Implementing Paris Alignment for Development Finance

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Aligning with the Paris Agreement

A joint project between I4CE and CPI

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)
• a Final Report (Part 2) on “Implementing Alignment with the Paris Agreement”.

Part 1 establishes a theoretical and conceptual basis for alignment.

Part 2 identifies the changes the Paris Agreement implies for the role of Development Finance Institutions (DFI) – specifically, members of the IDFC.
Financial Institutions are Committing to Align Activities

➢ Many will be called to directly contribute to the achievement of the long-term climate goals by shareholders;

➢ All will need to manage the risks and opportunities associated with the needed transformation of the economy and the financial environment;

➢ All will need to take into account and respond to the changing physical climate.
A Framework for Defining Alignment with the Paris Agreement

Three Dimensions for Defining Alignment

A Comprehensive Scope of Action:
Screen all activities for contribution to low-GHG climate-resilient development

A Long-Term Time Horizon to Guide Impact:
Ensure that near-term actions contribute to the achievement of long-term goals

An Ambitious Scale of Contribution:
Actively support national and international transformations across all activities
A Framework for Defining Alignment with the Paris Agreement

A Comprehensive Scope of Action

Screen all activities for direct or indirect contributions to low-GHG climate-resilient development

➢ **Sectors & Business Areas**: Consideration of all economic sectors and activities, not just ‘climate-related’ sectors.

➢ **Systems / Value Chains**: Take into account impacts and influence on systems and entire value chains, both at national and global levels.
A Long-term Time Horizon:

Ensure that near-term actions contribute to the achievement of long-term goals

➢ **Lock-in & Mal-Adaptation**: Prioritize actions that are consistent with both near- and long-term climate objectives and do not lead to lock-in or mal-adaptation.

➢ **Relative & Absolute Impacts**: Recognize that activities that result in ‘relative’ rather than ‘absolute’ emissions reductions or enhanced resilience may be insufficient or counterproductive to achieving long-term goals.
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**An Ambitious Scale of Contribution:**

The Paris Alignment ‘Bulls Eye’

- **DO NO HARM**
  - **Low-GHG Development:** Scale-down and stop non-consistent operations. Avoid locking-in emissions.
  - **Adaptation:** Avoid decreasing resiliency, increasing vulnerability, and contributing to maladaptation.
  - **Financial Flows:** Stop support of non-consistent flows whether direct or through intermediation.

- **SUPPORT PARIS CONSISTENT CLIMATE CO-BENEFITS**
  - **Low-GHG Development:** Contribute to the decarbonization of the entire economy and society.
  - **Adaptation:** Contribute to increasing adaptation, resilience and adaptive capacity of investments.
  - **Financial Flows:** Foster contributions of own flows and those of partners.

- **FOSTER TRANSFORMATIVE OUTCOMES**
  - **Low-GHG Development:** Facilitate the transformation to low-GHG systems and value chains.
  - **Adaptation:** Facilitate and reduce the cost of adaptation actions to long-term climate change.
  - **Financial Flows:** Support the ‘consistency’ of the broader financial system (regulation, norms, transparency)
CPI Study

- **Objective:** To identify concrete steps that DFIs can take to implement alignment

- Of the 24 IDFC members, we surveyed 8, representing 20% of total IDFC assets

- Further in-depth interviews were conducted with 6 members
Implementing Alignment in IDFC members across three levels

**Country Level**
- Policy advice
- Stakeholder dialogue
- Risk identification and mitigation
- Pro-active decision-maker relationships

**Strategic Level**
- Set institution-wide objectives
- Adjust incentive structures
- Update risk management framework

**Operational Level**
- Align investment criteria
- Prepare aligned projects
- Private sector participation
- Evaluate and report on progress

**Working Definition of Alignment**
- Comprehensive scope of action
- Ambitious scale of contribution
- Long-term time horizon
### Description of how an institution understands alignment in their own context

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<tr>
<th>Working Definition of Alignment</th>
<th>Comprehensive Scope of Action</th>
<th>Ambitious Scale of Contribution</th>
<th>Long-Term Time-horizon</th>
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<tbody>
<tr>
<td></td>
<td>✓ Covers all operations of an institution</td>
<td>✓ Supports Paris-Aligned climate co-benefits and fostering transformative change</td>
<td>✓ Short-term milestones contribute to long-term objectives</td>
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<td>✓ Recognizes the institution’s potential to affect systems and value chains</td>
<td>✓ Stops non-aligned activities</td>
<td>✓ References how targets will be regularly adjusted upwards based on progress</td>
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Working Definition of Alignment

Member Examples:

➢ One member is developing a working definition of alignment based on an article-by-article analysis of the Paris Agreement.

➢ One member has referenced 100% Paris compatibility in its working definition.

➢ Another member has established an internal task force to identify and evaluate among different definitions.
1. **Support governments to build capacity** on and develop forward-looking policy analysis and reform

*Member example:*

The AFD Adapt’Action Facility provides support for **translating NDCs into long-term sectoral public policies** focused on the most climate-vulnerable sectors.

*Agence Francaise de Developpement*
2. **Build in-country capacity** to identify and mitigate climate risks

*Member example:*

**DBSA is undertaking an expert study for its energy strategy that will inform a least cost approach; how to manage transition risk; and how to support a just transition.**

*Development Bank of South Africa*
3. **Work pro-actively with government stakeholders** to understand and prioritize alignment alongside development priorities

4. **Facilitate multi-stakeholder dialogue** to include ministries beyond environment, as well as the private sector and civil society

**Member example:**

The CABEI **Governors’ Assembly issued a Carbon-Zero statement** supporting the implementation of sector-specific low-carbon resilient pathways and greater transparency and accountability for green project outcomes.

*Central American Bank for Economic Integration*
1. **Adopt institution-wide objectives** to drive the phase-out of non-aligned projects and encourage projects that meet criteria for transformative change on the other.

**Member example:**

DBSA introduced a target for private finance mobilization. **Catalyzing finance is featured in their corporate scorecard.**
Setting Institution-wide objectives...

<table>
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<th>Paris-Aligned Share of Portfolio</th>
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<td>Projects that do no harm to climate objectives</td>
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<tr>
<td>Target for projects with climate co-benefits consistent with Paris Agreement (%)</td>
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<tr>
<td>Targets for projects with a transformative change element &amp; private sector mobilization (%)</td>
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Non-Aligned Share of Portfolio

Target date for complete phase out

... Accompanied by Robust Criteria

Develop new criteria:
- Systems impact
- Transformative change
- Long-term contribution

Update existing criteria:
- Institution-wide application
- Eligibility criteria
- Exclusion criteria
2. Build capacity and generate buy-in among staff to support implementation across all operations.

Member example:

Several members cited applying for GCF accreditation as important for shedding light on skills and capacity gaps, and serving as a starting point for knowledge exchange.
3. Encourage investments in aligned activities as well as manage climate risks.

Member example:

AFD scored each existing client in its loan portfolio against five major climate hazards and “attention flags” were allocated to some counterparties. This approach is also being integrated into the loan origination process at the country level.
1. Update investment processes and criteria across all operations, including direct lending, intermediary lending, procurement, and technical assistance.

Member examples:

Several IDFC members use exclusion lists and/or have declined project investments due to non-alignment with the Paris Agreement, including several highly emissive and/or high lock-in effect projects.
2. Support clients with development of aligned projects and programs from the earliest stages

Member example:

AFD’s SUNREF initiative supports local financial institutions with credit facilities and technical assistance in sustainable finance. Its success led to replication at scale with GCF support to transform local FIs’ lending practices in sustainable finance.

*SUNREF: Sustainable Use of Natural Resources and Energy Finance*
3. Increase use of modalities, such as risk mitigation instruments, that are effective at mobilizing private capital.

**Member example:**

DBSA has established an innovation unit to design financial instruments to improve project bankability.
4. Measure, evaluate and share knowledge on a regular basis. This will allow IDFC members as a whole to improve their approaches and methods over time.

Example:

IDFC Climate Facility established 2019
Room for Collaboration

- **Technical cooperation**
  - Definitions
  - Metrics
  - Methodologies
  - Modeling

- **Support**
  - Financial and capacity building
Implementing alignment for development finance institutions will not be easy, and it will take time – and therefore it should start now.

➢ DFIs benefiting from centralized leadership can start at the strategic level, focusing on how their mandate and accompanying mission statements, strategies, and risk management framework do or do not support alignment.

➢ DFIs with more challenging political environments can start from the operational level, focusing on proofs of concept, definitions and criteria for transformative change, and leveraging external resources.

➢ Ultimately, leadership at all levels is needed.
Please type questions into the chat box on the lower right-hand side of the screen.
Explore our work

Read the full report: climatepolicyinitiative.org/publications

Join our webinar for the 2019 Global Landscape of Climate Finance - Nov. 7&8: climatepolicyinitiative.org/events

Attend our COP workshop on alignment: contact caroline.dreyer@cpicclimatefinance.org
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