DI Analyse

Jens Asker Aarkrog Wahlgren (jwah@di.dk)
Josefine Sander Butler (josb@di.dk)

MARCH 2024

Climate finance is more important than ever before

Climate finance – what will be needed?

2024 is the year of climate finance

After a year of temperature records, with the European Union's Copernicus Earth Observation Programme concluding that February 2024 was the 9th temperature record-breaking month in a row, the need for climate action has never been greater. We are off-track to meet the Paris Agreement, and one way to get us back on track is to amplify climate finance and direct it to where it is most needed. As Executive Secretary to the UNFCCC, Simon Stiell, puts it, climate finance is the greatest enabler of climate action, and thus the importance of climate finance cannot be overstated.

2024 will be the year of climate finance. This will be evident at COP29 in Baku, where climate finance is expected to be the paramount issue on the agenda. Also, the events leading up to COP29, such as Copenhagen Ministerial in late March and New York Climate Week in September, will revolve around climate finance.

What is climate finance?

According to UNFCCC, "*Climate finance refers to local, national, or transnational financing, drawn from public, private and alternative sources of financing, that seeks to support mitigation and adaptation actions that will address climate change*." Climate finance can be derived from sources such as governments, development finance institutions, corporations, and households, and it can be used for both mitigation and adaptation efforts.

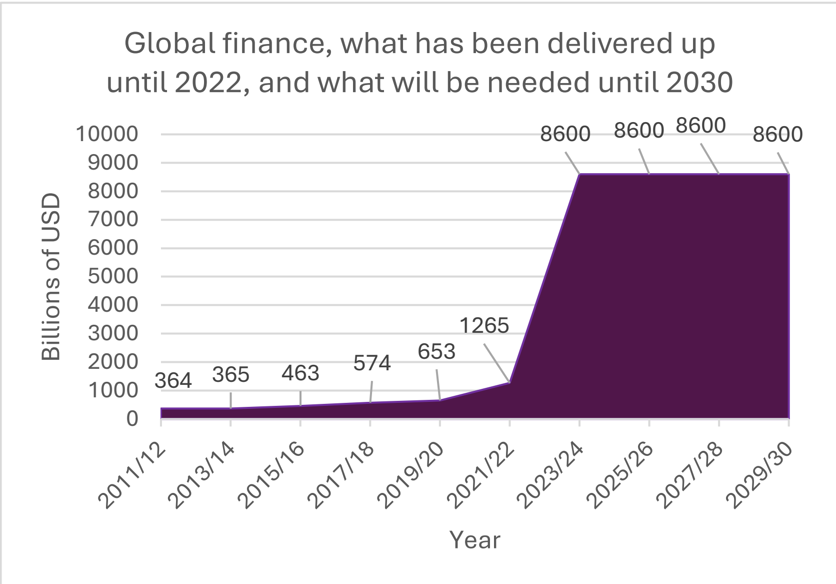
How much climate finance will be needed?

The analysis and advisory organisation, Climate Policy Initiative (CPI), estimates that average annual climate finance flows reached almost

USD 1,3 trillion in 2021/2022[1], approximately one pct. of global GDP, close to double of the climate finance flows the year prior. The rapid increase was primarily driven by mitigation finance, where the majority of the finance flowed to the following three sectors: Energy systems, transport, and buildings & infrastructure. The sources of the USD 1,3 trillion were split almost equally between public and private institutions.

Although USD 1,3 trillion may seem like an astronomical number, CPI estimates that approximately an average of USD 8,6 trillion of global climate finance will be needed every year until 2030 in order to align with the 1,5 degree Paris-agreement target. Thus, the world needs to see a rapid increase in annual climate finance every year until 2030 - a number that is expected to further increase on the other side of 2030 as the world seeks to reach climate neutrality.

Figure 1: Global climate finance, what has been delivered up until 2022, and what will be needed until 2030



Source: Climate Policy Initiative (2023)

*Up until 2021/22, the data is based on actual flows of climate finance. From 2022 on, it is based on CPI's estimate for needed climate finance flows.

[1] Climate finance flows are reported as an average of two year to account for annual fluctuations in data.

Dansk Industri

The Global South

If we look only at the Global South, excluding China, a key report from the Independent High-Level Expert Group on Climate Finance concludes that around USD 2.4 trillion of investments a year will be needed by 2030 to secure a just energy transition, adaptation, resilience, loss and damage, and nature conservation. This is four times as much as the current levels.

According to the 2023-report from the Independent High-Level Expert Group on Climate Finance, The Global South is falling behind in the low-carbon transition, with more than 90 pct. of the increase in clean energy since 2021 taking place in the Global North and China. The same goes for investments in nature, where 80 pct. of finance remains in the Global North and China, although the Global South accounts for an estimated 90 pct. of the investment opportunity in restoring and protecting nature.

Who can deliver the climate finance?

Whereas total climate finance flows reached USD 1,3 trillion, The International Monetary Fund estimates that fossil fuel subsidies globally accounted for USD 7 trillion in 2022. It is therefore imperative that these finance flows are swiftly directed towards climate finance instead.

The report from the Independent High-Level Expert Group on Climate Finance points to four sources of finance that all will be key to amplify climate action: domestic public resources, the private sector, multilateral development banks (MDCs), and concessional finance.

Private climate finance to accelerate action

The report concludes that at least USD 1 trillion a year of private climate capital with be needed in the Global South, excluding China, by 2030. It further estimates that private finance to the Global South will need to be increased by more than 15 times the current levels to deliver on climate mitigation goals. Thus, enhancing private climate finance will be a prerequisite to accelerating climate action. The problem with attracting private investments must be addressed. One way to do so is to ensure the right political framework is in place that best support and incentivise long-term private climate finance. Another way is to ramp up investments in public sector infrastructure to enable more private climate finance.

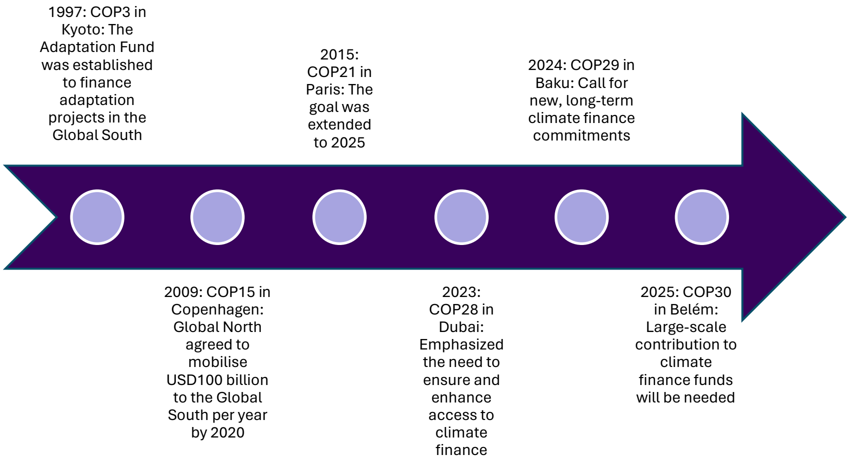
Climate finance at COP from then to now

Climate finance and COP – why does it matter?

COP provides the ideal international setting to establish an effective framework for climate finance that ensures the money flows where it benefits climate mitigation and adaptation the most. And although previous COP meetings have not resulted in the climate finance needed to effectively combat climate change, they have taken important steps in the right direction.

At COP28 in Dubai, the final global stocktake text emphasized the need to ensure and enhance access to climate finance in all geographical regions and sectors and it urged the Global North to take the lead in mobilising climate finance. The UNFCCC has stated that governments must establish new climate finance goals at COP29, reflecting the scale and urgency of the climate challenge. This requires an update of the commitments made by the Global North at COP15 in Copenhagen in 2009 to mobilise USD 100 billion per year to the Global South. Furthermore, COP29 must propose a new framework for long-term climate finance will be key to ensure the climate finance framework is ready for large-scale contributions at COP30 in 2025.

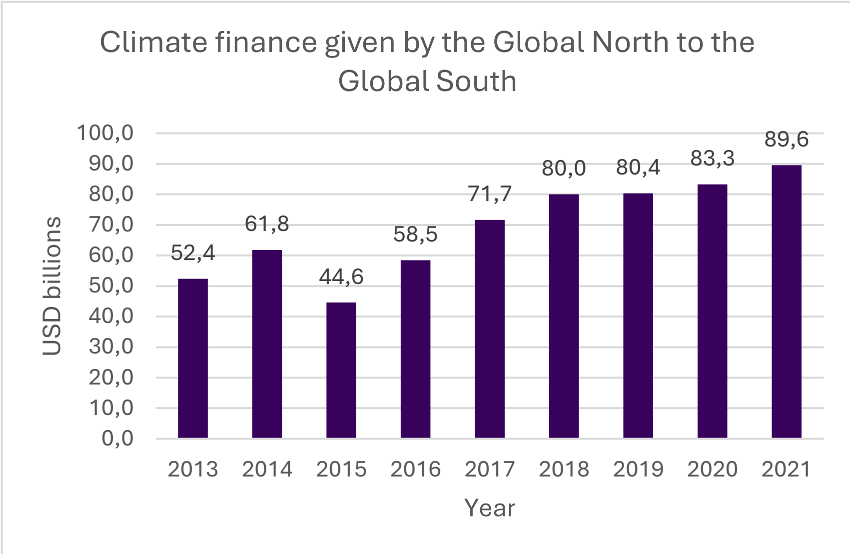
Figure 2: Timeline of climate finance at COP



Source: UNFCCC: Introduction to Climate Finance

As far as the USD 100 billion pledge goes, the Global North have so far underdelivered. Figure 2 visualises that climate finance has been on an upward trend; however, the developed economies still fall short of meeting the goal in 2021 by more than USD 10 billion.

Figure 3: Climate finance for the Global South



Source: OECD (2023)

According to the OECD, it is likely that the Global North met the USD 100 billion target in 2023, due to an increase in finance from multilateral development banks. But after years of failing to meet this target, the trust in the Global North has eroded. And not only that, the USD 100 billion is nowhere close to being sufficient to deliver the needed climate action, especially considered that the last three years of inflation have decreased the value of the USD 100 billion.

Denmark, climate finance – what is our role?

Denmark is increasing climate finance

Denmark has thrown itself into the global efforts to mobilise climate finance. The Danish government has stated in its green work programme from September 2023 that they expect Denmark to deliver at least one pct. of the agreed USD 100 billion goal in both 2023 and 2024. The Danish government has further set a Global Climate Action Strategy to shift financial flows to green by enhancing climate friendly investments. This includes supporting climate investments at home, but also increasing the mobilisation of climate finance to the Global South. This will be done in collaboration with the private sector.

Climate finance pledges have been made by both the public and private sector in Denmark. In 2019, Danish pension funds made a collective pledge to invest an additional USD 40 billion in clean energy to reach a total of USD 66,5 billion by 2030. The Danish government has also decided to increase the Investment Fund for Developing Countries (IFU)'s capital base by USD 2 billion. In 2021, the IFU mobilised over DKK 2 billion in finance for climate projects.

Why is it good for Danish companies?

We need to shift our focus from climate plans to climate action, and the companies will be at the forefront of this shift. Increased climate finance is great news for Danish companies. They have the skills to develop, supply, and export green solutions that can guarantee reductions in greenhouse gas reductions both inside and outside the Danish borders.

Sources

1. Copernicus (2024): Warmest February on record, the 9th consecutive warmest month: Warmest February on record, the 9th consecutive warmest month | Copernicus
2. CPI (2023): Global Landscape of Climate Finance 2023 - CPI (climatepolicyinitiative.org)
3. IMF (2023): Fossil Fuel Subsidies Data: IMF Fossil Fuel Subsidies Data: 2023 Update
4. Independent High-Level Expert Group on Climate Finance (2023): A-Climate-Finance-Framework_IHLEG-Report-2-SUMMARY_0.pdf (globalinfrafacility.org)
5. Ministry of Foreign Affairs of Denmark: Global Climate Action Strategy: Global Climate Action Strategy (um.dk)
6. OECD (2023): Climate Finance and the USD 100 Billion Goal - OECD
7. Regeringen (2023): Klimahandling: KP_23_pjece.pdf (kefm.dk)
8. State of Green (2023): Finansing the Green Transition: Financing the green transition | Get the white paper (stateofgreen.com)
9. UNFCCC (2023): Finance is the great enabler of climate action: "Finance is the great enabler of climate action": Simon Stiell at COP28 Green Climate Fund event | UNFCCC
10. UNFCCC: Introduction to Climate Finance: Introduction to Climate Finance | UNFCCC