

IDB GROUP AND CLIMATE ACTION

POSITION PAPER

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The IDB Group will lead with new targets on climate action

As one of the leading development partners for Latin American and the Caribbean (LAC), the Inter-American Development Bank Group (IDB Group) is fully committed to lead by example on climate change action. **Since the signing of the Paris Agreement, the IDB Group has provided over \$20 billion in Climate Finance, amounting to about 60% of all Climate Finance to the region from Multilateral Development Banks (MDBs).**

Our [Vision 2025](#) and our [Climate Change Action Plan 2021-2025](#), both published in 2021, respond to complex realities in LAC, which include planning for recovery post-COVID-19, increased fiscal constraints, and greater debt. The IDB Group sees opportunity amid the challenges with a pivot to a green recovery—**because it is a sustainable recovery**. In fact, we are working with our 26 borrowing member countries to ensure they have access to the resources and tools needed to promote a green, sustainable, and potentially transformational recovery. As a development institution, we are focused on addressing the causes of poverty and vulnerability: our work on climate will pave a new way to have greater impact in the long run.

We strive to enhance our role in the green economic recovery and respond with ambition and accountability to the mounting challenge of climate change. For this reason, **we set aspirational targets to align 100% of new operations with the Paris Agreement goals by January 2023, and to deliver a total of \$24 billion in green and Climate Finance in the next four years.**¹ We are also ready to redouble our efforts to mobilize private capital for climate action and to deploy capacity building efforts at a pace and scale that meet the magnitude of the challenge ahead.

To be accountable for these targets, the IDB Group is committed to improving the coherence and transparency of its reporting. **Throughout 2022 we will be developing a new green finance accounting methodology.** The new approach will allow us to fully capture the value of green contributions and incentivize the catalytic sustainability investments needed to shift emissions and climate vulnerability trajectories in the region.

These efforts will require us to build capacities at an unprecedented scale, both within our institution and on various external fronts. **To lead these efforts, we have already started placing climate change and sustainability specialists in country offices across the region. We have increased our presence from five countries in 2020 to 15 countries in 2021, aiming to cover all 26 countries by 2024.** These movements will better enable our country specialists to work with governments on climate policy and plans, align the array of the IDB's financial tools and technical know-how with national climate plans and policies, and **help countries access concessional finance and mobilize private finance** to deliver national commitments.

With our firm grasp of the key issues driving development and investment in the region, at the IDB Group will continue to help build the capacity of our partners. In doing so, we will ensure climate action is not merely compatible with economic growth; rather, **our raised ambition on climate and our commitment to work with our partners towards decarbonization, will be the drivers of innovation for a new era of competitiveness in the LAC region.**

¹ This commitment is pending approval by IDB Group's Board of Directors, expected in 2022.

Report card: IDB Group and Paris Alignment

- I. Our focus on climate change is outlined in our Vision 2025 roadmap as well as in our Second Update to the Institutional Strategy. However, we have taken the additional step of designing the **IDB Group's Climate Change Action Plan 2021-2025** that outlines how we will be first movers and leaders in LAC to address the risks of climate change and advance the goals laid out in the Paris Agreement. As part of our action plan, the IDB is committed to:
 - a. Full Paris Alignment of new operations from January 2023 onward.
 - b. Development of approaches to Paris Alignment that respond to countries' priorities and needs (see next section).
 - c. Internal and external knowledge and capacity building.
 - d. Improvements in our incentive structures to increase financial flows towards projects that make active contributions to climate and environmental objectives.
 - e. Movement toward a more ambitious climate target, setting a goal to provide \$24 billion for climate and green finance in the next four years, subject to country demand.
 - f. Expanded use of innovative solutions, tools, and financing structures.
 - g. Sustained action to promote Paris Alignment of internal activities at IDB Group.

A firm grounding on national realities and client's business models is a fundamental feature of IDB Group's Paris Alignment process; this is what fosters country-ownership and realistic implementation mechanisms to fully deliver on country-level climate commitments.

Figure 1. Key steps of IDB Group's approach to more ambitious climate action



Current state of climate action in Latin America and the Caribbean and the importance of a country-specific approach

The urgency of climate action in LAC cannot be overstated. Our estimates indicate that damage caused by climate change could cost the region \$100 billion annually by 2050. Climate change is already considered one of the major disruptors of agriculture and food systems; some of the worst impacts on sustainable development are expected to be felt among those whose livelihood depends on agriculture and the coasts.

This reality makes it so that, despite the socioeconomic setback generated by the COVID crisis, **14 of our borrowing member countries have updated their Nationally Determined Contributions (NDCs) since first submitting to the UNFCCC and, to date, six countries already have Long-Term Strategies (LTS) in place.** Yet, the technical and financial needs of LAC countries to transition to decarbonized climate-resilient economies are varied and vast. Investment is needed to decarbonize infrastructure, to halt and reverse deforestation, to develop and implement policies that manage climate risk and ensure the transition is just and inclusive, to manage its extractive sector, and to engage the private sector as a critical actor in climate action.

LAC is ready for ambitious climate action: nine countries have pledged net-zero targets,² and this number is continuously growing. That is why we are actively supporting our clients in the updating of their **NDCs and development of LTSs and** integrating climate factors in the formulation of **country and sector strategies** (see Figure 2). These are essential country- and client-led processes that will build the roadmaps our region needs for a decarbonized and climate-resilient future.

The IDB Group understands the challenge ahead, and for this reason **we have traced a roadmap that will take country-specific priorities and needs as a basis, and strategically intervene in ways that support further Paris Agreement alignment.** We are already working in this direction through the following actions:

- **Systematic incorporation of long-term decarbonization and climate resilience objectives in sector and country strategies**, ensuring they consider transition risks, contributions to a just transition, and tools to address the vulnerability of the country and sector to the impacts of climate change.
- **Strengthening of the collaboration between the public and private arms of the IDB Group**, in ways that help garner the multi-stakeholder support countries need to trace socially legitimate, technically robust, and financially viable net-zero pathways.
- **Increased efforts to provide technical and financial support to governments and private companies**, to implement decarbonization technologies and develop decarbonization financing schemes.
- **Support activities for ministries of finance and ministries of planning** to incorporate sustainability indicators into their decision-making on public expenditures and infrastructure planning. This is key in guiding national budgets toward the implementation of climate commitments as reflected in NDCs and LTSs.

² Argentina, Barbados, Brazil, Chile, Costa Rica, Dominican Republic, Jamaica, Panama, and Uruguay. Source: Climate Watch Net Zero Tracker.

- **Enhanced collaboration with the private sector and financial intermediaries**, using a bottom-up approach to promote their Paris Alignment. IDB Invest has already begun to assist private sector clients in the development of decarbonization financing structures to help them transition to low-carbon energy and transportation. We will continue to collaborate with MDBs to finalize guidance for operations with financial intermediaries, which will serve as a basis to establish similar collaboration arrangements with them. Together, these approaches will further support clients towards the progressive adoption of climate commitments appropriate to their market segments, stages of maturity, and evolving capacities toward sustainability.
- **Support for climate entrepreneurship through IDB Lab**, our innovation laboratory where we test, demonstrate, and help scale up the ideas and technologies that help partners accelerate the transition. This work has a crucial role in testing innovative actions in the areas of biodiversity, resilience, hydrogen, and retraining for the just transition, among others.
- **Advancement of an increasingly ambitious knowledge agenda**, which incorporates tools and approaches to raise awareness on science-based targets and climate investment trends that will shape the future of LAC markets; strategies to reduce the exposure to climate transition risks and costly stranded assets; to manage the fiscal impacts of decarbonization; and to harness opportunities for the catalytic mobilization of private capital.

Leveraging opportunity: Key milestones and progress of the IDB Group

Since the signing of the Paris Agreement, the IDB Group has approved more than \$20 billion in Climate Finance and built substantial knowledge on long-term [decarbonization](#) and [resilience](#). We have also offered a broad range of technical support options to member countries and clients for furthering their action on climate change (see Figure 2).

Our record of accomplishment, knowledge, and financial products fostering climate innovation, has helped us identify new avenues for more climate action. Ongoing operations that assist the economic recovery of countries already include green job promotion and support for re-skilling and up-skilling, in ways leading to economic diversification. Our technical assistance is also developing to span the design of climate-resilient social transfers, incentives for the development of sustainable livelihoods, progressive fiscal policies, and approaches for ecosystem services' valuation.

Our work on Paris Alignment leverages our ongoing contributions to net-zero and climate-resilient pathways on two key fronts: i) Flagship initiatives by the IDB Group in the LAC region that provide models for decarbonization, which can be replicated and/or scaled-up; ii) Innovative solutions and financing structures to catalytically mobilize private capital.

I. Flagship climate initiatives in the LAC region

We are supporting countries and clients to identify the specific policies, regulations, and investments required to fulfill their climate change commitments. Some of our efforts include:

- **The development of a [Platform for Ministries of Finance](#), to ensure climate becomes part and parcel of public investment decision**, a request of our member countries. We are working with countries to shape the platform around their specific needs and challenges. Emerging topics include green finance, taxation and climate risk, and sustainable infrastructure and the private sector. We expect to launch the platform soon after COP26.
- **Assistance provided to the Government of Chile in designing a national [Climate Change Financing Strategy](#)** with three pillars, short-term priorities, links to agendas on financial instruments, private sector involvement, and policy, including the design of the LTS.
- Approval of the [Decarbonization Policy-based Loan in Costa Rica](#), a first of its kind from a development institution.
- Support for the [updating of Peru's National Strategy on Climate Change by 2050](#), which incorporates a vision of carbon neutrality and long-term adaptation.
- **In Colombia, in addition to collaborating with the Ministry of Finance to develop a [Climate Change Fiscal Strategy](#), the IDB Group is supporting a sustainable climate-resilient economic recovery through two main initiatives.** First, by providing \$600 million in finance for the Program for Sustainable and Resilient Growth, **which has leveraged an additional \$600 million in donor funds**
- IDB Invest has worked on [several initiatives](#) to include improving our offer to clients of green financial products with the ability, for example to de-risk climate investments, if clients commit to long terms net zero strategies and managing climate risks, following the TCFD recommendations. As such, financial products are complemented with climate advisory services, through which we have delivered knowledge and training on topics such as **strategies to define corporate sustainability policy; tools for GHG accounting; portfolio studies for climate segmentation and design of new business lines; capacity-building on measuring ESG risk, and green frameworks**, among others.

Figure 2. IDB Group's ongoing support for climate action in LAC



Note: The IDB is in the process of initiating support for LTS development with approximately three more countries in the region, and more demand is foreseen.

II. Innovative solutions and financing structures

The IDB Group is constantly seeking to innovate in terms of the value proposition of financial products offered to countries and clients, with the aim of increasing climate action. Examples include:

- **Ongoing contributions to the creation of thematic bonds market**, including green bonds as a new asset class for a wide range of issuers both in the public and private sector. This has provided a decisive push to the development of the green and thematic bond market – the IDB Group has backed 30% of the issuance of green and sustainable bonds in LAC, helping finance green assets, primarily renewable energy, across the region.
- In this regard, we are announcing during COP 26 the **first ever Blue Bond in LAC**. This bond, with a nominal amount of \$37.45 million will provide long-term finance to eligible projects promoting the sustainable use of water resources for economic growth, improved livelihoods, and jobs, as well as ocean ecosystem health.
- We are continuing in our work to **increase capacity among Ministries of Finance to issue sovereign green bonds**.
- **The IDB Group has provided technical cooperation to 40+ National Development Banks (NDBs)**, crowding-in around 400 commercial banks, and 27 capital market operations, leveraging more than \$3 billion of IDB resources with an estimated support of \$450 million of international Climate Finance. By the same token, **IDB Invest has financed 45+ commercial banks and funds** in the last years, across 16 countries in the region, providing from 2016 to date \$820 million, and mobilization of private sector capital close to two times that amount, with an estimated impact of reducing an estimated of 42 million tons of CO₂ equivalent per year.
- Through **blended concessional finance**, the IDB Group has helped crowd in private sector investments that would otherwise not be available to finance projects with high development impact. **These funds have re-balanced risk-reward profiles** for pioneering investments and enabled them to happen. To date, we have leveraged \$5 billion of external investment, unlocking low carbon and climate resilient investments in the region.

For every dollar of blended finance, the IDB Group is leveraging between 9-10 dollars towards climate.

- **IDB Invest has increased its private sector adaptation finance tenfold between 2017 and 2020**, thus diversifying its Climate Finance away from typical renewable energy projects. We now have a specific team tasked with identifying, testing, replicating, and scaling successful private sector adaptation models. At the same time, we are formulating an action plan that further supports this vision.

- **The Accelerator Fund (ACL)**, which is focused on accelerating NDC investments, is one exceptional example of how relatively small amounts of grant funding deployed early can greatly improve the case to unlock the mobilization of large-scale finance for projects aligned with country-level climate goals. This Trust Fund was created in 2016, as a specific fund to target pre-feasibility assistance to accelerate investments. A recent evaluation of this ACL Trust Fund has shown that the overall effectiveness assessment at a portfolio and project level is particularly high when it comes to leveraging additional resources for projects during their pre-investment stages, with a **combined leverage of \$16.5 billion mobilized and unlocked**. This is nearly 1,200 times the amount invested by the ACL funds. Even without considering unlocked markets (which amount to over 85% of the additional leveraged resources), **this represents a ratio of \$74 of mobilized resources for every dollar invested by the donors**.
- **Green rebates are a potential new source of financial innovation** that the IDB Group is currently designing and piloting. These would consist of a discount given on the lending spread attached to IDB's financial products, awarded to countries or clients that achieve verifiable climate, disaster risk management, and biodiversity performance indicators at the project level. New pricing incentives such as this one will introduce versatility to our financial offering, reduce the risk of climate innovation, and further accelerate climate action in our region.

New pricing incentives, such as “green rebates” given to countries and clients that achieve sustainability performance indicators, are currently being tested at the IDB Group as part of our forward-looking approach to achieving flexible access to finance for climate innovation.

IDB Group's Roadmap to Strategic Recovery: The case for a climate-smart overhaul in the region using partnerships and innovation

The current economic juncture demands a **speedy economic recovery; the socioeconomic impacts of recent catastrophic climate events³ demonstrate the imperative need to make resilience one of the backbones for such a recovery**. The IDB Group sees potential for powerful synergies between economic stimulus and climate-smart investments. We must help countries focus their recovery on the sectors with the greatest need to adapt, and most likely to attract capital markets and institutional investors, which are increasingly looking for opportunities in emerging markets with certified sustainable and green investment propositions.

In this context, the climate mainstreaming work that the IDB Group has been leading and refining over the years, has become more relevant than ever. We have unique experience in developing models that de-couple growth from emissions and create the skills needed to face climate risks. This will provide a critical resource for countries to achieve economic recovery and **build back better, greening investments with a focus on long-term plans that are healthy for their population, sustainable for their economies, and competitive for growth**.

³ For example, hurricanes ETA and IOTA in Central America.

We will know whether we have achieved these transformational shifts in three main ways:

- i) First, the IDB Group is already working hard to respond to the needs of the pandemic with tailored investment solutions; **the diversification in range and segmentation of our financial products will guarantee an opportunity to jumpstart all LAC sectors at any development stage seeking to invest in a green and climate-smart recovery.**
- ii) Second, through technical support and financial assistance, we expect to **lead LAC countries into a new era of improved NDCs**, by ensuring they incorporate results and objectives and actions to effectively limit temperature rise, as defined in the Paris Agreement, in clear articulation with forward-looking **LTSS**.
- iii) Finally, we will work relentlessly until **NDCs become an essential component of national investment plans** in our borrowing member countries, and **LTSS serve as the technical basis for the prioritization and design** of sectoral infrastructure planning. In that sense the strategic shifting we are pursuing is to move from a project by project to programmatic approach in the dialogue with countries.

All of this while enhancing our partnerships and collaboration with other MDBs, public and private donors and private partners, to jointly create platforms, investment vehicles, and blended finance instruments that **increase the level of private capital mobilized in support of mitigation and adaptation investments.**

Synergies between economic recovery, climate action and the biodiversity agenda: The Amazon Initiative

The climate change and biodiversity agendas overlap and must be addressed jointly in the context of country-specific economic recovery strategies. This is the rationale behind IDB Group's enhanced efforts to generate nature-based solutions. This approach offers our clients **opportunities to mitigate emissions cost-effectively and strengthen adaptation capacities** to help countries manage the impacts and long-term hazards of climate change **while promoting SDGs.**

Such an approach is illustrated by our [Amazon Initiative](#), which touches on several of the pillars outlined in the IDB's Vision 2025 agenda, and lays out opportunities for spurring the region's recovery while addressing climate action. This flagship effort is devoted to mobilizing public and private resources, including from the multilateral banks, **to forge and implement sustainable development models based on human capital, natural wealth, and the cultural heritage of the Amazon region.** It is the result of seven amazon countries⁴ coming together in 2019 and signing the Leticia Pact to strengthen coordination on the sustainable development of the Amazon. This entails regional action to:

- i) **Promote resilient and diverse landscapes**
- ii) **Foster amazon-positive value chains**
- iii) **Support sustainability in commodity supply chains**

⁴ Signatories of the Leticia Pact are Bolivia, Brazil, Colombia, Ecuador, Guyana, Peru, and Suriname.

These main action lines will seek to tackle deforestation, selective logging, and illegal exploitation of minerals; accelerate restoration and reforestation initiatives in degraded areas; and strengthen the mechanisms that support and promote the sustainable use of forests in every segment of production lines. The collaboration will feature a strong focus on empowerment of Indigenous Peoples and Local Communities (IPLCs), with targets dedicated to ensuring the prioritization of IPLC as beneficiaries.

The Amazon is critically important to ecosystems worldwide: it provides between 35% and 40% of Latin America's fresh water, regulates air quality, stores net carbon emissions, and regulates nutrient and hydrological cycles for the South American continent. The Amazon region is also home to more than 30 million people, which include approximately 1.5 million indigenous people and more than 5 million people of African descent.

The launch of the Amazon Initiative **aimed for a total of \$1 billion in capital mobilization**; following an initial commitment by the IDB Group of **\$20 million in seed capital**, interested donors have committed a further **\$34 million** to establish the Amazon Bioeconomy and Forest Management Multi-Donor Trust Fund. Additionally, a **\$279 million investment from the Green Climate Fund (GCF)** has been recently announced in support for the **Amazon Bioeconomy Fund, with a total pool of \$600 million for the program**. This will encourage private investment in key bioeconomy areas: sustainable agroforestry, native palm cultivation, non-timber natural forest products, growing native species timber, aquaculture, and community-led nature tourism. Implementation will be carried out in close coordination with the Amazonian countries and the Amazon Cooperation Treaty Organization (ACTO).

The Way Forward: More ambitious targets, full Paris Alignment, and partnerships to catalyze private capital mobilization

Aligning our financial flows to the Paris Agreement and increasing our contributions to green investment in LAC is an ambitious and promising road for the IDB Group. There is a **growing momentum for climate action and interest among our partners and members** to do this, including public and private banks.

The IDB Group had established a Climate Finance floor of 30% of our total lending volume, as well as a mandatory 40% and 65% share of projects with climate components for IDB Invest and IDB, respectively.

In 2019, the IDB Group delivered almost \$4.9 billion in Climate Finance, amounting 29% of total lending volume. In 2020, COVID-19 redirected lending towards urgent fiscal and social measures, limiting opportunities for climate finance. Nonetheless, the IDB Group's active role in promoting a green and sustainable economic recovery has paid off, and in 2021 we are observing an uptick in our clients' interest for projects related to policies for a green and resilient economy, and new investments in low-carbon technologies.

Thus far in 2021, IDB and IDB Invest have already achieved climate components in 69% and 58% of projects, respectively. Conservative estimations for Climate Finance until the end of the year are close to 25% of long-term lending. We expect these levels to rebound as

countries begin their recovery, until it doubles 2020 levels by 2025, amounting to a total \$24 billion in the next four years.

To build an inclusive, low-carbon, and resilient economy, the region must increase investment in sustainable infrastructure, sustainable cities, and rural development. But the “narrow” definition of Climate Finance can be counter-productive in a context of sustainable recovery. As the economic recovery takes root, the IDB Group must not only focus its attention on nation-wide impacts; but also, **local environmental conditions must be a priority**. Countries and private clients in the region recovery need to include not only climate financing but also actions to reduce biodiversity loss, ensure sound management of chemicals and other environmental threats. As the region recovers from COVID-19, it will also need financing for its local ecosystems, supporting plans for a healthy sustainable recovery.⁵

In this context, it is clear to us that the appetite for economic stimulus coincides with IDB Group’s intention to increase the share of resources channeled to **green finance: including climate change investments but also going beyond by investing in an environmentally sustainable economy**. In line with Vision 2025, **enhanced corporate targets for green finance** will be an integral component of IDB Group’s approach to social and economic recovery in LAC.

Institutional investors are rising to become particularly powerful potential allies to bridge investment gaps in LAC by means of green finance, given their increasing interest in net-zero initiatives and Paris-aligned vehicles. The development impact of such a trajectory would be massive, as their participation would be a forceful signal for capital markets to invest in our region, allowing us to go [from billions to trillions](#) in private capital mobilization.

Accordingly, the IDB Group has the goal to harness these fast-paced capital dynamics and ensure they result in accelerated opportunities for green growth in the region. We are confident our commitment to ensuring Paris Alignment and bolstering green finance investment opportunities, paired with our ability to de-risk innovative solutions through blended finance, as well as mobilize private capital towards the Region, will be a winning formula that will make the hopes for a green recovery a solid reality.

⁵ Green finance investments are those that include pollution abatement, recycling and re-use, surface water, soil, and groundwater, healthy ecosystems, sustainable transport that reduces impacts connected to the movement of goods and people, environmental goods, and provision of environmental services, access to water quality efficient water supply, treatment, and sanitation. Green finance is the broadening of the environmental dimensions of investments, from projects in sustainable energy and resource (water and materials) efficiency, to all other types of projects that result in physical environmental benefits.