Climate Change Finance, Analysis of a Recent OECD Report:

Some Credible Facts Needed

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Abstract

The OECD in partnership with Climate Policy Initiative (OECD-CPI) recently released a paper “Climate Finance in 2013-14 and the USD 100 billion goal”. The paper has claimed significant progress towards that goal. The ‘preliminary estimates’ were that the mobilization of climate change finance from developed to developing countries had reached USD 62 billion in 2014 and USD 52 billion in 2013, equivalent to an annual average over the two years of USD 57 billion.

This paper examines carefully the OECD report’s accuracy, methodology and verifiability of the numbers reported. It finds serious problems on all counts. Numbers were derived on self-reported basis from self-interested players, and open to ‘gaming’ and exaggeration. Definitions of climate change finance used were not consistent with the Convention---to find more leeway to count progress? Methodologies used were inconsistent with the literature and best practice and even ‘bent’ in ways to find more flows than reality. Meaningful, independent verification was impossible since only aggregate numbers were reported---with lack of transparency. No serious consultations were done with developing countries themselves.

The paper discusses each of the main components of climate change finance identified in the OECD report, turn-by-turn. This includes ODA flows, MDB flows, and private sector flows. In each, methods and reports of counting and tagging were found to be seriously questionable---on both theory and on facts.

At best, the OECD report is at least partly right: ‘there remains significant work to be done to arrive at more complete and accurate estimates in the future’. That could well have been the title of the OECD report. There are some issues as to why there was so much rush to produce a document with inflated numbers, what has been termed as ‘green-washing’ of finance. We need to do better. At this time, the actual cross-border flows from 17 special climate funds since their inception are some USD 2.2 billion. This was reported by relatively independent and credible sources, as disbursements of climate change finance from developed to developing countries. This is far from the USD 100 billion a year goal.
Disclaimer

The views and analysis contained in this Discussion Paper do not necessarily reflect the views of the Government of India.
Foreword

At the recent Lima World Bank/IMF meetings, India had raised the issue on a roadmap for USD 100 billion in climate change financing a year by 2020. India had also raised questions on the correctness of the recent OECD report—which claimed that significant progress had already been made.

We asked our Climate Change Finance Unit of the Department of Economic Affairs, Ministry of Finance and its experts to undertake a careful review of that OECD report.

Their review paper is attached. Their conclusion: the OECD report appears to have overstated progress.

The attached discussion paper suggests that much more work has to be done. We need to establish more credible, accurate, and verifiable numbers on the true size of the mobilization of climate change finance commitments and flows from developed to developing countries.

Secretary, Department of Economic Affairs.

27 November, 2015.
Climate Change Finance, Analysis of a Recent OECD Report:

Some Credible Facts Needed

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Introduction

The OECD recently released a report ‘*Climate Finance in 2013-14 and the USD100 billion goal*’. Coming just before the upcoming Paris Climate Negotiations, it reported that developed countries and their private sector had provided some USD 62 billion in climate finance flows in 2014, up from USD 52 billion in 2013, and an average of USD 57 billion annually over the 2013-14 period. The Secretary-General of the OECD went on to say, “We are about halfway in terms of time [between the pledges made in 2009 and the deadline of 2020] and more than halfway there in terms of finance.” The French foreign minister, among others, welcomed the publication, saying ‘estimates demonstrate that considerable progress has been made. We must mobilize our efforts to provide the remaining USD 40 billion’.

The Financial Times headline (October 7th, 2015) on the story was however more circumspect: ‘Report on OECD contributions to combating climate change faces scrutiny.’ For good reasons. Information and credibility and realism must go hand-in-hand. The OECD is a club of the rich countries. After 2008, would we allow, for example, banks to regulate themselves, and then self-report on the progress they have made for a safer and sounder banking system? Scrutiny and skepticism is in order. 112 independent groups from around the world have also reported their concerns and sent a letter asking for ‘honest accounting’ (See text in Annex 1). Press reports from India similarly question the methods and accuracy of reporting, including the possibility of ‘green-washing’ (Sethi, Business Standard, Delhi, 23rd October 2015).

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1 Rajasree Ray, Shweta, and Salam Shyamsunder Singh.
Credibility, Accuracy and Fairness in Reporting

What are the problems with the OECD Report’s credibility and accuracy when we examine the Report in some detail? This Note lays out four main issues as regards its credibility, accuracy and fairness in reporting.

First, climate change finance flows need to be precisely that: measured flows, meaning, disbursed funds crossing borders. Not promises, pledges, or multi-year commitments about promised sums in the future. It has to be actual disbursements. The OECD counts commitments to arrive at its figure, not actual flows. If credible annual commitments can be demonstrated for several years, then possibly, we can start to use annual commitments as a short-hand for likely disbursements, not before.

Second, the definitional requirements are crystal clear: climate change finance has to be ‘new and additional’. The reason is simple: if monies meant for development are reallocated to climate, then we are robbing ‘Paul to pay Peter’, underfunding say primary health care or safe water to pay for climate mitigation. The OECD makes absolutely no effort at trying to measure and report what is new and additional.

One way instead is to ask how the ‘new and additional’ specific climate change funds specifically created for the purpose have done? Here are their numbers, the ‘hard’ facts, provided by a reasonably credible third-party source, as of June, 2015. Pledges to the climate funds have been significant, some USD 32 billion. But pledges are only that: promises. The catch is that as far as actual funds deposited from those pledges, the amount drops by one-half, to USD 17 billion. Now, those funds have to be actually committed to projects before they can flow. The amount drops further to about USD 14 billion. Then, flows to these projects have to disburse, actual climate change finance flows. How much till date? About USD 2.2 billion in all the special funds. All bilateral, multilateral, and MDB operated funds, some 17 of them. Not quite the OECD story, of some vast and growing amounts of climate finance funds flowing across borders from rich to poor countries? If the very same agencies had been doing such a wonderful job, why did we need to create the special climate funds?
Third, and worse, is if we ask the official aid agencies (and MDBs) themselves to ‘self-tag’ their projects, identifying those projects that they judge to be climate related. It’s called a ‘principal-agent’ problem in economics: setting up incentives for agencies to ‘game’ the system. All agencies have a huge natural incentive to over-report, to protect their jobs and occupations. The OECD report has gone ahead and done just that with its primary methodology—despite their supposed ‘due diligence’ (such as taking coal out from some of the reported climate projects!). It takes the MDB self-reported numbers at face value, adds it to the self-reported numbers by official aid agencies, export-credit agencies and even private market players, and then states, here it is, total climate financing provided by developed countries. Credible?

Our review of one case suggests (see more details below), for example, that MDBs may overstate their self-reported climate change finance project commitments by as much as three-fold in a generous interpretation. Using text analysis (searching by key words such as ‘climate, drought, floods, disaster, clean energy, solar, wind’) in all individual project titles and summaries, we are able to identify about one-third (US Dollar 3.4 billion) of the self-reported tally (USD 9.4 billion) of projects with significant climate ‘co-benefits’ as reported by the World Bank in 2014. Note, this is just the total amount for any project with supposed any climate ‘co-benefits’. When we repeat the analysis for 2015, the amount is even smaller (USD 3.2 billion, and 7.5 percent) of
total project commitments of USD 42.5 billion. The results are, moreover, 
*always worse* for projects committed out of the agency’s own resources (IBRD) than those 
with external resources (e.g., IDA financed) ---pointing, again, to mis-incentives to 
over-report?

We need independent, third-party verification that is responsible to all parties or 
principals, developed and developing. We need independent ‘forensic’ verification, 
down to the details of all purported specific projects, checking on expected gains 
with recipient countries and agencies. Just because the MDBs or aid agencies say 
they did large amounts of climate financing, retrospectively, does not make it so. 
Consider what might have happened in this ‘self-reporting’: (grossly) inflated claims. 
The MDBs commissioned a special report in 2014, back-tracking and tagging their 
lending to climate in 2013 and 2014. That is ‘retro-fitting’. The OECD relied on this. 
Credible? Hardly.

**Fourth**, we can count only the grant-equivalent element of any claimed climate 
change financing, not the gross face-value of all loans, guarantees, export credits 
and other elements. Why? Because that is what was agreed, is widely established, is 
part of the GCF agreement, for example, and makes economic sense: to identify the 
*additionality* to cover the risks and costs of climate externalities, as agreed under the 
Convention. Imagine, if a country borrows on near-commercial terms to pay for rising 
disaster risks from typhoon damages from global warming, say (as did the 
Philippines recently with an IBRD borrowing of USD 500 million) then the value of 
that is paid by the country itself. The country is financing it from future savings. The 
financial intermediary contributes nothing special---if it is not on terms specifically 
better than a standard sovereign borrowing from the market. It’s only the grant-
equivalent difference in terms of that finance that can be counted, nothing else. 
Adding the gross face value of loans, guarantees and private financing is thus 
creative accounting, not climate finance (as agreed under the Convention). If we 
used the grant-equivalent methodology, the reported numbers could drop further.

Squaring up the numbers, the reported USD 62 billion for 2014 could drop alarmingly 
by the following factors: (1) to USD 31 billion, if we assume that two-fold over-
reporting by agencies is standard and expected; (2) further down to USD 5.2 billion, 
when converted to grant-equivalent basis; (3) further adjusted down to USD 3 billion
as credible ‘new and additional’ monies, once we take out diversion of aid monies from other priorities; and (4) finally, actual annual climate change finance flows of less than USD 1 billion, given typical five to seven year standard commitment to project cycles. The point is obvious: we should not exaggerate the reported OECD numbers on new and additional climate change finance flows.

**A closer look at MDB flows:** A large share of flows as stated in the Report is from MDBs. One of the problems with such claims is that, as stated above, there is no credible evidence provided to support these numbers. It takes the MDB self-reported numbers at face value, adds it to the self-reported numbers by official aid agencies, export-credit agencies and even private market players, and then states the sum of all as climate finance.

To scrutinize this further we have analyzed the claim made by OECD report for the year 2014, using one of the largest MDBs. It was possible to do this thanks to the transparency made by them in their annual reports to their shareholders in the form of detailed sector/theme specific project wise commitments/flows to developing countries—unlike the OECD report.

Although the OECD report claims that the scope of mobilised climate change finance and a common methodology for tracking and reporting towards the USD 100 billion a year goal is based on common understanding of a group of 19 bilateral climate finance providers, the word “climate finance” itself appears only once or twice in the long 80-90 pages annual report of the largest MDB for the year 2014. However, their appendix table does shed some light on the project wise commitments/flows to developing countries.

For 2014, the lending for “climate change adaptation and mitigation” is reported to be USD 9.4 billion in the Appendix to their Annual Report. A very conservative estimate shows that out of this USD 9.4 billion, hardly USD 0.6 billion (6 %) lending could be attributed to climate related activities when we are parsimonious. When we are generous, even if we count investment related to drought, cyclone, energy, transport

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4 This estimate is based on only climate resilient activities (do not include investment related to energy, transport, drought related activities)
etc. this figure rises to roughly around USD 3.4 billion (36 %), still much less than the aggregate number reported.

What does this analysis show? As per the OECD report, MDB flows have gone up from USD 12.9 billion in 2013 to USD 18 billion in 2014. The climate related funding hardly sums up to USD 3.4 billion in the largest MDB even if we go by very liberal approach of climate related funding (as shown in above para). This number is just based on one of the largest MDBs’ own report. This only shows what we might expect from others? Therefore, the claim that MDBs flows have increased and is the biggest contributor towards USD 61.8 billion number is baseless.

The principles for attributing multilateral finance, such as MDBs, are also in serious doubt as used by the OECD. These are described in the OECD paper in some detail in Annex F of their Report. In particular, the OECD report relies on the recommendation of the Technical Working Group (TWG) that recommends that in the case of non-concessional finance---through resources raised in the bond markets (borrowings) or through retained earnings---attribution is determined by the share of developed countries in the two types of capital: paid-in and callable. Their argument: the MDBs’ AAA credit rating allows them to raise larger resources in the markets that are more attractive than if the banks’ borrowers had borrowed themselves. Accordingly, they attribute the developed country shares from their shares in paid-in capital and a discount to the amount of callable capital.

It turns out that in the literature on why MDBs have high credit ratings, paid-in or callable capital is only very partially the reason. Much more important is the banks’ credit rating because of the excellent credit repayment by the borrowers themselves, the borrowers providing sovereign guarantees and the preferred creditor status granted to the banks. In addition, callable capital, if it was ever exercised, has been never tested, and according to observers, if tested, would be tantamount to calling in question the banks’ survival themselves. Far more important are the borrowers’ role and the role of guarantees and preferred creditors, as well as the repayment history, and the larger role of many developing countries.  

Credit rating agencies in their assessments also point to the same aspects, as do the banks themselves in their presentations to the ratings agencies and debt-holders.

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If we therefore think about the attribution of MDB’s non-concessional loans, it is not at all correct that the method adopted in the OECD report is the right one. A cooperative credit institution with a complex history like the MDBs has much more complicated joint structures and attribution will always remain an inseparable joint one, leaning towards the role of the borrowers and the institutions themselves. The technical working groups report recommendations adopted by the OECD is not supported out by the facts.

**Official Development Assistance:** Another important component in OECD’s coverage of public climate finance data is Official Development Assistance (ODA). It is stated in the OECD Report that out of the total bilateral climate-related USD 24.6 billion average commitment in 2013-14, the level of ODA targeting climate change adaptation and/or mitigation as principal objective amounts to USD 14.5 billion (59 per cent). This appears to be exceptionally high and prone to double counting? What could have caused bilaterals to increase their climate related activities to such high reported amounts, and drop other priorities?

There is also a far bigger problem, of diversion. Net ODA from DAC members totaled USD 135.2 billion in 2014, level with a record USD 135.1 billion in 2013, and marking a 0.5 per cent decline in real terms. Net ODA as a share of gross national income was 0.29 per cent, also on a par with 2013. Bilateral aid to the least-developed countries fell by 16 per cent in real terms to USD 25 billion, according to provisional data. It has been seen that the 16 per cent decline in allocation of ODA to LDCs last year, perhaps, could be linked with a similar amount of total ODA being allocated to ‘climate related objectives’. We have looked precisely at this issue. The total ODA flows remain flat or declining since 2008 (Figure 2). By definition, any claim that shows large increases in climate change finance flows with overall flattening of ODA flows implies climate financing from ODA is being diverted from other uses. At the country level, this is also even more evident from the example of France, where overall ODA has been sharply declining since 2011 (Figure 3).

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Private Finance: Specifically on Private Finance, it is not surprising that the OECD/CPI Report has focused on the private sector investments. The Report has presented preliminary partial estimates of ‘mobilized’ private climate finance. The Report states that the average estimate for 2013-14 comprises USD 14.7 billion of ‘mobilized’ private finance per year (26% of total climate finance flows claimed in the report). A closer look at these numbers reveals that these are primarily co-finance led private finance and over 90 per cent of the private finance flows identified in the Report is targeted at mitigation. It has been stated in the report that “private co-financing was used as best available evidence of mobilization” and bilateral, multilateral as well as domestic public finance often work together, through blending at the fund level or co-financing at the project level. If the co-financing or blending is from the domestic private sector and national sources of financing—the so called “leveraged” by multilateral or bilateral public funds—it cannot be counted towards the goal of USD 100 billion per year committed by developed countries.
Further, a reading of the CPI's Report on “Global Landscape of Climate Finance 2015” published as recently as November, 2015, throws up a number of questions. The Landscape report is important to examine, because it is the source document for private finance we presume, because the CPI has been focused on that issue. The key points are:

- What is being referred to as climate change finance in the CPI’s report is actually investment (which can include national sources as well as normal activities unrelated to specific climate change finances). We can’t distinguish these investments from business as usual (BAU) investments and clearly cannot justify this as new and additional, needs based finance under the Convention. This is clear from the wordings in their own report: - “Private finance increased by nearly USD 50 billion in 2014 driven mainly by a record amount of new renewable energy deployment, particularly in China”, “Available data continue to show that private actors rely primarily on their own balance sheets to finance renewable energy projects (corporate and households’ financing), which accounted for 72% of total private investment in 2014. Mostly, they invested in high-income and upper-middle income countries such as Japan, the US and China”.

- What is even more alarming is that we don’t know who the recipients are, for a large proportion of cases. The Report acknowledges that the initial recipients of USD 56 billion of public finance (38% of the total) could not be identified. There are obviously some transparency issues quite endemic. It would be prudent that there is ‘book of accounts’ that is transparently available to both contributors and recipients of climate change finance, as is standard in all financial transactions.

- A look at the breakdown of total private investment by actors as stated in the CPI Global Landscape Report also points to the fact the ‘innovative’ financing, if any, is marginal. Project developers remained the most prominent private investor class in 2014, with 38% of total private climate finance and originated from, and were invested in, East Asia and the Pacific region (46%), Western Europe (25%) and the Americas (15%). Corporate actors invested about 24%, households’ investments accounted for 18% of the total private investment,

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7 CPI is the main collaborator with OECD on the report “Climate Finance in 2013-14 and the USD 100 Billion goal”
and commercial financial institutions provided 19% of total private climate finance in 2014. The only ‘innovative’ component in the whole break up is the private equity venture capital infrastructure funds amounting to USD 1.7 billion and institutional investors amounting to USD 0.9 billion. This is around 1 per cent of the total figures cited for private investment!

- It also turns out that all these claimed climate change finance flows have a significant share of national finance institutions, national projects. We don’t get a clear picture of cross border flows, i.e., flowing from developed countries to developing countries to take climate actions in line with the needs of developing countries. The Global Landscape Report states that private-oriented finance went mostly to mitigation projects in upper-middle or high-income countries. In terms of Geographies, CPI Report states that “92% of private investments were raised and spent within the same country”.

**Conclusion**

In conclusion, the Paris Conference and negotiators will unfortunately need to worry about the credibility of the new OECD report, and a continued search for credible means of financing of the INDCs. In a recent paper, we, as have others in different papers (for example, Nicholas Stern, Jean-Charles Hourcade, Jean Pisani-Ferry, Pascal Canfin, Mark Carney) are laying out a case for trillions, not billions, in new and additional innovative financing, including a role for central banks, for averting climate change disaster. The OECD report is deeply flawed and unacceptable (the authors are careful to say their report is preliminary and aggregate). It repeats a previous experience we had of double-counting, mislabeling and misreporting when rich countries provided exaggerated claims of ‘fast-start climate financing’ in the period 2010-12---which were widely criticized by independent observers.

We are very far from the goal of USD100 billion in climate change finance flows annually by 2020. This OECD report needs improvement. The credibility gap is too big. We have to have more credible facts, from a careful and continuous collaboration. Ambitions need to be set high, and not shirk even modest past responsibilities. A road map to raise climate change finance is urgent and a must in Paris. Climate justice, for poorer countries and future generations, needs no less. The amounts of annual climate change finance flows from rich to poor countries
which are new and additional remain extremely low. Everyone in this business knows this well. The only hard number we have right now is USD 2.2 billion in gross climate fund disbursements from 17 special climate change finance multilateral, bilateral and MDB funds created for the specific purpose---and not USD 57 billion average for 2013-14 as exaggeratedly reported by the OECD.
References:

Annex 1: Text of Letter: 112 groups demand grants and honest accounting for rich countries' promised $100 billion in climate finance

TEXT:

“7 October 2015

Dear Ministers,

We are writing to you in response to the “Joint Statement on Tracking Progress Towards the $100 billion Goal,” issued by your governments on September 6. We agree with and appreciate the recognition underscored in your statement of the need for developed countries to provide the promised $100 billion annually for developing countries for climate action, and to do so under transparent rules and guidelines. However, the exclusive intergovernmental process, as well as elements of the content of the joint statement, are flawed and require further attention:

- Inclusion, universality and UNFCCC forum. Accounting for climate finance will directly affect how much climate finance is delivered and in what forms, making it just as relevant to recipients as it is to contributors. Deliberations and decisions about transparency and how climate finance is defined and counted must be taken at the forum that is fully inclusive of all countries – i.e. the UN Framework Convention on Climate Change, especially its Standing Committee on Finance. A robust system of measurement, reporting and verification of finance under the UNFCCC is imperative.

- $100 billion pledged must equate to $100 billion delivered. Multiple studies contradict the statement’s claim, “We have fulfilled our 2010-2012 ‘fast start finance’ commitment.” Greater transparency is essential to ensure that what is counted as climate finance is in fact new and additional to existing international development commitments. Double-counting and counting funds with questionable connections to climate will not build trust at the climate negotiations. More importantly, it will not

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1 Australia, Belgium, Canada, Denmark, Finland, France, Germany, Italy, Japan, Luxembourg, Netherlands, New Zealand, Norway, Poland, Sweden, Switzerland, United Kingdom, United States, and the European Commission

deliver the needed changes on the ground – relief for the most vulnerable, and a just transition to a clean and sustainable economy for developing countries. Further, developed countries’ resistance to delineate a clear roadmap to the $100 billion, not to mention the need to scale up finance beyond 2020, calls into question the statement’s claim that “developed countries are well on their way to achieving this goal.”

- Grants and grant equivalents. Only public grants – or the grant equivalent of loans, guarantees and other financial instruments – should count as part of the $100 billion or any future climate finance targets. Estimates suggest that the costs for climate adaptation and loss and damage alone in developing countries already exceed $100 billion. Money that returns to developed countries (such as through the repayment of loans) and money that does not get spent (such as when a guarantee is provided but default does not occur) should not count towards the $100 billion. Further, climate finance must not add to the debt burden of fragile and highly indebted developing country economies.

- Private finance. Private investment in climate-friendly activities is vital and efforts to increase the transparency of these financial flows are welcome. However, private finance should not be substituted for public funding or counted towards the $100 billion. As the OECD Research Collaborative of Tracking Private Climate Finance acknowledges, there are inherent difficulties in ascribing causality in relation to private finance flows as well as practical difficulties in accessing information transparently (at best, these would be estimates). We find the stated intention to count private finance mobilized by “a public policy intervention, including technical assistance to enable policy and regulatory reform” to particularly stretch credibility and urge that any consideration of such practice be discarded. Furthermore, the purpose of private finance is different: by definition, its main purpose is to generate profits for investors, not to offer relief or justice for impacted people. Private investment cannot be a replacement for direct public support, especially for adaptation.

• Developing country as primary beneficiary. Climate finance must benefit the people of developing countries. Export credit agencies are by design meant to benefit the multinational corporations of the originating country. Thus, finance provided through developed countries’ export credit agencies should not count as climate finance.

• Harmonization with other tracking and reporting systems. Alignment should not be pursued with the Common Principles for Climate Mitigation Finance Tracking, adopted by multilateral development banks and the International Development Finance Club. Among other serious flaws, the Common Principles allow for fossil fuel financing and are inconsistent with keeping global temperature rise below 2°C, let alone 1.5°C. We note an essential step needed now to assure the world that developed countries are on track to provide $100 billion in climate finance by 2020 is for them to announce public adaptation and mitigation finance targets in Paris. We look forward to examining the common methodology developed under this initiative, including how you will systematically establish – on an activity-by-activity basis – a clear causal link between public intervention and private finance. We hope the merits and shortcomings of your proposed methodology can be debated openly at the UNFCCC, and that the aforementioned areas of concern are addressed.

Thank you for your consideration. We look forward to a response.

Sincerely,

[Signed 112 groups from around the world]