

Financing Urban Climate Action: Is the Issue *Really* Creditworthiness?



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Outline



- UCCRN and its work
- Urban climate finance issues
- Post-Paris financing efforts and initiatives
- Carbon ‘pricing’ and carbon risk disclosure – panaceas for financing problems?
- Potential impacts on climate adaptation, implementing the Paris Agreement, and attaining the SDGs

UCCRN and its work



Mission: Provide knowledge that enables cities and metropolitan regions to fulfill their climate change leadership potential in both mitigation and adaptation, with a focus on developing resiliency

- Over **700** scientists, scholars, and expert practitioners spanning a broad range of expertise
- More than **100** developed and developing cities around the world
- Formed in **2007** at the time of the C40 Summit in New York
- Launched the ARC3 Report Series in 2011

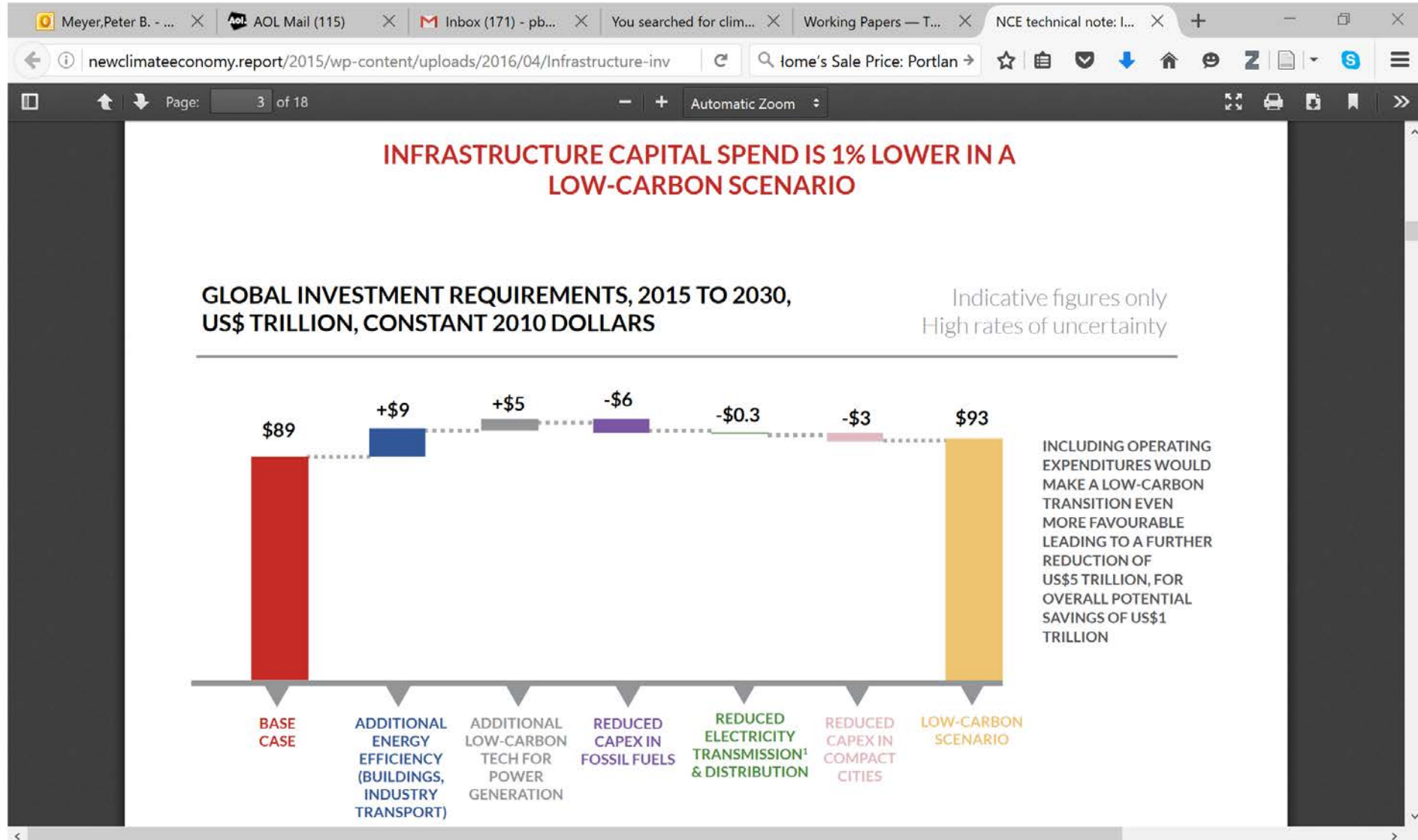
ARC3 Reports

- ***First UCCRN Assessment Report on Climate Change and Cities (ARC3)*** -- multi-year effort by **100 authors** from **50+ cities** around the world
 - Addressed the impact of climate change on cities with an emphasis on the urban poor
- ***Second UCCRN Assessment Report on Climate Change and Cities (ARC3.2)***
 - multi-year effort by **over 120 authors** with **115 city case studies** from across the globe
 - Provides guidance on city-level strategies to adapt to and mitigate climate change
 - **ARC3.2 Summary for City Leaders** was released at COP21 in Paris
 - Full report release is scheduled for Habitat III in Quito
- ***Docking Station*** with detailed case studies jointly prepared by practitioners and scholars available online as a reference for City Leaders preparing to act

Urban climate finance issues

- **The Need**: average annual infrastructure investment need of some US\$ 5.7 (WEF 2013) to \$6.5 (CCFLA 2016) Trillion
 - \$13.5 Trillion for energy just in LAC region over 2015-30 (IFC, 2016)
- **The Issue**: not enough financing – only US\$359 Billion invested internationally in 2012, falling to \$331 in 2015 (CPI)
- **The Perceived Problem**: **Only 4% of the 500 largest cities in developing countries were creditworthy in international financial markets and 20% are creditworthy in local markets**
- **The Reality**: infrastructure financing may be available but too expensive – or the needs may exceed even creditworthy cities' capacity to service the debt

Global Commission on the Economy and Climate



Some 'Solution' Attempts:



- In September 2013, the World Bank Group launched the **Low Carbon, Livable Cities (LC2)** initiative at the Clinton Global Forum in New York
- **World Bank's City Creditworthiness Initiative** – created by LC2, based on the calculation that US\$1 invested in creditworthiness can leverage over US\$ 100 in private sector financing
- **UN and partners' Compact of Mayors** – developing tracking and accountability protocols to encourage capital flows to cities
 - Now building on the Global Protocol for Community Scale Greenhouse Gas Emission Inventories (GPC)
- **Inter-American Development Bank's Emerging and Sustainable Cities Program** – reflects the multinational bank's commitment to working directly with cities, and is a technical assistance investment in their capacities to develop climate adaptation programs

CCFLA's problem diagnosis:

'Six major barriers that must be overcome

- '1. Uncertainty over regulatory and tax policies that affect low-emission, climate-resilient infrastructure;
- '2. Difficulty in incorporating climate goals into urban infrastructure planning;
- '3. Lack of city expertise in developing low-emission, climate-resilient infrastructure projects that can attract financing;
- '4. Insufficient city control over infrastructure planning and complex stakeholder coordination;
- '5. High transaction costs; and
- '6. Lack of proven funding models at the city level.'



The Global Economic Forum Perspective

The Global Risk Report 2016 summarized emerging risks:

‘The risk rated most likely was **large-scale involuntary migration**, with last year’s top scorer – **interstate conflict with regional consequences** – giving way to the **environmental risks of extreme weather events and the failure of climate change mitigation and adaptation** and followed by **major natural catastrophes.**’

It criticizes the financial sector: ‘Despite increasing recognition of the economic risks [of climate change], global financial systems are yet to incorporate them into financial decision-making.’

Beyond Capacity Building

- UNFCCC launched the Green Climate Fund (GCF) in 2010, with US\$10 Billion of initial pledges from donor countries and a target of \$100 B annually for developing countries by 2010, per the IMF proposal
- The UN's Sustainable Development Goals now explicitly focus on cities: **“Make cities and human settlements inclusive, safe, resilient and sustainable”**
- NAZCA reports **2364 cities** have taken some action on climate change
- ODI and CCFLA both call for adaptation by the **finance sector**, not just recipient cities, to better reach the most vulnerable cities and their residents
- **Many countries – and cities – manipulate fuel markets and could shift subsidies to renewables and more sustainable energy infrastructure**

.... *Let's not underestimate this last option*

'The IEA estimated that **fossil fuel subsidies in 2013 amounted to \$548 billion**. ... [over a third of] ... total primary energy spend of \$1.6 trillion per year... Add to this the estimated \$121 billion of global renewable subsidies in 2013 (IEA), and the extent to which the world is already manipulating energy markets becomes clear; **the challenge therefore is simply to adjust them in a different direction.**'

-- Citibank, *Energy Darwinism II* (p. 112)

But \$680 Billion is still only a small fraction of the \$6 Trillion in annual infrastructure investment needed for cities to adapt to and mitigate climate change threats.

Post-Paris financing efforts and initiatives

- New UNFCCC-governed mechanism as part of the Paris Agreement which enables international transfers of emission reductions while delivering overall mitigation in global emissions.
- China is to launch a national emissions trading scheme in 2017 across the most polluting sectors of the economy.
- Aviva, Aegon and Amlin, with assets of \$1.2 Trillion, just called on the G20 to end fossil fuel subsidies and investments by 2020
- CIFs are vigorously targeting pension funds' over \$35 Trillion assets
- Publicly-funded Green Investment Banks are getting more attention (OECD report), for their value in leveraging private investment and demonstrating that bankable projects are available to them.
 - US experience under ARRA illustrated value of guarantees and tranches with different risk levels

Recognized New Opportunities for profit ...

... Especially in a low interest global economy

- ✓ **Breakthrough Energy Coalition** – to ‘Form a network of private capital committed to building a structure that will allow informed decisions to help accelerate the change to the advanced energy future.’
- ✓ **Caring for Climate** – ‘an initiative mobilizing business leaders to implement and recommend climate change solutions and policies by advancing practical solutions, sharing experiences, informing public policy and shaping public attitudes.’
- ✓ **Global Alliance for Buildings and Construction** – ‘aims to gather countries, cities and public and private organizations of the building sector value chain, in order to scale up the implementation of ambitious actions toward the "below 2°C" pathway in buildings and construction sector.’

Example: International Solar Alliance (ISA)

In June 2016, WBG joined India and France, pledging \$1 Billion towards ISA's \$1 Trillion goal for new investment through 2030

BUT: *The Hindu*, 26 August, 2016:

- '... three factors continue to block the rapid scale-up of solar energy: **financing is still too costly for developers**; solar-related **plans and policies are often incoherent** and increase risks for developers and investors; and there is **insufficient ... R and D ...** investment in solar.
- 'ISA envisions that collective measures can facilitate the flow of over \$1 trillion into solar projects, by aggregating demand within countries, **standardised asset-structuring** across countries, and establishing an **ecosystem of financial instruments** to mitigate some of the investment risks.'

CURB – Valuing Infrastructure Investments

- Developed by WBG
- Piloted in 2015-16; new version out this month
- Used by Bangalore and Chennai to assess investment options
- Calculates emissions reductions associated with different infrastructure investments
- Determines return on investment and payback periods based on energy costs avoided
- Can thus provide borrowers and lenders with ‘bankability data’
- Permits project returns, not city creditworthiness, to be the bases for lending decisions
- Requires GHG inventory; will automatically upload the GPC template

The more standardized the data protocols and reporting, the clearer the risk and return profile will be for private investors

Climate Risk Accounting is Mainstreaming

- More and more business and investment institutes/accounting standards are requiring climate risk disclosure
- Many firms are already doing it, anticipating the requirements and trying to show off as good global citizens (greenwashing perhaps)
- The more this occurs in the private sector, the more **long term investors** – the ones with the most capital, such as pension funds and insurers (who need an assured source of liquidity) – will see public sector climate mitigation efforts as supporting their other investments
- Simultaneously, the same investors will be more inclined to look at the returns on climate change adaptation projects as **cost avoidance** benefits contributing to debt service capacities from borrowers

Carbon pricing and carbon risk disclosure – Panaceas for financing problems?

- New initiatives emerged from the COP2 process
 - **Partnership for Market Readiness** -- supports countries pursuing market-based carbon pricing, with a budget under \$200 Million
 - WB's **Transformative Carbon Asset Facility** as launched in Paris with a \$500 Million budget to 'create new classes of carbon assets' in developing countries
- **BUT:** EU and US experience with the effectiveness of carbon markets as inducements to GHG reductions is mixed
- **STILL:** Article 173 of the French Energy Transition Law (2016) has set a new global standard for carbon and climate risk disclosures for both companies and institutional investors.

Developing standards for pursuing finance

- *Global Protocol for Community-Scale Greenhouse Gas Emission Inventories* (long-time developed standard from WRI and WBCSD)
- *Measuring, Reporting, Verification (MRV) of Urban Low Emission Development* (ICLEI's GreenClimateCities Handbook)
- *City Infrastructure Investment Programming & Prioritisation Toolkit* (CDIA's tool for preparing a project for presentation to investors)
- *Making Carbon Markets Work for Your City: A Guide for Cities in Developing Countries* (in UN-Habitat's Cities and Climate Change Series)

The need is for a standard that can identify cash flow generated by a GHG emissions-reducing investment, so as to make the project bankable, even if the city is not creditworthy

A Market-Based carbon pricing process is the ideal basis for such a standard but is not yet available for wide-spread use

Potential impacts on climate adaptation, implementing the Paris Agreement, and attaining the SDGs

- ❖ A Carbon Price, a 'carbon risk pricing mechanism' or a form of 'blended value creation', movement toward a standard would have a major impact on availability of funds
- ❖ A nation or city that is willing to tax itself even if it does not charge for emissions, generates a greater capacity to pay back investors who commit funds to reducing emissions
- ❖ That capacity may be a necessary, albeit insufficient, condition for project financing, much the same as creditworthiness is for external financing of local purely public efforts



Insurers and pension funds need projects

- Asset Owners' Disclosure Project reports on some \$38 Trillion
 - Only 1% of insurers, 6% of pension funds, address stranded assets
 - 8% of insurers assess climate risk; 16% of pension funds do
 - There is opportunity to attract investment, if cities can limit risks
 - Only \$30 Billion of insurance assets are in low-carbon investments
 - Even pension funds have invested only \$63 Billion
- Risk management must address pension fund fiduciary obligations and insurers liquidity needs to attract capital
 - Carbon pricing may produce needed reliable cash flows
 - City project design can be modified to better assure cash flows
- The CCFLA and GEF problem and risk diagnoses are on target

More in common than different



New York City after Superstorm Sandy



Bangladeshi city after a cyclone hit

Progress????



- C40 reported last year that 70% of citywide climate action in global megacities was financed by the cities themselves
- ‘C40, Germany & IADB Achieve **Major Breakthrough(?)** For Developing Cities: **\$1 Billion** In Green Infrastructure Unlocked Within Four Years’
- The 4-year-old, EU-funded Urban-LEDS’ Solution Center has yet to release its Finance Tool – but the project Final Report is available!
- We’re a day late and in the wrong continent: the 2016 Forum of Standing Committee on Finance is in its second meeting day in Manila
 - The SCF will ‘share information on financial instruments that address the risks of loss and damage at local, national, regional and international levels.’
 - But their mandate excludes what should be our focus: loss avoidance through adaptation and mitigation ...

Thank you!

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