The Post-2012 Finance Architecture: How can Market Mechanisms fit in?

The CDM and Future Flexible Mechanisms Post-2012
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Dr. Jochen Harnisch
Coordinator Climate Change Policy
KfW Development Bank

KFW: A Brief Introduction…

- Promotional bank of the Federal Republic of Germany
- Founded in 1948 for implementation of Marshall Plan
- We finance investment in Germany and Europe
- We provide international project and export finance
- We provide support for developing countries
- Focus areas: environment and energy efficiency

2007 (partly estimates)	**KFW**	**European Investment Bank**	**World Bank**
Geographical Focus	domestic & international	regional	international
Balance Sheet	354 billion €	305 billion €	90 billion €
New Loans	75 billion €	43 billion €	20 billion €
Employees	3,700	1,500	10,000

What Needs to be Achieved?

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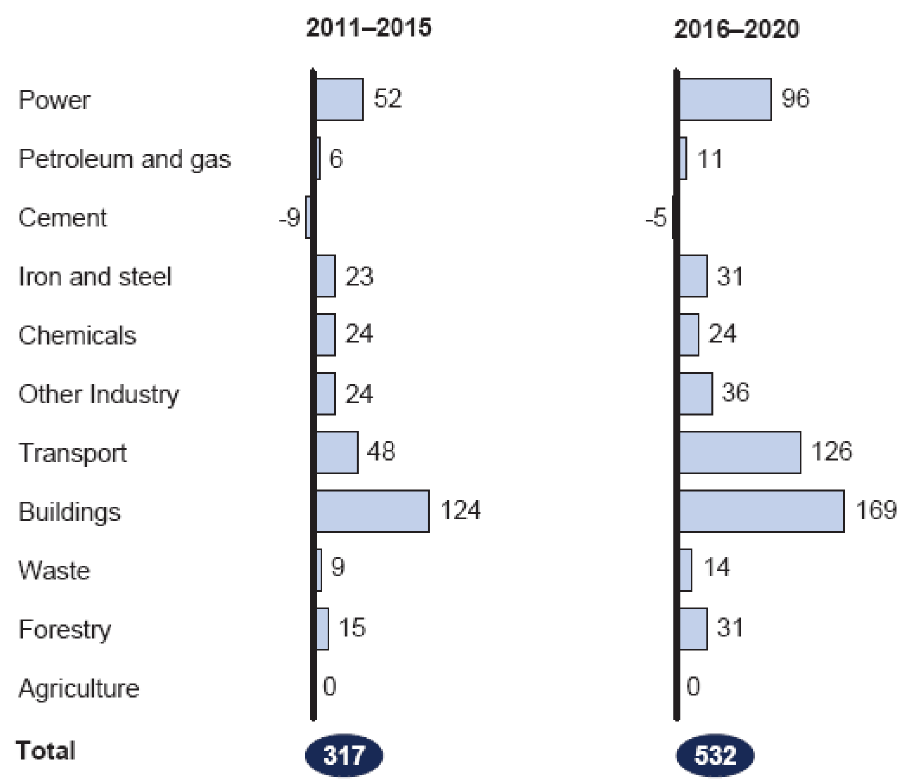
- Leverage private sector investment for large scale deployment of climate friendly technologies
- Provide economic framework for decades of successful operation of climate friendly technologies (e.g. CCS)
- Getting appropriate national policies in place: pave the road towards a unified global carbon market
- Achieve results which are monitorable, reportable and verifiable

⇒ Make climate friendly technologies
the „new business as usual“

McKinsey 2.0 Additional Investment: By Sector

Capital investment by sector incremental to business-as-usual for the abatement potential identified

€ billions per year; annual value in period



McKinsey 2.0 Additional Investment: By Region

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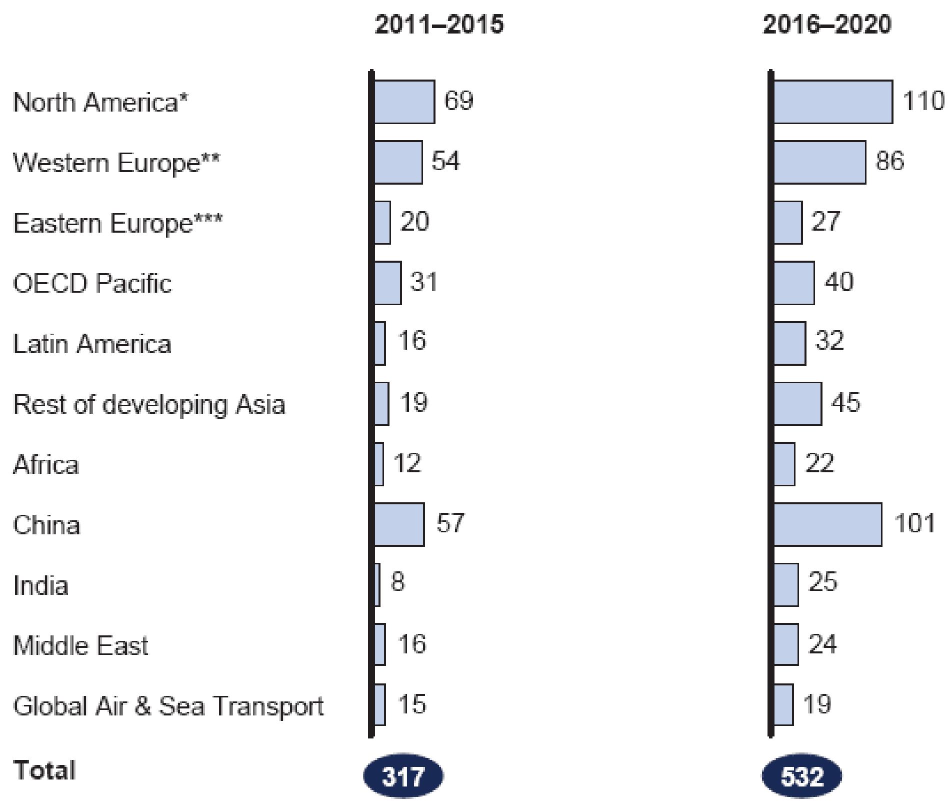
Capital investment by region incremental to business-as-usual for the abatement potential identified

€ billions per year; annual value in period



Principles for a Climate Finance Architecture: Scale, Speed, Results

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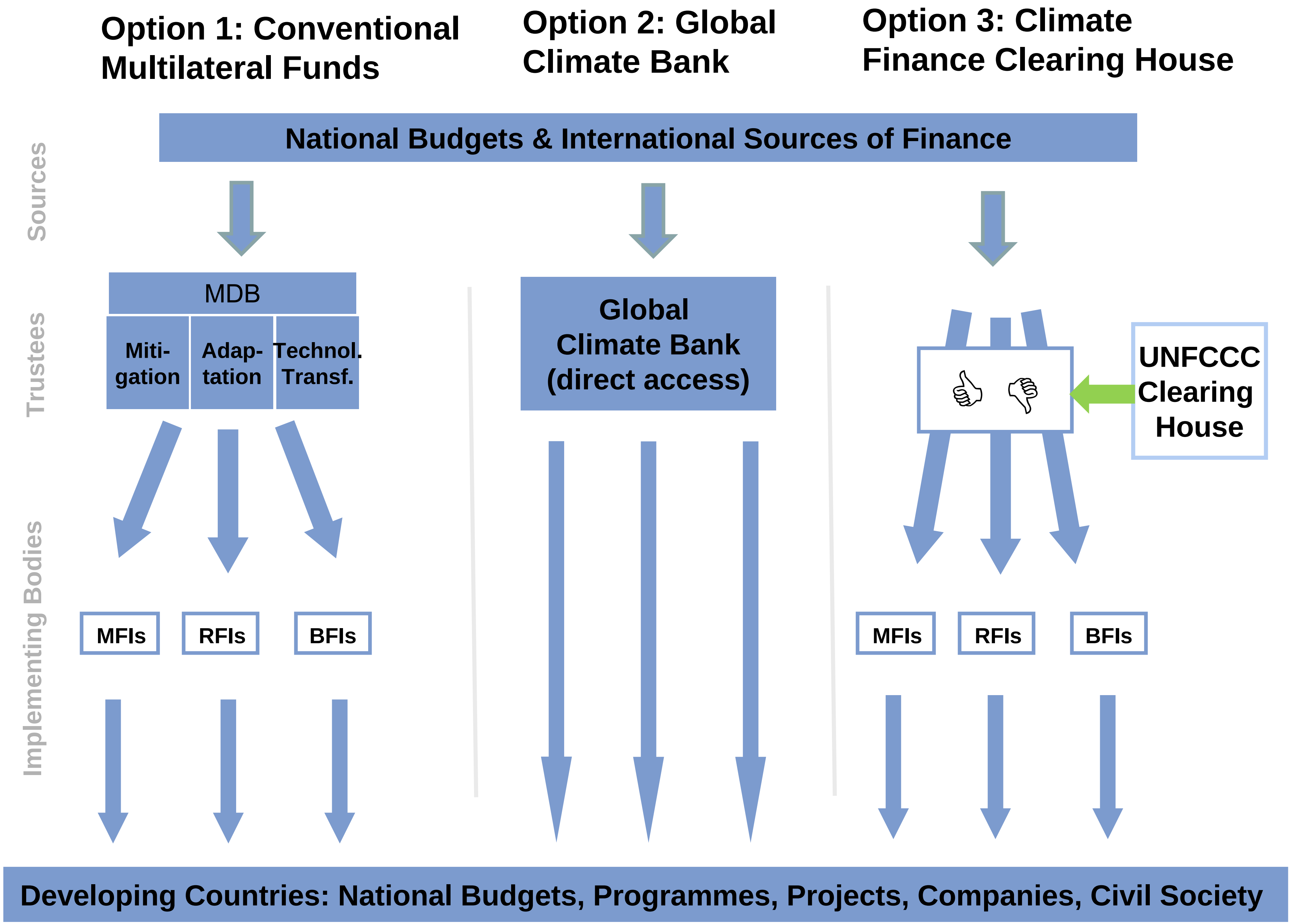
- Make full use of existing implementation capacity
- Use of bilateral, regional and other multilateral channels (Article 11 of Convention / KP)
- Start implementation by 2013, minimise „lock-in“
- Alignment of climate finance with ongoing development efforts
- Leveraging of private capital, avoid crowding out commercial finance products
- Differentiated portfolio of finance products in each field (mitigation, technology transfer and adaptation)

Advantages of International Financial Cooperation Approaches

Multilateral	Bilateral
Scale of individual funds	Decades of implementation experience
Uniformity of available products	Speed and flexibiliy
Ease of coordination of activities in developing countries	Acceptance by donor country tax payers and parliamentarians
One-stop shop for developing countries	Cooperation of equals, exchange of national policy and know-how



Option 1: Conventional Multilateral Funds
Option 2: Global Climate Bank
Option 3: Climate Finance Clearing House
Sources
Trustees
Implementing Bodies
National Budgets & International Sources of Finance
MDB
Miti-gation
Adap-tation
Technol. Transf.
MFIs
RFIs
BFIs
Global Climate Bank (direct access)
UNFCCC Clearing House
MFIs
RFIs
BFIs
Developing Countries: National Budgets, Programmes, Projects, Companies, Civil Society

Advantages of Climate Finance Clearing House

- Facilitates bundling of bilateral, regional and multilateral funding channels, pursuant Art. 11 of Conv. & KP
- Permits the combination of the major advantages of multilateral and bilateral cooperation
- Coordinates rather than disrupts existing development finance cooperation
- Makes full use of each system‘s competive strengths
- Provides framework for complementary financing approaches and products
- Ensures full transparency and accountability

Examples From Wish List for Mitigation and Technology Transfer

Concessional loans for:

national renewable energy investment plans

rehabilitation of fossil fuel power plants

incremental costs of super-efficient coal fired power plants

nuclear power plants

waste incineration projects

power T&Dinfrastructure

LNG infrastructure and NG pipelines

Equity and mezzanine finance for project finance and technology development

Grant money for:

CCS technology deployment

purchase and retirement of CERs or ERUs

national and regional tenders for renewable electricity generation

information and capacity building campaigms

forest protection or reforestation trust funds

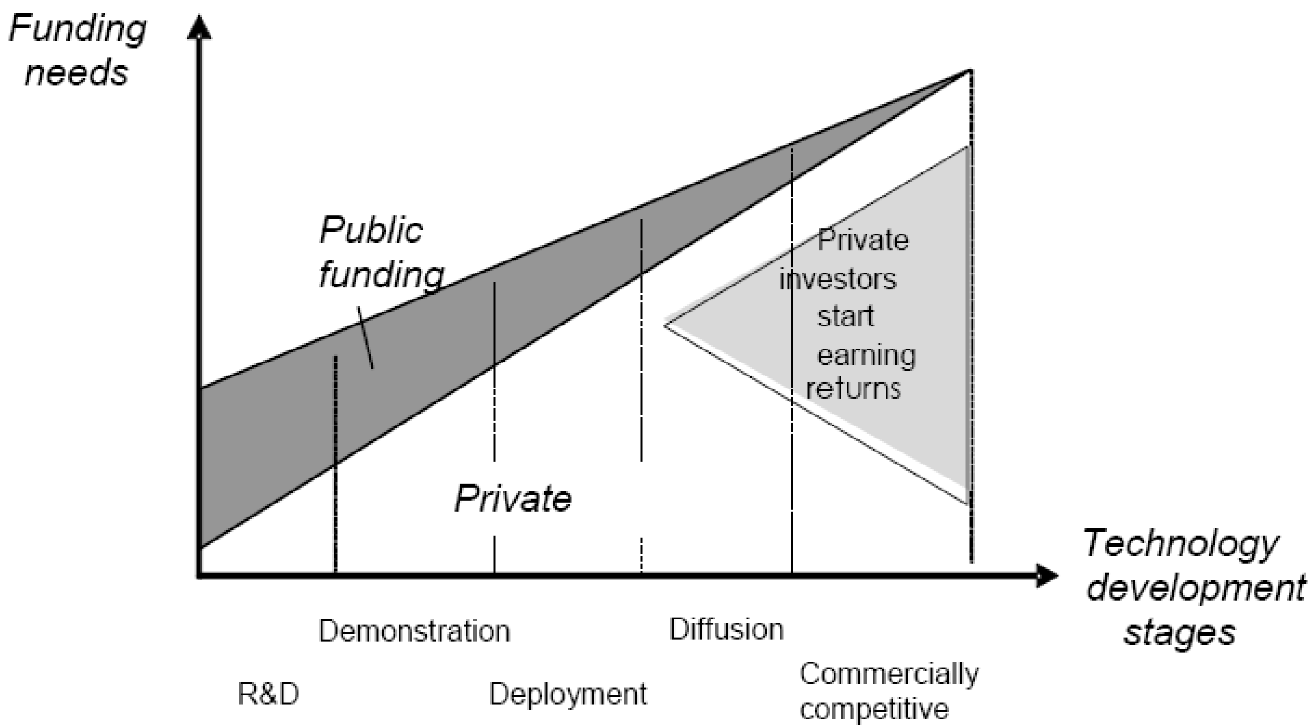
public R & D in developing countries

purchase of IPR and license agreements

Insurance for geothermal exploration risks or windparks

Guarantees for commercial loans

Roles of the Public & Private Sectors in Financing Technology Development



Source: UNFCCC, 2008

Leverage of Private Capital by Public Funding

Ratio of Induced Investment over Exogenous Economic Incentive:

- UNFCCC FF & I Study (2007): 4 for CDM in 2006
- UNEP SEFI Public Finance Mechanisms (PFMs): 3...15
- KFW Energy Efficient Housing in Germany (2008): 5 (3-12)
- Private households exhibit higher leverage factors: 5…50
- Analogy to energy savings pay back times in industry: 0,5…5
- No automatic positive leverage factor of public finance: can be ≤0
- Removal of non-economic implementation barieers can be crucial: potentially very high leverage factors

⇒ Leverage factor depends on sector, country and program design

Conclusions (I)

- Leverage factor of private investment by public finance can range from ≤0 to low single digit numbers to high values >10: depends on sector, country and program design.
- Emission mitigation costs (not the investment costs) have to be absorbed by the private sector and consumers (somewhere)
- The required net transfer of money between regions, sectors and groups can be achieved via the public and/or private sector
- Public finance is essential to remove implementation barriers, demonstrate technologies, mitigate country and policy risks,…

- Design of climate finance architecture and its subsequent capitalisation needs critically depend on design of transfer mechanisms like CDM, no-lose-targets, linked ETS, AAU trading

Conclusions (II)

- CDM is one out of several possible transfer instruments to finance emission reductions in developing countries
- CDM Strengths: focus on projects links well to private sector, direct link to UNFCCC system and obligations
- CDM Weaknesses: unflexible and slow process, potentially an obstacle to domestic climate policies in developing countries
- Future of CDM fundamentally depends on decisions on

  - reform of the CDM (post-Copenhagen)

  - types of developing country commitments (Copenhagen)

  - type and role of other transfer mechanisms (Copenhagen)

- There is more than one viable solution to the problem

Questions for the Discussion

- How to make full use of the private sector creativity and efficiency: CDM & JI, emission & white certificate trading, energy taxation, …?

- What are the advantages and disadvantages of integrating national climate policies and measures with international transfer mechanisms?

- How to sequentially reduce interdependencies from pre-Copenhagen negotiations: types of targets, levels of targets, transfer mechanisms, finance needs, climate finance architecture?

Thank you for Your Attention!

Further information:

Dr. Jochen Harnisch
Coordinator Climate Change Policy

KfW Development Bank
Palmengartenstr. 5-9
D-60325 Frankfurt
Germany
phone: +49 69 7431-9695
e-Mail: jochen.harnisch@kfw.de