Climate finance takes center stage at COP27

Climate finance explained through latest developments from 27th UN Climate Change conference

By Kim Yeon-ji

The 27th U.N. Climate Change Conference (COP27) was held in Sharm el-Sheikh, Egypt, from Nov. 6 to 20. World leaders kickstarted the conference on an urgent and somber note. The year 2022 has shown that climate change can indeed pose an existential threat to humanity, as the year has been marked with several devastating and unprecedented floods, heat waves, droughts and storms. Making matters worse were the geopolitical tensions leading to crises in energy, food, water and inflation.

At the World Leaders Summit, held over two days during the first week of the conference, U.N. Secretary-General Antonio Guterres said the world is on "a highway to climate hell" and reiterated that there is no time to lose in addressing the climate emergency. Barbados Prime Minister Mia Mottley surprised the unexpected audience by saying that it is time to revisit and reform the Bretton Woods institutions. Both the World Bank and the International Monetary Fund (IMF), created back in 1942 to help the rebuilding efforts following World War II, are outdated and require an overhaul to effectively address the challenges posed by climate change, argued Mottley. Other leaders shared similar sentiments and showed their support for such an initiative.

Just before COP27, it was unveiled that efforts remain insufficient to limit the global temperature rise by the end of the century to 1.5 degrees Celsius. Against this backdrop, Egypt's COP27 presidency chose "moving from negotiations and planning to implementation" as its vision for the 2022 conference (#togetherforimplementation). To be more precise, it is the implementation of the 2015 Paris Agreement on climate change.

Article 2, paragraph 1 of the 2015 Paris Agreement calls for a stronger global response to the threat of climate change, including by (a)

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Courtesy of Kim Yeon-ji

keeping the temperature increase to 1.5 degrees Celsius above pre-industrial levels, (b) increasing the ability to adapt to the adverse impacts of climate change and fostering climate resilience and (c) making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

It is Article 2.1(c) of the Paris Agreement that has huge implications for the global finance. All Parties to the Paris Agreement (193 states including the Republic of Korea, plus the European Union) have the obligation to actively align all public and private money with the goals of cutting emissions and strengthening climate resilience. In essence, it requires a complete overhaul and transformation of the global financial system — a kind that would effectively and systematically channel funds into climate action.

The term "climate finance" is generally used to refer to financing from all sources — public, private, bilateral and multilateral, including alternative sources — that is meant to support climate change mitigation (to curb emissions and transition to clean energy) and adaptation (to adapt to the adverse effects of the changed climate). Climate finance is a crucial means of implementation for the global, regional and national climate agenda, and it was hotly debated and discussed in the previous U.N. climate change conferences, including COP27.

What was notable in the recent COP27 negotiations was that the Parties came away with a breakthrough agreement to provide "loss and damage" funding for vulnerable countries hit hard by climate-fueled weather extremes and disasters. It marked the very first time that loss and damage was officially included in the U.N. climate negotiations agenda. "Loss and damage" goes beyond financing for mitigation and adaptation and thus, it is a new aspect of climate finance. A negotiator was quoted as saying, in a recent CNN news report, that it is because we did not mitigate sufficiently early enough, we are having to adapt so much. And it is because we didn't get to adapt to the changed climate early enough, we are now talking about the need for loss and damage funding.

Although governments took the ground-breaking decision to establish a new fund dedicated to assisting developing countries in responding to loss and damage, there are still many questions left unanswered. For one, the scope of loss and damage in climate disasters is not as clear, as well as who should pay and who exactly will qualify for compensation. Vulnerable countries have argued that the polluters, or wealthy countries responsible for historic emissions and a bulk of climate change, must pay up.

While the U.S. and European Union had resisted such campaigns, fearing spiraling liabilities, they changed their position during COP27. The EU has argued that China should pay into the loss and damage funding as the world's second-largest economy, although the country is classified by the U.N. as a developing country. However, China has not committed to any payment so far.

As the future of loss and damage funding is not entirely clear, I will use "climate finance" to refer to the money that is dedicated to financing climate change mitigation and adaptation in the remainder of this column. As we established above, climate finance by definition includes money from public coffers that flows from developed countries to developing countries or that is raised and committed by developing countries themselves, plus any finance that is mobilized by the private sector or other types of contributors like foundations or philanthropies.

This photo shows the closing plenary at the 27th session of the Conference of the Parties (COP27) to the United Nations Framework Convention on Climate Change (UNFCCC) in Sharm El-Sheikh, Egypt on Nov. 20.

Yonhap-Xinhua

While climate finance includes both public and private investment, it is true that public climate finance has served more like a first responder in dealing with the emergency and has been used in de-risking climate-related investments, often in the form of development aid. As for private climate finance flows, it is methodologically harder to compile and assess such data, as it is not often specified how the private funds are sourced, and whether the funds are received by public or private sector entities from developed or developing countries.

A popular reference figure in climate finance has been $100 billion. At COP15 held in Copenhagen in 2009, developed country Parties committed to a goal of jointly mobilizing $100 billion per year by 2020 to help developing countries pay for climate action. This goal was formalized at COP16 in Cancun and was reiterated at COP21 in Paris. However, the $100 billion commitments by the end of 2020 were not met, and this goal has been extended to 2025.

Although the $100 billion goal has not been met, there has been an upward trend in global climate finance flows. A recent biennial report by the Standing Committee on Finance (SCF) under U.N. Climate Change shows that global climate finance flows in 2019-20 reached an annual average of $803 billion, up 12 percent from the 2017-18 figures. This trend, the report says, was driven largely by increased investment in the energy efficiency of buildings ($34 billion increase), sustainable transport including electric vehicles ($28 billion increase) and adaptation finance ($20 billion increase).

The same SCF report indicates that more public finance flows from developed to developing countries were for mitigation than for adaptation, although adaptation finance has grown significantly through bilateral channels and multilateral development banks (MDBs). Another interesting finding from the report is that public adaptation financing was predominantly delivered through grants, while public mitigation financing predominantly took the form of grants in 2019-20.

The increased funding channeled for mitigation actions was more pronounced in the realm of private climate finance. The SCF's biennial report says between 2016 and 2020, private climate financing mobilized by developed countries for developing countries through bilateral and multilateral channels totaled $66.8 billion. Of this amount, 86 percent was mobilized for mitigation actions, particularly in the energy sector, while the rest was mobilized for adaptation actions targeting industry, mining and construction.

Private climate finance was mobilized through various mechanisms, although there was a dominance of direct investment in companies and special purpose vehicles. MDBs mobilized 57 percent of total estimated private climate finance, followed by bilateral providers and multilateral climate funds like the Green Climate Fund.

Despite the general upward trend in global climate finance flows, several estimates say we need substantially more climate finance in order to meet the Paris Agreement warming limits. The Intergovernmental Panel on Climate Change (IPCC) concludes that the level of climate-related investment in developing countries must increase by between four and eight times before 2030. That would bring annual climate investment in developing countries to around $2 trillion to $3 trillion annually, according to an analysis done by Carbon Brief.

The SCF under U.N. Climate Change issued another report on the climate finance needs of developing countries to implement their national plans, known as Nationally Determined Contributions (NDCs). This report says such needs are currently estimated at $5.8 trillion to $5.9 trillion for the pre-2030 period. The COP27 cover decision text — titled Sharm el-Sheikh Implementation Plan — also highlights that "about $4 trillion per year needs to be invested in renewable energy up until 2030 to be able to reach net zero emissions by 2050." Further, it is also noted in the cover decision that a global transformation to a low-carbon economy is expected to require investment of at least $4 to 6 trillion per year.

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