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# Policy Brief on Climate Finance

Review of the current global landscape in  
financing mechanisms for climate change

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Global Governance  
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# Policy Brief on Climate Finance



## Executive Summary

This policy brief provides perspectives on the current global landscape of climate finance mechanisms, identifying its suggested shortcomings and proposing solutions to increase climate finance mobilisation. It presents an overview of current climate finance flows, noting the growing gap between the financial costs of climate action and adaptation in the Global South and the finance mobilised by the Global North to address these needs, as well as the challenges with mobilising private climate finance in an effective and equitable manner.

It is noted that the lack of a clear definition of “climate finance” and insufficient financial flows to meet global climate goals pose major challenges for Global South countries seeking to mitigate and to address the impacts of climate change. Developed countries have fallen short of their pledge to mobilise \$100 billion per year by 2020, and a disproportionate focus on mobilising private finance rather than direct public funding has further complicated progress. The new collective quantified goal (NCQG) which commits developed countries to provide \$300 billion annually by 2035 is also likely to fall short of the needs of developing countries. This inadequate financial support

undermines climate action in the developing countries, and frustrates efforts to meet global mitigation and adaptation targets.

The brief cautions that efforts to drive technological and financial innovation for climate solutions must be supported by adequate financial flows, access to technologies for developing countries, and public investment in areas with high social returns but low private gains. To avoid “greenwashing,” it is essential to establish robust monitoring, verification, and regulatory frameworks that ensure the promised climate and biodiversity benefits are genuine and any negative impacts are minimised.

The brief further addresses the potential role of financial institutions, private climate finance and carbon pricing in helping to bridge current gaps and drive technological and financial climate innovation. Catalysing funding through regulatory change and avoiding the greenwashing too often seen in current private climate finance efforts are identified as critical to addressing current flaws within these structures.

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The brief identifies the following proposed solutions to the identified challenges:

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**1. Increase in Public Climate Finance:** Official public flows through bilateral and multilateral channels should be significantly increased and grant-based or concessional in nature. This will help meet the \$100 billion pledge and the NCQG without incurring additional costs or financial risk on recipient countries.

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**2. Reforming Multilateral Development Banks (MDBs):** MDBs must be provided with additional capital and mandated with clear climate finance goals. MDB voting and governance structures should be urgently reformed to reflect global economic shifts and better serve climate objectives.

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**3. IMF and MDBs Policy Reforms:** The policies of MDBs and the IMF often limit national capabilities for mobilising domestic resources and impose austerity, undermining climate action. Reforms should enable countries to spend more on mitigation and adaptation to achieve sustainability goals.

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**4. Progressive Taxation for Climate Finance:** Global cooperation must support progressive taxation strategies, including reforming outdated international tax systems, instituting higher global minimum tax rates for multinational corporations, and taxing high-wealth individuals. This would prevent the loss of resources through illicit financial flows and provide new resources for climate action.

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**5. Regulating and Monitoring Private Climate Investments:** A regulatory framework is needed to ensure private investments in low-carbon products and processes deliver promised climate outcomes. This includes mechanisms to monitor investments, set targets, assess de-risking, and impose penalties for failure to meet objectives.

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Based on the solution above, the brief makes the following recommendations regarding the further work and efforts of the Climate Governance Commission to support thought leadership and engagement on climate finance reform:

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**1. Climate Financing & Developing Country Participation:** Ensure that developed countries honour their commitment to mobilise \$100 billion annually in climate finance until 2025, and that they honour their new commitment to mobilise \$300 billion annually in climate finance by 2035. The new collective quantified goal must set a substantially higher financial target that is based on the needs and capacities of the developing world. This will promote more equitable and effective climate action.

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**2. Grant Financing for Low-Return Innovations:** Secure concessional or grant funding to drive innovation in areas with low financial returns, particularly for adaptation projects and loss-and-damage compensation. This will ensure underfunded sectors get the support needed to address climate impacts.

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**3. Public-Private Finance Mobilisation:** Support efforts to mobilise private finance by shaping regulations, conditions, and creating monitoring frameworks that prevent greenwashing. Public-private partnerships must deliver meaningful mitigation and adaptation results, avoiding financial inefficiencies.

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**4. Debt-for-Climate & Nature Deals:** Develop research to scale up debt-for-nature and debt-for-climate initiatives, ensuring they genuinely reduce sovereign debt while achieving climate goals. Caution is needed to prevent over-reliance on profit-driven intermediaries in these deals.

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**5. Fair Carbon Pricing & Taxes:** Design carbon pricing and taxes carefully to avoid them becoming protectionist tools that benefit developed countries at the expense of developing ones. Such policies should be fair, non-discriminatory, and support global climate justice.

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The brief also contains supplementary briefs, authored by Dr. Dhruva Purkayastha and Eoin Jackson, outlining: (a) Recent discussions / developments within and about the international financial architecture; and (b) recent proposals and discussions to mobilise private climate finance.

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# Introduction: global climate finance in the context of common but differentiated responsibilities



Brief by C. P. Chandrasekhar and Jayati Ghosh

## The global climate finance landscape is defined by the sources and directions of flow of resources supporting the projects and activities designed to mitigate ongoing climate change and enable adaptation to its effects.

More recently, emphasis has also been laid on finance for compensating the loss and damage resulting from extreme weather events and other natural disasters triggered by the effects of ongoing climate change. These flows occur within and between national jurisdictions. Cross-border flows are important given the vast differences in both responsibility for climate change and capacity to fund the required investments across developed and developing countries. The gap between cumulative carbon emissions and current emissions of the developed and developing countries (especially in per capita terms) is enormous, adding to the recognition that climate mitigation efforts must take into account the “common but differentiated responsibilities and respective capabilities of different parties.”<sup>1</sup> These factors warrant a much higher financial contribution from the developed countries through bilateral and multilateral channels to support climate alleviation efforts, and new approaches to raising the necessary international finance that recognize these dynamics.

These new approaches must include recognition of the need to raise more public revenues. This points to the importance of global initiatives on tax cooperation that are seen as adequate and fair, as demanded in a United Nations resolution calling for “a framework convention on international tax cooperation,” the negotiations for

which have just started at the UN. The process at the UN resulted after much pressure from developing countries (especially the Group of Africa) because of dissatisfaction with the OECD “Inclusive Process” with regard to Base Erosion and Profit Shifting (BEPS) by multinational companies.<sup>2</sup> This is a strategy of tax avoidance that involves shifting profits to low-tax or no-tax jurisdictions, depriving countries where the economic activity takes place of their taxing rights. The principles underlying the two “pillars” of the OECD agreement (the idea of unitary taxation of multinationals, treating them as one global company with taxing rights on its profits allocated to countries on the basis of a formula; and the idea of a minimum global corporate tax rate to prevent a race to the bottom) are sound. But the final compromise on the minimum tax rate was only 15%—close to the tax rate of a known tax haven like Ireland. And the proposal for unitary taxation was so watered down that it proposed taxation of only a small fraction of the global profits of a limited number of very large multinational companies, providing little gain to developing countries. In return for this meagre benefit, countries were required to abandon some lucrative taxes on multinationals that have already been imposed by several countries, such as digital services taxes that are providing significant revenues in some cases. But in any case, this “pillar” of the OECD proposal has not yet been agreed to by major countries like the US.

<sup>1</sup> There has been some pushback on this front, as developed countries feel the need to at least partially withdraw from this commitment. For example, in an official statement to the tenth session of the Open Working Group on Sustainable Development, the official Japanese delegate declared that: “CBDR is a principle related to environmental issue, global environmental degradation. We do not accept the extension of CBDR to other areas nor do we support the idea that CBDR is an overarching or guiding principle on SDGs as a whole... Furthermore, when we speak about official development assistance, it is not implemented from the viewpoint of fulfilling the responsibilities. For some countries it is done for charity, for others it is for solidarity. We hardly accept an idea to link CBDR with aid policy and we do not support an idea that developed countries have to provide ODA as a matter of responsibilities.” See [Statement by Hiroshi Minami, Deputy Director General for Global Issues of the Japanese Foreign Ministry, on Cluster 7, Means of Implementation and Global Partnership, at the tenth session of SDGs OWG](#), 2014.

<sup>2</sup> Leigh Thomas, “[UN vote challenges OECD global tax leadership](#)”, Reuters, 23 November 2023.



The discussions at the UN could significantly improve on this outcome, by ensuring a fair distribution of taxable profits. In addition, they can extend to wealth taxes, particularly on the super-rich, as several recent proposals have argued for, and as currently being championed also by the Brazilian Presidency of the G20. The automatic sharing of banking information is one important positive step in this regard, although more countries need to participate in this. Similarly, inheritance taxes, taxes on excess profits and similar sources of revenue raising should all be considered seriously—and ideally with international cooperation.

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Estimates in the [Global Tax Evasion Report](#) from the EU Tax Observatory<sup>3</sup> suggest that just the combination of proper taxation of multinational companies with a minimum global tax rate of 21%, along with a tax equivalent to only 2% of the wealth of global dollar centimillionaires, would yield more than \$500 billion per year—a very significant amount that could be utilised for meeting both mitigation and adaptation needs.

<sup>3</sup> EU Tax Observatory, [Global Tax Evasion Report 2024](#).

The Sixth Assessment of the Working Group III (hereafter WGIII6AR) of the Intergovernmental Panel on Climate Change (IPCC) reports that the cumulative share of North America, Europe, Japan, Australia and New Zealand in anthropogenic carbon emissions amounts to 43% of the global total.<sup>4</sup> With Eastern Asia, which includes China, that share rises to 55%.<sup>5</sup> Given differentiated responsibilities, expecting all countries to contribute to mitigation and adaptation purely on the basis of their own resources is obviously unfair. To the extent that developing countries responsible for a small fraction of cumulative emissions must redesign their development strategies, fairness requires, among other things, that developed countries contribute a reasonable share of the expenditures needed to facilitate the transition.<sup>6</sup> As WGIII6AR notes, the International Energy Agency (IEA) has noted that as much as two-thirds of future collective climate investments would have to occur in developing countries, which makes cross-border financial flows crucial.<sup>7</sup> Thus, cross-border flows from the “North” to the “Global South” are expected to be a key component of climate mitigation, adaptation, and loss and damage compensation efforts in the less developed and more vulnerable regions of the world. In recognition of this principle, there is considerable, though not exclusive, emphasis in policy and political discussions on climate finance, on the measurement of cross border flows.<sup>8</sup> However, progress on deciding the needed volume of such transfers has been far from satisfactory, and actual flows have been woefully inadequate, even negligible in relation to the need. This has enabled vague and even misleading characterizations,

**Clearly, a first and essential step in ensuring adequate climate finance is a clear, comprehensive and globally accepted definition of what it is. It is all the more remarkable that in the dozen years since the first promises for providing climate finance to developing countries were made in 2009, there is still no agreement on such a definition.**

whereby donor countries have effectively been free to designate anything they deem to be directly or indirectly contributing to mitigation or adaptation, as “climate finance”. As a result, a Reuter investigation of 2021<sup>9</sup> showed that claims of providing climate finance have included a subsidy for a retailer to open chocolate and gelato stores across Asia, a loan for a coastal hotel expansion in Haiti, a subsidy for producing a film of a love story set in an Argentine rainforest, finance for a new coal plant in Bangladesh and airport expansion in Egypt. In other words, any project that purportedly uses “green technology” or even promotes mitigation however indirectly, has been clubbed under climate finance by donor countries, even when it comes in the form of relatively expensive loans. This makes navigating the landscape of actual climate finance even more complicated. The demand for a precise and easily verifiable definition of climate finance that is accepted by all parties is therefore urgent.

<sup>4</sup> Intergovernmental Panel on Climate Change, [Sixth Assessment Report Working Group III Summary for Policymakers](#) (2022) Figure SPM.2

<sup>5</sup> Intergovernmental Panel on Climate Change, Sixth Assessment Report Working Group III Summary for Policymakers (2022) Figure SPM.2

<sup>6</sup> In a 2022 report, Nicholas Stern, Amar Bhattacharya and Vera Songwe estimated that spending on climate-related goals in emerging and developing countries (excluding China) would need to increase four-fold to reach \$2.4 trillion per year by 2030. Of this, in their view \$1 trillion per year would need to come from “external” sources, including \$500-600 billion from private businesses, \$250-300 billion from development banks and \$150-200 billion from other countries in the form of “**concessional and debt-free finance**”. Report of the Independent High Level Expert Group (IHLEG) on Climate Finance, November 2022, <https://www.ise.ac.uk/granthaminstitute/wp-content/uploads/2022/11/IHLEG-Finance-for-Climate-Action-1.pdf>.

<sup>7</sup> Intergovernmental Panel on Climate Change, [Sixth Assessment Report Working Group III Chapter 15 Investment and Finance](#) (2022) 1558.

<sup>8</sup> See for example the report of the Independent High Level Expert Group (IHLEG) on Climate Finance, and Oxfam, “Climate Finance Shadow Report 2023: Assessing the delivery of the \$100 billion commitment”, 5 June 2023, <https://oxfamlibrary.openrepository.com/bitstream/10546/621500/19/bp-climate-finance-shadow-report-050623-en.pdf>. The IHLEG concluded in 2022 that developing and emerging countries – excluding China – need to invest \$2.4 trillion every year, by 2030, to meet their climate goals—a fourfold increase from current levels.

<sup>9</sup> [A Reuters Special Report: Rich nations say they're spending billions to fight climate change. Some money is going to strange places.](#)

# Distinguishing between public and private climate finance flows



Not all climate finance flows are of the same nature. All actors engaging in economic activities that directly or indirectly contribute to carbon emissions are expected to contribute their share to expenditures aimed at curbing carbon emissions, reducing the damage created by changes in climate patterns through adaptation, and compensating for the loss and damage that is occurring and will occur because of past and ongoing global warming. Thus, the source of climate finance flows—both national and international—can be broken down by category of actor. The broadest level of that breakdown is between “official” or “public” sources of climate finance flows, and private flows. This distinction is partly because of the coexistence of public and private actors in economic decision-making, as all market economies today also have a substantial state presence. It is also because economic activities differ in terms of the net monetary returns or surpluses they generate: some offer average, above average or well above average returns; others offer less than average or miniscule monetary returns; and yet others offer no monetary returns.<sup>10</sup> Private actors making expenditures for profit will fight shy of investing in projects that offer no or low returns, or of undertaking expenditures, such as on emission reduction, that increase costs with no financial returns. They would also be unwilling to invest even in areas with prospects of reasonable profits, if there are investments with higher returns elsewhere, or if the risk that those profits will not materialise is also substantial or high.

<sup>10</sup> To quote Avinash Persaud former Special Envoy to the Prime Minister of Barbados on Climate Change and one of the architects of the Bridgetown Initiative: “While it is not always so, much climate mitigation and in particular the all-important energy, transport and agriculture transformation, generates revenues. With the help of our Global Climate Mitigation Trust then, mitigation can be funded primarily by the private sector. However, much climate resilience and adaptation does not have a revenue stream and can only be financed by the public sector. Given how little fiscal space developing country governments have we would love the private sector to do resilience too. There is much resistance to this conclusion from those who believe in the omnipotence of private capital. I can’t count how many times people outside developing countries have said that ‘resilient seeds’ proves me wrong. The cold reality is that the biggest ticket items in resilience costs are defences against sea-level rising, salinity intrusion and floods, more resilient road and bridge infrastructure and water conservation. Most hard-core climate resilience and adaptation costs cannot be shifted to a private sector or third balance sheet. It rests on government balance sheets where space is limited, cost of capital is high and as a result too little adaptation is being done. Loss and damage are rising exponentially as a consequence.” Avinash Persaud, “[Breaking the Deadlock on Climate: The Bridgetown Initiative](#)”, After Cop 27: Geopolitics of the Green Deal, Issue #3, Groupe d’études géopolitiques.

**By contrast, governments and other ‘public’ or philanthropic agents should be willing to forego pecuniary returns, if the expenditures concerned yield considerable social returns and/or deliver benefits to the public and the society at large, for which they are not expected to pay or be made to pay.**

Private agents would undertake such expenditures either when they are compelled to do so (for example through regulation) or are ‘incentivised’ with tax breaks, subsidies or other incentives, the transfer of risks to a third party, or compensation for any shortfall in profits from what is perceived to be ‘normal’.

A fundamental problem is that in market-based systems with a dominant role for private investments, accounting rules do not capture benefits for which there is no ‘market’ that offers a ‘price’ for those benefits that allow them to be monetised. For example, besides investments in renewable energy projects, where there is evidence of private (as opposed to social) returns (after accounting for implicit and explicit state subsidies) that are high enough to attract private investment, there are a large number of both climate mitigation and adaptation projects where private returns are low or absent. This is definitely the case with adaptation, where projects are preventive in nature and there is no clear principle to capture the value of the adverse effects that have been preempted. Even in the case of agriculture, which is estimated to account for close to 13–21 percent of greenhouse gas emissions (including land use change and livestock rearing), the private returns from mitigation measures are considered low. In these cases, while social benefits are large and cross-generational, most yield low or no profits; and even when they yield profits, they are associated with considerable risk.

This requires public agents or the public sector in general to play a major role, especially in low-profit or no-profit activities, since the state can factor in non-pecuniary gains when evaluating spending, as well as ‘cross-subsidise’ by taxing profitable activities to finance non-profitable ones. For that reason, the breakdown of national flows and international flows into flows from public and private sources is important. Public flows must necessarily be a large component of the total, given that low- or no-pecuniary return projects are likely to dominate adaptation, be present in mitigation investments, and loss and damage compensation falls in the no-return category by definition. Not surprisingly, only 1.6 percent of currently adequate adaptation funding comes from the private sector.<sup>11</sup> The presence of low- or no-return investments implies that many projects would not be able to raise the revenues needed to cover the costs of non-concessional, commercial credit. They would need to be financed with concessional credit or grants. So, within public flows, climate finance must have large components in the form of pure grants or concessional loans, rather than commercial loans or other instruments associated with significant charges.

In the case of both public and private sources, there are multiple institutions that serve as channels for the flow of climate finance. These institutions and their relative roles define the architecture of climate finance. Public finance can come directly from government, or be mediated through development banks that leverage seed capital and guarantees from the government to mobilise large sums from the ‘market’—private savers, high net worth investors and investment institutions—or through special vehicles established to channel climate finance. This is true for international (global and regional) as well as national sources.

<sup>11</sup> However, some see this as an aberration and argue, partly speculatively, that there are unutilised opportunities for profitable adaptation investments, and the low figure in fact signifies an opportunity. See for example, World Economic Forum, [Climate adaptation: the \\$2 trillion market the private sector cannot ignore](#), 1 November 2022.



# The crucial role of private climate finance



## Despite its prioritisation of profit over social benefits, the private sector must play a major role in the financing of climate mitigation and adaptation efforts.

The financing estimated to be needed to meet the goals set by the Paris Agreement is in “trillions of dollars,” and the low amounts and slow pace of current investment makes the requirements even higher over time.<sup>12</sup> At the same time, the share of the recorded profits of private actors in the economy-wide surplus (or the difference between revenues and normatively estimated warranted costs, which exclude potential surpluses that are diverted to wasteful consumption and unproductive expenditures) is high and has risen sharply in recent decades. If a significant share of those surpluses is not channelled into climate related activities, even modest climate alleviation goals are unlikely to be achieved. Therefore, almost all climate finance discussions refer to the required strategies to divert private finance to climate-friendly projects.

However, the task is made difficult not only because of the profit orientation of the private sector. Additionally, there is a proliferation of agents intermediating the flow of private financial surpluses, wielding instruments that are often designed to reveal as little as possible about their role and location.<sup>13</sup> The complexity of finance arises from the layered architecture of most “structured” financial transactions. Such structured arrangements are frequently used in the “innovative financial packages” aimed at drawing in private capital into unconventional areas like climate finance. Given the layers in a structured transaction, there are many players involved, each of which needs to be paid for the “expertise” it brings for the specific service it renders. These payments generate revenues and profits for the agents but add to the costs of the transaction. If the final project needs to be subsidised in order to make it viable, these additional costs would have to be covered, necessitating even larger public financial support to ensure execution. Such subsidies are also implicit in the derisking arrangements through which the public sector takes over and reduces private risk. Public sector agents not only have to absorb some (often the major part) of the risk, but subsidise the private sector simply to enable the transaction to go through.

<sup>12</sup> This argument is backed by estimates that the vast majority of the world’s financial assets, currently valued at roughly \$470 trillion, are privately held. Redirecting just 1% of these resources toward climate and development initiatives would go a long way. But often such estimates are used to argue that governments cannot come up with similar resources and therefore public monies should be used to incentivise and mobilise private investment. See Jayati Ghosh, “The ‘Billions to Trillions’ Charade”, Project Syndicate, 14 May 2024.

<sup>13</sup> These are complex derivative instruments deriving their value from layers of underlying assets, the most infamous of which were the collateralised debt obligations and credit default swaps that lost value during the North Atlantic financial crisis of 2008.

A typical example is the Espejo de Tarapacá renewable power project in the Atacama desert in Chile, which is designed to produce 300 megawatt of pump-storage hydroelectricity and 541 megawatt of solar power. Given the risks involved, private investors were unwilling to take it up. So the multilateral Green Climate Fund (GCF) provided \$60 million in direct equity to cover development expenses and facilitate a power purchase agreement with distribution companies in order to attract private investment.<sup>14</sup>

Such use of public resources is meaningful only if the ratio of private capital mobilised to the public resources expended is significant and economically defensible. The subsidy implicit in state-mediated power purchase agreements must be transparent and reasonable. And, the diversion of state resources to derisk public-private partnerships must not substantially curtail funds needed for projects in which the social benefits are high but the private sector would not choose to participate because of the low returns even after derisking support.

Plain vanilla debt, bonds, equity and insurance products are titles that are woefully inadequate to categorise and classify flows of private capital, which are mediated by increasingly opaque instruments. These private financial flows are underregulated and inadequately monitored. This helps private players skirt regulations designed to make them contribute a socially designated share of their surpluses to resolve the problems that they have historically contributed significantly to making.

**It is now evident that if private finance is to contribute in meaningful ways, this requires more than relying on the current trends in superficially “innovative” ways of making climate financing both socially beneficial and reasonably profitable.**

Recently ESG investing has come under attack, including from financial industry insiders. The problem is that projects that are actually meeting Environmental, Social and Governance (ESG) goals are inherently not all that profitable.<sup>15</sup> By implication, if the funds claiming to go into ESG projects are profitable, as many are, it is possible that they are not going to targets that can make a real difference to carbon emissions or adaptation on the ground. There are claims that evidence to the contrary has been manufactured.<sup>16</sup> Non-standardised ratings that provide ESG compliance scores to funds and projects are used to back claims of pursuing and realising social and climate goals.<sup>17</sup> The success of the ESG funds in delivering higher-than-benchmark returns, delivering profits to Wall Street and bonuses to fund managers, is presented as success in pursuing ESG goals. Highlighting such concerns, Tariq Fancy (who served as global asset manager BlackRock Inc.’s chief investment officer for sustainable investing) is of the view that the financial services industry that has promoted ESG investing, persuading environmental and social activists that big business can do good for the planet and redress inequality without damaging corporate bottom lines and depriving finance of lucrative margins, is “duping the public.”<sup>18</sup>

<sup>14</sup> See for example, Esther Sekyoung Choi, Lihuan Zhou and Valerie Laxton, “[How to De-risk Low-carbon Investments](#)”, July 2022, in World Resources Institute Insights, for a discussion on this and other examples. See also, Dhruba Purkayastha and Neha Khanna, “[Blog: Ways to de-risk Climate Finance](#)”, Climate Policy Initiative 2022.

<sup>15</sup> C. P. Chandrasekhar, [ESG Investing: A costly distraction](#) (2021).

<sup>16</sup> Tariq Fancy, [Financial world greenwashing the public with deadly distraction in sustainable investing practices](#) USA Today (2021).

<sup>17</sup> C. P. Chandrasekhar, [ESG Investing: A costly distraction](#) IDEAs (2021).

<sup>18</sup> See Tariq Fancy, “[The Secret Diary of a Sustainable Investor](#)”.

<sup>19</sup> See for example Andre Standing, [Sovereign ESG bonds in the global south: 10 questions for those concerned about debt and climate justice](#), Eurodad November (2023).

<sup>20</sup> Based on seven case studies stretching from Spain to Nepal, a Eurodad study found that “PPPs have failed on many different levels, with serious negative impacts on the citizens.” In addition: “All the cases studied came at a high cost for the public purse, an excessive level of risk for the public sector.” Eurodad (2022), [History RePPeated II: Why Public-Private Partnerships are not the Solution](#).”

Other studies have shown that ESG bonds do not always offer lower interest rates for low income country borrowers, are not transparent when it comes to assessing whether they actually deliver on environmental or social targets, and very often misrepresent benefits to win investor support.<sup>19</sup> The damage is not merely the failure to deliver on promises made to ethically concerned investors and the activists who lobby them. It is also to the climate cause itself, because the ESG movement is “a deadly distraction,” holding back the needed state action and regulation, in the belief that an ethical corner of the market would substantially deal with the crises on the climate, environment and social fronts that are crying for urgent attention.

The least that is needed, therefore, is that when public monies – national or international – are used to subsidise or derisk climate projects, there must be a monitoring and regulatory framework in place that ensures the “green” promises of the projects concerned are actually delivered. This in turn requires open and transparent information access, monitoring of the process and verification of the results. Often the bulk of the costs of climate investments are borne by public agents, but the results are meagre or absent, leading to complaints about “greenwashing.”<sup>20</sup> Working towards and ensuring genuinely useful climate finance innovation in drawing private finance to the climate arena—to achieve concrete climate mitigation and adaptation goals, vital to societies around the world—will require dealing with such dynamics, which can undermine key policy intentions



# The current financing gap –why is it still so wide?



Over the years since the first assessment report of the Intergovernmental Panel on Climate Change (IPCC), the ways to mitigate climate change by reducing greenhouse gas (GHGs) emissions and adapt to now-unavoidable changes have been set out in much detail. What has been less clear is how much finance is needed to achieve this goal and how much is actually being channelled for the purpose. The IPCC addressed the issue of financing in a dedicated chapter for the first time in 2014 in the report of Working Group III of its fifth assessment.<sup>21</sup> That discussion flagged the absence of a clear definition and estimation of climate finance flows, as noted above. Even though the 2015 Paris Agreement called for aligning financial flows to climate goals, Chapter 15 of the WGIII6AR notes that the absence of a clear definition of “climate finance” is “a difficulty that continues.”<sup>22</sup> Even given this serious deficiency, the available partial and imperfect data suggest that to meet assessed needs, yearly flows of climate finance would have to rise four- to eight-fold in developing countries, and two- to five-fold in rich countries.<sup>23</sup> Addressing such a huge shortfall definitely requires, in the first instance, more accessible, reliable and granular information.

Any useful evaluation of climate finance flows must estimate the actual volume of such flows and compare it with needs to achieve a specific target in terms of a ceiling on global warming in the future.

While assessing needs is likely to be controversial given differences even on the trajectory to be pursued by each country and its timeline, tracking actual financial flows should in principle be easier. But even this exercise is riddled with difficulties. To be relevant, it must separate out climate-specific finance that delivers climate benefits within and outside a source country. But as noted above, agreeing on which projects are climate-relevant, the kind of flows to count and the standards these flows must adhere to has proved to be difficult.

Recognizing the crucial role of finance in realising the climate agenda, Article 2.1(c) of the Paris Agreement called for “making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.” However, the principle that a reasonable share of these flows must be public was not emphasised. The Paris Agreement implicitly flagged the role of governments by including a rather general statement that “(d)eveloped country Parties shall provide financial resources to assist developing country Parties with respect to both mitigation and adaptation in continuation of their existing obligations under the Convention.” But instead of emphasising the flow of public finance from developed to developing countries, it called on the developed countries “to take the lead in mobilising climate finance from a wide variety of sources, instruments and channels, noting the significant role of public funds,” whatever that may mean in practice.

<sup>21</sup> Intergovernmental Panel on Climate Change, [Fifth Assessment Report Working Group III, Chapter 16 Cross-Cutting Investment and Finance Issues](#) (2014).

<sup>22</sup> Intergovernmental Panel on Climate Change, [Fifth Assessment Report Working Group III, Chapter 16 Cross-Cutting Investment and Finance Issues](#) (2014) 1210.

This vagueness has enabled a huge shrinking of the commitments made by developed country governments for targeted provision of climate finance—specifically the volume of public financial resources deployed to support developing countries. As far back as 2009, at the 15th Conference of Parties (COP 15) held at Copenhagen, participating countries signed an accord that included a financial promise on the part of the developed countries: “In the context of meaningful mitigation actions and transparency on implementation, developed countries commit to a goal of mobilising jointly USD 100 billion dollars a year by 2020 to address the needs of developing countries. This funding will come from a wide variety of sources, public and private, bilateral and multilateral, including alternative sources of finance.”<sup>24</sup> This clearly sidestepped the issue that it is public finance that is crucial and must be an important component in climate finance.

**The WGIII6AR reports that data from the Biennial Assessments of climate finance flows of the UNFCCC and the IPCC’s Special Report on Global Warming have placed the financing needs over the 2020-2030 period in order to contain global temperature rise to below 2°C by 2100 at \$1.7 trillion a year.<sup>25</sup> This excludes adaptation finance and financing to cover loss and damage, and is at best a conservative estimate of even mitigation financing needs. This makes the \$100 billion a year by 2020 committed at Copenhagen around 5% or less of what is required for mitigation alone.**

It is telling that even this low-ambition target has not been realised. According to estimates from the OECD, in 2021, total climate finance provided and mobilised by developed countries to developing countries was \$89.6 billion. Not all of this is public, and less than half is in the form of grants or concessional loans.<sup>26</sup> This also includes private finance said to be mobilised by public loan guarantees and loans given alongside private funds. Oxfam estimated that if only public finance is considered, and within that only grants and the grant equivalent of lending, the figure on transfers for climate falls to as low as \$19-22.5 billion in 2017-18.<sup>27</sup> Pledges for the second replenishment of the Green Climate Fund, the largest climate-dedicated multilateral fund, have been underway since the 5 October 2023 pledging conference. As of 30 June 2024, the sums committed had reached only \$9.3 billion from 45 countries.<sup>28</sup> This compares with \$10.3 billion that was pledged by 45 countries when the fund was created in 2014, and the \$10 billion committed by 32 countries during the first replenishment in 2019.<sup>29</sup> Though more pledges may be forthcoming, the failure to mobilise even a nominally higher sum for the second replenishment so long after the pledging conference is telling.

<sup>23</sup> United Nations Conference on Trade and Development, [World Investment Report](#) (2023) and United Nations Environment Program, [Adaptation Gap Report](#) (2022).

<sup>24</sup> United Nations Framework Convention on Climate Change Decision 2/CP.15 Copenhagen Accord.

<sup>25</sup> Intergovernmental Panel on Climate Change, [Sixth Assessment Report Working Group III Chapter 15 Investment and Finance](#) (2022) 1555 and Intergovernmental Panel on Climate Change, [Special Report on Global Warming of 1.5°C Chapter 2 Mitigation Pathways Compatible with 1.5°C in the Context of Sustainable Development](#) (2018).

<sup>26</sup> OECD, [Climate Finance Provided and Mobilised by Developed Countries in 2013-2021](#) (2023).

<sup>27</sup> Oxfam America, [True value of climate finance is just a third of that reported by developed countries](#) (2020). The OECD’s estimates have also been criticised for including committed or pledged rather than actual flows, and for being self-reported without any independent verification. Moreover, not all of these flows are “additional” as opposed to being the result of reclassification of parts of development aid.

<sup>28</sup> <https://www.greenclimate.fund/sites/default/files/document/2024-status-pledges-website-june-30.pdf>.

<sup>29</sup> Green Climate Fund, [Resource Mobilization](#).



There are claims that the \$100 billion official climate finance target set for themselves by the developed countries was achieved in 2023. And while there is talk that the \$100 billion figure will be exceeded thereafter<sup>30</sup> there is no assurance that the shortfall relative to the \$100 billion a year was made up with additional contributions in the years to 2025. Moreover, the much-needed step up from the \$100 billion figure is unlikely to materialise in 2025, even though global inflation in the years after the initial declaration has reduced the real value of committed amounts significantly. (Note that how much of this constitutes actual climate finance is still unclear.)

What we have is a cumbersome process to discuss and arrive at a higher annual financing number, a “new collective quantified goal,”<sup>31</sup> and there is as yet no indication of where that number would lie relative to needs estimates and what kind of financing that number would incorporate. An independent assessment of ongoing negotiations concluded the “deliberations on the new goal have been slow to date. Negotiators have yet to reach consensus on foundational questions, from the dollar amount of the goal to which countries should contribute.”<sup>32</sup> A summit convened by French president Emmanuel Macron in Paris in June 2023, sought to arrive at a “pact” between the global north and the global south to establish a new, fairer financial system. The outcome of the event was, however, underwhelming, and it has had little impact on the ongoing negotiations.

<sup>30</sup> Jo Lo, [Rich countries 'confident' \\$100bn climate finance delivered in 2023](#) Climate Home News (2023).

<sup>31</sup> For a full overview of COP-26 climate commitments see Heinrich Boll Stiftung, [“Glass less than half full” – Glasgow climate finance outcomes leave much room for improvements despite some wins](#) (2021).

<sup>32</sup> <https://www.wri.org/insights/ncqg-key-elements>.

The composition of cross border flows, in terms of public-private flows, and grants, concessional loans and credit on commercial terms, is also not inspiring. To start with, multilateral development banks, led by the World Bank dominated by the US, account for nearly two-fifths of the climate finance provided in recent years.<sup>33</sup> Given the conditionality associated with such lending, which is substantially on commercial terms, and the limited voice of vulnerable countries in decision making, reliance on this channel rather than special climate dedicated organisations within the UNFCCC framework is an issue.<sup>34</sup>

On the other hand, a consequence of the failure of the developed countries to provide adequate financing through grants and concessional credit is a shift of focus towards mobilising private finance. The emphasis is now being placed on using available public finance to mobilise private finance. According to WGIIIAR6, a crucial priority is to “expedite the operational definition of blended finance and promote the use of public guarantee instruments.”<sup>35</sup> This is because “[p]rivate flows to accelerate the low-carbon transition in developing countries would benefit enormously, by gaining clearer access to public international funds and support defined on a grant equivalent basis.”<sup>36</sup> However, as noted earlier, the evidence on blended finance and public-private partnerships thus far is not encouraging.

**A recent IMF report<sup>37</sup> points out that, to ensure a fivefold increase in green energy investments to \$2 trillion annually by 2030 to achieve net zero emissions by 2050, emerging markets will need the private sector to supply between 80 and 90 percent of that capital. But the private sector is currently funding only 40% of green energy investment in developing nations.**

In sum, more than 15 years since the Copenhagen Accord and almost ten years since the Paris Agreement, the developed country record of meeting their responsibility to advance a fair share of needed climate finance has been disappointing, if not dismal. This poor track record is further illustrated by the NCQG established at COP29 aiming for at least \$300 billion annually from developed countries by 2035 - a target which is unfortunately not sufficient to meet the needs of developing countries. This is despite their capability to provide such finance. In this context, it is unsurprising that the drive originating from the developed countries (which have contributed disproportionately to greenhouse gas emissions) to get developing countries to embrace net-zero strategies and phase out fossil fuels is seen to lack legitimacy and has received insufficient support. Climate finance does not appear to be a joint responsibility as it is meant to be, and the basic principles of Global Public Investment that should apply to what is clearly a global public good are rarely invoked and never sought to be applied.<sup>38</sup> Developing countries like India increasingly link their climate commitments and targets to certain levels of cross-border financial flows they must receive. And developed countries talk of measures that suggest that the flow of new grant money is not the priority. Against such a backdrop, the international foundation for the plans and strategies being advanced to limit global warming—necessitating sufficient and defined flows of climate finance—is weak or missing.

<sup>33</sup> <https://www.carbonbrief.org/qa-did-world-bank-and-imf-spring-meetings-help-to-scale-up-climate-finance/>.

<sup>34</sup> However, the IHLEG suggested that MDBs need to collectively triple their annual lending volumes to \$180 billion over the five years starting 2023. They provided \$60.9billion to developing countries in 2022.

<sup>35</sup> Intergovernmental Panel on Climate Change, [Sixth Assessment Report Working Group III Chapter 15 Investment and Finance](#) (2022) 1560.

<sup>36</sup> *ibid.*

<sup>37</sup> See <https://www.imf.org/en/Blogs/Articles/2023/10/02/emerging-economies-need-much-more-private-financing-for-climate-transition>.

<sup>38</sup> See <https://globalpublicinvestment.net/what-is-gpi/> for a brief overview of these principles.

# The need for technology innovation and scalable solutions



The inadequate financial response to the climate challenge has been associated with some efforts to develop new technologies to address the problem, to scale up new innovations to make them effective and to deploy these technologies in all contexts where they are needed. Two kinds of innovations are seen as crucial in the battle to combat global warming and erosion of biodiversity. The first consists of technological innovations across a diverse set of areas varying from renewable energy technologies at scale to carbon capture and sequestration mechanisms.

**The other is financial innovation, ranging from the use of public funds to trigger large private investments that deliver verifiable results to swapping debt for nature or climate. In practice, the effort at generating and deploying such innovations needs to be pursued in simultaneous and combined fashion.**

Progress in arriving at scalable and cost-effective technological solutions in the many areas in which research and development has been underway, has been uneven. Some potentially breakthrough technologies like carbon capture and sequestration are still at a very incipient stage. Few have progressed to deliver cost effective solutions, let alone delivering reasonable pecuniary returns while ensuring climate or biodiversity gains, and the possible unanticipated effects of such technologies are still inadequately studied. Progress is needed in three related areas. First, there is a need to ensure adequate financial flows and the provision of significant incentives to accelerate technological innovation. Second, there is a need to provide access to these technologies at low cost or free of cost to all players, especially those in developing countries. And, third, there is a need to mobilise public resources to ensure innovation and the deployment of innovative technologies in areas where social returns are high but private, monetary returns are low or non-existent.

One danger when pursuing these objectives is that valuable resources may be diverted to projects that have been “greenwashed” and claim to deliver benefits far in excess of those that they actually provide.<sup>39</sup> Hence, along with the effort to incentivise technological innovation and deployment, it is crucial to develop monitoring and verification mechanisms and a regulatory framework to ensure that the promised benefits are real and present, and that adverse consequences are limited.

<sup>39</sup> See for example Florence Jones, [UN secretary-general calls out carbon capture as greenwashing](#), *Offshore Technology* (2023).



# Incentives for technology investment to accelerate climate solutions



Historically, governments in market economies have resorted to a range of measures to accelerate technological innovation, often as part of an effort to develop and/or strengthen national technological capabilities. Incentives can activate climate conscious technological development in multiple ways. They can accelerate development of products and services that emit less carbon and substitute them for high emitting sources currently in use. They can help develop less emission-intensive inputs for use in emission intensive processes. And, they can encourage development of processes that reduce pollution intensity per unit of output. The global evidence suggests that accelerated depreciation allowances for low carbon emitting technologies and tax credits or subsidies for Research and Development encourage development of lower-emission inputs and incentivise efforts to reduce pollution intensity. It can be argued that imposing a price on carbon emissions through appropriate taxes could discourage use of high-emission technologies and encourage innovation of low-carbon technologies, but such measures can have predictable and unexpected adverse collateral effects, such as raising the costs and challenging the viability of activities employing significant numbers of workers and adding to international inequalities.<sup>40</sup>

A still ongoing experiment at deploying such measures in the interests of forcing the pace of climate-related innovations and their deployment is the Inflation Reduction Act of 2022 in the US. The Act provides for \$373 billion in spending to support “energy security, climate change and drought resiliency,”<sup>41</sup> using the money either to spend on infrastructure or to provide incentives to trigger private investment in climate-friendly projects. Estimates place

the reduction in emissions relative to 2005 on account of the IRA at 40% by 2030.<sup>42</sup> While this is far from an adequate reduction for the US, it is nevertheless a significant step forward, though it is as yet unclear the extent to which the current administration will hamper efforts to implement the IRA. Even with the uncertainty posed by the current administration, the Act had already disappointed critics because it also commits funding for fossil fuel infrastructure, but promises to ensure heavy investments in renewable energy and thereby contribute to progressive “green growth.”<sup>43</sup> According to an estimate by the Political Economy Research Institute, the implementation of the provisions of the Act would lead to the creation of 9 million jobs over a decade.<sup>44</sup> The redistributive frame of the Act is also reflected in the provisions to fund the programme by imposing a minimum tax of 15 percent on the biggest corporations, levying a small tariff on corporations that buy back their own stock, and giving the government revenue service the needed resources to fight tax evasion.

Incentives provided by the European Union are similar but of a lesser order. Once again, in Europe as well as in the US, the incentives for climate mitigation investment are smaller than the explicit and implicit subsidies for fossil fuels, a contradiction that reinforces the political complexity of attempts to ensure that finance flows in the socially and environmentally desirable directions rather than to activities that worsen global warming.<sup>45</sup> Meanwhile, with regard to the strategies of both the US and the EU, there are concerns that the attempts to prevent cross-border “free-riding” or exploitation of carbon emission-limiting regulations are associated with protectionist policies that

<sup>40</sup> OECD, Promoting Technological Innovation to Address Climate Change, 2011, at <https://www.oecd.org/env/cc/49076220.pdf>.

<sup>41</sup> [Inflation Reduction Act](#).

<sup>42</sup> Congressional Research Service, [Inflation Reduction Act of 2022 \(IRA\): Provisions Related to Climate Change](#) (2023) 2.

<sup>43</sup> Climate Justice Alliance, [The inflation reduction act is not a climate justice bill](#) (2022).

<sup>44</sup> Political Economy Research Institute, [Job Creation Estimates Through Proposed Inflation Reduction Act](#) (2022).

adversely harm developing country producers even as access to green technologies remains constrained for them.

The country that has made the most remarkable strides in developing “green” technologies, particularly in renewable energy and in electrification of transport, is China—and here it is clear that direct investment by the state combined with subsidies and directed finance provided to private players, along with clear conditions, were the most important factors. What the Chinese experience also suggests is that such a strategy is more effective if it occurs by encouraging competition within a broadly planned framework, recognising the interdependencies across sectors and activities and seeking to ensure that specific supply bottlenecks do not emerge to constrain the process.

In 2020, Chinese President Xi Jinping pledged to reduce his country’s emissions by 65 percent from their 2005 level by 2030 and reach carbon neutrality by 2060. Central to realising this pledge is a transition away from carbon-intensive energy sources to renewables. The 14th Five Year Plan (2021-25) requires non-fossil power generation to account for almost two-fifths of the total power generation by 2025. But the plan is to “establish before breaking,” which requires building low-carbon infrastructure before winding down polluting capacities. The result has been a rapid growth in China’s renewable power capacity, consisting largely of solar and wind capacities, investment in which had initially been supported with massive government subsidies. China has thus taken a place of global leadership in both renewable technologies and capacities. This has reduced the need for subsidies, especially for solar power. Notably, China has not used its developing country status to provide for climate finance from the developed countries in its nationally determined contributions. Instead, in 2015 it established a “south-south cooperation fund” to support the climate efforts of other developing countries.<sup>46</sup>



<sup>45</sup> European Parliament Thinktank, [EU's response to the US Inflation Reduction Act \(IRA\)](#) (2023).

<sup>46</sup> See “The Carbon Brief Profile: China” at <https://interactive.carbonbrief.org/the-carbon-brief-profile-china/>.



# How can private finance and R&D investments support innovation?



As discussed, given the “trillions of dollars” that are needed worldwide for the climate cause, public resources alone cannot help close the gap. Thus climate-related financial innovation and technology deployment efforts aim to draw out private spending and investment for this purpose. In the dominant perspective, getting private investors to park their savings in assets devoted to financing climate-friendly projects requires changing risk perceptions and designing special instruments that assure individual investors of a reasonable hedge against inflation, while providing them a relative return that more than compensates for any possible risk relative to simple bank deposits. But others have noted that this in itself is still insufficient: it is also necessary to disincentivize certain other types of investment that are currently profitable but work against climate goals in the medium term. This essentially means shaping markets in ways that would redirect private investment towards social and planetary goals.

# Catalysing the Role of Financial Institutions



**This may require regulatory and other changes in how both banks and non-bank financial institutions (NBFIs) function. Banks normally abjure directly engaging in such financing because of the liquidity and maturity mismatches involved.**

They mobilise their capital from depositors with a low preference for risk and a high preference for relatively liquid assets. Using that to finance projects that require large loans with long repayment periods raises the possibility that the deposits would be locked up in illiquid assets with extended maturities, which makes banks vulnerable. Moreover, with capital adequacy requirements for banks being tightened under successive versions of the Basel guidelines, they would be less willing to hold assets rated as being of above-normal risk, because they would have to maintain higher volumes of regulatory capital, which increases costs.

However, these difficulties have been and can be partly addressed, with the creation, for example, of specialised institutions such as climate focused national development banks. The need for liquidity does not necessarily require a financial institution to sell an asset (such as a renewable energy or low emission transportation project) when unusual redemption demands from depositors increases the need for liquid resources. What is needed is the ability to convert the financial asset, which embodies the value of the underlying real asset that backs it, to a liquid form. This can happen if such financial assets can be easily traded or provided to an agency like the central bank as the basis for refinancing. Banks themselves can support such institutions. They can invest in bonds issued by an NBFIs (which is barred from accepting public deposits), which in turn can provide the credit or the guarantees that the entity undertaking the sustainable development project needs. If unforeseen liquidity requirements arise, the banks can trade the bond if an active bond market is available, or turn to the central bank for refinance, if the prevailing rules permit. The ability to convert the bond into liquid resources would be even easier if, as part of the sustainable development thrust the government, a regional development bank or a bilateral donor provides an explicit or implicit guarantee for the bond.



An example of using guarantees to help catalyse the long term financing market for infrastructure is a credit enhancement scheme that provides a partial credit guarantee to enhance the rating of the instrument and make it an eligible investment for subscription by entities required to invest in highly rated bonds. Thus, when a special purpose vehicle (SPV) operating an eligible climate-related project issues a bond, a financial institution provides a first loss guarantee raising the bond's rating.

This enables the project to attract funding. Such guarantees have been crucial in mobilising funds to support debt-for-nature swaps through financial packages structured by the private sector.

# Recent Private Financing Initiatives



The effort at channelling private finance to climate-related projects was seen as having received a boost at the COP26 Summit in 2021, when the Glasgow Financial Alliance for Net Zero (GFANZ), chaired by Mark Carney, the then UN Special Envoy on Climate Action and Finance, was launched. This was seen as marking the entry of the world's largest asset owners and managers, controlling over USD\$37 trillion, into the UN's Race to Zero campaign. Identified as "a global coalition of leading financial institutions committed to accelerating the decarbonization of the economy,"<sup>47</sup> GFANZ consists of seven alliances, covering asset owners, asset managers, banks, insurers, investment consultants and other financial services providers. But since then, things have not gone as intended. Some major players unable to meet the commitments required of them have withdrawn from the alliance. By mid 2023, Munich Re and Zurich, two global insurance majors had withdrawn from the Net-Zero Insurance Alliance.<sup>48</sup> Vanguard, which has \$7 trillion in assets under management, left the asset managers' alliance.<sup>49</sup> Two pension funds, Australia's Cbus Super and Bundespensionskasse of Austria, have quit the Net Zero Asset Owner Alliance and the Paris Aligned Asset Owners, respectively. GFANZ is in crisis rather early in its life.<sup>50</sup>

**This does not mean that there are no wealth holders with a conscience who are looking to put their money in projects that do least damage or even do some good.**

Nor is it the case that there are no individual fund managers who are fired by a passion to make the world a better place. It is merely to recognise that a highly concentrated financial system that is geared to maximising returns has found ways of dipping its hands into the ESG investing pot, diverting large sums to projects that yield money but generally do not deliver on the intended goals. Wall Street gains, while humanity and the planet do not get the promised benefits.

It is true that there are efforts underway to improve disclosure and data reporting standards, develop better and standardised ESG scores, and make outcome assessment independent.<sup>51</sup> But as of now, there is not enough progress to see this form of private finance as being of significance. The UN-sponsored Principles for Responsible Investing (PRI) was launched in 2006 and was expected to become the leading standard for sustainable investing. Though voluntary, most of the world's leading pension funds and asset managers signed on. Emboldened by the response, the PRI made the process of reporting compliance to its standards more stringent. This was opposed by stakeholders as being too onerous, and the launch of new reporting requirements had been postponed. Those in charge have admitted the changes were "too ambitious" and apologised for the "mistake."<sup>52</sup>

- <sup>47</sup> Glasgow Financial Alliance for Net Zero, [About Us](#) (accessed 19 March 2024).
- <sup>48</sup> Todd Philips, [Munich Re and Zurich withdraw from Net-Zero Insurance Alliance](#) Green Central Banking (2023).
- <sup>49</sup> Ross Kerber, [Vanguard quits net zero climate effort, citing need for independence](#) Reuters (2022).
- <sup>50</sup> Camilla Hodgson, [Two pension funds quit Mark Carney's green alliance](#) Financial Times.
- <sup>51</sup> OECD, [ESG Investing: Practices, Progress and Challenges](#) (2020).
- <sup>52</sup> C. P. Chandrasekhar, [ESG Investing: A costly distraction Ideas](#) (2021).



# Can carbon pricing mechanisms be deployed to realise climate goals?



It is often argued that the task of raising finance for climate projects can be combined with mitigation efforts. To that end, carbon trading was launched following the signing of the Kyoto Protocol, which required emission curtailment commitments on the part of the developed countries that could partly be met by acquisition at a cost of Certified Emission Reductions (CERs) generated through projects funded in developing countries under the Clean Development Mechanism (CDM). But carbon trading as an instrument for emissions control was undermined by the excessive offsets permitted and the ease of generation of carbon credits because of inadequate verification of their quality. The result was an oversupply of CERs reflected in the low prices of carbon credits. A UN high level panel examining the performance of the CDM in 2012 concluded that it had nearly collapsed.<sup>53</sup> This meant that the carbon market did not play its expected role.

## The European Emissions Trading System (ETS) was created in 2003 to generate market-driven price signals that would influence the volume of emissions by firms.

Higher carbon prices, or the value of one unit of an EU allowance (EUA) that gives the holder the right to emit one tonne of carbon dioxide (or its equivalent of other greenhouse gases), were expected to trigger emissions reduction. Combining that with lower caps on total emissions, it was argued, would help move in the direction of goals for emission reduction being set as part of an effort to keep global warming below 2°C and as close to 1.5°C as possible. If permits to pollute are more expensive, it would make business sense to reduce emission levels, by investing in emission reducing technologies and processes and exiting from emission-intensive sectors.

<sup>53</sup> United Nations Framework Convention on Climate Change, [CDM Policy Dialogue Final Report](#) (2012).

Based on this perspective, a strong market-mediated component as an instrument to curb emissions and limit global warming has been embraced by many governments. High carbon prices in that market are seen as needed to trigger the necessary investments in carbon saving technologies and the transition out of carbon-intensive sectors. In fact, an international carbon-pricing commission chaired by Nicholas Stern and Joseph Stiglitz had argued in 2017 that even with substantially enhanced carbon emission reduction efforts, the social cost of carbon in 2030 would be closer to \$100 a tonne of CO<sub>2</sub> equivalent, as opposed to the \$50 estimate that came from the Obama administration.<sup>54</sup> Putting carbon prices on a trajectory that takes them close to such an appropriate social cost of carbon emissions, triggering an adequate emission reduction response, would require limiting the supply of carbon allowances. If the ambition is right and allowances are reined in, the market can deliver the desired result, the argument went.

However, matters are not as simple. In practice, the prices of EUAs rise not only because of excess demand from those who would use these allowances to neutralise their emissions, but because of the entry of financial firms wanting to play with this new commodity (carbon) and the tradable securities (carbon allowances) deriving from it. Looking to profit from an environment in which enhanced climate ambition is likely to lead to a significant lowering of the cap on the available number of EUAs, they expect the market to tighten and prices to rise into the future. These players—energy traders, hedge fund managers, and banks such as Morgan Stanley, Goldman Sachs and JPMorgan—have been in the carbon market for some time now, often moving in when prices tended to rise and pulling out when prices fell. But the prospect of a tightening of

emission regulations has heightened investor interest. Financial investors are betting on prices rising in the medium and longer term and rushing into the carbon market, pushing up prices even though the current demand-supply balance at the level of actual user firms is not one that would deliver a spike. Once they enter, the spiral of speculation unfolds. Increasingly the activity of these speculative players, rather than carbon credit demands from emitting firms, is the determining influence on the price of carbon allowances. In principle, speculation could be reined in with regulation. But the experience since the banking crisis of the 1980s and through the 2008 crisis indicates that speculators have ways of sidestepping regulation, which itself is difficult to implement.

Recently, Morgan Stanley reportedly advised clients of a “buying opportunity” in EU carbon permits, which have fallen to €52 per tonne, down from a peak of just over €100 last February. Reduced demand from European companies because of high emerging prices and slack economic conditions was reducing total demand, while governments were increasing supply of permits to help companies with lower prices and in the hope of mobilising funds for green investments. That increase in supply was to be ensured by bringing forward the distribution of permits scheduled to be issued in the three years from 2027. Sensing that that would squeeze supply in the years ahead, Morgan Stanley was clearly sensing an opportunity to buy cheap and sell dear. Elsewhere in the UK, the World Carbon Fund of \$330 million managed by Carbon Cap Management, took some short positions aimed at making money as carbon prices fell. A particularly lucrative short was a bet on the UK carbon price, which crashed as the government expanded the permit supply as part of a retreat from green policy.<sup>55</sup>

<sup>54</sup> Stern, N., Stiglitz, J.E., et al, [Report of the high-level commission on carbon prices](#) World Bank. (2017).

<sup>55</sup> See [“Carbon markets: not for the faint-hearted”](#) in Financial Times, March 1 2024.



## For quite some time, the situation in the EU carbon market has been one of excess supply, which kept carbon prices low.

Surpluses began accumulating after 2009 because of the recession that followed the Global Financial Crisis, which brought prices down. The surplus amounted to around 2 billion allowances at the start of Phase 3 of the EU ETS that was to stretch from 2013 to 2020. The problem of excess supply has plagued carbon trading regimes since their inception. Confronted with the problem in 2013, the European Commission decided to hold back the flow of allowances into the system by “backloading” the issue of new allowances, or reducing annual issues during 2014-2016, by postponing the scheduled issue of 900 million allowances to 2019-20. In 2019, the Commission set up a market stability reserve to which a rule-determined number of surplus allowances were transferred, some of which were to be eventually withdrawn if the surplus crossed a certain threshold. Managing the EUA surplus to make ETS effective was the main concern of those overseeing the regime.<sup>56</sup> However, the situation of excess supply was further aggravated by the production declines and demand recession that followed the onset of the COVID-19 pandemic.

<sup>56</sup> C. P. Chandrasekhar, Carbon Markets: Another frontier for finance (2021).

Given this background, the sharp increase in prices witnessed during 2021 was indeed surprising. As noted above, one factor was the role of financial investors, soaking in cheap liquidity, who have rushed into this new 'commodity' or alternative asset. The ETS, established in 2005, is the most developed of carbon markets and the test case. All EU countries and Iceland, Liechtenstein and Norway participate in the ETS, which accounts for close to 90% of the global carbon market valued at Euro 229 billion (\$272 billion) in 2020 by Refinitiv. The ETS also accounts for an overwhelming share of the 10.3 billion allowances traded globally. The rules that apply under the ETS are tightened across phases, with the fourth such phase having begun in 2021. Tightening involves hastening the pace of reductions in permitted emissions, increasing the share of allowances available at a price determined in auctions rather than free of cost, and raising the penalty for non-compliance (specified in dollars per tonne of carbon equivalent). In the fourth phase of the EU ETS, stretching to 2028, the total number of emission allowances will decrease at an annual rate of 2.2%, compared to 1.74% during the period 2013-2020.<sup>57</sup> This is seen as in keeping with the July 2021 decision of the European Commission to legislatively bind itself to achieving net zero emissions in 2050, with an intermediate target of an at least 55% net reduction in greenhouse gas emissions by 2030. To realise the latter, the sectors covered by the ETS must reduce their emissions by 43% compared to 2005 levels.

### **It is this ambition that has whetted the appetite of financial investors, as they expect the heightened emission reduction commitment to support an increase in EUA prices.**

Their intervention amplifies that price increase. It could be argued that by raising EUA prices, speculators play a positive role. But there are two problems here. First, financial investor presence increases price volatility, to a far greater degree than results from changing production and emission levels associated with the business cycle. Periods of recession see a decline in demand for permits and a fall in prices. And demand for EUAs spikes in buoyant economies, raising prices. Superimposed on this 'fundamental' volatility is the volatility which results from the speculative forays of financial investors. Such speculation induced volatility is hardly suited to a smooth market-led transition to a climate-friendly economic structure. Carbon prices that trigger a switch out of, say, coal, could subsequently fall to levels where from a pure profit maximisation perspective the switch may appear completely unwarranted. What such uncertainty would do to business decisions is unclear.

Second, with widely different emission reduction targets and the uneven spread of regulatory carbon trading systems across jurisdictions, businesses in some locations would face greater pressure to transition to high-cost technologies and processes that reduce emissions or shift out of carbon intensive sources of energy supply. European businesses, for example, may find the requirements they face much more stringent than their global competitors, leading to them being outcompeted by imports. This concern has generated pushback from the profit-driven private sector, which in turn can trigger potentially destabilising policy responses.

<sup>57</sup> C. P. Chandrasekhar, Carbon Markets: Another frontier for finance (2021).



One example of this is the EU decision to institute the carbon border adjustment mechanism (CBAM), which, starting 2026, would impose levies linked to the level of EU carbon prices on imports of steel, aluminium, fertiliser and cement seen as originating from factories that do not meet EU emission standards. The EU claims that the levy is not a protective tariff against a nation but a penalty imposed on individual polluting firms. Nevertheless, the initiative threatens to trigger a trade war, with many nations exporting to the EU raising objections to this perceived protectionism.<sup>58</sup> It is particularly resented because it is not being accompanied by financial and technology transfers that would enable developing countries to shift their own production processes more feasibly.

The fundamental problem lies in the position that in an increasingly integrated world of nation states with different laws and rules, carbon markets and the prices they throw up can be expected to incentivise profit-seeking firms to smoothly transit to climate-friendly technologies and sectors. That is difficult in itself, given the fundamental instability of market economies. If in addition, carbon markets are allowed to be distorted by speculative investors who expect to reap profits by out-guessing rivals, volatility and uncertainty are likely to inflict much collateral damage even when the objectives with which those markets were created remain unrealised.



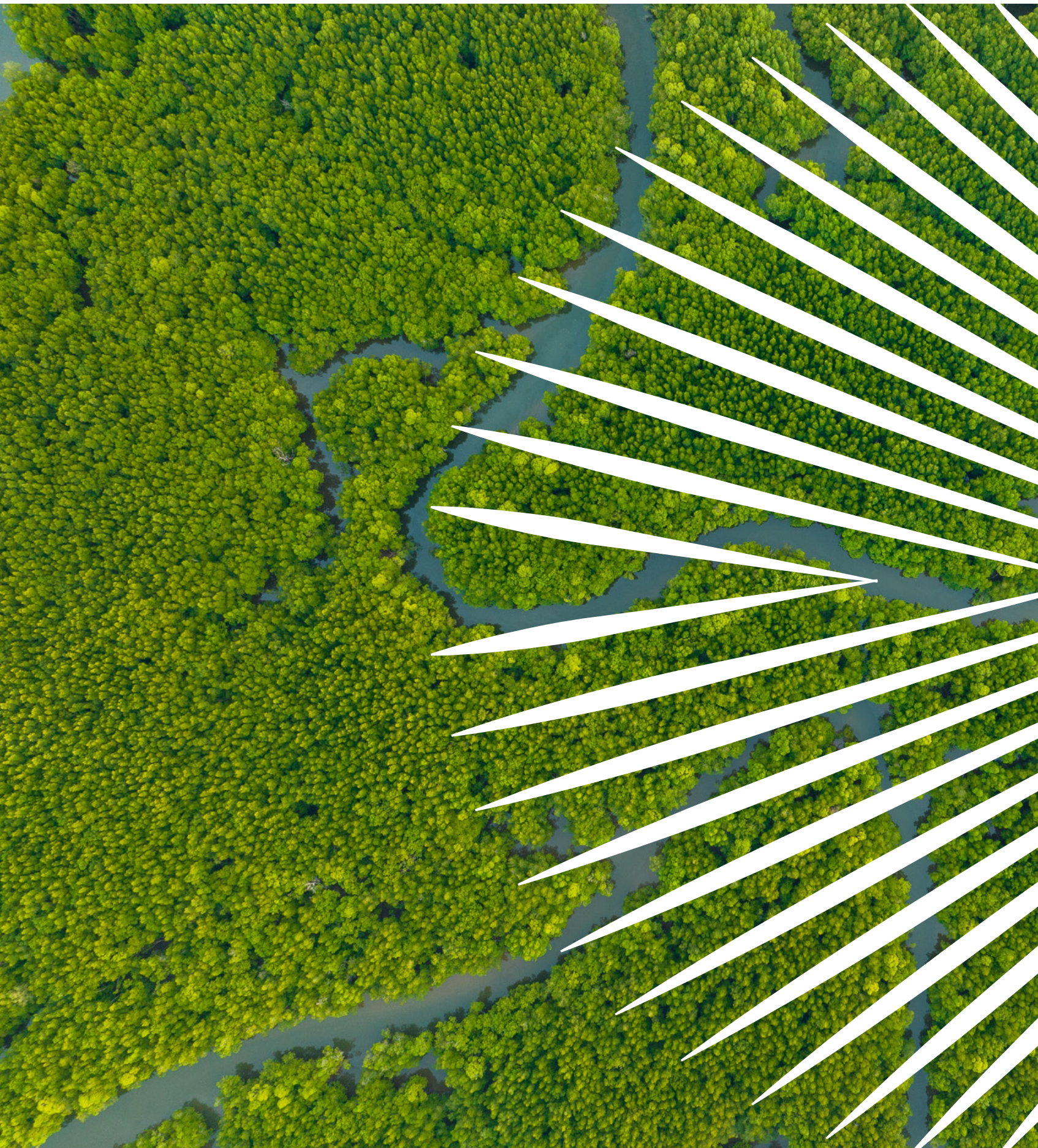
<sup>58</sup> C. P. Chandrasekhar, *Carbon Markets: Another frontier for finance* (2021).

# What can be done: moving to solutions



Brief by C. P. Chandrasekhar and Jayati Ghosh

## Official public flows (both via bilateral and multilateral channels) must be significantly increased and concessional in nature.



The implications of the above brief discussion for climate finance policy are manifold. A central requirement is to enhance the flow of climate finance through bilateral and multilateral channels. The purpose is not just to meet (belatedly) the \$100 billion pledge, and/or to ensure the NCQG is met, but to work out appropriate channels to enable recipient countries to have a voice to direct these funds to the best and most needed projects.

For reasons already discussed, these “official flows”, that are by definition public, must also be concessional in nature.

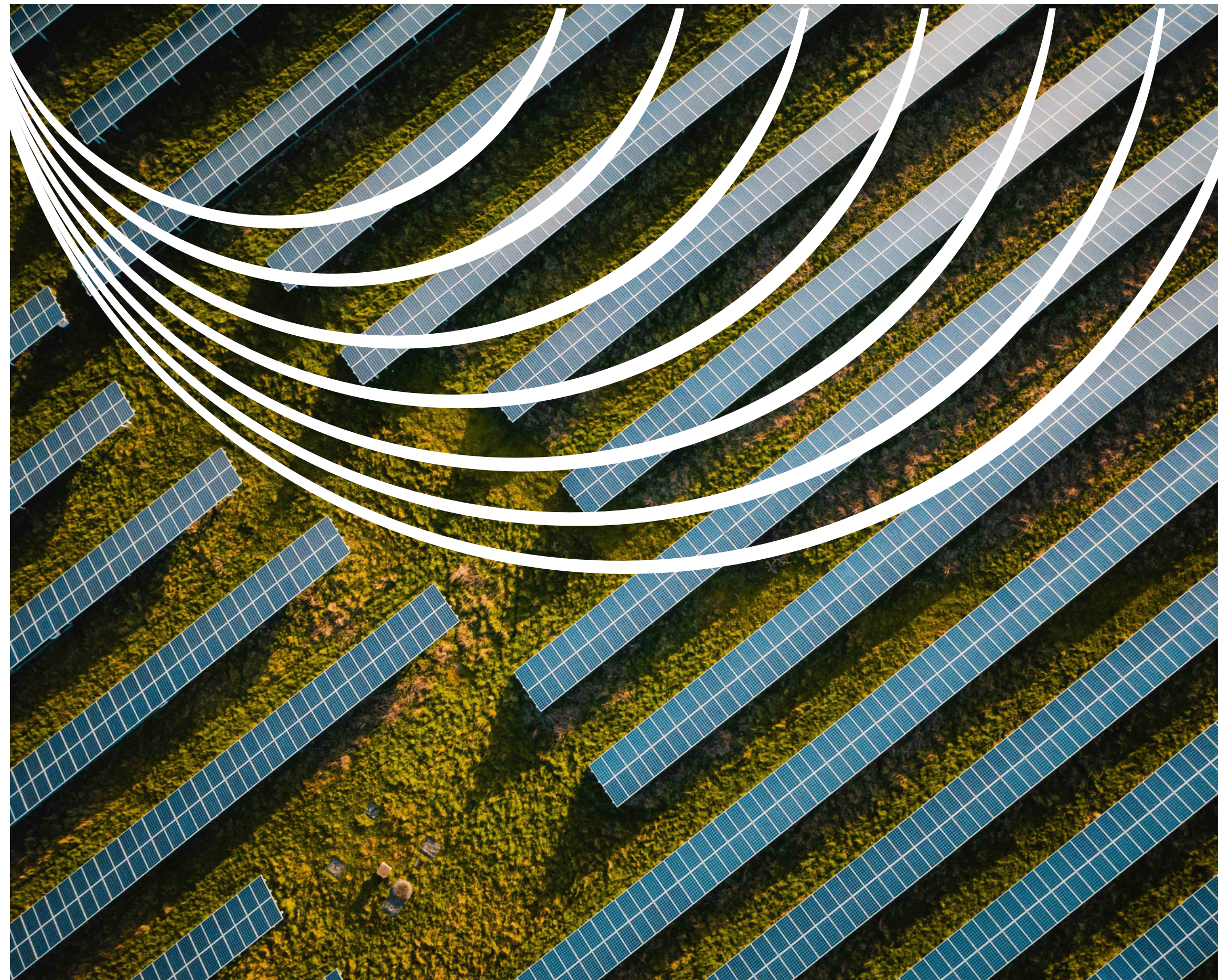
# Multilateral development banks must be seeded with additional capital, and mandated with climate finance goals, and their voting and governance structures reformed.



The existing multilateral development banks, such as the World Bank, also need to be seeded with additional capital, rendered capable (through the implementation of the G20's capital adequacy framework, for example) of leveraging that capital to mobilise additional resources, and mandated with clear climate finance goals. In addition, the long pending reform needed to make the voting and governance structures in these organisations reflective of changes in geo-economic conditions and relative economic position of different nation states needs to be urgently implemented.

A strong empirically grounded view is that the role of these organisations and the International Monetary Fund, has been to institute policies that limit national capabilities to mobilise and independently direct domestic financial resources, increase external vulnerability and undermine resilience, and in contexts of balance of payment stress enforce austerity.<sup>59</sup>

**All of these constrain national spending on mitigation and adaptation, to the detriment of advancing the sustainability and carbon emissions reduction drive.**



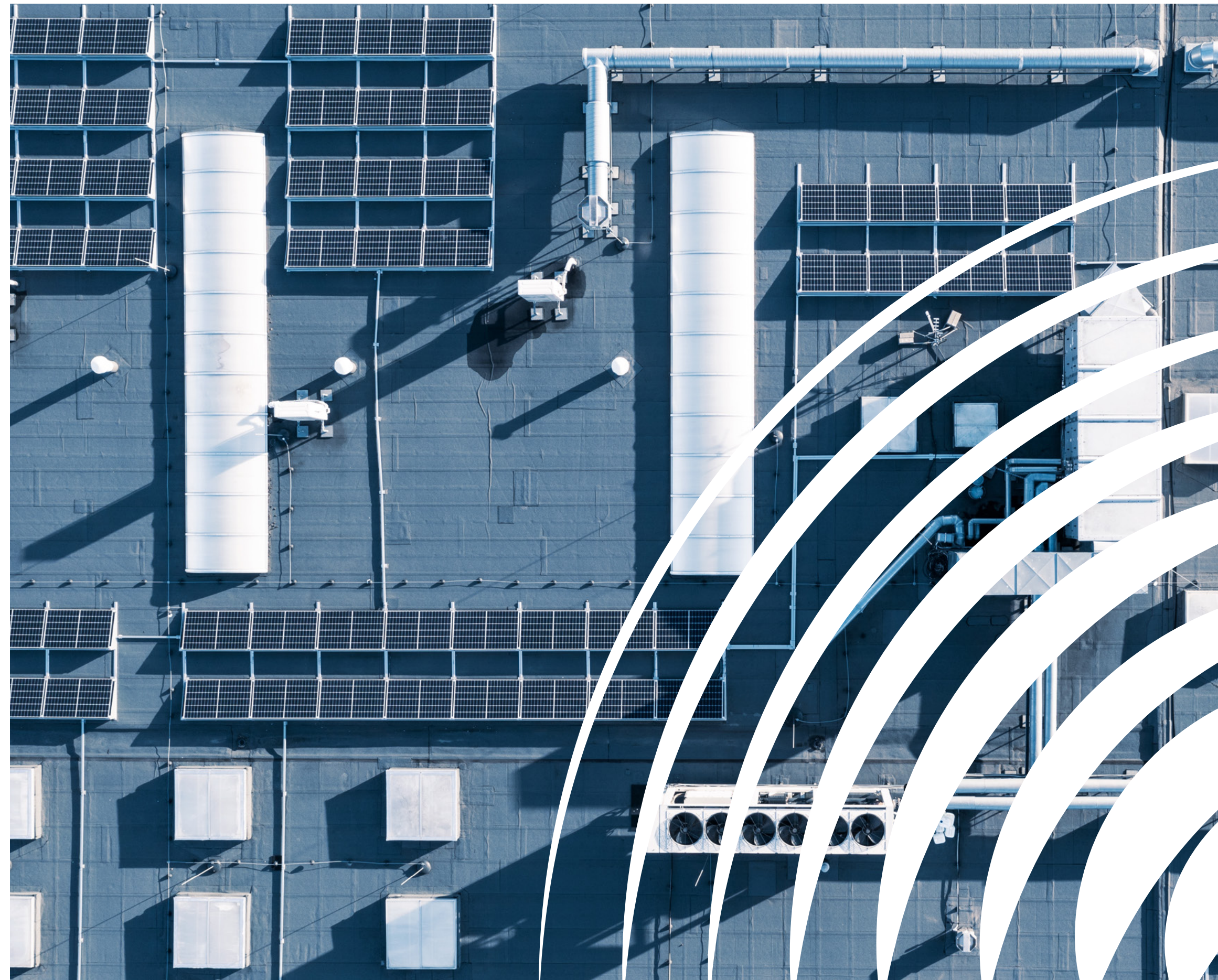
<sup>59</sup> Bretton Woods Project, [What are the main criticisms of the World Bank and the IMF?](#) (2019).

# Global cooperation must support and enable progressive taxation strategies that would allow governments, especially in low and middle income countries, to raise some of the necessary resources

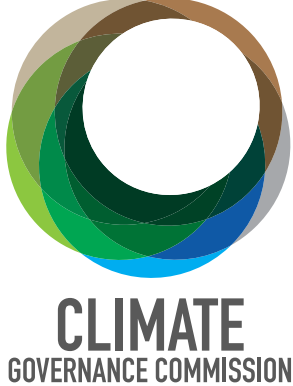


The out-of-date international taxation system, which emerged more than a century ago when multinational corporations were not so important and it was not so easy to store private wealth in tax havens, must be reformed. To reduce and prevent illicit financial flows stemming from tax evasion, exchange of banking and other information across tax authorities is essential. The unitary taxation of multinational companies, with formulary apportionment of taxable profits and a higher global minimum tax rate (of 21-15%), should be enabled by international agreement. There should be a similar minimum tax rate on extremely wealthy individuals (amounting to 2 percent of assets) which would operate no matter where such wealth is held. Other taxation possibilities such as a tax on financial transactions, should also be considered.

**These strategies have more potential because of the ongoing negotiations at the UN, which need to be strongly supported.**



# Mechanisms to monitor, regulate and enforce delivery of commitments of private investments in climate finance are required.



In addition, efforts should be made to galvanise private investments in low carbon emission products and processes.

In this area, a disproportionate emphasis has been placed on derisking and incentivising investments in sustainable and climate-sensitive activities and projects. It is indeed true that partial guarantees, equity contributions, viability-gap funding, tax breaks, and subsidies can play a role in pushing the required investments. But global, including financial sector, concerns about green-washing and absence of promised outcomes from structured finance deals has underlined the need for developing an appropriate monitoring and regulatory framework to assess the extent of derisking needed in different activities and individual cases, set targets proportionate to public financial support, monitor delivery and fix appropriate penalties for failure to deliver.

# Further proposed work within the Climate Governance Commission

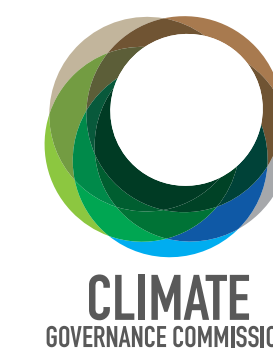


Given this climate finance landscape, the Climate Governance Commission (CGC) can play an important role through supporting thought leadership and engagement on this topic in multiple spheres. Key issues on which it might convene action-focused expert groups, drawing from international think tanks, CSOs and NGOs, and work with such like-minded actors to advocate for progress at UN climate and biodiversity COPs, among other international meetings, include:

1. ensuring that developed country governments deliver and go substantially beyond their \$100 billion climate financing goal and the NCQG, with processes that give greater voice to developing countries in the determination of the new collective quantified goal based on an assessment of needs and their own respective capabilities.
2. ensuring the availability of concessional or grant financing to spur technological innovations in areas where monetary returns are low, to help deploy those innovations and to allocate larger sums for low-return adaptation projects and to compensate for loss-and-damage.
3. while supporting efforts to mobilise private finance, contributing to shaping regulation and conditionalities, and to developing monitoring and verification frameworks for such private finance mobilisations. These are necessary to ensure that public-private partnerships and the use of public resources to incentivise private investments do yield significant mitigation and adaptation benefits and not become the losses suffered because of greenwashing in various ways.
4. providing research and ideas to see how debt-for-nature and debt-for-climate deals can be scaled up, made more effective and actually contribute meaningfully to both sovereign debt reduction and climate-related goals, and avoid excessive reliance on profit-oriented private intermediaries for their operationalisation
5. ensuring that carbon pricing and carbon taxes are carefully and fairly designed, and do not become discriminatory and protectionist instruments used as a means of advancing domestic development and interests in the developed countries at the expense of developing countries.

# Recent Developments/Discussion within and about the International Financial Architecture

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Briefs by Dr. Dhruba Purkayastha and Eoin Jackson



There have been some recent developments within the current international financial architecture that may present an opportunity to increase financial flows for climate investments to low-and middle-income countries, provided they are accompanied with the requisite increase in ambition from developed countries, and associated accountability and transparency mechanisms to ensure adherence to climate finance commitments made by the Global North.

The Bridgetown Initiative, co-led by the Prime Minister of Barbados and the UN-Secretary General, has sought to address the immediate needs of countries facing debt distress and liquidity challenges in relation to making climate investments.<sup>60</sup> The Initiative has pursued several agenda items, including the following six priority objectives:

1. Provide immediate liquidity support including rechannelling at least \$100 billion of unused Special Drawing Rights through the IMF and multilateral development banks.
2. Restore debt sustainability today and in the long-term and support countries in restructuring their debt with long-term low interest rates.
3. Dramatically increase official sector development lending to reach \$500 billion annual stimulus for investment in the Sustainable Development Goals (SDG Stimulus).
4. Mobilise more than \$1.5 trillion per year of private sector investment in the green transformation.
5. Transform the governance of international financial institutions to make them more representative, equitable, and inclusive.
6. Create an international trade system that supports global green and just transformations.<sup>61</sup>

<sup>60</sup> UN Press Office, [With clock ticking for the SDGs, UN Chief and Barbados Prime Minister call for urgent action to transform broken global financial system](#) (26 April 2023).

<sup>61</sup> UN Press Office, [With clock ticking for the SDGs, UN Chief and Barbados Prime Minister call for urgent action to transform broken global financial system](#) (26 April 2023).

## Implementation of the Bridgetown Initiative would significantly bolster the opportunities for low-and middle-income countries to channel finance and investment into sustainable development, including climate mitigation and adaptation.

Additionally, Brazil, which is President of COP30, has an opportunity to use its platform to take cognizance of this Initiative which could include placing further emphasis on support for green projects at COP30.<sup>62</sup>

The G20 Sustainable Finance Working Group also published a detailed report in 2023 following the meeting of the G20 in India.<sup>63</sup> This report provides a series of goals and follow-up objectives to the G20 Sustainable Finance Roadmap.<sup>64</sup> The report recommends and supports: 1) mechanisms for the mobilization of timely and adequate resources for climate finance; 2) enabling finance for the Sustainable Development Goals (SDGs); and 3) capacity building of the ecosystem for financing toward sustainable development.<sup>65</sup> To this effect it has issued several specific recommendations which include:

Governments should introduce appropriate policy and regulatory frameworks that incentivizes corporate investments in R&D for climate innovation, facilitates business set-up, and incentivizes support for climate technology start-ups.<sup>66</sup>

Public and private climate technology investors should engage with relevant experts and platforms, including, for example, the International Energy Agency's Tracking Clean Energy Progress (TCEP) assessment, to develop a shared understanding of those technologies whose levels of technology readiness may be currently off-track for achieving Paris-aligned pathways, and to consider which of those technologies may require more targeted climate finance interventions.<sup>67</sup>

Relevant public sector authorities, including public development banks and multilateral funds, and private investors should pursue public-private climate technology incubators and accelerators, including projects that facilitate the flow of capital to enterprises in emerging and developing markets.<sup>68</sup>

Governments and international organizations should consider measures leading to the development of a robust pipeline of investment-ready social impact projects, with associated financing solutions.<sup>69</sup>

Governments, international organizations, and other stakeholders should cooperate to share best practices, build expertise across the public and private sectors, and seek opportunities to collaborate on voluntary approaches for designing and scaling social impact investment instruments, recognizing country context.<sup>70</sup>

Relevant authorities, international organizations, initiatives, and networks should be encouraged to support and further develop nature-related reporting standards and frameworks with the goal of promoting greater interoperability and accessibility of nature-related data and reporting.<sup>71</sup>

<sup>60</sup> UN Press Office, [With clock ticking for the SDGs, UN Chief and Barbados Prime Minister call for urgent action to transform broken global financial system](#) (26 April 2023).

<sup>61</sup> UN Press Office, [With clock ticking for the SDGs, UN Chief and Barbados Prime Minister call for urgent action to transform broken global financial system](#) (26 April 2023).

<sup>62</sup> Ishac Diwan, [Developing Countries' Liquidity Crisis Is Not Over Project Syndicate](#) (16 April 2024).

<sup>63</sup> G20 Sustainable Finance Working Group, Deliverables (2023).

<sup>64</sup> G20 Sustainable Finance Working Group, Sustainable Finance Roadmap (2021).

<sup>65</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 3-4.

<sup>66</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 12.

<sup>67</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 13.

<sup>68</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 18.

<sup>69</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 18.

<sup>70</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 19.

<sup>71</sup> G20 Sustainable Finance Working Group, Deliverables (2023) 23.

The COP26 and COP27 Presidencies, together with the UN Climate Change High-Level Champions, extended the mandate of the Independent High-Level Expert Group on Climate Finance (IHLEG) in July 2022, to prepare a second report for COP28.<sup>72</sup> This report, released in 2024, highlighted that an integrated finance framework is needed to achieve the Paris Agreement, and that what is needed from the global finance system is a purposeful approach with strong and committed engagement of all key stakeholders –governments, the private sector, the multilateral development banks(MDBs), donors and private philanthropy.<sup>73</sup> It also identified that concessional finance is the scarcest and most vital source of finance for meeting urgent and high priority needs and a five fold increase in concessional finance is needed by 2030 to achieve climate goals.<sup>74</sup>

**This expert group and its conclusions played an important role in shaping the agenda for COP29, which was viewed by stakeholders as the “finance COP”.<sup>75</sup>**



<sup>72</sup> High-Level Expert Group on Climate Finance, [A climate finance framework: decisive action to deliver on the Paris Agreement](#) (2023).

<sup>73</sup> High-Level Expert Group on Climate Finance, [A climate finance framework: decisive action to deliver on the Paris Agreement](#) (2023) 4.

<sup>74</sup> High-Level Expert Group on Climate Finance, [A climate finance framework: decisive action to deliver on the Paris Agreement](#) (2023) 5.

<sup>75</sup> Lee Harris and Attracta Mooney, [Climate finance must be COP29 summit priority, UN leaders say](#) Financial Times (14 March 2024).

<sup>76</sup> Homi Kharas and Charlotte Rivard, [Swimming against the tide on financing for development](#) Brookings (11 April 2024).

<sup>77</sup> Aime Williams, Rich nations pledge \$11bn to World Bank for climate and global crises Financial Times (20 April 2024).

<sup>78</sup> Josh Gabbatis, Q&A: Climate finance at World Bank and IMF spring meetings 2024 Carbon Brief (23 April 2024).

<sup>79</sup> Josh Gabbatis, Q&A: Climate finance at World Bank and IMF spring meetings 2024 Carbon Brief (23 April 2024).

<sup>80</sup> G7, Finance Ministers and Central Bank Governors Statement (2024) 16.

<sup>81</sup> G7, Finance Ministers and Central Bank Governors Statement (2024) 20.



Most recently, the World Bank and IMF 2024 Spring Meetings provided an opportunity to discuss and consider new and enhanced means of increasing climate finance and international financial institutional architecture reform.<sup>76</sup> Wealthy nations including the US, Germany, the UK, and Japan pledged a combined \$11bn to fund World Bank efforts to tackle global challenges such as climate change and pandemics.<sup>77</sup> Additionally, representatives from a group of wealthy and low-and-middle-income countries met on the sidelines of the meeting for the second in-person meeting of the international tax task force.<sup>78</sup> The goal of this task force is to analyze and design new forms of taxation that could be used to raise money for climate and development needs. Options being considered include taxes on fossil-fuel producers, shipping fuel, air travel, and financial transactions.<sup>79</sup> At the sidelines of these meetings, the G7 Finance Ministers and Central Bank Governors issued a statement reaffirming their commitment to “paving the way to the global transition towards a carbon-neutral economy. This requires implementing effective policy frameworks to mobilise the substantial public and private investment that is necessary.”<sup>80</sup> Further, they reiterated their commitment to evolve and strengthen Multilateral Development Banks (MDBs) to address the most pressing development and global challenges.<sup>81</sup>

The need for new means of increasing climate finance and international financial architecture reform was further illustrated in the deep divides which emerged during the efforts to establish a new collective quantified goal (NCQG) at COP29.<sup>82</sup> At COP29, countries agreed on a new collective quantified goal (NCQG) on climate finance, aiming for at least \$300 billion annually from developed countries by 2035, with a broader aim of securing the efforts of all actors to work together to scale up finance to developing countries, from public and private sources, to the amount of \$1.3 trillion per year by 2035.<sup>82</sup> This new goal met with significant criticism from many developing countries, who viewed it as insufficient to meet their climate mitigation and adaptation needs.<sup>83</sup> Additionally, the recent

withdrawal of the US from the Paris Agreement complicates efforts to meet this goal due to the significant contributions made by the US to previous climate finance targets.<sup>84</sup> The process by which the goal was agreed to also illustrated some broader vulnerabilities in the COP process, as outlined in the Club of Rome's COP Reform letter released during COP29 with the support of the Climate Governance Commission.<sup>85</sup> Efforts will continue at COP30 to strengthen the implementation of the NCQG, which may provide further opportunities to discuss governance reforms which could raise additional sources of climate finance.

<sup>82</sup> Carbon Brief, [What is the New Collective Quantified Climate Finance Goal on Climate Finance](#) (4 November 2024).

<sup>83</sup> Fiona Harvey, [COP29 agrees \\$1.3tn climate finance deal but campaigners brand it a 'betrayal'](#) (23 November 2024) The Guardian.

<sup>84</sup> See e.g. Anatha Lakshmi, [US Pulls out of Flagship 45bn Global Climate Finance Coalition](#) (6 March 2025) Financial Times.

<sup>85</sup> Club of Rome, [Open Letter on COP Reform](#) (2024).

Other civil society organizations and G20 affiliated groups have published new proposals for international financial architecture reform. The “One Campaign”, supported by more than 75 former heads of state, economists, and activists has proposed a 10 point plan for the IMF Managing Director. This includes a proposal for the Director to “acknowledge the systemic nature of the debt crisis on humanity, stability and ecology and update Debt Sustainability Frameworks to ensure debt restructurings are faster and preserve fiscal space for climate and development action,”<sup>86</sup> and Champion a new SDR General Allocation to support development, the energy transition and climate adaptation.”<sup>87</sup> The G20 Independent Expert Group on Strengthening Multilateral Development Banks has also published a status review on the implementation of reforms of multilateral development banks. It identified that multilateral development banks have taken control of the reform agenda but are allowing shareholders to guide the speed and scope of change.<sup>88</sup> Further, the report stated that while experts are positive about the multilateral development banks efforts to support the mission, prioritization, and collaboration, with regard to global challenges like climate change, experts are less positive about the multilateral development banks’ efforts to partner with other actors.<sup>89</sup> Experts are also skeptical about the likelihood of multilateral development banks achieving current targets on scaling up resource flows,

being particularly negative about targets relating to the tripling of concessional finance and the quadrupling of private capital mobilization.<sup>90</sup> Similarly, the Expert Panel tasked with the Independent Review of Multilateral Development Banks’ Capital Adequacy Frameworks also published a G20 funded report on boosting MDBs’ investing capacity. This includes proposals to give more importance to callable capital, expand the uses of financial innovations to create more usable capital or shift loan risks to willing counterparties, and to improve credit rating agency assessment of MDB financial strength, among other proposals.<sup>91</sup> Subsequently, the Independent Expert Group (IEG) commissioned by the G20 Indian Presidency published the Triple Agenda Report which lays out a triple agenda for MDB reform designed to triple annual sustainable investing levels.<sup>92</sup> These proposals include for MDBs to convert their operational model to shift away from individual projects towards programs where national governments take a strong lead in identifying multi-year transformations with sectoral focus, achieved through scaled-up investments, as well as for MDBs to focus their operations on helping countries create and operationalize such platforms for the highest priority SDG and GPG sectors or themes. They also suggested bringing the private sector to the center of MDB operations, and working out mechanisms for guarantees and financing of global public goods which are not country specific.<sup>93</sup>

<sup>86</sup> G20 Independent Expert Group on Strengthening Multilateral Development Banks, [Implementing MDB Reforms: A Stocktake](#) (2024) 17.

<sup>87</sup> Expert Panel tasked with the Independent Review of Multilateral Development Banks’ Capital Adequacy Frameworks, [Boosting MDBs Investment Capacity](#) (2022) 6-11.

<sup>88</sup> Triple Agenda Report, [Volume 2 Strengthening Multilateral Development Banks](#) (2023) 11-59.

<sup>89</sup> Triple Agenda Report, [Volume 2 Strengthening Multilateral Development Banks](#) (2023) 11-59.

<sup>90</sup> John Ainger, [COP29 Climate Summit Countdown Starts With Finance at Forefront](#) Bloomberg (25 April 2024).

<sup>91</sup> Organization for Economic Cooperation and Development (OECD), [Scaling Up the Mobilisation of Private Finance for Climate Action in Developing Countries: Challenges and Opportunities for International Providers](#) (2023) 4.1 Recommendation 2.

<sup>92</sup> *ibid* 4.1 Recommendation 3.

<sup>93</sup> International Monetary Fund (IMF) Staff Note, [Mobilizing Private Climate Financing in Emerging Market and Developing Economies](#) (2022) 22.



If global climate investments are to be met for keeping the world aligned to UNFCCC Paris Agreement goals, it is important the appropriate global institutional mechanisms for climate funding such as Global Risk Mitigation Facilities, including FX risk management and increased use/reallocation of IMF SDRs (Special Drawing Rights), matters largely avoided at COP29, but which should be discussed at future COPs. This will also provide a critical platform for low-and middle-income countries to voice their concerns at the lack of progress on climate finance, as well as build on commitments to push for existing commitments, climate finance governance reforms and greater access to concessional finance and to risk-mitigated channels of accumulated global private capital, such as the Glasgow Financial Alliance for Net Zero (GFANZ), among other innovative mechanisms.<sup>94</sup>

<sup>94</sup> ibid 22.

# Solutions to Mobilise Private Climate Finance

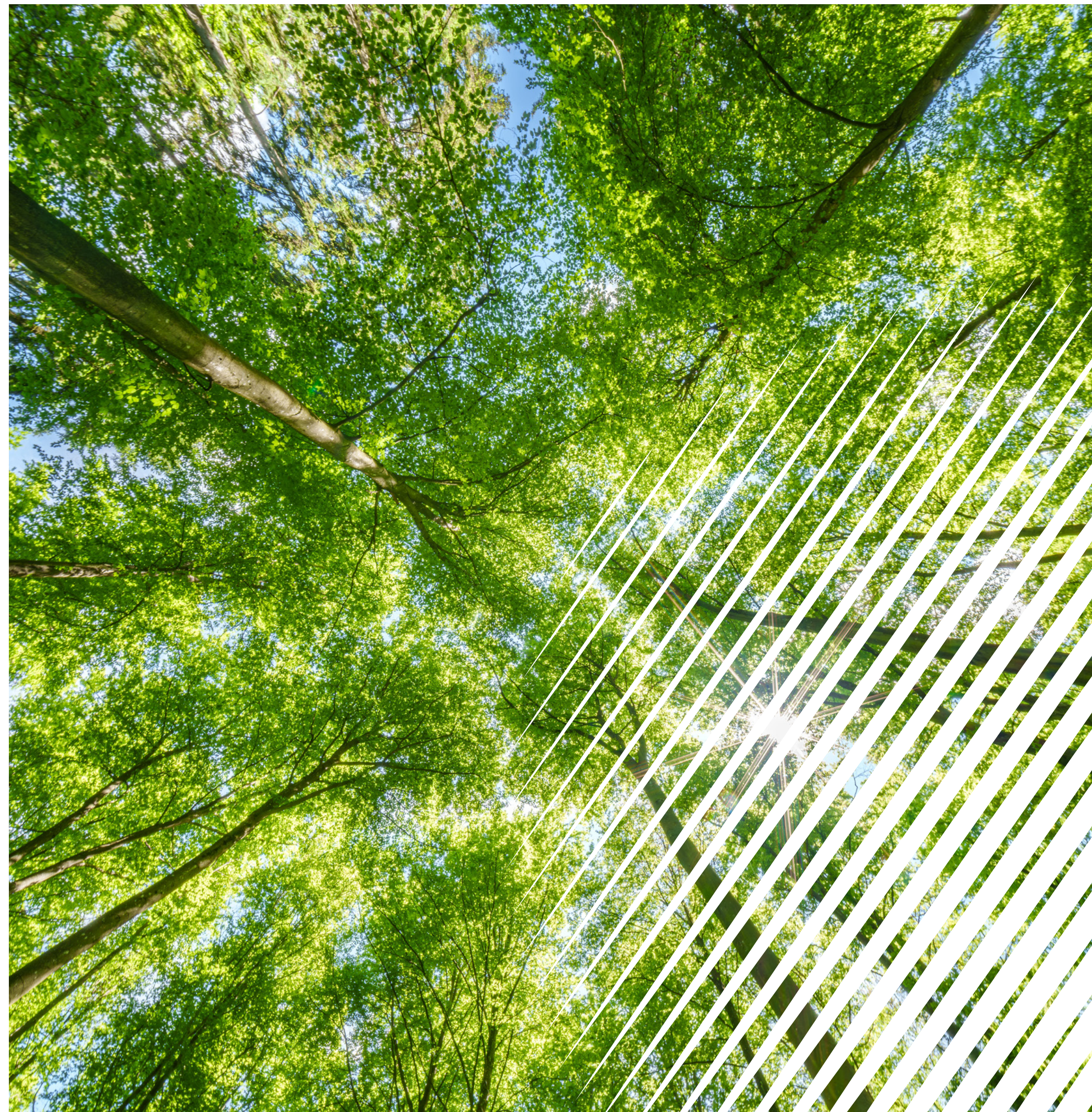
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Briefs by Dr. Dhruba Purkayastha and Eoin Jackson

Mobilising private climate finance to supplement an expansion of public climate finance is critical to ensuring we can meet the needs of low- and middle-income and other climate vulnerable countries. Mobilising the private sector to boost its climate finance investment will require innovative thinking and new global governance solutions.

A number of proposals have been put forward by multilateral organizations and civil society to mobilise private climate finance. The OECD has proposed that in more mature markets, loans and debt instruments should be reoriented toward private finance mobilization. This would include the use of syndicated loans to mitigate the challenge with mobilising private finance in sectors with high upfront capital costs e.g. large-scale green energy projects.<sup>95</sup> They also suggest scaling up the use of guarantees to optimize the terms and conditions of debt through extended maturities and lower interest rates.<sup>96</sup>



<sup>95</sup> ibid 22.

<sup>96</sup> ibid 22.

Staff at the IMF have proposed several means by which MDBs could play a role in attracting private finance. These include using their surveillance, capacity development, risk assessments, and climate diagnostic tools to help attract private investment in countries with a higher risk profile,<sup>97</sup> using the IMF Resilience and Sustainability Trust (which these authors argue should be scaled up dramatically as noted in our proposals for the reallocation of special drawing rights) to catalyze the implementation of private finance,<sup>98</sup> supporting the public sector with its investment into the infrastructure necessary for profitable and beneficial private investment,<sup>99</sup> and the harmonization of taxonomies and data to allow investors to make better-informed decisions.<sup>100</sup> In particular the IMF staff note the relative lack of funding from the private sector into climate adaptation projects, and that it would therefore be good to identify and segregate specific adaptation projects that are suitable for large-scale private sector investments and those projects more appropriate for public sector investment.<sup>101</sup>

World Resources Institute (WRI) has highlighted that a critical problem for private investors in increasing their climate finance portfolio is the high risk profile of some of the most climate-vulnerable countries.<sup>102</sup> To address these concerns, they propose that MDBs play a key role in de-risking private climate investment.<sup>103</sup> However, this would require an overhaul of the international financial architecture to allow for broader de-risking strategies to be effectuated. De-risking strategies proposed by WRI, include working through MDBs towards enhanced data transparency by increasing access to credit and probability of default/default rate data,<sup>104</sup> positioning de-risking as a mechanism for sector transformation by addressing risks from the entire life cycle of a project within a sector instead of a single asset,<sup>105</sup> and encouraging stakeholders including the governments of the countries in question to share and exchange lessons and conditions for scaling with the investors.<sup>106</sup> While these proposals are useful, the gravity and scale of the climate emergency shows a need to dramatically increase climate investments to at least \$5.9 trillion per annum till 2030, which in turn will require fundamental reforms greater than these strategies.<sup>107</sup>

## The Center for Strategic and International Studies (CSIS) has put forward similar solutions regarding derisking.

These include financing projects in the local currency to offset currency risk,<sup>108</sup> increasing the use of guarantees from MDBs for climate investments,<sup>109</sup> providing risk subsidies to lower the cost of capital,<sup>110</sup> and assisting governments and private investors with project preparation through Project Preparatory Facilities, which could be set up by MDBs.<sup>111</sup> In this regard, they highlight the work of the Indian government in facilitating private investment into solar panels. India uses its local authorities and state agencies to purchase land and power evacuation systems suitable for solar power in advance, and then auction on a tariff based bidding to project developers. This model reduces risks associated with planning and land development, thereby encouraging private investors.<sup>112</sup> However, while this approach is useful for domestic financing, it does not address cross border capital flows, which, as this paper has discussed, requires country level risks to be addressed through models like a global green/climate guarantee facility.<sup>113</sup>

The variety and scale of solutions put forward by multilateral organizations and civil society show that a whole-of-system reform approach to mobilising climate finance is both necessary and feasible to ensure the private sector can play a valuable role in supplementing the public sector in meeting global climate investment goals.

<sup>97</sup> *ibid* 24.

<sup>98</sup> World Resources Institute (WRI), [Mobilizing Private Investment in Climate Solutions: De-risking Strategies of Multilateral Development Banks](#) (2023) 2.

<sup>99</sup> *ibid* 2 and 4.

<sup>100</sup> *ibid* 2.

<sup>101</sup> *ibid* 2.

<sup>102</sup> *ibid* 2.

<sup>103</sup> UNFCCC, [First report on the determination of the needs of developing country Parties related to implementing the Convention and the Paris Agreement](#) (2021 ) 5.

<sup>104</sup> The Center for Strategic and International Studies (CSIS), [Private Capital Mobilization for Climate Finance in an International Context](#) (2023) 5.

<sup>105</sup> *ibid* 5.

<sup>106</sup> *ibid* 5.

<sup>107</sup> *ibid* 8.

<sup>108</sup> *ibid* 8.

<sup>109</sup> Climate Policy Initiative, [Proposal for a Global Credit Guarantee Facility \(GCGF\)](#) (2023) 4.

<sup>110</sup> *ibid* 5.

<sup>111</sup> *ibid* 8.

<sup>112</sup> *ibid* 8.

<sup>113</sup> Climate Policy Initiative, [Proposal for a Global Credit Guarantee Facility \(GCGF\)](#) (2023) 4.

# Policy Brief on Climate Finance

By C. P. Chandrasekhar and Jayati Ghosh

