

Post 2025 Climate Finance Architecture — through a climate justice lens



Photo: Paul Jeffrey/ACT

Part A: Foreword

Climate financing is urgently needed for systemic transitions towards zero-carbon societies. The need to act robustly to avoid the most damaging impacts of the climate crisis is increasingly clear. From experience we know that developing countries have faced difficulties mobilising and accessing agreed-upon support. For poor and vulnerable communities, the lack of action is life threatening - their future depends on the actions of major polluters around the world.

Advancing climate justice has been the guiding principle of ACT Alliance campaigns for several years. It entails a call for climate finance, and support for mitigation, adaptation, and loss and damage in the Global South.

Negotiators from developing and developed countries should set and implement a new climate finance goal for the post 2025 period. The success of its delivery hinges on a reflective process of the USD 100 billion promise, extensive and meaningful consultations with all stakeholders and centring the needs of vulnerable nations in its elaboration. The new and repurposed financial architecture must enable ease of access to finance for climate action and avoid placing frontline nations into further debt stress.

It is our ambition that the new goal and its regime will galvanise climate justice action and make it possible for the world's vulnerable and disenfranchised to rise above the impacts of climate change.

To make post 2025 climate finance count for vulnerable and marginalised communities, we must learn from the problems characterising the existing system of climate finance. That is the purpose of this paper: to review the problems, learn from them and create solid recommendations for a post-2025 climate finance regime that leaves no one behind.



Rudelmar Bueno de Faria

General Secretary, ACT Alliance

How to use this paper

This paper aims to assist reader's understanding of climate finance: how it operates; the shortfalls; the opportunities; and in particular the changes required to the architecture in order to deliver a climate just post 2025 finance regime. The intended audience for this paper is broad and includes UNFCCC participants and negotiators, political leaders and decision-makers, designers and operators of climate funds and facilities, financial institutions, climate project developers, NGOs, media, and ACT Alliance's member base, including youth ambassadors around the world. Please use this paper and its recommendations for enhanced awareness, decision-making, and advocacy and campaigning for developed countries to deliver climate finance to developing countries equalising their transition to a low carbon climate resilient future with reduced loss and damage.

This paper will explore six key themes related to climate finance challenges, accompanied by voices from the global south which bring these challenges to life. Each theme is described in terms of:

- Situation analysis;
- What should be done; and
- Recommendations.

Acknowledgements

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Part B: Recommendations

This paper makes seven recommendations for the successful negotiation of a post 2025 global climate finance agreement, based on the experience gained from existing climate finance arrangements and the need for urgent action in light of the accelerated pace and impacts of climate change. It is crucial that countries and key stakeholders reach agreement during the next round of international climate negotiations and are prepared to take climate finance and action one step further for the post 2025 period. The following recommendations cover important topics for consideration and inclusion in the post 2025 climate finance architecture.

1. Definitions

The new climate finance agreement for the post 2025 period must include clear definitions about: a) which activities/projects should count as climate finance and; b) what should be the methodological approach used to calculate the amount mobilised with a view to enhance comparability of data and transparency in reporting.

2. Modalities

A defined target and agreed reporting methodologies are required for mobilised resources of each category of climate finance flow (grants, loans, etc.), with the majority of funds mobilised being grant-based and concessional loans.

3. New and additional

An internationally agreed definition of “new and additional” must be set for the post 2025 period climate finance framework, while upholding the critical climate finance principle of additionality to ODA. A guiding principle must be to establish a baseline for future ODA commitments and ensure that climate spending reflects a significant increase beyond this level.

4. Scale

Both developed and developing countries should agree on a new climate finance commitment for the post 2025 period, taking the existing USD 100 billion goal as a floor and complementing this with the best available and credible science-based estimates for the cost of addressing greenhouse gas mitigation, climate adaptation and loss and damage in developing countries.

5. Allocation

Clear, individual, and measurable financial target allocations should be set for each of the three areas: mitigation, adaptation and loss and damage.

6. and 7. Special attention

The post 2025 climate finance regime should have a special target for locally led adaptation to ensure that resources will reach and empower those who are the most vulnerable and need it most.

The process of accessing climate finance should be streamlined and take into consideration developing countries' immediate needs and capacities, reducing or eliminating existing barriers and avoiding the creation of future obstacles.

Part C: Introduction

Context

According to the IPCC's Sixth Assessment Report, it is unequivocal that human influence has warmed the atmosphere, ocean and land, and human-induced climate change is already affecting many weather and climate extreme events in every region across the globe¹. Vulnerable populations are already suffering from the effects of climate change, especially in developing countries. Therefore, it is urgent to take action to mitigate greenhouse gas (GHG) emissions and to implement adaptation solutions, following the principle of climate justice, as the temperature is about to rise above 1.5° C above pre-industrial levels during the 2030s.

Climate finance is one of the main mechanisms through which climate action and justice can be enhanced. Climate finance is a means of implementation, an enabler of climate action. Therefore, the amount of finance availed, accessed, and delivered to developing nations should be based on their climate needs and economic circumstances. Mobilising climate finance is not only a matter of following international agreements, but of ensuring justice for those who are most vulnerable and hard-hit by climate change, now and in the future.

Climate finance is one of the main mechanisms through which climate action and justice can be enhanced.



The climate emergency is already a reality and ambitious actions are needed now. Rich nations have an obligation under the UN Framework Convention on Climate Change (UNFCCC) and the Paris Agreement to stand in solidarity with vulnerable nations by providing finance at increased scale and speed. Implementing a human rights approach to the way climate finance is mobilised provides a tool to consolidate climate justice at a global scale. The post-2025 vision for the climate finance landscape, therefore, must include a climate justice and human rights perspective.

Brief overview of the problem

The idea of a collective goal to mobilise USD 100 billion per year by 2020 for supporting climate action in developing countries was born during the 15th Conference of Parties (COP15) of the UNFCCC in Copenhagen in 2009,. Even though the Copenhagen Accord was non-binding, setting this political target was crucial for the evolving climate diplomacy at the time and delivered a quantifiable benchmark for mobilising finance. Developing nations capacity to deal with climate impacts is tied to developed nation's delivery of their climate finance obligations.

During the **15th Conference of Parties (COP15)** of the UNFCCC in Copenhagen in 2009, the idea of a collective goal to mobilise **USD 100 billion per year by 2020** for supporting climate action in developing countries was born.

Developed countries agreed to the USD 100 billion goal at COP16 in Cancun and reiterated their commitment during COP21 in Paris. Article 9 of the Paris Agreement stipulates that:

“Developed country Parties shall provide financial resources to assist developing country Parties with respect to both mitigation and adaptation in continuation of their existing obligations under the Convention”².

Developing nations' capacity to deal with climate impacts is tied to developed nations' delivery of their climate finance obligations. The climate finance commitment made by developed countries, though a starting point in climate finance mobilisation, still fell short of what was expected in view of developing countries' evidence-based needs for climate action. Nevertheless, achieving this target between 2021-2025 as required under the Paris Agreement and accounting for shortfalls in its delivery in the pre-2020 period is paramount to demonstrate proof of engagement and is a critical step to keep building the trust necessary to allow climate negotiations to continue progressing.

Despite efforts since 2009 to mobilise climate finance, as well as to improve the transparency of climate finance reporting, recognised published data and studies show that developed countries are failing to meet this goal. As a single action, meeting the USD 100 billion target will not be enough to enhance climate action at a sufficient pace to cope with the effects of climate change. With the IPCC 6th Assessment Report showing more urgently than ever the need to take action against climate change, the international community will need a more ambitious and thorough plan, as well as a more efficient financial architecture for the post 2025 period.

The envisioned climate finance regime for post 2025 must start from a positive outcome from the COP26 in Glasgow, where a new climate finance goal will be discussed. More ambitious NDCs and financial commitments from developed countries, as well as agreements on climate finance definitions and methodological approaches will help shape the post 2025 climate finance regime.

The contributions presented in countries' updated NDCs still fall short of the ambition required to reach the global warming targets. **If the international community wants to keep its commitment to the Paris Agreement and pursue efforts to limit the temperature increase to 1.5°C above pre-industrial levels, more ambitious actions and increased resources will be needed, and the mobilisation and equitable distribution of climate finance will be a crucial step.** Governments, civil society, and other key stakeholders will have to engage and proactively cooperate towards building a climate resilient future for the next generations.

This evidence-based paper has been prepared in the context of the 2021-2023 Global Stocktake of the Paris Agreement, which aims to assess the world's collective progress towards achieving the purpose of the agreement and its long-term goals. The paper analyses developed countries' recent efforts to

mobilise climate finance, their results, and the consequences. This analysis includes recommendations for the upcoming post 2025 climate finance agreement. Six key themes are identified to improve the effectiveness and fairness of climate finance mobilisation and its contribution to the climate emergency.

Part D: Six themes

1. Definitions - unpacking climate finance accounting



**RAJAN
THAPA
NEPAL**

"Internationally, climate finance does not have a common definition. This creates major hurdles in terms of meeting climate finance commitments, clarity on what can be classified as climate finance, and transparent reporting. Therefore, accurate and independent analysis of climate finance is essential and urgently needed."

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1.1 Situation analysis

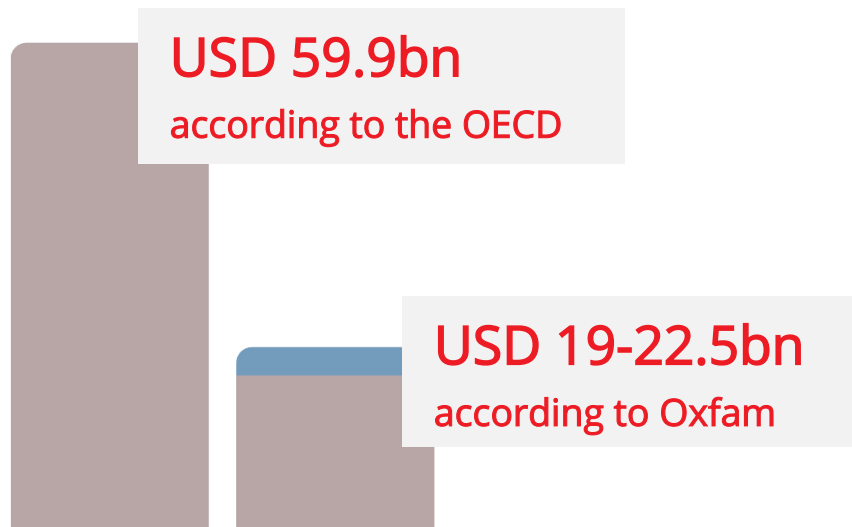
The USD 100 billion climate finance target was an important milestone in international climate negotiations. However, 12 years after the COP15, there is still no clear definition of what counts as climate finance³.

Several organisations have assessed progress towards the USD 100 billion goal. For example, the OECD, at the request of donor countries, publishes a yearly report analysing climate finance flows from different sources. The UNFCCC Standing Committee on Finance also publishes biennial assessments of global climate finance, as have civil society organisations and academics. Recent data shows that, although there has been an upward trajectory in climate finance globally over the past few years, it is very likely that developed countries have not yet reached the USD 100 billion goal. Due to time lags in official reporting and the different datasets in use, 2020 figures are not yet available. However, the most recent report from OECD shows that **in 2019, climate finance reached USD 79.6 billion, an increase of only 2 per cent from 2018⁴. Therefore, it is unlikely that climate finance has been mobilised at a sufficient level and pace since 2019 to achieve the target.**

In addition, the methodology used by the OECD to calculate the amount mobilised towards the USD 100 billion target has been disputed by different actors worldwide. International NGOs such as Oxfam and CARE, as well as Government and peer-reviewed scientific studies⁵, for example, have argued that actual climate finance flows are, in fact, much lower than the OECD estimates. According to Oxfam,

climate-specific net assistance provided by developed countries between 2017 and 2018 may have been between USD 19 and 22.5 billion⁶, while data from the OECD indicates a figure of USD 59.9 billion.

The methodology used by the OECD to calculate the amount mobilised towards the USD 100 billion target has been disputed by different actors worldwide. Between 2017 - 2018, climate finance mobilised by developed countries



The difference in the reported numbers is due to the approach used to calculate climate finance mobilised by developed countries. The UN and OECD have noted the existence of data issues that affect the quality of the results. Beyond the availability and quality of data, there are other issues related to counting climate finance. The Katowice rulebook indicates that parties should count all modalities and the OECD aligns with this rule, counting all instruments, including grants, loans, equity investments and export credits, both from public and private sources from developed countries. However, while the Katowice rulebook is clear on modalities, it is less clear on what activities should be counted as climate finance.

Many international stakeholders have argued that current reporting practices lead to overcounting of climate finance resources mobilised and question whether these practices constitute a just approach for climate finance accounting. Already in 2015, a discussion paper released by the Indian Ministry of Finance argued that the OECD report overstated progress and the methodologies were inconsistent with the best practices and literature⁷.

The Rio Marker methodology, one of the main approaches used to define the climate relevance of projects, leads to significant overcounting of climate finance. According to this methodology, a project with only a small element dedicated to climate issues can be classified as either 'principal' or 'significant' and have 50 per cent or 100 per cent of its budget accounted as climate finance, increasing the figures of financial flows without having the same impact on climate actions on the ground. Furthermore, adaptation activities include those that many in developing countries would count as loss and damage activities. The variation in reporting practices makes it difficult to assess and compare data between countries.

1.2 Accountability and monitoring

The lack of definitions about which activities should count as well as how the resources should be categorised also impacts the ability to monitor climate finance flows and ensure accountability. A clear and agreed definition and guidelines for climate finance and its accounting approaches is needed for keeping track of whether pledges are being met and to monitor, for example, whether financial flows

are really shifting from polluting sectors towards low carbon climate resilient pathways, contributing to a sustainable economy⁸.

According to the Independent Expert Group on Climate Finance⁹, despite the efforts to improve consistency, comparability, and overall transparency of reporting on climate-specific finance, two methodological problems remain:

1. The methodology used to determine climate-specific finance when reporting under the UNFCCC is not applied on a consistent basis across reporting countries for both bilateral and multilateral providers;
2. There is no consistent methodology applied to account for private finance mobilised via MDBs and bilateral agencies

The lack of clear definitions and accounting rules fuels mistrust among countries, creating a serious challenge for climate diplomacy¹⁰. Broken climate finance promises, combined with the absence of definitions and agreement on how to interpret the decisions, hinders accountability. Recurring conflicts arise during climate negotiations as a result of the ensuing lack of trust between governments and stakeholders. This creates obstacles to achieve ambitious commitments and jeopardises the progress made to date, as the climate agenda is side-lined. Consequently, the existing governance framework is not favourable to enhance accelerated action on climate change, and furthermore, has been perceived as advantageous to those evading their climate obligations, including climate finance commitments.

To define what counts as climate finance, including activities, modalities, and financial flows, as well as who is responsible for assessing it, we urgently need to avoid contradictory claims regarding the fulfilment of the agreed commitments¹¹. Only when climate finance definitions and standardised methodological approaches of accounting are internationally agreed will the climate finance framework be transparent and set the basis to inform the delivery of fair and accessible financial support¹².



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Photo: Simon Chambers/ACT

Many developing countries are attempting to better understand incoming climate finance flows by implementing tracking tools like the Climate Public Expenditure and Institutional Review, which

classifies and categorises public climate change spending by government and CSOs, and in some cases by private investors. This “bottom up” approach may help to triangulate and clarify whether the total amount of climate finance promised has been delivered.

1.3 “What should be done?”

A transparent climate finance framework for the post 2025 regime will require agreement on defined concepts and methodologies. However, it is also important that policy makers stand in solidarity with vulnerable communities who are already battling against climate impacts. Policy makers must agree on a process that ensures enhanced accountability to these communities.

Any climate financial agreement set for the post 2025 period will need to include clear and internationally agreed definitions of the key concepts related to climate finance. Therefore, the governments and stakeholders should draw from the debates, research and lessons learned during the 2009-2021 period to avoid confusion, conflicts, and stalemates, and to work towards establishing recognised definitions for a transparent and impactful climate finance regime for the post 2025 period.

1.4 Recommendation

The new climate finance agreement for the post 2025 period must include clear definitions about: a) which activities/projects should count as climate finance and; b) what should be the methodological approach used to calculate the amount mobilised with a view to enhance comparability of data and transparency in reporting.

2. Modalities – availability and application of financial instruments



PATRICIAH ROY AKULLO
UGANDA

“The Government of Uganda received an Adaptation Fund grant to increase the resilience of communities at risk of floods and landslides. This result is far from being realised! There appears to be no long-lasting impact, the project is soon ending and the region still faces floods and landslides. The solution is to scale-up this project with additional grants as as Uganda is highly indebted and cannot take on more loans, especially for climate.”

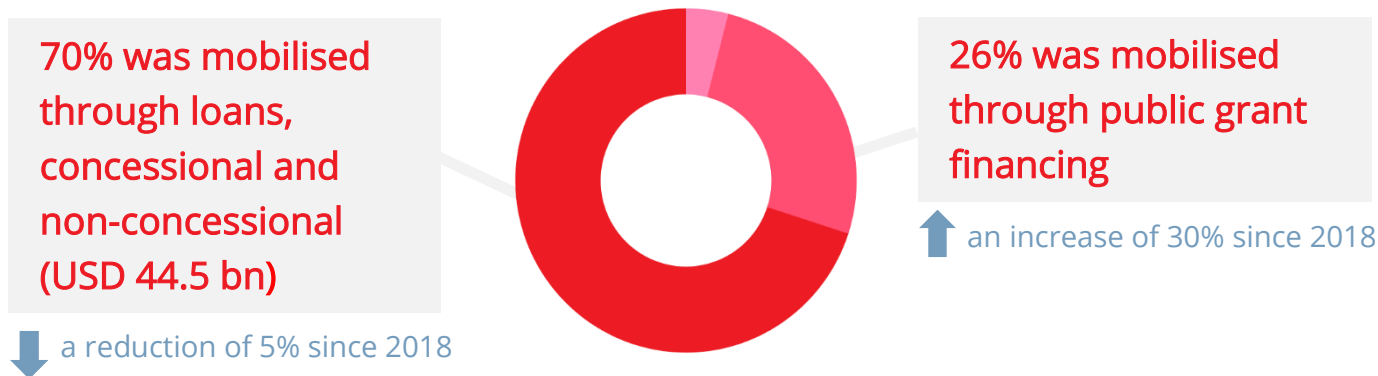
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2.1 Situation analysis

Financial instruments used to channel resources for climate action in developing countries include grants, concessional and non-concessional loans, guarantees, equity investments, insurance, and others. The sources of funds are mainly governments, international development agencies and the private sector. In terms of the share of each modality used, according to the latest OECD report, in 2019,

70 per cent of the public climate investment to developing countries was mobilised through loans, both concessional and non-concessional, the equivalent to USD 44.5 billion, and a reduction of 5 per cent compared to 2018. Meanwhile, public grant financing increased 30 percent in comparison to 2018, but it is still responsible for only 26 per cent of the total share¹³, and private finance is mostly mobilised through direct investments in companies and projects.

According to the latest OECD report and based on the share of each modality used, in 2019:



The imbalance between loans and grants creates challenges for advancing climate action in developing countries. While grants do not need to be repaid, loans need to be repaid with interest. As a consequence, loans tend to be provided for projects that demonstrate capacity to generate returns on investment, which has led to a skewed funding balance in favour of GHG mitigation projects like power generation – even where countries are in dire need of adaptation financing. A focus on financial payback also disadvantages poorer countries and communities with limited productive resources. Furthermore, it downplays the relative attractiveness of mitigation and adaptation projects that generate significant social and environmental co-benefits in the form of public goods (reduced air pollution, improved water quality, increased biodiversity, etc.).

2.2 “What should be done?”

Following the compensatory principle of climate justice, developed countries should focus efforts on mobilising climate finance through modalities and financial instruments that best respond to developing countries’ financial/economic status, needs and most vulnerable populations. The option of grants should be prioritised as well as concessional loans, versus non-concessional loans. Work in determining how to assess the concessionality of loans, guarantees and blended finance must be undertaken and can be informed by the OECD Development Aid Committee’s recommendation on grant-equivalent reporting and other defined methodologies.

2.3 Recommendation

Each financing modality requires a defined target and agreed reporting methodologies for mobilised resources, with the majority of the total climate finance mobilised taking the form of grants and concessional loans.

Many mitigation activities generate financial returns and can be supported in part via loans and equity investments. This approach can help crowd in private sector resources and align incentives in favour of project sustainability. However, these activities also generate societal co-benefits that have

characteristics of public goods (e.g., reduced air pollution, watershed restoration, enhanced climate information and early warning systems), which justifies grant support¹⁴. The reality for many indebted and climate vulnerable developing countries is that, in taking on a loan to respond to climate change, the burden of risk is increased, leaving these countries exposed to greater vulnerability in being saddled with debt. Irrespective of the theoretical, financial, or economic benefits of the investment. Where non-grant climate finance instruments are provided to developing countries, a grant equivalent should be calculated to demonstrate that these resources are being provided on a concessional basis.

3. New and additional – going beyond existing efforts and ODA



**NUSHRAT
CHOWDHURY**

BANGLADESH

“Bangladesh is projected to lose 17% of its land by 2050. The future of millions of people is uncertain though it invests USD 1 billion to adapt to climate change annually. For climate vulnerable countries like Bangladesh, there is no alternative other than new and additional climate finance.”

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3.1 Situation analysis

One of the main demands from developing countries was for “new and additional” resources to be mobilised and disbursed for climate finance support. This means that the resources allocated to support developing country climate action should go beyond existing efforts and Official Development Assistance (ODA).

However, in the absence of an internationally agreed definition of the term “new and additional”, each country tends to adopt its own interpretation. Norway, for example, recognises that climate finance should be additional to the international development aid goal of 0.7 per cent of Gross National Income (GNI)¹⁵. Other countries calculate “new and additional” as any resources above an agreed baseline, or beyond current ODA. Most of the definitions are ambiguous and do not allow for a transparent comparison to assess the overall performance of climate finance mobilised.

The lack of definition for the term “new and additional” contributes to the problem of monitoring climate finance flows and evaluating if targets are being met. The major concern behind the lack of definition of what constitutes “new and additional” funds is that the finance mobilisation for climate action may result in reductions of existing ODA resources earmarked for other development needs. In other words, ODA resources that are currently being directed to important sectors such as education or healthcare could be reprogrammed to climate finance, creating new challenges for developing countries that depend on these sectoral funds. Even though developed countries agree that all ODA

resources should consider environmental issues, climate adaptation requires specific action. Therefore, if the climate finance is not “new and additional” to other development aid, vulnerable countries will continue facing a worsening climate crisis with even fewer assistance resources allocated to other important sectors, increasing their vulnerability.

3.2 “What should be done?”

There is a recognition that ODA spending should avoid activities that contribute to GHG emissions or maladaptation. However, addressing climate challenges should not conflict with other sustainable development goals. It is crucial for the future of climate negotiations and advancing climate action that parties reach agreement on what should be considered as “new and additional” funds, without jeopardising other sectors that already depend on resources from ODA.

3.3 Recommendation

An internationally agreed definition of “new and additional” must be set for the post 2025 period climate finance framework, and this definition must uphold the critical climate finance principle of additionality to ODA. A guiding principle must be to establish a baseline for future ODA commitments and ensure that climate spending reflects a significant increase beyond this level.

The new architecture must ensure, and avoid, the potential risk of developed countries reducing support for, and therefore compromising, developing countries’ other critical development needs (healthcare, education, shelter etc). The potential ‘watering down’ of ODA funds, in favour of re-directing those funds to the “new and additional” basket as an attempt to scale-up climate finance would be unjust. While recognising that developed countries should avoid supporting highly emitting or maladaptive activities in their normal funding, the expectation is that overall funds must be increased rather than merely diverted or reprogrammed.

4. Scale – agreeing USD ? billion to fight global climate change

4.1 Situation analysis

Although setting the USD 100 billion target was considered a success for climate diplomacy, the overall cost to address climate challenges is much higher and meeting this initial target will not be sufficient to address climate change impacts and risks. The costs of climate change to poor countries will exceed the finances they would receive through the different climate finance instruments, leading to ineffective and unjust outcomes.

According to UNEP’s 2020 Adaptation Gap Report: “adaptation costs in developing countries alone are currently estimated to be in the order of USD 70 billion, with the expectation of reaching USD 140-300 billion in 2030 and USD 280-500 billion in 2050”¹⁶. The Green Climate Fund claims that the infrastructure investment gap could reach a cumulative value of between USD 14.9 and 30 trillion by 2040, due to the insufficient pace and scale of global climate action¹⁷. The International Energy Agency analysed what would be needed from the energy sector to limit the global temperature rise to well below 2°C and the results showed that USD 3.5 trillion in energy-sector investments would be necessary on average each year until 2050¹⁸.



Adaptation costs in developing countries alone are currently estimated to be in the order of USD 70 billion, with the expectation of reaching USD 140-300 billion in 2030 and USD 280-500 billion in 2050.

Photo: Sean Hawkey / Life on Earth

Resources mobilised to date are barely enough to meet current obligations, which highlights the need to urgently scale up the resources dedicated to climate action. The OECD reports have made clear that donors need to step up efforts and address imbalances in climate finance¹⁹. This means both meeting the USD 100 billion target, but also going beyond it in the post 2025 climate finance regime.

At the same time, a large amount of funding is still being mobilised to support polluting industries and sectors. In 2019, the top 33 banks alone allocated USD 654 billion to the fossil fuel industry, more than double their commitments to sustainable finance²⁰. If developed countries and key climate finance stakeholders want to ensure that climate action will be implemented at a sufficient level, the scale of climate finance mobilised will have to increase significantly, even as finance moves out of high-emissions and maladaptive investments.

In 2019, the top 33 banks alone allocated USD 654 billion to the fossil fuel industry, more than double of their commitments to sustainable finance.



4.2 "What should be done?"

Considering the scale of the climate change problem, the USD 100 billion goal should be considered as a floor for any future international climate finance commitment, as stated in the Paris Agreement. The process of scaling up climate finance in the period post 2025, and consequently advancing with climate action, must demonstrate a strong needs-based focus with costed estimates from developing countries

informing efforts to ramp up grant based and concessional financing by developed nations. Climate stabilisation and adaptation will require major investments in green technology, combined with a shift away from providing subsidies for fossil fuels and other polluting sectors, and towards a low carbon, climate resilient economy. These investment shifts are in addition to the commitments made by governments to international climate finance, as well as innovative ways of leveraging finance and engaging different stakeholders.

Creating fair and just carbon pricing systems, forging public-private partnerships, and advancing green bonds are some practical examples of what can be done to leverage climate finance beyond the existing commitments made by Governments.

4.3 Recommendation

Both developed and developing countries should agree on a new climate finance commitment for the post 2025 period, taking the existing USD 100 billion goal as a floor and complementing this with the best available and credible science-based estimates for the cost of greenhouse gas mitigation, climate adaptation and loss and damage in developing countries.

The determination of climate finance needs of developing countries through a fair and inclusive process is integral to setting a new climate finance goal. This goal should be over and above identified economic development needs of developing countries. Moreover, the process should be participative and include voices from the south, with special attention to representatives from vulnerable communities and groups, ensuring procedural climate justice.

The identification of country specific climate needs is also integral to setting a new climate finance target. These are often presented at a high level in countries' NDCs and National Adaptation Plans, however, more support is required to articulate downscaled sectoral and project-level priorities.

5. Allocation – Adaptation *versus* Mitigation *versus* Loss and Damage



**JULIUS
MBATIA**

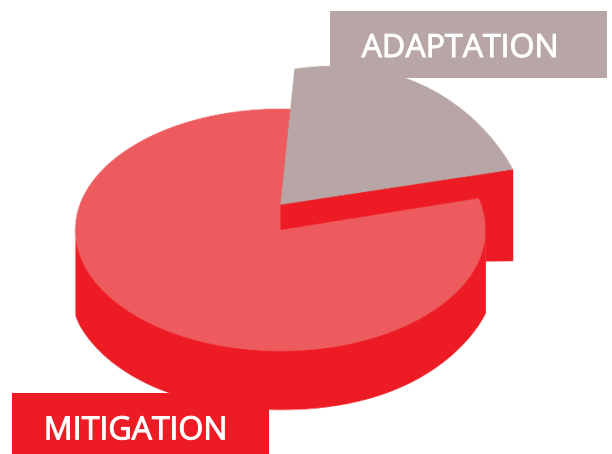
KENYA

“Climate change continues to place additional burden on Kenya and increasingly retracts development gains. Adaptation is the country’s priority and finance must be scaled-up along with access by local communities. The discrepancy between mitigation and adaptation finance remains disheartening. Mitigation accounts for 55% of total international public finance while adaptation gets a lower share of 23%. This gap must be bridged by developed nations and needs-driven financing must be adopted.”

5.1 Situation analysis

According to the Paris Agreement, the provision of climate finance resources should aim to achieve a balance between adaptation and mitigation investments, both of which are necessary to limit the impacts of climate change. However, there is no consensus on the appropriate ratio between these elements, nor how this ratio might vary according to different regional and developing country contexts. Recent data from the OECD²¹ shows that although there was a 20 per cent increase in adaptation finance in 2019, mitigation still represents two-thirds of total climate finance mobilised by developed countries. From the climate finance investments reported by the European Union in 2018, only 36 per cent went towards adaptation²², while the MDBs committed in 2020 only 24 per cent to adaptation, the equivalent of USD 16.1 billion of their climate finance resources²³. The climate-finance allocation for adaptation remains inadequate and far from balanced.

Although there was a 20% increase of adaptation finance in 2019, mitigation still represents 2/3 of total climate finance mobilised by developed countries.



The smaller share of climate finance going towards adaptation can be attributed largely to the fact that many mitigation projects are more “bankable” than their adaptation counterparts. These mitigation projects often generate short-term financial flows for private investors especially since there are mechanisms that allow investors to monetise GHG emission reductions, which allows mitigation projects to more easily crowd in private sector finance²⁴. In addition, there are established metrics for evaluating mitigation projects over both the short and long term, which makes them more attractive to donors. By comparison, many adaptation investments are defensive in nature, the benefits are probabilistic (for example, reducing losses from future droughts and temperature increases) and more effort is required to monetise these benefits. Data from the OECD²⁵ shows that between 2016-18, 93 per cent of private finance mobilised by developed countries focused on mitigation, predominantly in the energy sector, which attracted 60 per cent of the total.

While mitigation efforts are crucial to reduce GHG emissions and avoiding critical climate tipping points, adaptation is needed as a strategy to significantly reduce the economic, social, and environmental impacts that are already a reality in many parts of the world and will increase, with cascading effects, even if GHG emissions ceased tomorrow.

It is challenging to obtain credible estimates of the cost of adaptation. However, according to the UNEP 2020 Adaptation Gap Report²⁶, developing country adaptation costs are currently estimated to be around USD 70 billion per year, and could range from USD 140 billion to USD 300 billion annually by 2030. By 2050 this could rise from USD 280 billion to USD 500 billion. When compared to the data on

climate finance resources being invested in adaptation strategies by different sources, the adaptation financing gap is clear. This state of affairs is particularly unjust since it is usually people in the poorest countries that are most vulnerable to climate hazards, bear the greatest burden in addressing climate impacts, and are most in need of adaptation finance. The adaptation finance shortfall is failing the people who need it most.

5.2 Loss and Damage



**SOSTINA
TAKURE**
ZIMBABWE

"Cyclone Idai in 2019 resulted in the loss of lives and livelihoods in Zimbabwe. Targeted funding towards climate induced-losses and damages is crucial to ensure the survival of vulnerable countries affected more severely than adaptation financing can address. As the world reduces emissions, this compensation remains crucial."

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Despite the efforts to mitigate emissions and adapt to climate change impacts, some negative consequences are now unavoidable. These unavoidable climate costs are categorised as “loss and damage”. Loss and damage accounts not only for economic losses, but also non-economic losses that include for example, health, life, mobility, cultural heritage, biodiversity, and ecosystem services that may well be more significant than economic losses²⁷. International climate negotiations have recognised the obligation for developed countries to address these loss and damage costs, via a ‘third pillar’ of international climate finance based on the “polluter pays” principle.

There is limited data available on the financial costs of loss and damage to date. However, studies estimate that developing countries will face financial losses between USD 300 billion and USD 4 trillion per year by 2030²⁸. Nevertheless, the impacts of loss and damage will be global, affecting for example supply chains and migration. According to a recent study, the global economic cost of climate change could be six times higher than previously estimated and global GDP could be 6 per cent lower in 2100²⁹.

Studies estimate that developing countries will face financial losses between USD 300 billion and USD 4 trillion per year by 2030.



The international community has made some effort to address loss and damage associated with climate change impacts in highly vulnerable developing countries. The Warsaw International Mechanism for Loss and Damage (WIM) was established during the COP19 in 2013 and its mandate includes: “Enhancing action and support, including finance, technology and capacity building to address loss and damage associated with the adverse effects of climate change”³⁰. However, little progress has been made in this regard. The Santiago Network was created to catalyse technical assistance related to loss and damage, but will not be operationalised until after COP26. If climate finance for adaptation is already considered inadequate, the mobilisation of resources to address loss and damage is even more challenging. Some existing humanitarian and development financial flows address loss and damage, but the lack of agreement about specific climate focused loss and damage finance makes it challenging to monitor and report.

Without international climate finance support to account for transient and lasting damages related to climate change, developing countries will very likely face increasing economic losses, which can reduce resources available to tackle other priorities, and add to social unrest, political instability, conflicts, and migration –further increasing the vulnerability of those most in need³¹. Therefore, there is an urgent need for advancing the debate around loss and damage, and establishing an action plan to deliver concrete results.

5.3 “What should be done?”

Considering the present situation, the consequences, as well as the commitments made by the international community to advance climate action, the way climate finance allocations are divided between mitigation and adaptation strategies must change. Adaptation is a priority for the world’s poorest countries and urgently increasing their share of grant-based climate finance dedicated to adaptation is an matter of climate justice. Moreover, loss and damage deserves its own category as a separate topic for future climate finance allocations and for inclusion in the negotiations for the post 2025 climate finance agreement.

5.4 Recommendation

The post 2025 climate finance agreement should include clear, individual, and measurable financial target allocations for each of the three priority areas: mitigation, adaptation and loss and damage.

As a starting point for negotiations on the relative costs of tackling loss and damage compared to these other challenges, and with the impacts of climate change already being felt around the world, a new target should be set with specific science-based allocations for each category, mitigation, adaptation and loss and damage, with funds being channelled through different instruments.



**NOP
POLIN**
CAMBODIA

“The most vulnerable communities, in particular smallholder farmers, have faced multiple challenges due to extreme weather events such as floods and droughts. Farmers have lost their crops, livestock and other economic assets. Farming communities are responsible for our food security, yet generally operate in an unsupported environment. It is important to acknowledge and include their needs in the global climate finance negotiations.”

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6.1 Situation analysis

Climate change does not have the same impact on all countries or populations. Poorer countries and especially vulnerable communities will bear the overwhelming majority of human, environmental and economic costs of climate change³². The higher incidence of extreme weather events such as cyclones, hurricanes, storm surges, sea level rise and more severe droughts, heatwaves, and wildfires, for example, will have a disproportional impact on vulnerable populations, as well as marginalised groups, including women and youth, as they have less capacity to withstand climate shocks.

Article 7 of the Paris Agreement recognises the significant need for adaptation, and notes that adaptation measures should follow a country-driven, gender-responsive, participatory, and fully transparent approach, taking into consideration vulnerable groups, communities, and ecosystems. However, there is no mechanism or policy to ensure that climate finance reaches countries most in need or responds effectively to their priorities³³. According to the most recent OECD data³⁴, climate finance provided and mobilised for Least Developed Countries (LDCs) increased in 2019, reaching USD 15.4 million, an amount considered low given their level of vulnerability and capacity. **For Small Island Developing States (SIDS), which have increased vulnerabilities, the resources mobilised in 2019 decreased to USD 1.5 billion, in comparison to the USD 2.1 billion provided in 2018.**

While the resources mobilised for climate change action remain insufficient given the magnitude of the problem, the entry points to finance and means for channelling and delivering finance, especially over the last few years pose a further challenge. Climate finance providers have a fiduciary duty to manage donor / investor funds responsibly, but this due diligence imposes high transaction costs that create a bias for large projects, with teams that can navigate bureaucratic processes. Barriers such as unclear and complex application requirements, project eligibility limitations, timelines, speed of delivery of finance, reporting expectations, as well as institutional capacity constraints, become obstacles and prevent effective access to climate finance by the people who need it most³⁵.

In addition to the low share of climate finance disbursed to the most vulnerable countries and the difficulties to access the funds, only a small part of the allocated resources reach local communities. According to an IIED report, in 2016 less than 10 per cent of climate finance resources from international climate funds were directed to local level activities³⁶. Most adaptation decisions were made at higher and centralised decision-making level, thereby missing insights and experiences from the subnational and local levels, which can create inefficiencies and waste resources. Mitigation and adaptation initiatives that strengthen local communities' agency across all steps of the development and implementation process are more likely to prove effective because they draw on context-specific and democratic³⁷ inputs. However, depending on the mechanisms channelling climate finance, resources are rarely available to local initiatives. Local actors are instead forced to access, where available, small, and short-duration grants, hindering their ability to develop long term capabilities and track records. Initiatives such as the Global Commission on Adaptation have been working on advocating for increasing the volume of funding available to local actors.

6.2 "What should be done?"

As noted previously, the fight against climate change is a fight for justice³⁸, therefore, ensuring that climate finance reaches those who are most vulnerable and marginalised is crucial for achieving climate justice. Not only should developed countries take more ambitious action to increase the volume of funding mobilised for climate change, but they also should improve the ways in which climate finance is accessed and delivered.

To address the problem of access to finance, donor countries and key stakeholders, e.g., multilateral funds, should advocate to donor countries to review their procedures and policies by which beneficiaries can access climate finance. A more efficient process would reduce the time needed to disburse funding and accelerate the outcomes in the most vulnerable countries, especially SIDS and LDCs, who receive fewer funds and face more difficulties to attract investments in climate action. At the same time, developing country recipients of these funds should work towards enhancing national capacity on climate issues, as well as improving transparency in public management. Another important step will be the enabling and inclusion of local communities in the decision-making process and implementation of climate action. **Locally led adaptation should become a priority for climate finance in the post 2025 context.**

6.3 Recommendation

The post 2025 climate finance regime should have a special target for locally led adaptation to ensure that resources will reach and empower those who are the most vulnerable and need it most.

The emphasis of this target should be on ensuring that decisions about climate investments reflect the clearly stated priorities, resources, and constraints facing members of affected communities, even if regional and state institutions need to be involved in delivery. This might occur via active local engagement in the design of larger projects, dedicated small grants windows, support for organisations that work at the local level, the establishment of national or regional climate funds that sponsor local initiatives, and other mechanisms.

The process of accessing climate finance should be streamlined and take into consideration developing countries' immediate needs and capacities, reducing or eliminating existing barriers and avoiding the creation of future obstacles.

Governance and leadership of different finance mechanisms should ensure that decisions made on availability, accessibility, distribution and balancing of funds to adaptation and mitigation are well thought-out and represent the interests and needs of the most affected countries.

Part E: Conclusion

Given the urgency to mitigate GHG emissions and address observed and future climate change impacts, especially in the most vulnerable countries, the post 2025 climate finance regime must draw on the lessons learned from the current climate finance landscape and set more ambitious targets to support climate action. The analysis presented in this paper offers a summary of the challenges we as a global community face with the limitations of the USD 100 billion goal, and furthermore, what needs improve over the next few years to create a positive outcome for the post 2025 climate finance regime.

The desired future climate regime will need intense negotiation efforts starting at the COP26. Significant institutional and systemic changes will be needed from the international community to achieve a new collective climate finance goal and post 2025 financial architecture. The future finance landscape must focus on enhanced reporting and accounting methodologies, as well as strengthened integration of finance innovation, always keeping in mind a climate justice and human rights approach. New targets, definitions and methodological approaches should be evidence-based and account for the needs of developing countries and especially the most vulnerable communities.

The recommendations provided in this paper reflect our understanding of the current climate finance regime and our contributions to foster the debate at the international level. We expect this will support the development of a more ambitious and efficient climate finance architecture, that is able to enhance climate action and guarantee a better future for all.

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² Paris Agreement

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