IEU LabReport No. 1

# INDEPENDENT EVALUATION OF THE GREEN CLIMATE FUND APPROACH TO PRIVATE SECTOR[1]

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## BACKGROUND

The Green Climate Fund (GCF) serves the Paris Agreement. In doing so, it also contributes to the three objectives of the Paris Agreement, including "making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development" (hereafter, Article 2.1c). The Updated Strategic Plan (USP) for the GCF 2020-2023 identifies a two-pronged long-term strategic vision:

a) "Promote the paradigm shift towards low-emission and climate-resilient development pathways in the context of sustainable development; and

b) Support developing countries in the implementation of the Paris Agreement and the United Nations Framework Convention on Climate Change (UNFCCC, or Convention) within the evolving climate finance landscape."[2]

The latter of these objectives includes a **key goal identical to Article 2.1c:** "making finance flows consistent with a pathway towards low emissions and climate resilient development". The USP makes several further references to this goal, especially in paragraph 7, strategic priorities, and strategic objectives. This goal also provides the background for the private sector related strategic objective (para 21).

## OPERATIONALIZATION OF ARTICLE 2.1C

Experts have recognized that Article 2.1c of the Paris Agreement **is brief in text but of enormous consequence**.[3] The Agreement itself does not provide guidance on operationalizing Article 2.1c, but several groups have independently considered this. For instance:

a) According to a World Resources Institute framework, there are three dimensions to align with Article 2.1c: (1) drive action to mobilise and shift finance; (2) track progress against Article 2.1c; and (3) increase ambition. The tools identified by the authors include financial policies and regulations, fiscal policy levers, public finance, and information instruments.[4]

b) According to Organisation for Economic Co-operation and Development, there are four characteristics of support that aligns with Paris Agreement.[5] To be aligned with Paris Agreement, development cooperation has the following four characteristics:

   i) does not undermine the Paris Agreement but rather contributes to the required transformation

   ii) catalyses countries' transitions to low-emissions, climate-resilient pathways

   iii) supports the short- and long-term processes under the Paris Agreement

   iv) proactively responds to evidence and opportunities to address needs in developing countries

c) Yet another group of authors identifies the following actions for national, regional and international development finance institutions: providing innovative instruments to develop green markets, using risk screening and shadow prices to make investment decisions.[6]

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[1] This series is designed to socialize early 'pre-findings' from the independent evaluation of the Green Climate Fund's approach to the private sector. The contents of this series are a preliminary reflection and will inform the final report, but do not constitute findings and recommendations.

[2] Decision B.27/06. It should be noted here that this strategic vision is consistent with the vision laid out in the initial Strategic Plan of the GCF.

[3] Independent Expert Group on Climate Finance (2020) Delivering on the $100 Billion Climate Finance Commitment And Transforming Climate Finance. Available: https://www.un.org/sites/un2.un.org/files/100_billion_climate_finance_report.pdf

[4] Whitley, S., Thwaites, J., Wright, H. and Ott, C. (2018) Making finance consistent with climate goals Insights for operationalising Article 2.1c of the UNFCCC Paris Agreement. Available: https://www.wri.org/publication/making-finance-consistent-climate-goals

[5] OECD (2019), Aligning Development Co-operation and Climate Action: The Only Way Forward, The Development Dimension, OECD Publishing, Paris, https://doi.org/10.1787/5099ad91-en

[6] Climate Transparency. (2017). Financing the transition from brown to green: How to track country performance towards low carbon, climate-resilient economies. (ODI and HVGP). Berlin, Germany. Available: https://www.climate-

Overall it is clear that the **implementation of Article 2.1c requires an overall transition in current financial systems.** In the words of an independent expert group on climate finance, this implies that: "Deep decarbonization of the economies and strengthening resilience to the impacts of climate change will require alignment with climate objectives of all "financial" or capital flows, both public and private - including those that follow purely a commercial logic, those that flow across borders, as well as those that stay within national economies."[7]

The COP26 Private Finance Hub has developed a framework that at the outset identifies the objective: **"ensure that every professional financial decision takes climate change into account**". To this end, the Hub has developed a four-point framework that includes:

- Reporting: improving the quantity, quality and comparability of climate related disclosures by implementing a common framework built on the Taskforce for Climate-related Financial Disclosures recommendations.
- Risk management: ensuring that the financial sector can measure and manage climate-related financial risks.
- Returns: helping investors identify the opportunities in the transition to net zero and report how their own portfolios are aligned for the transition.
- Mobilisation: increasing private financial flows to emerging and developing economies, by connecting available capital with investable projects and encouraging new market structures.[8]

## GCF AND ARTICLE 2.1C

What exactly is the pathway available for an organization like the GCF? A submission from Climate Policy Initiative [9] to the United Nations Framework Convention on Climate Change provides suggestions for development partners to support countries, including:

- Policy advice: Supporting governments to build capacity on and develop forward-looking policy analysis and reform to devise low greenhouse gas, climate resilient development pathways.
- Coordination: Facilitating multi-stakeholder dialogue to include ministries beyond environment including among others finance, development, planning, and sectoral ministries such as agriculture and energy, as well as the private sector and civil society.
- Risk mitigation: Building in-country capacity to identify and mitigate climate risks, including physical, liability, and transition risks.
- Pro-active decision-maker relationships: Working pro-actively with government stakeholders who have oversight over member institutions (Board, Assembly, etc.) to understand and prioritize alignment alongside development priorities.

**There are several characteristics within the GCF that can allow for the delivery of the mandate.** Firstly, country ownership is a recognized principle in the Governing Instrument and indeed in the context of the private sector. In practice, many countries have developed coordination committees, which can facilitate broad dialogue. Second, the GCF places emphasis on direct access. In theory, direct access entities are placed within country systems and would allow for transition using domestic financial systems. Many direct access entities are national banks, which have an important role in this transition. Thirdly, the GCF business model in theory allows for policy and technical assistance, which can be used to develop policy analysis and create enabling environments.

However, as Paris Agreement is driven by country ownership, currently **the GCF is not in a position to deliver on Article 2.1c** because:

1. The GCF is not integrated into countries to provide policy advice. The GCF business model remains supply driven and is contingent

transparency.org/wp-content/uploads/2017/12/Financing_the_transition.pdf

[7] For a detailed review of the literature, please refer: Rydge J (2020) Aligning finance with the Paris Agreement: An overview of concepts, approaches, progress and necessary action. London: Grantham Research Institute on Climate Change and the Environment and Centre for Climate Change Economics and Policy, London School of Economics and Political Science. Available: https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2020/12/Aligning-finance-with-the-Paris-Agreement-3.pdf

[8] Carney M. (2020). Building a private finance system for net zero: Priorities for private finance for COP26. Available: https://ukcop26.org/wp-content/uploads/2020/11/COP26-Private-Finance-Hub-Strategy_Nov-2020v4.1.pdf

[9] Climate Policy Inititave (2019). Implementing alignment recommendations for the International Development Finance Club. Available: https://unfccc.int/sites/default/files/resource/Aligning%20with%20the%20Paris%20Agreement%20-%20Part%202%20-%20CPI-I4CE.pdf

upon the project brought forward by accredited entities.

2. Country ownership is a weakly utilized criterion (refer: Independent Evaluation of GCF's Country Ownership Approach).
3. Investment decisions are not based on country ownership, (refer: Independent Evaluation of GCF's Country Ownership Approach).
4. And finally, the GCF does not incentivize alignment with Paris Agreement, nor does it measure its performance on this criterion nor measure the impact or results. (refer: Independent Evaluation of the GCF's Results Management Framework).
5. The USP identifies this as an overall goal, but there is no further clarification on this within the USP or the Secretariat workplans.