Climate finance landscape overview
Presentation October 14
Topics of this presentation

• What is climate finance?

• What are the elements of the climate finance landscape?

• What are the current climate finance flows? What is the relative order of magnitude of current flows?

• What is the potential development of flows in the short term (2010-12) and the long term (2020)?

• What are the issues in tracking climate finance? What to track and who is tracking what?

• What are the key questions to be addressed?
What is climate finance?

<table>
<thead>
<tr>
<th>Definition</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Climate finance is all financial flows ...</td>
<td>• Excluding all domestic flows</td>
</tr>
<tr>
<td>... from developed to developing countries...</td>
<td>• Excluding flows between developed countries only</td>
</tr>
<tr>
<td>... covering climate-specific support for mitigation, adaptation, capability building, and technological R&amp;D, potentially furthering economic development...</td>
<td>• We aim for a broad definition which can be shaped based on the specific context</td>
</tr>
<tr>
<td>... including public and private flows...</td>
<td>• Public flows covering e.g. MDB grants and most adaptation efforts</td>
</tr>
<tr>
<td>... including incremental cost and investment capital...</td>
<td>• Private flows covering e.g. private MDB co-financing, investments in renewable energy production, or carbon offset markets</td>
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<tr>
<td>... counted as gross flows</td>
<td>• Distinction between the two concepts should be made clear wherever possible</td>
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<tr>
<td></td>
<td>• Net flows are an important ‘lens’ on climate finance and can be calculated where appropriate</td>
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</tbody>
</table>
### What are elements of the climate finance system?

<table>
<thead>
<tr>
<th>Sources</th>
<th>Intermediaries</th>
<th>Instruments</th>
<th>Uses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Carbon market revenues (ETS auctions)</td>
<td>Domestic</td>
<td>Incremental</td>
<td></td>
</tr>
<tr>
<td>Innovative finance mechanisms</td>
<td></td>
<td>Capital</td>
<td></td>
</tr>
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<td>General tax revenues (incl. ODA)</td>
<td></td>
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<td></td>
</tr>
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<td>International transport fuels</td>
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**Source:** McKinsey analysis
What are elements of the climate finance system?

**Sources**
- Carbon market revenues (ETS auctions)
- Innovative finance mechanisms
- General tax revenues (incl. ODA)
- International transport fuels

**Intermediaries**
- Domestic Public budget

**Instruments**
- Bilateral development agencies
- International agencies/funds

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**Instruments**
- Grant instruments
- Market based
  - Income enhancing (e.g. FIT, AMC)
  - Risk reduction mechanisms
  - Finance enhancing mechanisms
  - Payment for ecosystem services

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**Uses**
- Adaptation
- Mitigation

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**Uses**
- Adaptation
- Mitigation

**Carbon offset finance**

**SOURCE:** McKinsey analysis
What are elements of the climate finance system?

**Sources**
- Carbon market revenues (ETS auctions)
- Innovative finance mechanisms
- General tax revenues (incl. ODA)
- International transport fuels
- Carbon offset markets

**MDB finance**

**Intermediaries**
- Domestic Public budget
- Bilateral development agencies
- International agencies/funds

**Instruments**
- Grant instruments
- Market based
  - Income enhancing (e.g. FIT, AMC)
  - Risk reduction mechanisms
  - Finance enhancing mechanisms
  - Payment for ecosystem services
- Carbon offset finance
- MDBs (leverage effect)

**Uses**
- Adaptation
- Mitigation

**Capital**
- Debt
- Equity

SOURCE: McKinsey analysis
What are elements of the climate finance system?

**Sources**
- Carbon market revenues (ETS auctions)
- Innovative finance mechanisms
- General tax revenues (incl. ODA)
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- Domestic Public budget
- Bilateral development agencies
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**Instruments**
- Grant instruments
- Market based
  - Income enhancing (e.g. FIT, AMC)
  - Risk reduction mechanisms
  - Finance enhancing mechanisms
  - Payment for ecosystem services
- Carbon offset finance

**Channel**
- Different disbursement channels
- Adaptation
- Mitigation

**Uses**
- Incremental cost
- Capital investment
- Capital
  - Debt
  - Equity

**Private finance**

**Private finance (incl. FDI)**

**SOURCE:** McKinsey analysis
**What are current flows?**

### Sources
- Carbon market revenues (ETS auctions) (~0.2)
- Innovative finance mechanisms (<0.5)
- General tax revenues (incl. ODA) (~10-14)
- International transport fuels (0)
- Carbon offset markets (1-3)
- Private finance (incl. FDI) (56)

### Intermediaries
- Domestic Public budget (~0.2)
- Bilateral development agencies (~7-9)
- International agencies/funds (4-5)
- MDBs (leverage effect) (4)

### Instruments
- Grant instruments (11-14)
- Market based (0.4)
- Income enhancing (e.g. FIT, AMC)
- Risk reduction mechanisms
- Finance enhancing mechanisms
- Payment for ecosystem services
- Carbon offset finance (1-3)
- Capital (Debt, Equity) (52)

### Channel
- Rough estimates

### Uses
- Adaptation
- Mitigation

**Source:** McKinsey analysis
What are current flows?

Sources
- Carbon market revenues
- Innovative finance mech.
- General tax revenues
- Intern'l transport fuels
- Carbon offset markets
- Private capital

Intermediaries
- Domestic public budget

Instruments
- Bilateral, multilateral funds
- Grant instruments
- MDBs
- Carbon offset finance

Channels
- Adaptation
- Market-based

Uses
- Mitigation
- Capital (debt, equity)

ROUGH ESTIMATES

SOURCE: McKinsey analysis
What are future flows?

Finance flows required; developing countries; USD bn p.a.

<table>
<thead>
<tr>
<th>Current</th>
<th>Copenhagen Accord pledges (2020)</th>
<th>Technical potential</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Low case of country proposals</td>
<td>High case of country proposals</td>
</tr>
<tr>
<td></td>
<td>Incremental cost (mitigation &amp; adaptation)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>15</td>
<td>10</td>
</tr>
<tr>
<td>2011-15</td>
<td>80</td>
<td>280</td>
</tr>
<tr>
<td>2016-20</td>
<td>120</td>
<td>170</td>
</tr>
<tr>
<td>2021-25</td>
<td>150</td>
<td>130</td>
</tr>
<tr>
<td>2026-30</td>
<td>240</td>
<td>90</td>
</tr>
</tbody>
</table>

Note: 1. For Low and High cases, the investment capital in year 2016-2020 corresponds to abatement from actual country pledges. Data for other years are extrapolated using a linear percent reduction in full technical potential scenario.
2. Transport Air and Transport Sea are excluded.

Source: McKinsey Global Abatement Cost Curve v2.1
What are the issues in tracking climate finance?

- Rapidly developing landscape of tracking functions – covering current and prospective emissions and finance
  - Rapidly developing emissions tracking
    - Fast developing methodologies for tracking current emissions
    - Some promising initiatives to develop perspectives on expected future emissions based on pledge tracking
  - Rapidly developing finance tracking
    - Well developed systems for tracking current government spending (ODA), but relatively immature tracking of government spending on climate related causes
    - Good tracking of current carbon market flows
    - Fragmented tracking of current (private) investment capital flows
    - Multiple efforts to ‘predict’ future capital flows, but not one that is comprehensive in its scope
- No consistent methodology to calculate finance flows
  - Differences in what types of finance count for specific categories of finance
- No current tracking of effectiveness of climate finance spent
## What to track and who is tracking what?

<table>
<thead>
<tr>
<th>What to track</th>
<th>Countries</th>
<th>International institutions</th>
<th>MDBs</th>
<th>NGOs</th>
<th>Academics</th>
<th>Private</th>
</tr>
</thead>
<tbody>
<tr>
<td>Track commitments (GT, degree)</td>
<td>Country governments</td>
<td>UNDP, UNEP</td>
<td>WB, ADB, AfDB, EBRD, IDB, IFC</td>
<td>WRI, Project Catalyst</td>
<td>✓</td>
<td>Ecofys</td>
</tr>
<tr>
<td>Track finance sources - public ($)</td>
<td>OECD, UNFCCC, UNDP, UNEP-Risoe, UNEP-SEFI</td>
<td>WB, ADB, AfDB, EBRD, IDB, IFC</td>
<td>WRI, ODI/ HBF, Climate Analytics, AidData, Ecosystem Marketplace Project Catalyst</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Track finance sources - private ($)</td>
<td>UNEP-SEFI, UNEP-Risoe, UNFCCC, OECD</td>
<td>REN21</td>
<td>WRI, ODI/ HBF, Climate Analytics, AidData, Ecosystem Marketplace Project Catalyst</td>
<td>✓</td>
<td>Commercial data providers (e.g. Dealogic, DB, Bloomberg NEF, PointCarbon)</td>
<td></td>
</tr>
<tr>
<td>Track finance effectiveness (GT, $)</td>
<td>Sustainability reports of MDBs</td>
<td></td>
<td></td>
<td></td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>MRV methodology</td>
<td>OECD, IEA</td>
<td>WB</td>
<td>WRI, IIED, AidData…</td>
<td></td>
<td>✓</td>
<td></td>
</tr>
</tbody>
</table>
## Key questions to be addressed

| Panel 2 - How to define and calculate finance flows? | • What is a reasonably broad and mutually agreeable definition of climate finance flows?  
• How can these climate finance flows be calculated?  
• What flows count for which categories of finance? |
| --- | --- |
| Panel 3 - How to evaluate the effectiveness of finance flows? | • How can effective and efficient spending of climate finance money be prepared ex ante?  
• How can the effectiveness and the efficiency of spending be measured and evaluated ex post? |
| Panel 4 - How to reduce the risk of investing into climate finance? | • What are the most relevant risks around investments in climate finance?  
• How can the risks of investing in climate finance be mitigated (e.g. risk-sharing mechanisms)? |
| Concluding panel - What is needed to make climate finance successful? | • How do we define and measure success of climate finance?  
• What does it take to achieve successful climate finance? |
APPENDIX
What are future flows?

USD bn, Annual average for 2010-12

Fast Start Finance

- **Bilateral funding**: 7
- **Climate Funds**: 4
- **Total public finance**: 11
- **Carbon offset finance**: 3-5
- **Total incremental cost finance**: 14-16
- **Capital investment**: 50

1. Includes climate finance pledges of Australia, Canada, EU (EU commission and member states), Japan, Norway, and US; numbers may not sum to total due to rounding. Exchange rate from April 26, 2010 used ($1.33 to €1)
2. Multilateral funds include the World Bank climate funds, GEF, and other funds providing concessional climate-related financing; excludes general funding for the World Bank and other development bodies; share for some donor countries based on historical allocation of multi- and bilateral funding
3. Expected CDMs issued from 2010-2012 at an assumed price of EUR 10-15 per tonne CO2
4. Based on 2009 extrapolation

SOURCE: Climatefundsupdate.org; press search; interviews; McKinsey analysis