Climate finance: challenges and opportunities for the Asia-Pacific

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Facts

As climate change is posing increasing risks for both human and natural systems, a shift toward low-carbon and green economic development is needed to meet future challenges. In order to switch from the sole pursuit of economic growth to a sustainable development path, transformational changes in both public and private sector investments are of paramount importance. Climate finance, defined as capital flows targeting low-carbon and climate-resilient development with direct or indirect greenhouse gas (GHG) mitigation or adaptation objectives, offers a great opportunity that should not be ignored.1

In 2012, annual global climate finance settled at $359 billion2, or $1 billion per day, still below the levels needed to limit warming to 2°C Celsius. The public sector contributed $135 billion, or around 38% of global climate finance flows, while the private sector provided the lion’s share of global investments, contributing $224 billion, or 62% of the total. The majority of these investments were directed at mitigation measures, whereas adaptation finance seems to lag behind. In the same year, $182 billion were invested in developing countries, of which $131 billion (72%) stemmed from domestic sources. Asia-Pacific has received the largest volume of public climate finance so far. However, the distribution of finance within the region has been uneven, China,

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1 In the absence of an internationally-acknowledged definition of climate finance, international organisations and research centres have each tried to pin down the term. The most accurate definition is the CPI’s, which limits climate finance flows to “climate-specific finance”, which includes only capital flows targeting low-carbon and climate-resilient development with direct or indirect greenhouse gas (GHG) mitigation or adaptation objectives.
2 Figures are in US dollars.
India and Indonesia being the largest recipients of funding: they have received 49% of the funding approved for Asia since 2003. Over two thirds of the climate finance directed to Asia-Pacific since 2003 has supported mitigation initiatives, while the remaining funding supported adaptation activities, REDD+ and multiple foci programs.

Asia-Pacific, with a 6% annual growth, has the potential to produce 44% of global GDP by 2035. In this “Asian Century” scenario, the region’s share of world energy consumption will rise from a third in 2010 to 51%–56% by 2035. Renewable energy sources represent the only valid alternative for a low-carbon future, even though the financing of clean energy is declining from its 2011 peak of $317 billion. Asia-Pacific, excluding China and India, however, saw a 47% rise in the financing of clean energy to $43 billion, Japan being the biggest contributor: its solar sector boom helped to drive an 80% increase in renewable energy investments totaling $29 billion. Solar and wind power represent the vast majority (90%) of green investment in the region, with $43.3 billion spent in the first half of 2013, China, Japan, India and Australia being the main contributors.

Opportunities

The Asia-Pacific region presents both challenges and opportunities to investors in climate finance. Currently, 21 climate funds and dedicated initiatives are active in the region, including 15 multilateral funds, 5 bilateral initiatives, and 1 national fund. The largest contribution comes from the World Bank’s Clean Technology Fund (CTF), which so far has approved $763.25 million to fund nineteen projects, mainly in the form of concessional loans.

The key to maximise both public and private sources of funding is an efficient combination of resources from different instruments, while at the same time encouraging low carbon and climate-resilient development. The most immediate challenges to be addressed in financing low-carbon development are:

- Facing high upfront costs to be borne in the transition to low emission and energy efficient alternatives
- Leveraging public funds to focus on long-long-term objectives, on the one hand; and address perceived risks related to greening the economy, thus creating an enabling policy environment, in order to encourage private sector investments, on the other hand
- Integrating low-carbon and climate resilience into national development plans through regulatory reforms

A successful policy framework, together with government incentives and shared initiatives, could prove fundamental in the region’s transition to a sustainable green economy. Furthermore, climate banking is slowly emerging, and some commercial banks are establishing specialised climate finance facilities to address mitigation and adaptation measures. As the majority of the investments in clean energy consist in asset financing, which usually includes a debt component,
alternative asset investments may present new opportunities for additional funding. Particularly, climate bonds are expected to undertake a growing trend.

Both the financial sector and the capital markets remain crucial in shaping a country’s economic activities. The UNFCCC expects additional investments especially through carbon markets. The Clean Development Mechanism (CDM) under the Kyoto Protocol has a great potential to leverage domestic and international investments, but needs to be further expanded. In addition, carbon funds constitute a critical feature of the carbon markets, and they have rapidly increased in number in the last few years, growing from 3 in 2000 to 54 in 2007.

**Lessons from China**

The world’s emissions trading schemes are valued at about $30 billion, with China now housing the world’s second largest carbon market, after the European Union, covering the equivalent of 1,115 million tons of carbon dioxide emissions. According to the UNFCCC, China’s estimated annual emission of 9,860,000 tons of CO₂ emissions in 2013 makes it a dominant player in the CDM market, being the source of 50.59% of the global annual registered projects as of October 2013. As of the same year, China also issued 61.22% of the total certified emission reductions (CERs). In the long term, the country is committed to reduce its GHG emissions per unit of GDP by 40–45% by 2020 with respect to 2005 levels.

In 2013, China launched its pilot emission trading scheme (ETS), with the objective of developing seven pilot projects in Beijing, Shanghai, Tianjin, Chongqing, Guangdong, Hubei and Shenzhen. The Shenzhen ETS was the first cap-and-trade program to be launched and it covers 635 companies from various industries. So far, six out of seven pilot projects entered the pipeline: as soon as the last one, Chongqing, starts this year, the aggregate of regulated emissions in China will become the world’s second largest after the European Union.

Despite the challenges that the project faces, it will represent a significant capacity building tool for both the government and the companies. It also represents a move away from the more traditional policy-based approach to climate change that has characterized China so far and marks a shift towards market-based strategies.

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