

Climate Change Adaptation Finance: Opportunity to Build a more Resilient Recovery

by Jamal Saghir
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1. Context¹

Climate-change impacts are mounting, and with them the need to advance on adaptation.² Even if emission-reduction efforts succeed and the world meets the goal of holding average temperature increases to below 2°C, there are some changes already locked into universal systems that will have unavoidable consequences and therefore the need to adapt. Recent progress on adaptation and in particular in raising funds has slowed. Finance is critical to accelerating climate adaptation, but flows remain far short of what is needed given escalating climate risks. The post-COVID pandemic economic recovery plans provide a unique opportunity to make economies and communities more adapted and resilient to climate change.³

Before the current COVID crisis, US\$ 30 billion in adaptation finance flowed on average annually in 2017 and 2018, already far below the expected needs of up to US\$ 300 billion annually by 2030. Almost all adaptation finance tracked was funded by public actors and in particular Development Financial Institutions (DFIs) alone accounted close to 80 percent of

¹ This viewpoint is based on our detailed assessment in the Finance chapter of the Global Center on Adaptation State and Trends in Adaptation Report 2020.

<https://www.cas2021.com/press/documents/reports/2021/01/22/state-and-trends-in-adaptation-report-2020>.

² The terms ‘adaptation’ and ‘resilience’ are used as defined by the Intergovernmental Panel on Climate Change (IPCC).**Adaptation:** the process of adjustment to actual or expected climate and its effects. In human systems, adaptation seeks to moderate harm or exploit beneficial opportunities. In natural systems, human intervention may facilitate adjustment to expected climate and its effects. **Resilience:** the ability of a system and its component parts to anticipate, absorb, accommodate, or recover from the effects of a hazardous event in a timely and efficient manner, including through ensuring the preservation, restoration, or improvement of its essential basic structures and functions.

³ Saghir, J. & E.J. Ijjasz-Vasquez. (2019). Climate Adaptation in Post-Pandemic Economic Recovery. *Global Governance Lab Policy Brief*. Montreal, Canada: Institute for the Study of International Development, McGill University.

total adaptation finance in 2017-18, while less than US\$ 500 million of tracked adaptation finance flowed from private actors.⁴

On the other hand, trillions of dollars were pledged so far to recover from the Covid-19 pandemic. They represent both an opportunity and a potential threat to help accelerating adaptation. As stated in the premier international organisation, the Global Centre on Adaptation (GCA) analysis, the amount - \$12 trillion to date in G20 recovery packages - is an opportunity because climate adaptation has the potential to significantly enhance the effectiveness of economic recovery plans. Dollar for dollar, climate adaptation earns higher returns than traditional investments, delivering benefits worth between 2 and 10 times the original cost.⁵

Importantly, the recovery plans announced so far largely overlook the opportunity of investing in climate adaptation to help communities recover better from Covid-19, as well as prepare them for future challenges. These include other pandemics as well as climate change. Governments must put climate adaptation at the heart of their recovery plans. Building resilience to climate impacts should be integrated into every aspect of the global recovery.

Faced with bigger public debt burdens due to emergency spending and lower tax revenues, some G20 nations are already cutting overseas aid. The financial market turmoil that followed the coronavirus outbreak has raised significant barriers for many climate-vulnerable and indebted countries in accessing international credit markets. Across the globe, countries will have less fiscal space in the coming years to deal with climate and other systemic shocks, which makes investing now to reduce the impact of future disasters even more important.

This viewpoint argues that approach need not restrict or subvert other investment priorities. However, as the GCA analysis shows it is now the opportunities for triple wins between economy, health and climate in health and sanitation, agriculture and infrastructure, including through a focus on nature-based solutions as a powerful job creator. To support governments in capturing these opportunities, public development banks and other multilateral institutions have a huge role to play. Climate sensitive COVID-response facilities, enhanced risk pooling, debt relief, and new climate resilience bonds are some of the instruments that must be rolled out.⁶

2. Climate adaptation underfunded, short of need

Climate adaptation is not only underfunded, but also under-represented in the broader field of climate action, constituting according to OECD only 5 percent of global finance flows. Moreover, according to GCA's recent analysis and report, funds for adaptation are broadly distributed across three sectors: water and wastewater management (\$9.8 billion); agriculture and land use (\$6.9 billion); and disaster risk management (\$6.3 billion). But these funds do not always go to the most climate vulnerable regions. East Asia and the Pacific received almost double the adaptation finance (35 percent of the total) as Africa (19 percent), and almost three times as much as Latin America and the Caribbean (11 percent). This mismatch between financial flows

⁴ Adaptation Finance in the Context of COVID-19: The role of Public Development Banks in promoting a resilient recovery GCA/CPI. 2020. <https://gca.org/wp-content/uploads/2021/01/GCA-Adaption-in-Finance-Report.pdf>

⁵ Global Centre on Adaptation State and Trends in Adaptation Report 2020. <https://www.cas2021.com/press/documents/reports/2021/01/22/state-and-trends-in-adaptation-report-2020>.

⁶ Adaptation Finance in the Context of COVID-19: The role of Public Development Banks in promoting a resilient recovery GCA/CPI. 2020. <https://gca.org/wp-content/uploads/2021/01/GCA-Adaption-in-Finance-Report.pdf>

and the vulnerability of different regions should be addressed in greater detail when designing policy support, ensuring that physical climate risks are integrated into fiscal and financial decision-making.⁷

3. The challenges of private sector leverage

Private sources accounted for less than \$500 million a year of the \$30 billion in annual adaptation finance tracked in 2017-18.⁸ Furthermore, just 3% of private finance mobilized under the Paris Agreement goal in 2018 went towards adaptation ends, with over 95% going towards mitigation.⁹ While there are gaps in the global data, the low figure indicates that the private sector - businesses and financial institutions alike - are failing to respond to the climate risks in their midst. A number of reasons may account for this low level of engagement including assessing and pricing climate risk and the fact that private sector is not obliged to disclose physical climate risks at present.

Several initiatives such as the Coalition for Climate Resilient Investments are working to develop the tools and methodologies for firms to price climate risk into their decision making. There is also a role for DFI in de-risking private investment, providing technical assistance to potential investors, and providing concessional resources where projects have a strong public good element, particularly in least developed and vulnerable countries. Recent developments in the use of new financial instruments, for example through the first dedicated Resilience Bond launched by EBRD in 2019,¹⁰ show evidence of new approaches with potential for replication.

4. Diversification of financial instruments

There is evidence of a current over-reliance on project-based loans in the delivery of adaptation finance. Many international players including the World Bank¹¹ called on the diversification of instruments used to deliver climate finance, including an increased up of policy-based finance to complement the majority-share project-based financing.¹²

In addition to finance for preparedness, the Covid-19 crisis has highlighted the value of channels such as national disaster funds, contingent credit lines, insurance policies, and catastrophe bonds, that can ensure the quick delivery of finance following a shock. Going forward, it will be important to consider lessons learned, and ensuring a risk finance landscape that is prepared to deal with both climate and health shocks in a way that protects the most vulnerable and complements investment in ex-ante resilience investment.

In the context of Covid-19 and the looming debt challenges many countries will face, debt instruments such as green bonds - including climate resilience bonds - may, in certain cases, offer

⁷ Adaptation Finance in the Context of COVID-19: The role of Public Development Banks in promoting a resilient recovery GCA/CPI forthcoming GCA/CPI. 2020

⁸ <https://www.climatepolicyinitiative.org/publication/global-landscape-of-climate-finance-2019/>

⁹ [Climate Finance Provided and Mobilised by Developed Countries in 2013-18 | en | OECD](#)

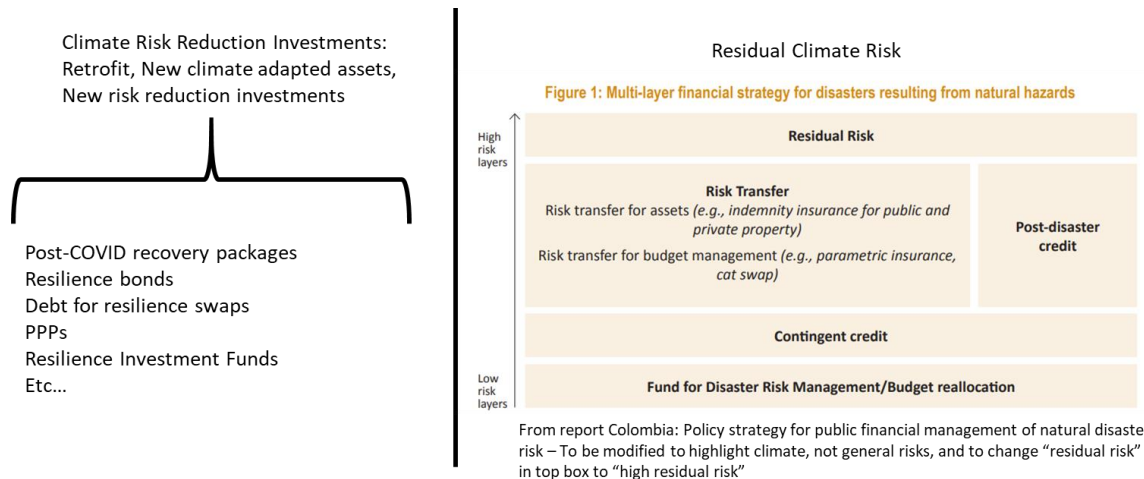
¹⁰ <https://www.ebrd.com/news/2019/worlds-first-dedicated-climate-resilience-bond-for-us-700m-is-issued-by-ebrd.html>

¹¹ World Bank, 2018, *Action Plan on Climate Change Adaptation and Resilience*

¹² World Bank, 2020, *Transformative Climate Finance: A new approach for climate finance to achieve low-carbon resilient development*

a much-needed way to leverage short and medium-term private finance for resilience aims. There is a need for new and coordinated instruments development at scale.

Financing for Adaptation and Resilience Needs New and Coordinated Instruments at Scale



Innovative finance structures should enable developing countries to continue investing in resilient, post-Covid recoveries without increasing their sovereign debt burdens. One such innovative mechanism is the ‘debt-for-climate swaps’¹³ initiative, in which there is a partial cancellation of debt by the creditor government, transformation of the remaining debt into local currency, and direction of the proceeds towards investment in climate action.

There is also a need for blended finance using philanthropic and public funds - typically provided through development finance institutions - to de-risk private investment in new markets, technologies and practices. This co-financing model uses public resources to leverage much larger private financial flows to scale up investments in adaptation, through a risk-sharing mechanism between public and private sectors.

5. Conclusion

In the Covid-19 induced economic context of constrained fiscal space and reduced investor appetite, it may be more important than ever to consider how DFI partners can leverage private finance for adaptation. Funding for climate adaptation needs to increase ten-fold - to an estimated \$140 billion to \$300 billion a year by 2030 - to meet the growing needs of vulnerable communities in the World¹⁴. New dedicated financial products such as climate resilience bonds could help climate-stressed countries tap institutional finance. Blended finance could also help de-risk private-sector investment in new technologies and climate-adaptive solutions. Lastly, a number of countries are exploring innovative financing instruments—such as debt-for-climate swaps—to increase their access to climate finance without increasing their sovereign debt.

¹³ <https://pubs.iied.org/16674IIED/>

¹⁴ <https://www.cas2021.com/press/documents/reports/2021/01/22/state-and-trends-in-adaptation-report-2020>.

Together, these instruments would help shift more financial flows towards a low-carbon, climate-resilient future. It would also enable developing countries to catalyse much needed private finance to scale up climate action.

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