

Policy Brief: Enhancing Private Sector Finance through the Transparency Framework of the Paris Agreement

Access to finance is a critical enabler for Sub-Saharan African countries' to meet their NDC commitments under the Paris Agreement. Giving climate finance a more prominent role in the Convention's communication requirements, including reporting on countries' climate finance strategy and architecture and how they will attract and channels funds, will help to build investor confidence and open new markets.

KEY MESSAGES

- Sub-Saharan African countries are mostly dependent on external financial support at a scale that is currently not available. International and domestic private investment flows are essential to fund African countries' NDCs.
- To ensure financing of Sub-Saharan African countries' NDCs, current guidelines under the Paris Agreement Transparency Framework need to be updated to explicitly include these countries climate finance approaches and the role of the private sector.
- Resulting reporting in turn should feed the participatory discussions of the Convention, namely the global stocktake dialogue and the SCF Forum to inform Parties in updating and enhancing their next round of NDCs.
- The financial and technical support available through the Convention should have an increasing focus on reporting on Sub-Saharan African countries' climate finance architecture and include training of government officials within the ministries.
- A sector-based approach to financing the NDCs overseen by multi-sectoral governance could lead to transformative public and private investment flows in Sub-Saharan African countries.
- The financial sector should be included as a distinct prioritised sector in low emissions development strategies with a focus on governance, regulation, and capacity building in order to support the radical and effective transformation of the productive sectors in Sub-Saharan African countries.

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Introduction

Financing countries' Nationally Determined Contributions (NDCs) in the short, medium and long term is a key challenge that needs improved coordination if it is to be mainstreamed in the economies of Sub-Saharan African countries. Much of the finance needs for the green infrastructure transition is pertinent to the developing world, however, currently only around 3% of this amount is used to fund low carbon development and climate resilience in Sub-Saharan African countries (CPI, 2017). The continent faces a huge infrastructure and finance gap that will need to be resolved taking into account both the Paris Agreement and the Sustainable Development Goals (SDGs) to avoid expansion into carbon-intensive capital stocks and being locked-in to pathways of increasing GHG emissions well into the post-2020 era. Sub-Saharan Africa is currently not only underrepresented in global climate finance flows, but is characterised by poor investment climates and low investor confidence due to a number of factors which include high risk profiles, capacity gaps, underdeveloped markets, policy uncertainty and high transaction costs. In addition, research conducted by the authors suggests that most Sub-Saharan African countries are dependent on external financial support at a scale that vastly exceeds the amount that is currently pledged by developed countries (SouthSouthNorth, 2019). Sub-Saharan African countries will thus need to further improve their enabling environments to attract climate finance.

During COP24 in Poland in 2018, governments adopted a robust set of guidelines for implementing the Paris Agreement. The resulting Katowice Climate Package includes modalities, procedures and guidelines that will operationalize some of the key features of the Agreement, including a transparency framework for action and support, the global stocktake process, and the finance provisions. The transparency framework provides common reporting guidelines setting out how countries will communicate information about their planned and realised domestic climate mitigation and adaptation actions as well as details on the means of implementation in particular related to finance needs and support. On finance, COP24 agreed a process to establish a new quantified higher goal for climate finance prior to 2025 to follow-on from the current target of mobilizing USD 100 billion per year from 2020 to support developing countries.

Developing country reporting on financial needs is unlikely to drive significant private sector investment. Thus a parallel process is required where developing country parties report on their climate finance and investment strategies.

The financial provisions of the Paris Agreement (Article 4, paragraph 2; and Article 9, UNFCCC, 2015) oblige developed countries to mobilise and provide financial resources to developing countries from a wide variety of sources, instruments and channels, and report on progress. Meanwhile developing countries are required to report on financial, technology transfer and capacity-building support needed and received (Article 13; UNFCCC, 2015). However there are currently no specific guidelines for countries to report on national or sectoral climate finance strategies, investment plans and investment portfolios.

Developing country reporting on financial needs is unlikely to drive significant private sector investment. Thus a parallel process is required where developing country parties report on their climate finance architecture and investment strategies including plans to attract and receive private sector funds to support the implementation of their NDCs. If developing countries develop and communicate such plans, this could increase investor confidence, stimulate peer-learning between developing countries, enhance both public and private sector climate finance, and ultimately make finance flows compatible with Article 2c of the Paris Agreement.

Current climate finance communication of Sub-Saharan African countries

In order to track progress and financing needs under the Paris Agreement, all countries must provide figures on support provided, national contributions, and investment needs with respect to both mitigation and adaptation action in a clear and preferably harmonised manner. Research conducted by the authors as part of the PRINDCISSA Project (SouthSouthNorth, 2019), highlighted that significant gaps remain in countries' reporting on finance needs and support received to date.

Research from the AfDB (AfDB, 2015) reveals that 75% of Sub-Saharan African countries in the study were assessed as having "low ambition" for their unconditional mitigation contributions. When the conditional parts of their NDCs were evaluated, half of the countries were categorised as having "high ambition". This suggests that adequate levels of climate action in these countries is mostly dependent on external financial support and makes the availability of international climate finance, and additional leveraged private sector finance, crucial to achieve Paris Agreement goals. Our research highlights that the climate finance required by just 13 of the 49 Sub-Saharan African countries, based on the conditional part of their NDCs, amounts to at least USD 102 billion per year. This figure excludes large economies such as Nigeria, for which the conditional funding portions have not been identified or are unclear (SouthSouthNorth, 2019).

Climate finance needs of Sub-Saharan African countries:

The costs associated with the adaptation needs range between USD 1 billion (Angola) and USD 98 billion (South Africa) for the period from 2020 to 2030. The costs associated with the mitigation needs range between USD 2 billion (Burkina Faso) and USD 734 billion (South Africa) on aggregate for the same period. In total investment needs for climate action in all Sub-Saharan African countries could amount to over USD 150 billion per year up to 2030.

Source: own research (SouthSouthNorth, 2019)

The share of conditional finance needed for these countries amounts to 83% of total finance requirements on average, suggesting that currently Sub-Saharan African countries do not believe they are capable of raising adequate amounts of domestic finance. The funding need for the conditional portion of 13 countries in the region is higher than the total amount pledged for all developing countries across the globe (i.e. USD 100 billion/year from 2020), thereby highlighting a significant funding shortfall. Prior to 2025, a “new collective quantified goal” for climate finance higher than the current goal of mobilizing \$100 billion a year by 2020, will be set by the Parties to the Paris Agreement. It is clear that the conditional targets and commitments from developing countries combined cannot be financed by the industrialised countries unless additional large amounts of climate finance are pledged, and these funds are used to effectively leverage private sector finance.

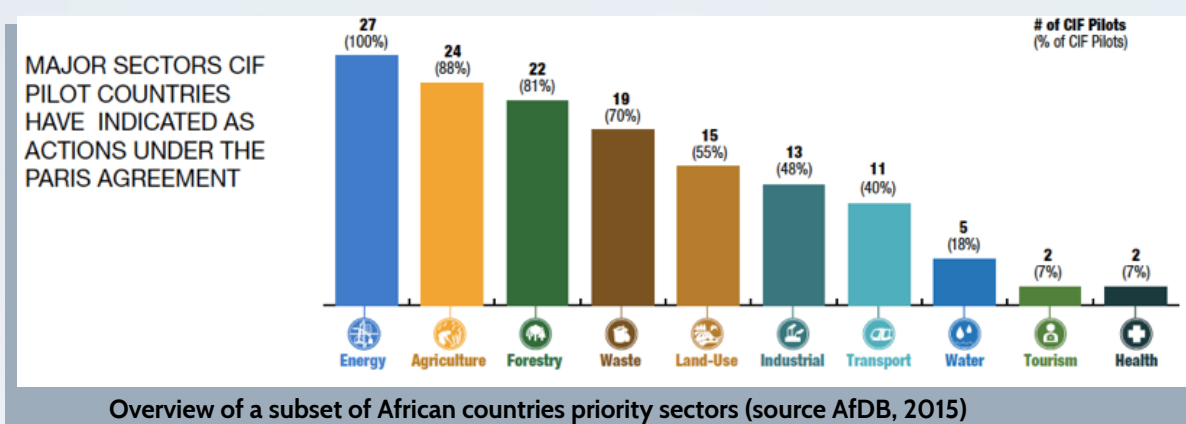
The authors believe that there is an urgent need by Sub-Saharan African countries to develop sectoral climate finance strategies and investment plans and communicate these under the Convention. Currently this information is broadly lacking in the current reporting requirements^[1] under the Convention (SouthSouthNorth, 2019) and there is an opportunity to address this gap in the next round of reporting in 2020 through the Biennial Transparency Reports (BTRs) and the updated NDCs. In addition, there is not much coherence between these various reporting outputs in terms of climate finance elements, nor harmony between the reporting of different countries.

[1] National Communications, Biennial Update Reports, and INDCs

Sector-based approaches to climate finance

Research makes the case that a sector-based approach is essential to unlock the barriers to reach the objectives of the Paris Agreement and should therefore be adopted for revision of NDCs (COP21 RIPPLES Consortium, 2018). The literature indicates that the economic, technical and political transformation challenges are largely sector-specific and as such require targeted approaches and policies (COP21 RIPPLES Consortium, 2017). A survey conducted by the UNDP revealed that more than a third of developing countries have developed sectoral mitigation plans (UNDP, 2016). If well developed, sector-based approaches provide a medium- to long-term vision for sectors of the economy, they could shift the conventional investment domain to Paris compatible investments and present investment opportunities for the private sector.

A sector-based approach to implementing and financing the NDCs would convey government commitment, vision, clarity, and could lead to enhanced investment flows and transformative finance through increased investor confidence, especially if the approach includes sector investment plans and sectoral mitigation and adaptation project portfolios. National cross-sectoral governance would secure policy coherence, harness synergies, and provide the coordination to make sure aggregate sectoral efforts deliver NDC targets. A sector-by-sector assessment would also avoid being locked-in to carbon intensive investments, as opposed to a more priority-driven approach, and provide the tools for the ambition needed to reach the long-term goals of the Paris Agreement. For instance if a country invests in renewable energy, it should simultaneously divest coal and phase out fossil fuel subsidies. Moreover, such an approach would facilitate coherence and integration with Sub-Saharan African countries' development objectives. Sectoral Investment Plans would communicate a long-term policy signal, provide the instruments and programmes to stimulate private sector financing of the NDCs and could be repeatedly updated and improved over time. These plans would form the pillars of a national investment plan, embody a framework for mitigation and adaptation investment, and serve as the bridge between policy and implementation.



Our research found that 9 countries out of 27 included in the study indicate some level of investment strategy, plans or thinking in their NDCs. Five of these are viewed by the authors as a low level of development, while four point to a medium level (SouthSouthNorth, 2019). It should be noted that some countries have started developing climate finance strategies and plans after their first NDC was published. Also, several countries included in this study have developed sectoral investment plans that have not been mentioned in their NDCs. The detail of mitigation policy is marked high for only four countries (16.7%), and medium for almost half of the countries (AfDB, 2015). A vision and high level of detail of national policies indicates countries' commitment and is as such generally considered to increase investor confidence, and may form the basis for sector investment plans.

Case Study: Leveraging Private Sector Investment in NDCs

A sector-based approach to financing NDCs may be an effective way to overcome economic, technical and political barriers in Sub-Saharan African countries, leading to enhanced and transformative public and private investment flows. SouthSouthNorth (SSN) is implementing a programme funded by the German Government under the International Climate Initiative (IKI) to leverage private sector investment for the implementation of NDCs in seven developing countries across Africa, Asia and Latin America. In Kenya, which is a focus country for the Mobilising Investment programme, a scoping study identified bioethanol for clean cooking for low-income households as a sector with significant potential. A triple bottom-line study analysed the social, environmental, and economic benefits provided by a move to bioethanol for clean cooking and developed a clear evidence base for policymakers to make informed decisions. The study was used successfully to lobby the Government of Kenya (GoK) to zero-rate bioethanol for VAT in the 2019 budget, making the cost of bioethanol competitive with charcoal and kerosene for cooking.

As a follow up and in order to stimulate the sector and build investor confidence, SouthSouthNorth, together with Dalberg Advisors and a cross-ministerial government working group, has developed a clean cooking master plan for Kenya. The master plan evaluates sugarcane and cassava as bioethanol feedstocks for future supply and demand scenarios and quantifies investment opportunities for the sector. A set of policy recommendations suggests a roadmap for the GoK to enable the growth of the sector while managing food security concerns. This is likely to have significant impact by promoting agriculture livelihoods, reducing indoor air pollution, curtailing deforestation and cutting emissions from the use of dirty cooking fuels whilst leveraging the Kenya's bio-economy potential.

Using the Paris Agreement Transparency Framework and reporting requirements to enhance private sector finance

Sub-Saharan African countries will need to address the barriers to climate finance. Developed countries have an obligation to provide finance, and the international private sector will choose which projects in which countries they fund. In light of the current finance gap and the historic and current perception of the investment climate in Sub-Saharan African, countries will need to compete with each other to attract the international funds for NDC implementation. Assessments of risk and return will in large part drive these investment decisions, particularly for private sector players driven by shareholder value creation.

Ample opportunity exists to enhance private sector finance flows in Sub-Saharan Africa, and progress has already been made through domestic policies and international programmes and mechanisms. Yet current efforts are incremental, small-scale and take too long. Since the scale of climate finance needed to implement the current NDCs is vast, and will only increase over time, a holistic approach should be taken. Investor appetite and confidence must be enhanced through country-tailored policy design, appropriate financial instruments, embedded in a long-term vision. In addition there is a need for the development of climate finance strategies and investment plans per sector, coupled with the formation of NDC project portfolios.

A starting point for this holistic approach can be efforts made by national governments through the UNFCCC processes. Finance is a major topic in the negotiations, and initiatives such as the Finance Mechanism, the Standing Committee on Finance, with its Forum and dialogues, its biennial assessments and overviews of climate finance flows, the multilateral funds including the Green Climate Fund with its Private Sector Facility, the guidelines on reporting on climate finance for Parties, are all steps in the right direction, but may prove to be insufficient.

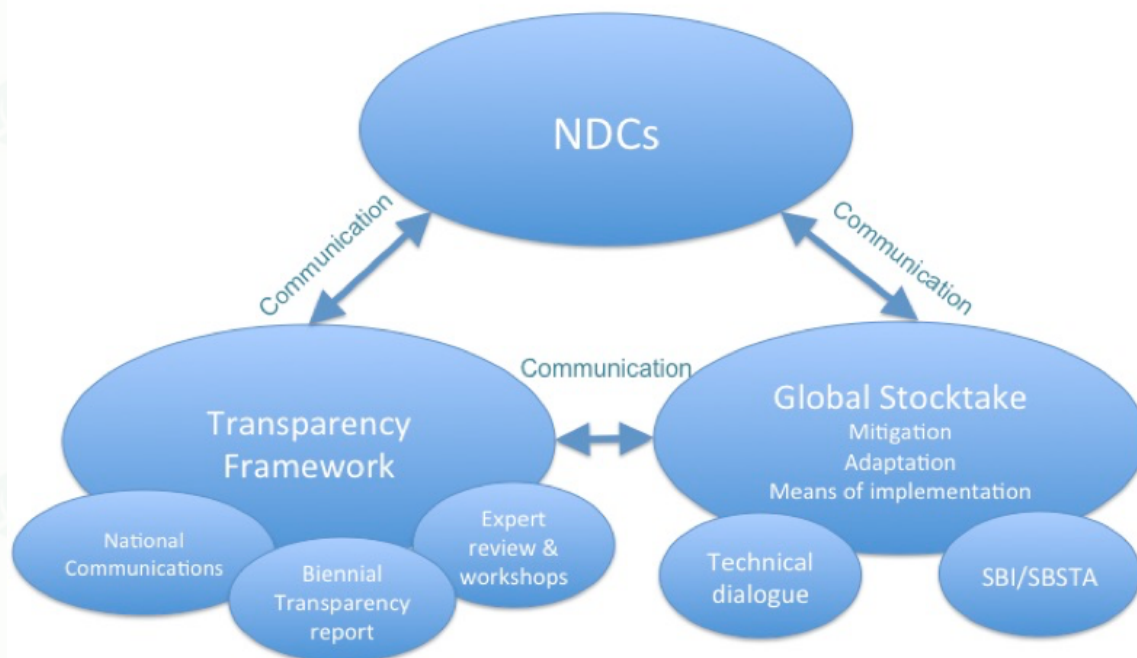


Figure 2: The Paris Agreement Ambition Mechanism

Climate finance must have a more prominent role in the Convention's reporting requirements and dialogue. Currently there is very little discourse on climate finance strategies, investment plans and portfolios, and related capacity building needs and efforts in the reporting of the UNFCCC processes. There are no requirements to include such elements in country communications beyond finance needs and support received. The authors recommend that the new format of documentation (NDCs and/or BTRs) should include more detail on investment strategies and plans, specifically including a focus on private sector engagement.

The Transparency Framework reporting and dialogue can stimulate further climate action and public and private sector climate finance flows. The reporting and dialogue sessions should stimulate peer-learning through knowledge exchange between developing countries on best practise and failures. To support this process current guidelines under the Transparency Framework would need to be updated to explicitly include developing countries climate finance approaches and the role of the private sector within those plans. The financial and technical support available through the Convention for reporting should include training of government officials on climate finance approaches.

Greater detail could be presented in the BTRs, while the NDCs should provide the comprehensive headlines. These reports will then serve the discussions in the periodic participatory dialogue sessions, the global stocktake, and the SCF Forum. Updating the guidelines of the reporting with the Transparency Framework to include specific guidelines on how to report on these climate finance issues is recommended. Not only should the progress of climate finance support flows be recorded, but also the progress on the evolution of countries climate finance architecture. Guidelines should also address coherence between the various reporting outputs, i.e. the NDCs, National Communications, BTRs, etc. The reports should be coherent and refer to each other, for instance with extensive detail in the biennial transparency report, and headlines and referral in the NDC.

These processes provide the opportunity to assess collective progress towards achieving the ultimate aims and long-term goals of the agreement by taking stock of climate finance efforts, flows and gaps, and the investment and development paths of Sub-Saharan African countries. Moreover it provides an opportunity to further improve and enhance both public and private sector finance flows and strategies through peer learning and knowledge exchange between developing countries on best practise and failures. The outcomes will inform each subsequent round of NDCs and the evolution of countries' policy framework. To be effective in the light of climate finance, these sessions will need to maximise private sector participation.

Article 2.1.c of the Paris Agreement calls on parties to make finance flows consistent with a pathway towards low GHG emissions and climate-resilient development. Climate finance is a central cross-cutting issue through all sectors and subsectors of the economy. Sub-Saharan African countries will need to develop investment plans and strategies per prioritised sector, which can be subsets of – and should be coherent with – national development plans. In the long run these investment plans need to be mainstreamed across the entire economy. Due to the impact of the financial sector on the necessary low-carbon systemic transformation of the economy, this long-term objective could be interpreted as a need to transform the financial sector itself. This may be done by treating the domestic and international financial sector as a distinct sector and transforming it along with the productive sectors of the economy, and developing strategies to build capacity and to attract climate finance.

Currently the financial sector does not have the capacity, knowledge, and mandate to transform the economy. Current incremental efforts of capacity building and the use of standards and sustainability indices will not suffice to reach the objectives of a carbon neutral society by mid century. Transforming the financial sector would include setting goals for the speed of divestment to avoid carbon-lock in, rapidly phasing out fossil fuel subsidies, and mainstreaming green finance and debt. The decision-making process for every stock, loan, bond or investment opportunity would need to be dependent on its assessed climate change performance and impacts.

The Importance of NDC Investment Plans

The Paris Agreement puts the onus on developed countries to mobilise and provide financial resources, however, a parallel process is required of developing country Parties providing transparency and considering finance options for their NDCs, i.e. through communicating not only their financing needs in a detailed and consistent manner, but by developing and communicating a NDC Investment Plan and the associated intended supporting policy framework. An NDC Investment Plan could be sector-based and would involve budgeting of planned adaptation and mitigation measures at economy-wide scale, identification of barriers for each activity and developing the appropriate supporting policies and financial instruments, and identification of potential finance sources for each activity and ways to access these. This should lead to a portfolio of bankable mitigation and adaptation projects.

At the same time developing countries will need a clear mitigation and adaptation policy framework and incentive structure for the private sector. It would arguably serve all countries to develop a specific strategy to engage the financial sector in the implementation of the Paris Agreement. Depending on country specifics, such strategies could include capacity building activities and an incentive framework for the local financial sector in order to mainstream climate finance and bring interest rates down. Developing NDC or sectoral investment plans would require collaboration and coordination between ministries, which is often lacking, especially between the Ministries of Environment who generally drive the countries climate plans and the Ministries of Finance who are responsible for channeling and administering climate finance.

As the transition to low-carbon economies has become more pressing than ever in history, it is crucial to raise funds at an accelerated pace and allocate these funds to pressing mitigation and adaptation interventions that form part of a holistic long-term strategy and implementation plan in a coherent manner. Sub-Saharan African countries will develop at a fast pace, so in light of the Paris goals, it is important to incorporate and justify climate action and avoid carbon lock-in.

Recommendations for policy-makers

This policy brief has argued that Sub-Saharan African countries must use the Paris Agreement Transparency Framework reporting and dialogue provisions to communicate their climate finance architecture and investment planning in order to enhance private sector climate finance. Communicating these plans through the UNFCCC channels would have multiple benefits, it would keep track of countries' efforts in terms of attracting climate finance, signal which countries may be lagging behind and need support, stimulate peer-learning among countries, and enhance investor confidence by sending a message to the market place.

Key policy insights include:

- To ensure financing of Sub-Saharan African countries' NDCs, current guidelines under the PA Transparency Framework need to be updated to explicitly include these countries climate finance approaches and the role of the private sector.
- Resulting reporting in turn should feed the participatory discussions of the Convention, namely the global stocktake dialogue and the SCF Forum to inform Parties in updating and enhancing their next round of NDCs.
- The financial and technical support available through the Convention should have an increasing focus on reporting on Sub-Saharan African countries' climate finance architecture and include training of government officials within the ministries.
- A sector-based approach to financing the NDCs overseen by multi-sectoral governance could lead to transformative public and private investment flows in Sub-Saharan African countries.
- To support the radical and effective transformation of the productive sectors in Sub-Saharan African countries as required by the PA the financial sector should be included as a distinct prioritised sector.

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