The billion dollar bill: Australia's climate finance requirement, 2016-2020

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Date : November 27, 2015

Next week's climate change conference in Paris, COP 21, has called forth not only some 150 national climate change mitigation commitments but also a good number of climate finance commitments covering the period between about now and 2020. In fact many of the mitigation commitments from developing countries depend explicitly for their full realization upon the availability of the resources promised by, in the main, wealthy countries. More immediately, reaching any kind of an agreement in Paris depends critically, just as it did in Copenhagen, on developed countries' coming good with climate finance.

The Paris conference is by no means a fundraising event, but any wealthy countries that have not yet indicated at least broadly how much climate finance they intend to provide up to 2020, including the US and Australia, are likely to experience strong pressure to do so and considerable criticism if they don't—particularly, in Australia's case, from Pacific leaders.

This post looks broadly at the status of OECD governments' climate finance pledges, discusses what a credible Australian COP 21 finance pledge might look like, and concludes with some observations on what would be the key elements of an adequate overall financing outcome in Paris, encompassing all official sources. (It consciously avoids discussion of financing channels and private finance, large subjects in their own right.)

First, let's take a quick look at what happened with wealthy countries' collective 'fast-start' climate finance pledge of US$30 billion for the period 2010-2012, which included A$600 million from Australia, i.e. A$200 million per annum. This commitment is self-reported to have been met in aggregate, in fact exceeded (Australia's national spending report is here). Fast-start finance included some US$5 billion in export credits and non-concessional loans, mainly from Japan and the United States. These are Other Official Flows (OOF) in OECD parlance, as distinct from Official Development Assistance (ODA). A detailed analysis of contributions and allocations can be found here [pdf]. The following chart, lifted from the same source, shows where the largest components of fast-start finance came from.

After the delivery of the fast-start commitment, there were no further collective or individual pledges covering any fixed, multi-year period from 2013 on. Nevertheless, total commitments of the same kind of money can safely be assumed to have exceeded US$10 billion each year in 2013 and 2014 by a considerable margin. That might seem an understatement given the big headline numbers in a recent and controversially rosy report from the OECD's Environment Directorate, which included a bilateral public finance estimate of US$23 billion for each of 2013 and 2014. However, an earlier report from the OECD's Development Cooperation Directorate found that bilateral ODA with climate mitigation or adaptation as its primary purpose, together with climate-related bilateral OOF, totaled US$13.4 billion in 2013. (For some reason, the more recent OECD report did not isolate primary-purpose expenditure.) The volume of core contributions to multilateral funds for climate-related purposes is seemingly not calculated anywhere, but would have to be added to this figure for comparability with fast-start numbers. Anyway, the number is well north of US$10 billion per annum but probably well south of US$23 billion.

Moving to active pledges, there is a collective commitment dating back to the Copenhagen Accord [pdf] in 2009, and subsequently formalised in the 2010 Cancun Agreements [pdf], to 'a goal of mobilising jointly US$100 billion per year by 2020 to address the needs of developing countries … from a wide variety of sources, public and private, bilateral and multilateral, including alternative sources'. There has never been any agreement, or even much discussion, about how to break this number down. People involved in UN climate finance negotiations tend to adopt as a rule of thumb the assumption that this funding might be split evenly between public and private sources.

With the approach of the Paris conference focusing minds, various national pledges have appeared in the course of this year which relate to the period between now and 2020. The UK government announced in late September that it would provide £5.8 billion over the period. Germany said two weeks earlier that it would at least double its current level of annual expenditure, which is about €1.7 billion, by 2020. France said, immediately after the UK announcement, that it would increase its annual funding from €3 billion now to €5 billion by 2020. The EU has said that it will more than double its climate financing by 2020, to 20% of its overall budget which implies about €14 billion. And so on. A recent UNFCCC compilation of pre-Paris pledges, not including the US$3 billion pledge from China, is here.

In terms of projected 2020 annual expenditure, all of this newly pledged public finance might well add up to something in the vicinity of US$50 billion—true to the rule of thumb. It should be noted though that any total derived from the pledges listed by the UNFCCC would include outflows from multilateral organisations to developing countries that in many cases will also have figured in bilateral donors' pledges as inflows to the organisations concerned. So there will be some level of double counting. The UNFCCC itself has not ventured to give a bottom line as the various pledges are fiendishly difficult to align.

The two largest donors, Japan and the US, have not at this point made climate finance commitments for the period 2016?2020. Nor have some other donors more in Australia's league, such as Norway and Canada. However, these last two are quite likely to do so, given Norway's strong track record on climate finance and Canada's recent change of government. More importantly, the weight of commitments already on the table looks to be enough to create strong momentum for additional commitments by other OECD countries. So, if we assume for the sake of argument that Australia does face substantial pressure, in the context of the wider negotiations on a mitigation agreement, to announce its financing envelope for 2016-2020, what might a credible number be? (Politically credible that is, as distinct from morally defensible. There are sometimes attempts to develop metrics determining what constitutes a donor's 'fair share' given their historical emissions, capacity to pay and economic strength, but the present post is not one of them.)

One particularly crude way of arriving at a figure, in answer to the question just posed, is based on the observation that Australia's share in various largely OECD-supported multilateral funds tends to be around 2%. Combining this with the rule of thumb, that half of the US$100 billion to be spent in 2020 might be public money, yields an Australian annual expenditure level of US$1 billion in 2020. One can discount this number somewhat because a significant proportion of the US$50 billion in public finance would be non-concessional lending by multilateral development banks and their bilateral equivalents. This is 'mobilised' by shareholders' capital subscriptions with no need for grant backing by donors. Based on the OECD Development Cooperation Directorate's report on 2013 expenditure, linked above, at the very most half of all public finance would be in this category. Therefore a conservatively discounted level of Australian 2020 expenditure would be US$500 million or so, which is around A$700 million at the current exchange rate.

Another way of working out what might be an expected Australian contribution, on the back of a different envelope, is to assume current annual expenditure by all donors of over US$10 billion and also assume a general nominal doubling by 2020 in line with recent pledges. On this basis, in 2020 bilateral donors would spend over US$20 billion in current prices. We can't know what proportion of 2020 ODA that will represent, but it represents about 15% of current ODA from OECD donors. 15% of today's Australian aid program would be A$600 million, which is in the same ball park as the A$700 million figure derived on other assumptions above. This is all extremely rough, obviously, but rough is as good as it gets in this line of work.

In sum, a politically credible commitment by Australia might well involve spending A$600?700 million per annum on climate change mitigation and adaptation by 2020, and that's quite a conservative estimate. What the current baseline is, nobody can be sure, but with the government's late-2014 funding commitment to the Green Climate Fund and various other climate-relevant mainstream programs, Australia might be able to to claim spending of close to the A$200 million per annum that was achieved over the fast-start period. In fact, the OECD calculated that US$177 million of Australia's bilateral flows were principally related to climate change in 2013 (contributions to multilateral climate funds, if any, would need to be added to this). Even with this high baseline and a back-loaded spending profile (as preferred by finance ministers), delivering on such a commitment would probably entail additional expenditure of at least A$1 billion over the period 2016-2020.

One illustrative spending scenario is provided below. Spending above business-as-usual, in this conservative scenario, totals A$950 million between the 2016 and 2020 financial years. Total spending, including the baseline amounts, is A$1.95 billion.

In short, if the dynamics of COP 21 are such that Australia's representatives cannot exit Paris without giving some sort of signal about the level of new or total climate finance to be provided over the 2016-2020, it seems likely that signaling a figure any less than A$1 billion (new) or A$2 billion (total) would attract justified criticism.

If the government was moved to make a commitment of this magnitude in the heat of the moment, where would the money come from? References to climate financing as ‘new and additional’ still abound in multilateral declarations but climate finance commitments, where concessional, are almost entirely drawn from aid budgets. There is no live debate about their ODA-eligibility. Moreover, there isn’t much pretence these days that climate commitments represent additional ODA (either in the sense of ‘additional to business-as-usual’, somehow defined, or in the sense of ‘additional to 0.7% of GNI’). The UK government, for example, was keen to reassure voters via press release that its 2016-2020 finance commitment ‘is part of the UK’s ODA budget, so is all from within the budget set in legislation at 0.7% of GNI’.

In Australia’s case, there are several options for sourcing this money. The government could decide that a static, A$4 billion aid program should cop the costs, if it were prepared to take the ‘robbing Peter to pay Paul’ flak. Alternatively, and at about the same net cost to the balance sheet, it could create an international version of the Clean Energy Finance Corporation (as canvassed in this article). This amounts to setting up a bilateral Development Finance Institution, which is not inherently a bad idea, but the government would need to accept that most of the expenditure of any such body would not be scored as ODA, since it would make heavy use of guarantees and equity investments. This course of action would also generate flak from the Pacific island countries, who would prefer to see Australia’s money, ODA or not, spent on adaptation.

The simplest, if not cheapest, option would be to use a climate finance commitment to start building Australia’s aid budget back toward A$5 billion per annum, or more. On this course of action, any climate finance commitment would be additional to the current base of A$4 billion per annum, though not all future spending above that base would necessarily be climate finance. Australia’s 2016-2020 pledge would be sourced from a recovering aid budget.

If Australia, and perhaps some other wealthy countries, were to make commitments for 2016?2020 in Paris, there is a further question about what they, and also the earlier pledgers, should be looking for by way of overall financing outcomes. Australia, for one, would be well placed and duty bound—given its role in the Pacific—to argue for a reaffirmation of the principle that adaptation funding should no less than mitigation funding. In addition, all countries with pledges on the table for the 2016-2020 period would have an interest in establishing, for the first time, how much of the US$100 billion target for 2020 should come from public sources, so that the size of the gap left by the non-pledging donors would be apparent. And, finally, pledging countries would preferably underline, for example in their statements about how finance would be allocated, their common interest in supporting developing country participation in future global, regional or bilateral carbon trading arrangements that would, over time, reduce mitigation-related calls on the public purse.

According to Greg Hunt, the environment minister, the Prime Minister ‘may have some very prospective and constructive things to propose’ on the first day of the Paris conference. It is hard to see how he could really be prospective and constructive without saying something specific about Australia’s medium-term financing intentions. Foreign minister Julie Bishop will lead for Australia in the second week of the negotiations, in which finance will loom large. If either Turnbull or Bishop is presented with a billion dollar bill in the course of the next two weeks and feels a desire to pay it, they will have an opportunity to increase Australia’s international standing substantially on both the climate change and development fronts.

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