POLICY BRIEF BY GERMANWATCH, CARE AND OXFAM

G7 in 2022: Five areas for advancing climate finance

The Group of 7 (G7), comprising leading industrialised countries and historically major contributors to the climate crisis, has a particular responsibility to not only deliver its fair share in the globally needed mitigation effort but also to support both necessary social-ecological transformation and management of climate risks and impacts in developing countries. Key aspects in these efforts are strategies to enable swift implementation of the Paris Agreement (especially within this decade), keep the 1.5°C limit within reach, enable all people to adapt to a changing climate, and address unavoidable loss and damage.

While developed countries failed to meet their commitment to provide US$100 billion per year by 2020, the G7 process in 2022 under the German presidency offers the opportunity to take important steps towards a new paradigm for climate finance that is based on needs in recipient countries, in conjunction with improving quality - including through people-centered and rights-based approaches, focusing on the most vulnerable people and countries, enabling easy access and enhancing gender equality, participation and leadership of women and girls. Against that backdrop, this policy brief formulates five key asks to the G7 governments.

Five key asks to the G7 governments

1. Meet and surpass the US$100 billion goal with new and additional finance.
2. Significantly scale-up grant-based adaptation finance.
3. Increase finance for the just-transition and meaningful partnerships – and completely end fossil fuel finance.
4. Provide adequate and additional needs-based climate finance to address loss and damage.
5. Support a needs-based post-2025 climate finance goal.

All relevant ministries – environment, development, and finance – should actively address these areas in the G7 process. Germany, in serving as the G7 presidency, bears a particular responsibility for initiating relevant processes to advance the climate finance agenda together with the G7 partner countries. Moreover, the G7 should agree on taking stock of progress towards its commitments, including at the leader and ministerial levels, in the 2023 and 2024 G7 work programmes.

1 Meet and surpass the US$100 billion goal with new and additional finance

While the G7 has repeatedly reaffirmed[1] developed countries' goal of ramping up climate finance support to developing countries to reach US$100 billion per year, the goal's 2020 deadline was not met. All governments also noted this with deep regret at COP26 in Glasgow. In their *Climate Finance Delivery Plan: Meeting the US$100 Billion Goal*, developed countries suggested they might reach the US$100 billion level by 2023. However, a 3-year delay would accumulate to a sizable shortfall by which the countries would fail to meet their commitment, unless this was compensated for by exceeding $100 billion in later years.

Not all forms of finance are of equal value. Providing climate finance via instruments other than grants, even if concessionally, means developing countries may pay for funded programmes themselves (e.g. when repaying loans). While under the right circumstances this can work for profitable mitigation projects, it is highly problematic for adaptation projects that in many cases will not generate (adequate) return. Instruments such as loans may also worsen what are already highly problematic debt levels in many recipient countries, especially when additional crises, such as the COVID-19 pandemic, exert more pressure on already scarce resources and strained social systems. Also, counting their full nominal values instead of their grant equivalents overestimates the net value of actual support provided. Likewise, mobilised private investments are critical for transforming countries' economies, but they fail to address the existing financing gaps to cover the additional cost of action. Another task is further improving the quality of climate finance, including through better integration of gender equality. This leaves further tasks ahead for the G7, as recognised in 2021.[2]

During the G7 process 2022, the G7 governments should

- Commit to ramping up climate finance support over the coming years. This commitment must be with a view to reaching the US$100 billion level in 2022 and ensuring that in 2020–2025, an average of at least US$100 billion per year in climate finance is delivered to developing countries. This should be on top of finance to meet the goal of providing 0.7% of gross national income (GNI) as development assistance.
- Commit that future climate finance increases are implemented primarily by increasing public grant finance and its share in climate finance, and that accounting is applied more accurately and transparent, including through more honest tagging of the funds' actual climate-relevance, reporting the grant-equivalent of non-grant instruments and providing further qualitative information such as on gender-responsiveness.
- Commit to enhancing people-centred, rights-based, and gender-responsive approaches in climate finance. Accomplish this with a focus on adaptation finance for the most vulnerable countries and people, particularly affected local communities and marginalised populations, while also enhancing climate finance accessibility, especially for countries with capacity constraints.

[1] E.g. paragraph 40 of the Carbis Bay G7 Summit communiqué; see https://www.g7uk.org/wp-content/uploads/2021/06/Carbis-Bay-G7-Summit-Communique-PDF-430KB-25-pages-3-1.pdf. Last retrieved: 2022-02-16.

[2] G7 Gender Equality Council 2021: Building back better for women and girls. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1028387/Report_of_the_G7_Gender_Equality_Advisory_Council_2021-_Building_Back_Better_for_Women_and_Girls_.pdf. Last retrieved: 2022-02-16.

Germany, holding the G7 presidency, should

- Commit to increasing its federal budget allocations for climate finance, to reach at least €8 billion per year by 2025; i.e. with finance mobilised on capital markets for public loans and mobilised private investments on top. Additional climate finance should also be provided to address loss and damage.

2 Significantly scale-up grants-based adaptation finance

Contrary to the agreed upon balanced provision of finance for mitigation and adaptation (within the US$100 billion goal), in 2019, only US$20 billion of about US$80 billion (i.e. about a quarter of all finance reported in the context of the US$100 billion goal) was provided to support adaptation. This falls substantially below the agreed goal as well as real needs in developing countries, meaning that especially in the more vulnerable countries, critical programmes such as those related to supporting food security and access to clean water, or protecting people against worsening climate risks, remain underfunded. This situation risks further increasing gender and other inequalities. Adaptation costs are also set to rise; in its recent Adaptation Gap Report[3] the United Nations Environment Programme (UNEP) estimated an increase of up to US$300 billion per year by 2030. This has been a concern for many years, and in recognising the need to act, COP26 urged developed countries to double adaptation finance between 2019 and 2025, leading to around US$40 billion annually by 2025. It is a small step forward, and still falls woefully short of achieving a true balance between adaptation and mitigation and meeting existing needs.

During the G7 process 2022, the G7 governments should

- Commit to leading efforts to double (from 2019 levels) developed countries' collective provision of climate finance for adaptation by 2025, and set concrete steps towards achieving this.
- Commit to reaching a 50% share for adaptation within G7 countries' individual climate finance provisions by 2025, and advocate for this goal in all public finance institutions in which they are shareholders.
- Commit to ensuring that adaptation finance, including future increases, will be provided in grants rather than loans, and be guided by the Principles for Locally Led Adaptation.[4]

Germany, in holding the G7 presidency, should

- Lead by example and commit to at least doubling its provision of adaptation finance by 2025. Do this through increasing grant-based finance, especially to vulnerable countries, people, and populations.

[3] UNEP, 2021: Adaptation Gap Report 2021; see: https://www.unep.org/resources/adaptation-gap-report-2021. Last retrieved: 2022-02-16.

[4] As developed by the Global Commission on Adaptation; see https://files.wri.org/s3fs-public/uploads/Locally_Led_Adaptation_Principles_-_Endorsement_Version.pdf. Last retrieved: 2022-02-16.

3 Increase finance for the just-transition and meaningful partnerships – and completely end fossil fuel finance

Until 2020, G20 countries, through their public finance institutions and multilateral development banks, still financed greater amounts of fossil fuels internationally than renewables. Oil Change International reports that fossil fuel financing was at least US$63 billion per year between 2018 and – 2020 – two and a half times the investment for renewable energies.[5] Following the exclusion of international coal finance by the last coal financers – China, Japan, and South Korea – COP26 might have been the turning point for all international fossil fuel financing. All G7 countries except for Japan joined the Statement on International Public Support for the Clean Energy Transition, which defines that no direct fossil fuel finance that is not aligned with a 1.5°C degree pathway will be provided. It is crucial that this statement rapidly takes effect in the G7's financing behaviour and extends to non-direct investments. As an alternative and to facilitate social-ecological transformation in partner countries, the G7 should – jointly or bilaterally – support implementing climate and energy partnerships, such as the newly established one with South Africa.

During the G7 process 2022, the G7 governments should

- Commit to setting up and adequately financially support new climate and energy partnerships with emerging economies and developing countries to achieve a just energy transition that provides an attractive alternative to fossil fuel investments. These must be democratically owned partnerships based on local expertise, knowledge, and needs, including workers' needs and rights.
- Commit to working with non-G7 countries in international forums such as the Organisation for Economic Co-operation and Development (OECD) and G20 to increase countries that end export and development financing for fossil fuels.
- Commit to voting in accordance with the signed COP26 statement in all public finance institutions in which they are shareholders, to end fossil fuel finance, for all investment types.

Germany, in holding the G7 presidency, should

- Commit to, by the end of 2022, ending all fossil fuel finance (including infrastructure programmes that directly or indirectly extend the lifetime of fossil fuel use) provided through its export and development financer KFW Bankengruppe.

4 Provide adequate and additional needs-based climate finance to address loss and damage

Climate change-related loss and damage threatens lives and livelihoods, food security, human security, and sustainable economic development, as well as cultures and heritage, particularly in developing countries. Estimated costs of residual loss and damage will rise as high as US$580 billion by 2030, only for developing

[5] Oil Change International/Friends of the Earth 2021: Past Last Call. Available at: http://priceofoil.org/content/uploads/2021/10/Past-Last-Call-G20-Public-Finance-Report.pdf. Last retrieved: 2022-02-16.

countries.[6] However, to date, no specific percentage of international climate finance is assigned to loss and damage. The G7 countries, as the historic major contributors to the climate crisis and as leading industrialised countries, have a special responsibility to support vulnerable countries in dealing with climate impacts that can no longer be adapted to. In the past, the G7 announced its willingness to 'intensify our support particularly for vulnerable countries' own efforts to manage climate change related disaster risk and to build resilience.[7] Particularly as part of the G20-V20 InsuResilience Global Partnership, enhancing insurance coverage for the most vulnerable and developing new insurance and other types of climate and disaster risk finance solutions have been supported, including through commitments to strengthening gender integration. Adequate and additional needs-based support to avert, minimise, and address loss and damage comprehensively is, however, insufficient. Additionally, support regarding coverage of slow-onset processes and non-economic loss and damage is still largely absent. COP26 also failed to provide sufficient support to the most vulnerable people and countries. In this context, the G7 is expected to demonstrate leadership in delivering solutions that tackle loss and damage.

During the G7 process 2022, the G7 governments should

- Commit to providing adequate and additional needs-based funding to address loss and damage for developing countries at a scale commensurate to existing and future needs, taking equity considerations into account.
- Commit to developing, jointly with vulnerable countries, a system of global protection. This should provide financial and other support for comprehensive, poverty-oriented, gender-responsive solutions for managing climate risks and address impacts from rapid-onset events and slow-onset processes. This should include:
    - Increased support and suitable institutional arrangements for effective financial protection through pro-poor[8] climate risk insurance approaches, contingency funds, social protection schemes, and assorted national loss and damage mechanisms, additional to other suitable arrangements to directly fund addressing loss and damage, including recovery from it.
    - Assistance for countries to address non-economic loss and damage, such as by establishing and supporting mechanisms for rapid assistance to protect and preserve cultural heritage and minimise loss of culture in crisis situations.[9]
- Commit to engaging constructively in the Glasgow Dialogue to advance long-term arrangements on supporting vulnerable countries in addressing loss and damage. This should include finance, including from innovative sources, and necessary institutions to channel this finance to the most vulnerable.

Germany, in holding the G7 presidency, should

- Initially provide €1 billion in grants as a German start-up contribution, as part of Germany's overall contribution to address loss and damage, to initiate a pledging round of G7 countries for the global protection system.

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[6] Markandya, A./ González-Eguino, M. 2018: Integrated Assessment for Identifying Climate Finance Needs for Loss and Damage: A Critical Review. In: Mechler R./ Bouwer, L./ Schinko, T./ Surminski, S./ Linnerooth-Bayer, J. (eds): Loss and damage from climate change. Concepts, methods and policy options. Springer, 343-362.

[7] Leaders' Declaration. G7 Summit. 7–8 June 2015. Available at: https://sustainabledevelopment.un.org/content/documents/7320LEADERS%20STATEMENT_FINAL_CLEAN.pdf. Last retrieved: 2022-02-16.

[8] Pro-Poor Principles of the InsuResilience Global Partnership. Available at: https://www.insuresilience.org/wp-content/uploads/2019/06/insuresilience_propoor_190529-2.pdf. Last retrieved: 2022-02-16.

[9] KulturGutRetter https://www.kulturgutretter.org/ (mentioned in the German coalition treaty). Last retrieved: 2022-02-16.

5 Supporting a needs-based, post-2025 climate finance goal

While developed countries collectively failed to deliver on the US$100 billion target by 2020, and, at the least, should deliver on this as soon as possible, COP26 has kickstarted negotiations on a new collective quantified goal on climate finance. The South African minister bluntly proposed $US1.3 trillion in 2030. The actual requirement, however, is a set of sub-goals based on developing countries' climate finance needs. This should reflect both key quantitative and qualitative aspects. Notably, the actual climate finance needs remain largely unknown. This is crucial, however, for mobilising the investments and providing the support needed to get on a 1.5°C path, adapt to worsening climate impacts, and address loss and damage.

COP26 has thus far resulted mainly in the agreement to start a more in-depth technical work programme aiming to reach a proper agreement by the end of 2024. Initial conversations have shown that divergences exist both about the scale of the goal and its nature and scope, drawing on experience from the US$100 billion goal. While deliberations on the new goal take place under the United Nations Framework Convention on Climate Change (UNFCCC), the G7 governments could give high-level support of the process, and build developing countries' confidence.

During the G7 process 2022, the G7 governments should

- Commit to constructively engaging in UNFCCC work on the post-2025 finance goal for adopting the new goal in 2024. This can include means such as providing dedicated financing through a suitable channel to support efforts to assess developing countries' climate finance needs, to inform the goal.
- Recognise that the new goal will also cover financial support for addressing (including recovering from) loss and damage. It should also, through its scope and structure, address the different needs related to mitigation, adaptation and loss and damage, including means such as setting differentiated sub-goals, and reflect on the varying usability of different financial instruments, climate finance accessibility, and other qualitative criteria.
- Reaffirm that the G7 and other developed countries must take the lead in mobilising finance and provide their fair shares in assistance to developing countries, especially grant-based finance, under the new goal. This should be consistent with Articles 9.1–9.3 of the Paris Agreement and ensure that countries contribute to climate finance based on their responsibility for causing the crisis and on their capabilities to act.

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