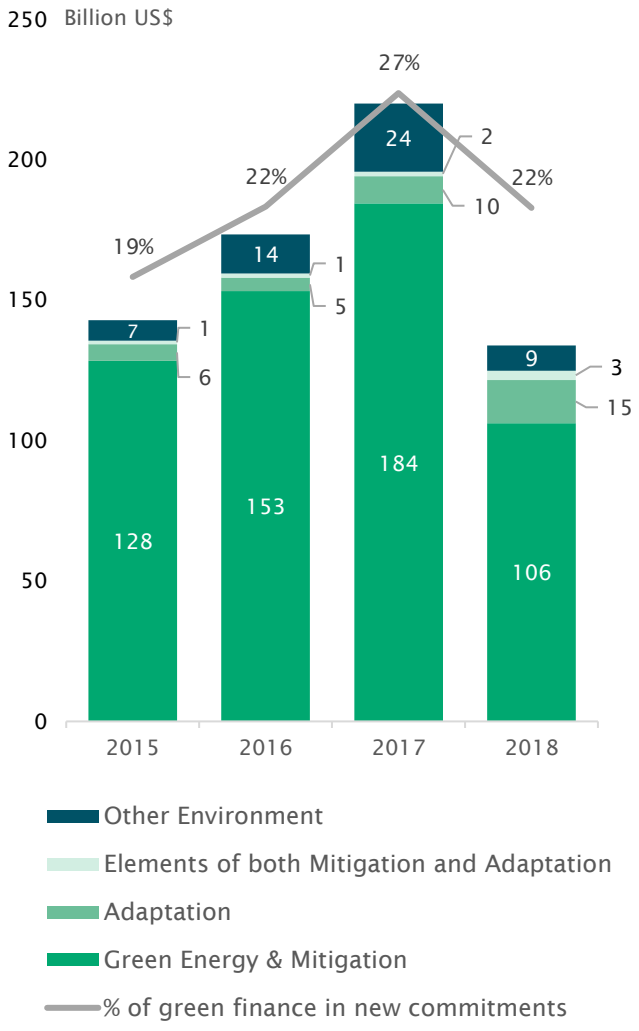
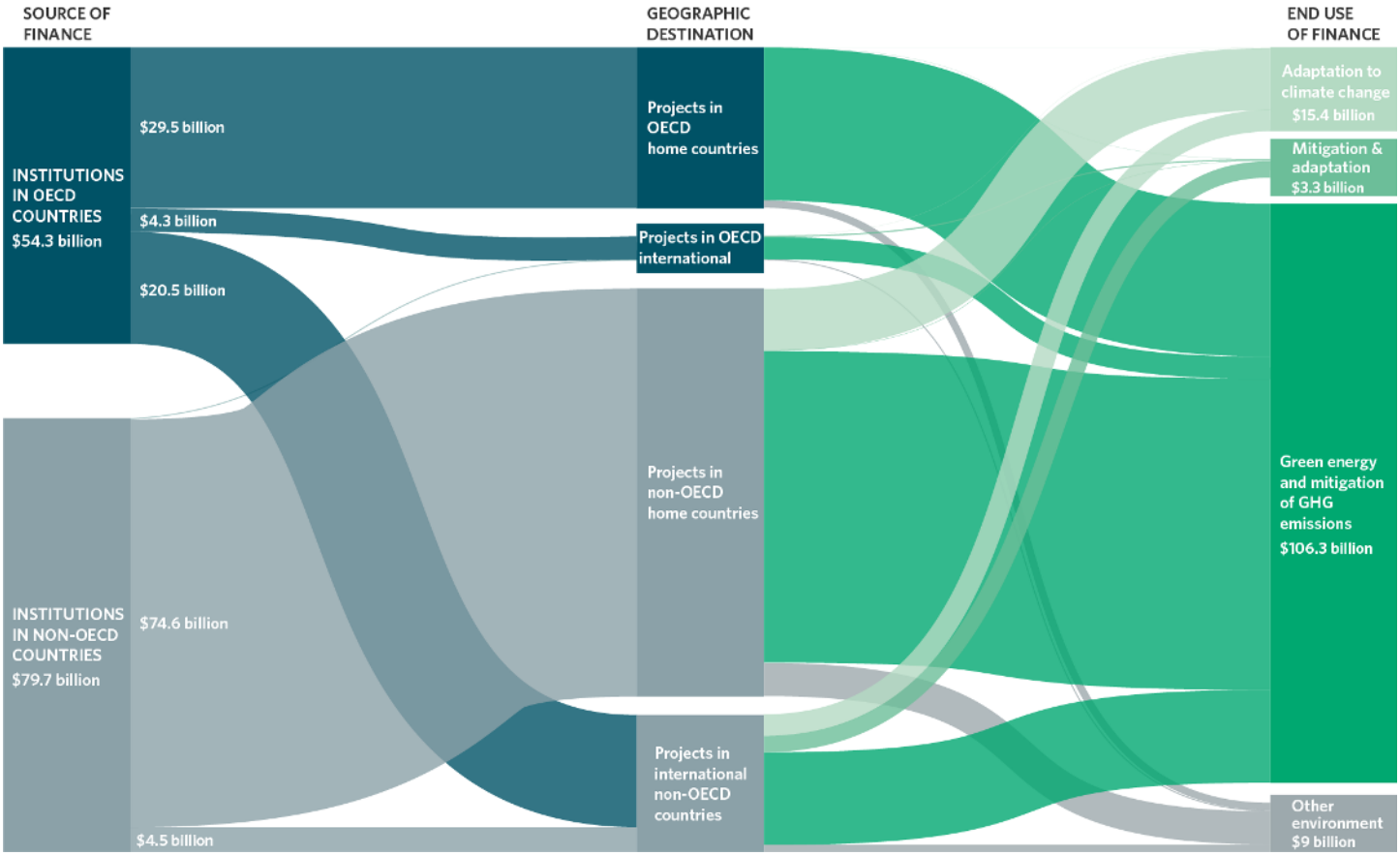


Figure 3:Green finance commitments in 2018 by origin, destination (OECD/non-OECD), and category



- IDFC institutions based in non-OECD countries committed $80 billion, a smaller proportion (59%) of the total than in previous years. This decrease reversed an upward trend in the non-OECD share of IDFC green finance, which reached 75% ($166 billion) in 2017 and 68% ($118 billion) in 2016.
- Green finance commitments have become more regionally balanced. While the East Asia and Pacific region again accounted for the largest share of commitments at 56%, this was lower than in 2017 (72%). As in 2016 and 2017, the East Asia and Pacific region was followed by the EU (22%), Latin America and the Caribbean (9%) and South Asia (6%), as the leading destinations of finance (Figure 4).
- The share of total green finance commitments made in the home country of the relevant IDFC member institution was 78% ($104 billion), while 22% ($30 billion) was spent internationally.
- Flows from institutions in OECD countries to non-OECD countries represented 69% ($21 billion) of international green finance commitments.
- Flows from institutions in non-OECD countries represented 17% ($5 billion) of international green finance commitments.
- Most commitments were provided in the form of loans, at $129 billion, or 96% of total green finance (down from 97% in 2017), while $3.4 billion, or 2.3% of commitments, were provided in the form of grants (up from 1.5% in 2017).

Improving Green Finance Mapping Methodology

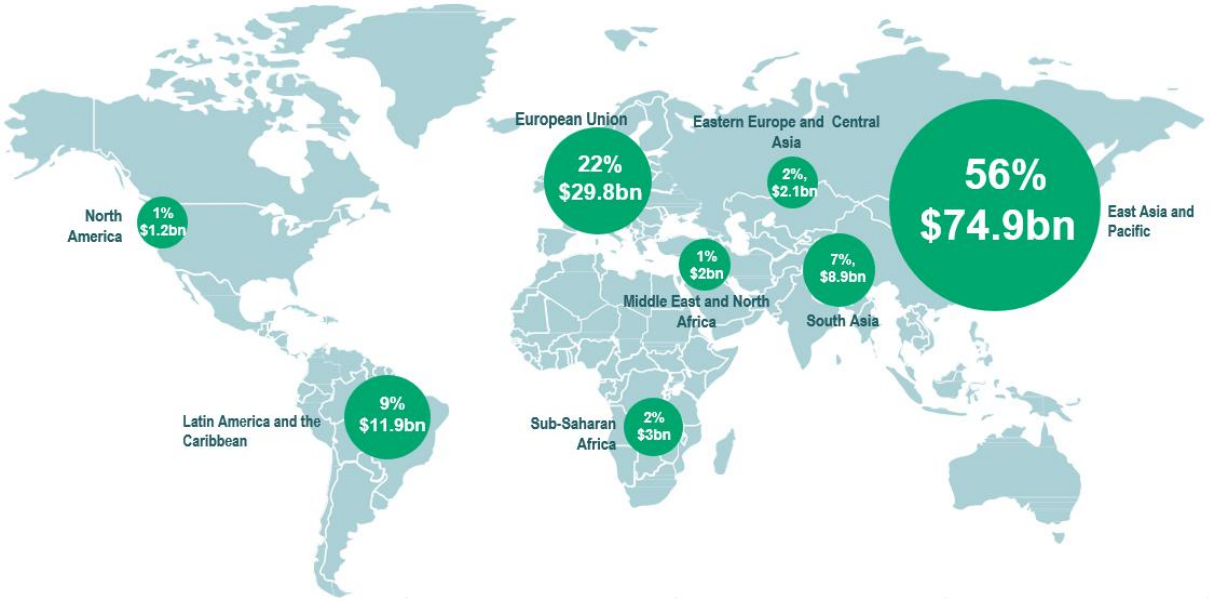
To inform this exercise, IDFC members complete a survey template, from which the data are checked for consistency and aggregated. The number of reporting institutions for 2018 is 17 out of 24.

The IDFC survey uses the Multilateral Development Banks (MDBs) and IDFC Common Principles for Climate Mitigation and Adaptation Finance Tracking. The specific list of reporting institutions and reporting coverage across all categories vary from year to year. Following the Common Principles, uncertainty is overcome via the principle of conservativeness where climate finance is preferred to be under-reported rather than over-reported. In

particular, adaptation commitments are expected to be conservative, since activities which count as adaptation are broadly context-specific and institutions are not always able to apply consistent category markers.

Another challenging area of reporting is estimating private sector co-investment mobilized by IDFC members. IDFC could consider developing and applying common methodologies to estimate, track and report on private finance mobilized in coming years, potentially via the pilot IDFC Climate Facility, launched in September 2019. The Facility will help build capacity and knowledge among member institutions to work on climate objectives. Improved reporting can help increase the effectiveness and catalytic potential of green finance committed by IDFC members.

Figure 4: Regional distribution of green finance in 2018



ABOUT IDFC

IDFC, created in 2011, is a leading group of 24 national and regional development banks from all over the world. IDFC members have the unique function of supporting domestic policies while transferring international priorities into their own constituencies. IDFC members are aligned with and work together to implement the Sustainable Development Goals (SDGs) and the Paris Climate Agreement agendas. Through IDFC, and in close partnership with other development bank networks, members join forces as a platform to promote and leverage sustainable development investment worldwide.

The green mapping report exists to illustrate the contributions that IDFC members provide to green and climate finance. The report is constantly improving the reporting methodology and hopes to further member efforts in tracking and reporting on green finance flows.

More information about the IDFC can be found at www.idfc.org. This year's green mapping report was prepared with the support of Climate Policy Initiative (www.climatepolicyinitiative.org)

IDFC Members

- Agence Française de Développement (AFD)
- Banco del Estado de Chile (BE)
- Bancóldex S.A.
- Banco Nacional de Desenvolvimento Econômicoe Social (BNDES)
- Banque Ouest Africaine de Développement (BOAD)
- Black Sea Trade and Development Bank (BSTDB)
- Development bank of Latin America (CAF)
- Caisse de Dépôt et de Gestion (CDG)
- Cassa depositi e prestiti (CDP)
- Central American Bank for Economic Integration (BCIE/ CABEI)
- China Development Bank (CDB)
- Corporación Financiera de Desarrollo S.A. (COFIDE)
- Croatian Bank for Reconstruction and Development (HBOR)
- Development Bank of Southern Africa (DBSA)
- The Eastern and Southern African Trade and Development Bank (TDB)
- Industrial Development Bank of Turkey (TSKB)
- Islamic Corporation for the Development of the Private Sector (ICD)
- International Investment Bank (IIB)
- Japan International Cooperation Agency (JICA)
- KfW Bankengruppe
- Korean Development Bank (KDB)
- Nacional Financiera (NAFIN)
- Small Industries Development Bank of India (SIDBI)
- State Development Corporation (VEB)

Compilation of individual information and recent commitments by different IDFC members to promote the development of sustainable alternatives to fossil fuel

AFD

Since 2011, 50% of AFD's financing approvals in developing countries have a direct positive contribution for climate mitigation and adaptation. In 2013, the AFD's board decided that the AFD would no longer finance coal power plants. In 2017, AFD's board adopted the goal to become "100% Paris agreement compliant", that is to stop financing projects inconsistent with pathways towards low greenhouse gas emissions and climate-resilient development as per Article 2.1.c of the Paris agreement. In 2019, AFD's board adopted a new Energy Transition Strategy confirming strong support to renewable energy production and reinforcing the exclusion of financing fossil fuel related projects, including power plant projects from fuel oil or diesel only (excluding hybridization), exploration or production projects, or dedicated exclusively to the transport of Coal, Gas and Oil, and infrastructures associated with a fossil fuel exploration, production or storage unit (mines, processing units, refineries, storage, etc.).

BICE[1]

As a sustainable development bank, BICE promotes projects with positive social and environmental impact : 40% of BICE's current project portfolio applies the Social and Green Bond Principles of the International Capital Markets Association

In September 2018, BICE signed up to The Climate Action in Financial Institutions Initiative.

In December 2018, BICE launched the first Sustainable Bond in South America for USD 30 MM. With the issuance of this Bond, BICE integrated the financing of green projects destined to mitigate climate change effects and projects with positive social impact, with significant contribution to 7 of the 17 sustainable development goals (SDGs).

BICE signed a first Credit Facility with GCF in April 2019 promoting risk mitigation and finance for renewable energy efficiency investment.

In June 2019 BICE signed the Argentinian Sustainable Finance Protocol aiming at starting moving towards Sustainable Development, facilitating and encouraging in every Argentine financial entities, the implementation of international practices and policies that promote an integration between economic, social and environmental factors.

BNDES

BNDES adopted since mid-2000s innovative strategies regarding the financing of the power sector, aiming at contributing to the expansion of alternative energy sources and promoting investments with high social and environmental returns. In 2016, BNDES decided to stop its support to thermal power plants powered by coal and fuel oil, and prioritize renewable energies, energy efficiency and clean technologies, by providing more favorable financing conditions while stimulating private investment in this class of assets.

BOAD

Through its 2015-2019 Strategic Plan, BOAD is committed to providing support to member states, with a view of strengthening climate resilience in order to achieve sustainable and inclusive growth.

To this end, BOAD has secured strategic accreditation with the UNFCCC financing mechanisms dedicated to the environment and the climate namely,

- The Climate Change Adaptation Fund (accreditation obtained as of 2011),
- The Global Environment Fund (accreditation obtained as of 2015),
- The Green Climate Fund (accreditation obtained as of 2016).

Having joined the Mainstreaming Climate Action within Financial Institutions initiative, BOAD wishes to develop a range of climate integration tools in its operations, in order to develop its climate finance offer and better control its risks. BOAD aims to promote principles and mechanisms of climate finance in the West African Economic and Monetary Union Region and, more broadly, in Africa.

[1] BICE is in the process of becoming member of IDFC

CABEI

CABEI recognizes that the impacts of climate change and climate variability represent a clear threat to economic and social development. In this regard, the bank is committed to helping the Central American Region and its member countries to fight against the adverse effects of the change climate. It is a long term commitment which has been embedded within its institutional strategy and delivered by committing 35% of its annual approvals for the financing of operations to mitigate and adapt to climate change. To increase the flow of financial resources to support climate change operations, CABEI has been accredited to the Adaptation Fund and Green Climate Fund, and established long term partnerships with other bilateral and multilateral agencies. CABEI´s commitment on addressing climate changes challenges has been also expressed though several high level statements as follows:

In 2015, the Board of Directors reiterated the Bank's commitment to support projects aimed at reducing greenhouse gas emissions, mainly in terms of generation of clean energy, sustainable transport, urban development and food production.

In April 2016, the Board of Governors issued a Declaration of Commitment to Promote and Support Actions to Finance Adaptation and Mitigation to Climate Change Climate. This declaration reiterated CABEI's commitment to support its member countries to achieve the goals established at the XXI Conference of the Parties on Climate Change (COP 21), as a fundamental step to combat climate change and promote measures and investments to a future that is low in carbon emissions, resilient and sustainable.

In April 2019, the Board of Governors adopted the Zero Carbon Statement expressing its commitment to the adoption of specific measures to support climate change adaptation and mitigation. The Bank adopts the following principles: i) Refraining from financing projects related to the exploration and extraction of coal and to the generation of energy based on coal; ii) Participating actively, and together with other multilateral development institutions and agencies, among others, in the structuring and development of financial instruments oriented or in support of mitigation and prevention in the face of climate change, support to the strengthening of low carbon economies, societies resilient to climate changes, sustainable food production, clean energy generation and energy efficiency.

CAF

CAF has recently set a green finance goal of 30% of its overall yearly approvals by 2020, 40% by 2025, and 50% by 2030. CAF has also recently approved a new Water Strategy 2019-2022 framed within the guiding principle of water security, seeking to support universal access to drinking water and sanitation, while paying particular attention to waste water treatment and the preservation of aquifers, thus contributing to an holistic sustainable economic, social and environmental approach and increased resilience. Additionally, given CAF's active role at the subnational level, CAF has launched a "Cities with Future" initiative to not only promote the inclusion of green finance components (mitigation, adaptation and environment) into projects and programs financed by CAF, but also address other SDGs related to social needs, such as education, gender equality, nutrition, local economic growth and circular economy, amongst others.

CAF aims to become a carbon-neutral institution in the short term, reducing its waste, energy, paper and carbon footprint, and compensating the emissions of its own operations. In 2020, on its 50 year anniversary, CAF intends to compensate the carbon footprint of its 50 years of operations.

CAF has not directly financed coal projects in the last 30 years, and it is currently in the process of enacting a policy to preclude financial support to coal based projects in the near future.

CDP

With the new 2019-2021 Business Plan, CDP has decided for the first time to orientate its strategic perspective towards the Sustainable Development principles within the framework defined by the UN 2030 Agenda. CDP has therefore made a specific commitment to finance new investment in Energy Transition and Climate Change favoring a paradigm shift to a low carbon economy in accordance to SDG7-13 and to the Paris Agreement ambitious targets.

DBSA

In its continued bid to contribute and influence investment and policy shift in the Republic of South Africa, DBSA has worked with its partners to provide a detailed study on the risks associated with transitioning from the country's carbon-based power sector as well as the exportation of oil and coal. Having identified transition risks associated with these key economic activities, DBSA is proactively exploring solutions, which will include commissioning another study on the best approach towards transitioning from intensive to low carbon investments. The objective is to address the transitioning risk, focusing on the least cost approach, providing insight on how to manage it and support a just transition. DBSA intends to apply knowledge acquired through this study to inform its strategy on financing energy projects going forward.

JICA

JICA is considering a new paper following the Long-Term Strategy under the Paris Agreement of the Government of Japan.
The Long-Term Strategy under the Paris Agreement was decided by the cabinet on June 11, 2019.
https://www.env.go.jp/press/802.pdf

KfW

In 2018, KfW committed around 40% of the overall promotional business volume to environmental and climate protection. From 1 July 2019, a group-wide new 'Exclusion List and Sectoral Guidelines of KfW Group' apply that contains an explicit exclusion for the financing of coal-fired power plants. KfW furthermore launched several landmark projects on sustainability like the "Clean Oceans Initiative" (2018) and the "Circular economy Initiative" (2019) together with its partners. In 2019, KfW also updated the group's sustainability mission statement and sustainability action areas with explicit reference to SDGs, Paris Agreement and German Government's sustainability strategy and launched its newly-developed own group-wide SDG mapping.

TSKB

TSKB aims to set the share of its sustainable and inclusive finance portfolio in the total loan portfolio, except for the finance sector, at 60% minimum by the end of 2020 by considering renewable energy, energy and resource efficiency investments in Turkey, while also taking the repayment of previous loans into account. As being a Founding Signatory of the Principles for Responsible Banking developed by the United Nations Environment Programme Finance Initiative (UNEP FI), TSKB is planning to participate in the Phase II of the UN Environment Finance Initiative (UNEP FI) in the working group of the TCFD. Some other related activities of TSKB are listed below:

- As a signatory of UN Global Compact Initiative, TSKB adopts the 10 Principles and acts to deliver on the SDGs.
- Having published the first GRI-approved Sustainability Report in the banking sector.
- Reports CDP Climate Change Report annually about climate actions taken with a continuous improvement approach.
- Holds ISO14001 certification for its Sustainable Management System and ISO 14064 certification regarding the calculation and verification of greenhouse gas emissions from its operations.
- Retains its position on BIST Corporate Governance Index, BIST Sustainability Index and FTSE4Good Emerging Markets Index.

Mainstreaming Climate Action in Financial Institutions

Illustrating IDFC's role as platform for advocacy, vision, and action, many Club members are supporting the 5 Principles for Mainstreaming Climate Action in Financial Institutions (www.mainstreamingclimate.org), aiming at facilitating and promoting the systematic integration of climate change considerations by the financial community at large, in line with the macro-objectives of the Paris Climate Agreement. As of today, an unprecedented coalition of public and private financial institutions around the globe, representing USD 13 trillion in assets, have joined the initiative since its launch at COP21.





Aligning with the Paris Agreement

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September 2019

A CPI and I4CE Executive Summary

Foreword

On 12 December 2015, the 196 Parties to the UN Framework Convention on Climate Change (UNFCCC) offered an unprecedented example of reconciliation as they agreed to put a world increasingly fractured by climate change on a pathway towards sustainable, low-carbon, and resilient development trajectories. Five years later, as we must switch gear from summits to solutions, aligning with the Paris Agreement has become a business case for all financial actors, national and regional development banks leading the way. This endeavor involves taking into consideration the upcoming risks and opportunities which underpin climate change.

At a time when climate action is most needed, it is an honor to present this groundbreaking report, produced by independent think tanks CPI and I4CE, which provides a robust framework usable by the members of the International Development Finance Club (IDFC) – a unique group of 24 national and regional development banks – and the financial community at large. This study includes a number of actionable recommendations designed to align any financial institutions' vision with the goals of the Paris Agreement at country, strategic, and operational levels.

National and regional development institutions are best placed to enable strong interconnections between public and private sectors as well as between local governments and global stakeholders. In particular, IDFC members can act as game-changers in the achievement of long-term national climate objectives. Endowed with an important capacity to redirect financing flows towards climate action, these institutions have already demonstrated their power of action.

To consolidate such results and ensure their stability over time, the IDFC needs to act now in fashion that is fully consistent with the Paris Agreement. And this report, of utmost analytical and operational importance, also highlights the fact the growing responsibilities and financial weight of IDFC members, combined with the urgent need to harness their full potential, require giving them a strong mandate to embark on this journey to alignment and support the objectives of the Paris Agreement as well as deploying those of the 2030 Agenda.

Aligning our financial flows with the Paris Agreement is a challenge but our strength lies in our interactions as a Club. Besides, the newly created IDFC Climate Facility will be a place to share our respective experiences on alignment and further concretize it within our respective institutions and in cooperation with all other willing partners.

In short, implementing an ambitious alignment strategy requires strong leadership and inventive ways of doing business, while seizing the opportunities of financing resilient and low-carbon development.





Rémy Rioux

Chief Executive Officer, Agence Française de Développement

Chair, International Development Finance Club

Executive Summary of Joint Research Project

Mandated by the International Development Finance Club (IDFC) and the European Climate Foundation (ECF), Climate Policy Initiative (CPI) and the Institute for Climate Economics (I4CE) have conducted a research project in two parts, resulting in a **Discussion Paper** (Part 1) and a **Final Report** (Part 2) on "**Aligning with the Paris Agreement**".

Part 1 led by I4CE establishes a theoretical and conceptual basis for alignment, analyzing and describing the emerging interpretations of the definitions, principles, and approaches across the financial community, and building on the experience of the Climate Action in Financial Institutions Initiative[1].

Part 2 led by CPI identifies the changes the Paris Agreement implies for the role of Development Finance Institutions (DFI) – specifically, members of the IDFC – and how they may implement these changes, through a targeted set of activities.

Part 1: I4CE Discussion Paper[2]

Alignment with the Paris Agreement: Why, What and How for Financial Institutions?

The Paris Agreement: reframing climate action around the long-term transformation of economies and societies

The Paris Agreement has reframed climate action from a focus on the near-term incremental increase of adaptation and mitigation actions to emphasize the long-term transformation of economies and societies. The Agreement highlights the importance of bottom-up country-led low-greenhouse gas (GHG) emissions climate-resilient development pathways to simultaneously achieve both climate and sustainable development objectives. Governments now have the responsibility to put into place the policy and investment frameworks to support the 'consistency' or 'alignment' of all social and economic activities with the long-term goals of the Paris Agreement.

Financial institutions - whether seeking sustainable development impacts or with a commercial focus – are increasingly committing to align their activities with the long-term goals of the Paris Agreement given that:

- Many will be called to directly contribute to the achievement of the long-term climate goals by shareholders and other stakeholders;
- All will need to manage the risks and opportunities associated with the needed transformation of the economy and the financial environment; and
- All will need to take into account and respond to the changing physical climate.

A Framework for Defining Alignment with the Paris Agreement

I4CE's discussion paper proposes a framework that can be used by financial institutions seeking to align strategies and operations with the Paris Agreement. The framework specifies three dimensions for action:

A Comprehensive Scope of Action: Institutions should seek to directly or indirectly support low-GHG climate-resilient development across all business areas – and take into account impacts on broader systems and value chains. This goes beyond measuring investment in activities supporting mitigation or adaptation outcomes; rather, it implies that all activities are carried out in a manner consistent with the long-term goals of the Paris Agreement.

A Long-Term Time Horizon to Guide Impact: Institutions should prioritize actions that are consistent with both near-term climate objectives and long-term goals and do not lead to lock-in or mal-adaptation. It is essential to recognize that some activities that result in 'relative' rather than 'absolute' emissions reductions or enhanced resilience may be counterproductive to achieving long-term goals.

An Ambitious Scale of Contribution: Institutions should seek to contribute to the ambitious goals of the Agreement through activities that:

- **Do No Harm**: All activities should neither hinder nor be counterproductive to the achievement of climate objectives and should be consistent with long-term national sustainable and low-GHG, climate-resilient development pathways;

1 https://www.mainstreamingclimate.org/

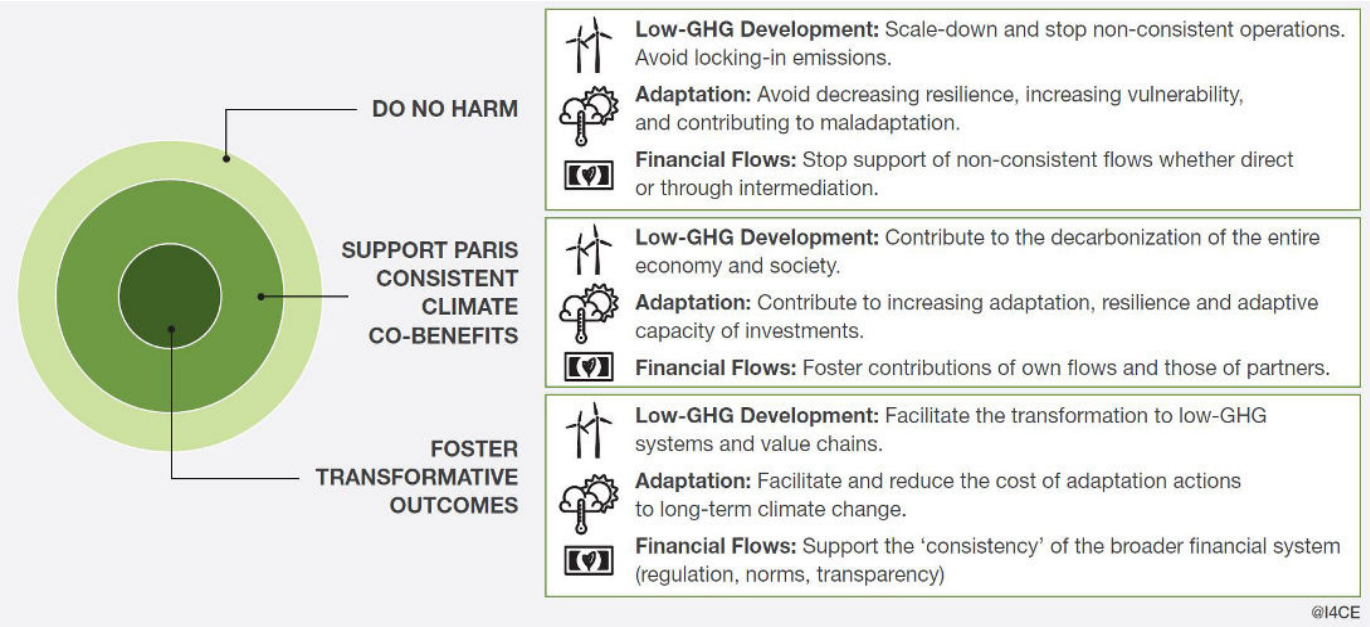
2 To read the full I4CE Discussion Paper, please see Cochran, Ian and Alice Pauthier (2019) Alignment with the Paris Agreement: Why, What and How for Financial Institutions? I4CE – Institute for Climate Economics. https://www.i4ce.org/download/framework-alignment-with-paris-agreement-why-what-and-how-for-financial-institutions

- **Support Paris-Consistent Climate Co-Benefits**: Whenever possible, institutions should prioritize activities with direct or indirect mitigation and adaptation co-benefits that are consistent with the national attainment of the long-term goals of the Paris Agreement;
- **Foster Transformative Outcomes**: Whenever possible, institutions should prioritize activities with 'transformative outcomes' that reduce the barriers to and support the large-scale, systemic and structural changes needed for the transition of economic, social and natural systems across and within national economies.

From Theory to Practice, Financial Institutions Can Build on Existing Approaches to Overcome Barriers

Whether institutions are principally focused on sustainable development impacts or commercially-oriented, a commitment to 'Paris Alignment' is a commitment to adopt the high level of ambition that is embodied in the Paris Agreement. The scale of contribution of financial institutions will vary as institutions may be involved in different types of business lines that have impact-oriented objectives or more commercial objectives. Nevertheless, for all financial institutions aligning with the Paris Agreement goals must scale-down and halt activities inconsistent with these goals and contribute whenever possible to national attainment of low-GHG climate-resilient development.

Figure 1: The Paris Alignment 'Bulls Eye': actively support national and international transformations across all activities



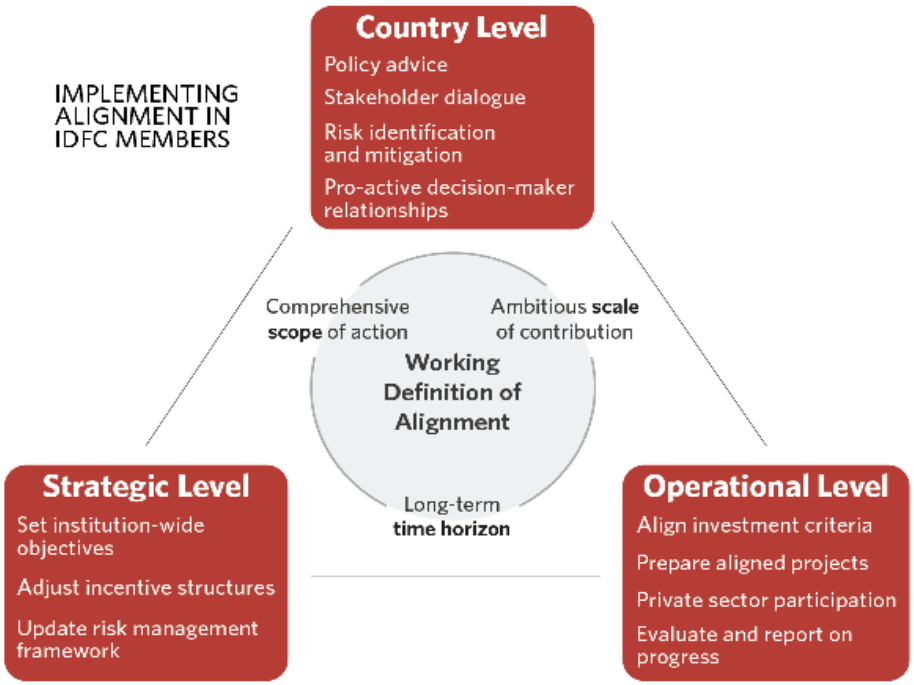
Source: I4CE

Furthermore, Paris alignment should take into account national contexts and support shared pathways or 'visions' of how long-term climate goals could be met nationally and internationally. Assessment of activities should consider both current country contexts and national forward-looking pathways for decarbonized and resilient development. When insufficient or not available, institutions may need to fall back on global projections and scenarios to achieve the long-term goals of the Agreement.

Doing this in practice requires financial institutions to integrate considerations of the Paris Agreement goals into their overarching strategies and operational frameworks and procedures for decision making and investment. Ensuring that all of an institution's activities are consistent with long-term goals is important. However, it is also important for institutions to determine and act on how they can best leverage their potential to support low-GHG climate-resilient transformations in their countries and sectors of operations.

The financial sector is not starting from zero and institutions can build on existing and emerging climate mainstreaming and climate risk management approaches. However, while addressing many similar issues, these approaches in their current form alone may not lead to institutions rapidly scaling down all 'harmful' activities and reorienting capital to scale up transformative contributions supporting long-term low-GHG and climate-resilient development. As a result, existing approaches may need to be adapted to take into account the changes around scope of action, time horizon of impact, and scale of contribution introduced by the Paris Agreement.

Figure 2: Recommendations for implementing alignment



Source: CPI in collaboration with I4CE

Part 2: CPI Final Report[3]

Implementing Alignment: Recommendations for the International Development Finance Club (IDFC)

Members of the IDFC, 24 national, bilateral, and regional development finance institutions with more than USD4 trillion in assets under management, can play a critical role in supporting the economic transformation of their countries of operation towards Paris alignment. IDFC members' close relationships with national and sub-national governments allow members to provide direct input and feedback on policy design and influence project pipelines (Crishna Morgado et al. 2019), and their diversity of clients in the public and private sectors allows them extraordinary reach across investment value chains and their enabling environments.

In 2018, the IDFC released a Position Paper on Alignment,[4] which all members committed to. The Position Paper spells out the members' specific understanding of alignment, establishes their role in implementing the requirements of the Paris Agreement, and lists a set of commitments to which members agreed.

This Part of the report describes how IDFC members can implement alignment in their institutions, using Part 1's framework of scope, scale, and time horizon as a guide to develop recommendations and taking into consideration IDFC specificities. While IDFC members vary greatly and no two IDFC members may approach alignment in the same way, all play a key role in advancing the alignment agenda through their practices and their ability to support their countries of operation in meeting the goals of the Paris Agreement.

All IDFC members will need to make changes to the way they do business to support the long-term transformational change required. The report proposes that alignment implementation can be facilitated by focusing on the following areas (see Figure 2).

3 To read the full CPI Final Report, see https://climatepolicyinitiative.org/publication/implementing-alignment-recommendations-for-theinternational-development-finance-club

4 https://www.idfc.org/wp-content/uploads/2019/04/idfc_alignment-with-paris-agreement_position-paper_12_2018.pdf

Institutions can take a first step towards alignment by developing an internal working definition.

An internal working definition of alignment can serve as a common basis for implementation throughout the organization by clearly articulating how the institution will contribute to the Paris Agreement objectives and by sending a clear signal to staff, external market participants, and other stakeholders that climate action underpins the institution's development objectives. The working definition can describe how the scope, scale, and time horizon dimensions of alignment apply to the institution.

Alignment of IDFC members is dependent on their relationships with government, and often vice versa

For publicly mandated development finance institutions, the ability to implement alignment will be greatly facilitated – or constrained – by their countries of operation, both through enabling environments as well as the influence of governments on IDFC members through their Boards. However, IDFC members are also uniquely positioned and trusted to support governments to contribute most effectively to the objectives of the Paris Agreement to which they have all agreed. Therefore, we propose in this study that alignment starts with the special relationship IDFC members have with the governments in their countries of operation.

Specifically, members can support countries in implementing commitments to the Paris Agreement through multiple levers:

- Policy advice: Supporting governments to build capacity on and develop forward-looking policy analysis and reform to devise low-GHG, climate-resilient development pathways.
- Coordination: Facilitating multi-stakeholder dialogue to include ministries beyond environment including among others finance, development, planning, and sectoral ministries such as agriculture and energy, as well as the private sector and civil society.
- Risk mitigation: Building in-country capacity to identify and mitigate climate risks, including physical, liability, and transition risks.
- Pro-active decision-maker relationships: Working pro-actively with government stakeholders who have oversight over member institutions (Board, Assembly, etc.) to understand and prioritize alignment alongside development priorities.

Action on alignment is greatly facilitated by executive leadership and institution-wide strategies

Paris alignment will require executive leadership to influence how decisions are made and the modalities to execute them. Alignment can be embedded in the strategic level of the organization by adopting:

- **Institution-wide objectives:** Adopting institution-wide objectives based on the working definition, encapsulating both a long term vision as well as near term milestones, and accompanied by appropriate metrics, can measure progress and incentivize increasing ambition. These objectives should drive the phase-out of non-aligned projects on the one hand, and encourage projects that meet criteria for transformative change on the other.
- **Well-structured incentive and support system:** Adjusting the incentive structures and support system of the institution to build capacity and generate buy-in among staff to support implementation across all operations.
- **An updated risk management framework:** Updating the organization's risk management framework can both encourage investments in aligned activities as well as to manage climate risks. The risk management framework should take advantage of existing unused risk capacity to seek transformative investment opportunities. On the other hand, the DFIs' focus on development benefits means that projects with heightened climate risks might still warrant further preparation and investment – either with accompanying risk mitigation measures or by exploring alternatives that achieve similar levels of development benefits.

At the operations level, alignment requires changes in how investments are assessed and how capital is deployed.

All investments across the institution's operations will need to be assessed against alignment criteria, and capital should be deployed using modalities that help deliver the transformative change necessitated by the Paris Agreement. An aligned IDFC members will undertake the following actions:

- **Update investment criteria:** Develop and integrate alignment assessment processes and decision-making criteria into its investment decisions across all operations, including direct lending, intermediary lending, procurement,

and technical assistance. These assessment processes and criteria should define and distinguish between investments that do no harm, have climate co-benefits, and contribute to transformative change, as well as those that are not-aligned at all. They should also establish a priority for emissions reductions and resilience in the long term, and will therefore need to guide the institution in decision-making under uncertainty.

- **Support early stage project preparation:** Support clients with development of aligned projects and programs from the earliest stages. Later stage projects that seek development finance are often more difficult to make modifications to due to the extensive planning that has already occurred.
- **Promote private sector participation and market development:** Increase use of modalities, such as risk mitigation instruments, that are effective at mobilizing private capital yet are often under-utilized in development finance institutions, including as a result of internal accounting methodologies and individual performance metrics.
- **Evaluate and report on progress:** Measurement and knowledge sharing will allow IDFC members to improve over time.

No IDFC member is currently fully aligned – this is a journey for all members, and they will each approach this differently

The development finance community is faced with a complex challenge in aligning itself with the goals of the Paris Agreement. IDFC members are critically important actors in both laying out and implementing a clear vision for what alignment means. In collaboration with governments, Members can be an effective bridge between the supply and demand for aligned finance.

While IDFC members share a common goal, the differences between them in terms of internal capacity, mandate, national circumstances, and resources imply a range of possible short-term paths. However, these must nonetheless converge with urgency towards activities reflecting the full scope, scale, and time horizon of the Paris Agreement objectives. Multiple options exist to progress towards the Paris goals:

- IDFC members benefiting from centralized leadership can start from the top – with a review of the mandate and development of working definition and targets that then disseminate throughout the organization.
- IDFC members with more challenging political environments can start from the bottom – by proving that climate and development are compatible, and by demonstrating new ways of doing business. An innovation unit can be helpful in this regard to generate internal buy-in.
- Accessing international climate resources – such as from the Green Climate Fund and Global Environment Facility, as well as from other DFIs – can also help drive internal change by building capacity and increasing focus on climate issues.
- Finally, members can leverage collaboration within the IDFC to learn from each other's experiences and harmonize approaches when possible.

The transition to alignment for the IDFC, individually and collectively, will not be easy, and it will take time – and therefore it should start now. With the roadmap to alignment presented here as a guide, members can scale up and build upon successful examples of existing practices with the sustained, focused effort required across all activities for the Paris Agreement's goals to be met.

While meeting this challenge will require unwavering commitment and engagement from members themselves, partnerships with others outside the IDFC will be vital. Collaboration with other financial institutions, both public and private, will be needed to streamline methodologies, metrics, and programming; reduce duplication; and accelerate the development of appropriate policy and financial instruments. Most crucially, IDFC members will need support – both political and financial - from the international community and shareholder governments to reach their potential to drive investment towards a Paris-aligned future.

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About CPI

With deep expertise in finance and policy, CPI is an analysis and advisory organization that works to improve the most important energy and land use practices around the world. Our mission is to help governments, businesses, and financial institutions drive economic growth while addressing climate change. CPI has six offices around the world in Brazil, India, Indonesia, Kenya, the United Kingdom, and the United States.

About I4CE

I4CE – Institute for Climate Economics is a think tank that provides public and private decision-makers with expertise on economic and financial issues related to the energy and ecological transition. We strive to implement the Paris Agreement, and make global financial flows compatible with low-carbon development that is resilient to climate change. I4CE is an initiative of Caisse des Dépôts and Agence Française de Développement and is also supported by the ADEME and Morocco's Caisse de Dépôts et Gestion.

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Strategic Partnership between IDFC and the Green Climate Fund (GCF)





Summary

The GCF promotes the paradigm shift towards low-emission and climate-resilient development pathways by providing support to developing countries to limit or reduce their greenhouse gas emissions and to adapt to the impacts of climate change. Considering the objective of supporting GCF's mission, and IDFC's commitment to align with the Paris Agreement and redirect financial flows in support of transitions towards low-carbon and climate resilient sustainable development, GCF and IDFC are well matched to become strategic partners for each other.

IDFC and the GCF already share a long-standing and successful history of collaboration since their respective establishment in 2011 and 2010, with numerous contributions, exchanges and activities of common interest: 11 members of the IDFC are already accredited and 12 projects amounting to close to USD 850 million were approved by the GCF and co-financed with accredited IDFC members.

As a way of increasing climate ambition and making the financial system shift towards climate- projects, programs and policies, the Green Climate Fund and national, regional and international development banks of the IDFC decided to strengthen and formalize their collaboration to play a leadership role together to serve the needed transformations to achieve the Paris Agreement objectives while promoting the key role of direct access national and regional development banks to provide, intermediate, implement and/or mobilize domestic and international climate finance.

Building on that strategic position, a Statement of Partnership was signed on June 26th, 2019 between IDFC and the GCF. The Statement of Partnership establishes a framework for collaboration to strengthen climate action and the promotion of joint initiatives in the following areas:

- Sharing knowledge for climate finance and action
- Integration of climate considerations within financial institutions
- Facilitation of access to GCF resources with co-financing from IDFC members and support to capacity building activities
- Outreach and awareness raising

Full statement of partnership: www.idfc.org/wp-content/uploads/2019/06/statement-of-partnership_idfc-gcf_20190626.pdf

IDFC Climate Facility

IDFC decided to create a Climate Facility as an operational and innovative tool to bring IDFC members to a higher level of **partnership and cooperation.** The Facility aims at strengthening knowledge and leveraging resources in the area of climate change mitigation and adaptation with the view to:

- **Meet the national, regional and international development banks' needs for appropriate frameworks and strengthened methodologies in the field of climate change.** Climate action comes out as one of the top priorities for IDFC members. Key challenges to be addressed range from further integrating climate change considerations into their mandates, developing innovative and more flexible financial products, mainstreaming climate finance into operations, and developing private sector engagement.
- **Address the lack of capacity building dedicated to development banks, despite their key role in driving the climate agenda.** Most of the existing facilities focus on providing assistance to developing countries. However, development banks are seldom identified as beneficiaries for capacity building and knowledge sharing despite the instrumental role these institutions play to spur climate action in their constituencies.

The equivalent of **10 MUSD** have been allocated by the IDFC members to implement the first 4-year pilot phase with the objectives to foster **knowledge sharing** and provide **capacity building to IDFC members**, through the following 6 activities:

Knowledge Sharing Activities

- **Online knowledge experience**: the online library will gather reference and organize knowledge material developed by IDFC members as well as additional relevant knowledge material from external sources.
- **Events and networking:** the Climate Facility will organize regional and global forums (including workshops, presentations, trainings and networking sessions), which will institutionalize ways to collectively share knowledge, lessons learned and best practices.
- **Online project market place**: the online project market place will consist in an online platform where members' projects will be promoted in order to attract co-financing partners among other members.

Capacity building activities

- **Training**: the Climate Facility will organize online and "in-person" training modules in response to IDFC members' needs. The Facility will provide training tailored to the specific context of financial institutions, and offer a platform for exchange and harmonization of skills and practice standards.
- **Coaching Programme**: The Climate Facility will constitute a group of IDFC members' staff ready to provide, as "coaches", targeted support and expertise to other IDFC member's employees.
- **IDFC toolbox:** The IDFC Toolbox will be a set of climate-related tools, adapted to the level of expertise and the needs of IDFC members, which can be used for each step of the project cycle to ensure integration of climate considerations, opportunities and risks.

On a pilot basis, the Facility will also aim at supporting project preparation and the facilitation of access to international climate resources such as the Green Climate Fund.



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