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THE OECD REPORT ON CLIMATE FINANCE

The Hindu
Paper - III (Environment & Ecology)

A new report, published by the Organisation for Economic Cooperation and Development (OECD), showed that economically developed countries fell short of their promise to jointly mobilise $100 billion a year towards climate mitigation and adaptation needs of developing countries in 2021 — one year past the 2020 deadline. The report said that developed countries mobilised $89.6 billion in 2021 and that finances for adaptation fell by 14% in 2021 compared to 2020.

Why is the OECD report important?

The OECD is largely a group of rich countries including the U.S., the U.K., Germany, France, Switzerland, Canada, and others. The report, as such, offers a peek into their idea of climate finance ahead of the COP28 climate talks in the United Arab Emirates (UAE) next week, where the topic is expected to be a key bone of contention.

The report also comes against the backdrop of a pledge by the bloc of developed nations at the COP26 talks in Glasgow, in 2020, to double adaptation finance. Parties to the United Nations Framework Convention on Climate Change (UNFCCC) had also said at Glasgow, "with deep regret", that the developed nations bloc hadn't met the $100 billion climate finance goal in due time in 2020. The failure to mobilise adequate climate finance lowers capacity in developing countries to address climate mitigation (like emissions reduction with renewable energy) and adaptation needs (like developing and incentivising climate-resilient agriculture), and reduces trust among the world's poorer countries that the developed world is serious about tackling the climate crisis.

How is climate finance accounted for?

The OECD report showed that of the $73.1 billion mobilised in 2021 by the public sector via bilateral and multilateral channels, $49.6 billion was provided as loans. While the report doesn't classify them in terms of the rates at which they're provided, data available elsewhere sheds light on the extent to which rich countries rely on loans at commercial rates to fulfil their climate finance obligations. For example, an assessment by the American non-profit research group Climate Policy Initiative of global climate finance flows between 2011 and 2020 found that 61% of climate finance was provided as loans, of which only 12% was at concessional interest rates.

So, when the OECD report states that two-thirds of public climate financing was provided as loans, it means the conditions attached to such financing could further exacerbate debt stress in poorer countries. This is also a critique of the OECD report as it considers loans at face value, not the grant equivalent, when arriving at total climate finance figures. This means that while poorer countries shell out money towards repayment and interest, the loan is still counted as climate finance provided by the developed world.

What is additionality?

Another issue in the OECD report pertains to additionality. The UNFCCC states that developed countries "shall provide new and additional financial resources to meet the agreed full costs incurred by developing country Parties in complying with their obligations under the convention". This means that developed countries cannot cut overseas development assistance (ODA) in order to finance climate needs because that would effectively rob Peter to pay Paul. In real-world terms, it would mean cutting off support for healthcare to reallocate that money to, say, install solar panels.

The "new and additional finance" also means that developed countries cannot double-count. For example, a renewable energy project could contribute to both emission reductions and overall development in a region. However, as per the UN Convention, donor countries cannot categorise such funding as both ODA and climate finance because it wouldn't fulfil the "new and additional" criterion. Yet they do. A few years ago, European Union officials admitted to double-counting development aid as climate finance.

What counts as climate finance?

At present, there is no commonly agreed definition of 'climate finance' because developed countries have endeavoured to keep it vague. For example, at the COP27 in Egypt last year, Australia and the U.K. even sought to end discussions to define 'climate finance'. In the run up to the COP26 in Glasgow, the U.S. led an effort to block debate on a common definition, alongside Switzerland, Sweden, and some other developed countries.

The lack of definitional clarity has reportedly led to ridiculous situations like the funding of chocolate and gelato stores across Asia and a coastal hotel expansion in Haiti being tagged as climate finance. The ambiguity works in favour of richer countries because it leaves the door open to arbitrarily classify any funding, including ODA and high-cost loans, as climate finance and escape the scrutiny that a clearer definition might bring. Therefore, while developed countries can claim they have provided billions in climate finance, the actual flows need to be checked to know whether they went into climate mitigation and adaptation in developing countries or something else.

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How much financial assistance do developing countries need?

The latest OECD report claims, based on preliminary and as-yet-unverified data, that the $100 billion goal was likely met in 2022. But the data is neither finalised nor published, and the advisable take-away is scepticism. It is also important to note that the figure of $100 billion came out of thin air at the COP15 talks and isn't based on an assessment of how much climate investment developing countries actually need. The OECD report added that by 2025, developing countries are estimated to require around $1 trillion a year in climate investments, rising to roughly $2.4 trillion each year between 2026 and 2030. The $100 billion goal pales in comparison, dwarfed further by the fact that it remains unmet.

What role can the private sector play?

To meet the scale of the challenge, people like the U.S. climate envoy John Kerry and World Bank President Ajay Banga have routinely emphasised the role the private sector could play.

But the OECD report itself threw cold water on such hopes, showing that private financing for climate action has stagnated for a decade, while public funding from multilateral channels, both multilateral development banks (MDBs) and multilateral climate funds, increased in the same period. In 2021 in particular, it showed that private funding reverted to its 2019 level following a slight dip in 2020.

As a course-correction measure, the OECD report suggested de-risking with government intervention and called on MDBs to integrate private finance mobilisation strategies as part of their core objective. Its reasoning is that the private sector can help enable climate action but that it "requires the proactive involvement of governments and international institutions to support, incentivise and de-risk individual projects, as well as to create the necessary conditions for investment in developing countries more generally".

But as of today, there aren't any signs that the private sector is interested in massively scaling up its climate investments. The problem is particularly worse for climate adaptation, because investment in this sector can't generate the sort of high returns that private investors seek and which the mitigation sector — like a solar or wind farm — could generate.

At the end of the day, the ball rolls back into the court of public funding, that is governments in the developed world plus multilateral development banks. The OECD report shows that even those who place hope in higher private funding for climate action in the future recognise that it is governments and MDBs that are the enabling parties here.

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Expected Question

Que. Consider the following statements in the context of climate finance

1. Last year at COP 27 in Egypt, Australia and the UK defined 'climate finance'.
2. Currently, there is no agreed definition of 'climate finance'.

Which of the statements given above is/are correct?

(a) Only 1

(b) Only 2

(c) Both 1 & 2

(d) Neither 1 nor 2

Answer : b

Mains Expected Question & Format

Que.: What is climate finance and why is climate financing needed? What role can the private sector play?

Answer Format :

- Discuss climate finance and the need for climate financing in the first part of the answer.
- In the second part, discuss what role the private sector can play in this.
- Finally give a conclusion giving suggestions.

Note: - The question of the main examination given for practice is designed keeping in mind the upcoming UPSC mains examination. Therefore, to get an answer to this question, you can take the help of this source as well as other sources related to this topic.