Risks and opportunities

G7 Environment Workshop: Multilateral Development Banks supporting the Paris Agreement and the Agenda 2020

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March 28th, 2017

ODI OILCHANGE INTERNATIONAL

Empty promises

G20 subsidies to oil, gas and coal production

Elizabeth Bast, Alex Doukas, Sam Pickard, Laurie van der Burg and Shelagh Whitley

Report
November 2015

THE NEW CLIMATE ECONOMY
The Global Commission on the Economy and Climate

ODI

Working Paper

Fossil Fuel Subsidy Reform: From Rhetoric to Reality

Shelagh Whitley and Laurie van der Burg

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Executive Summary

Worldwide, a significant proportion of the private sector receives some level of support, interventions and subsidies from the public sector. In the specific case of energy subsidies (of which fossil fuels are a subset) their use has been historically linked to supporting energy security, domestic energy production and access to energy.

In recent years, however, accounting for the full economic, social and environmental costs and benefits of subsidies for fossil fuels, along with the development of other government interventions to achieve the same objectives, has led to demands to start removing them. This report outlines the economic, social and environmental costs of fossil fuel subsidies, emerging evidence of the benefits to be derived from their reform and opportunities and processes to support such reform.

Fossil fuel subsidies can inhibit sustainable economic development by creating a burden on government budgets, reducing resources that could be put to more efficient use within the economy; increasing inequality and undermining access to affordable energy by benefiting the rich rather than the poorest members of society; decreasing the competitiveness of key industries, including low-carbon businesses, by discouraging investment in renewable energy and energy efficiency; increasing the risk of stranded assets (in the event of climate regulation) by encouraging exploration for and production of unburnable carbon; compromising energy security (compared to subsidising alternatives such as renewables and energy efficiency); damaging public health by increasing air pollution; and negating carbon price signals.

Despite this mounting evidence of the costs of fossil fuel subsidies, and the potential virtuous cycles that could result from their removal, governments are often reticent to undertake reform. Researchers have identified several specific reasons for the persistence of subsidies. Some of these are

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March 2017

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Policy briefing

Six development finance proposals to expand climate investment

Ilmi Granoff, Darius Nassiry, Neil Bird, Christopher Humphrey, Paddy Carter, Alberto Lemma and Annalisa Prizzon

Key messages

- This policy brief describes six promising finance proposals to support greater ambition for low-carbon development:
  1. Increase multilateral development bank (MDB) loan to capital ratios.
  2. Expand development finance institution (DFI) use of guarantees.
  3. Encourage DFIs to invest in clean technology deployment.
  4. Strengthen MDB support of national financial intermediaries.
  5. Scope a new Green Cities Development Bank.
  6. Deliver green debt reimbursement in low-income countries.
- In assessing these proposals in terms of their potential impact on climate investment, we highlight two points. First, there will be differences in the relative cost of political capital required to implement each proposal, which may vary over time and circumstance. Second, each proposal might enlarge the size of the development finance envelope generally or boost funding for climate-related investment more directly.
- Many of the proposed changes require better leveraging of existing resources, rather than new flows and will use existing resources more effectively. The proposals have also not been a significant part of climate finance discussions to date.
- These proposals have the potential for material, scalable impacts and are compatible with climate investment needs.

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G20 commitment to phase out fossil fuel subsidies
Where do we stand?

- Commitment first made in 2009 at Pittsburgh G20 Leaders' Summit: **"rationalize and phase out over the medium term inefficient fossil fuel subsidies that encourage wasteful consumption"**

- Has been reiterated every year since (parallel commitment by APEC)

- Little progress aside from procedural: "peer review" process has undefined methodology, no consistent definition of subsidies, and only a few participants (albeit big countries – US, China, Germany, Mexico) – and coverage of **fossil fuel production subsidies**

- **G7 call for all countries to phase out fossil fuel subsidies by 2025**

- Still no robust framework to track / monitor implementation, which makes assessing progress or comparing countries very difficult

- Also parallel inclusion under the Sustainable Development Goals as a means of implementation of Goal 12 (sustainable production and consumption)

What are subsidies?

A subsidy is any financial contribution by a government or agent of a government that is recipient-specific and confers a benefit on its recipient in comparison to other market participants. (as defined under WTO Agreement 150+ signatories)

Subsidies include:

- all financial contributions or direct support from a government (national subsidies);
- foregone revenue through tax breaks (national subsidies); and
- transfer of risk through provision of debt, equity and guarantees (public finance);
- provision of infrastructure, goods and services below market value (investment by state-owned enterprise).

Direct Spending
(OECD)

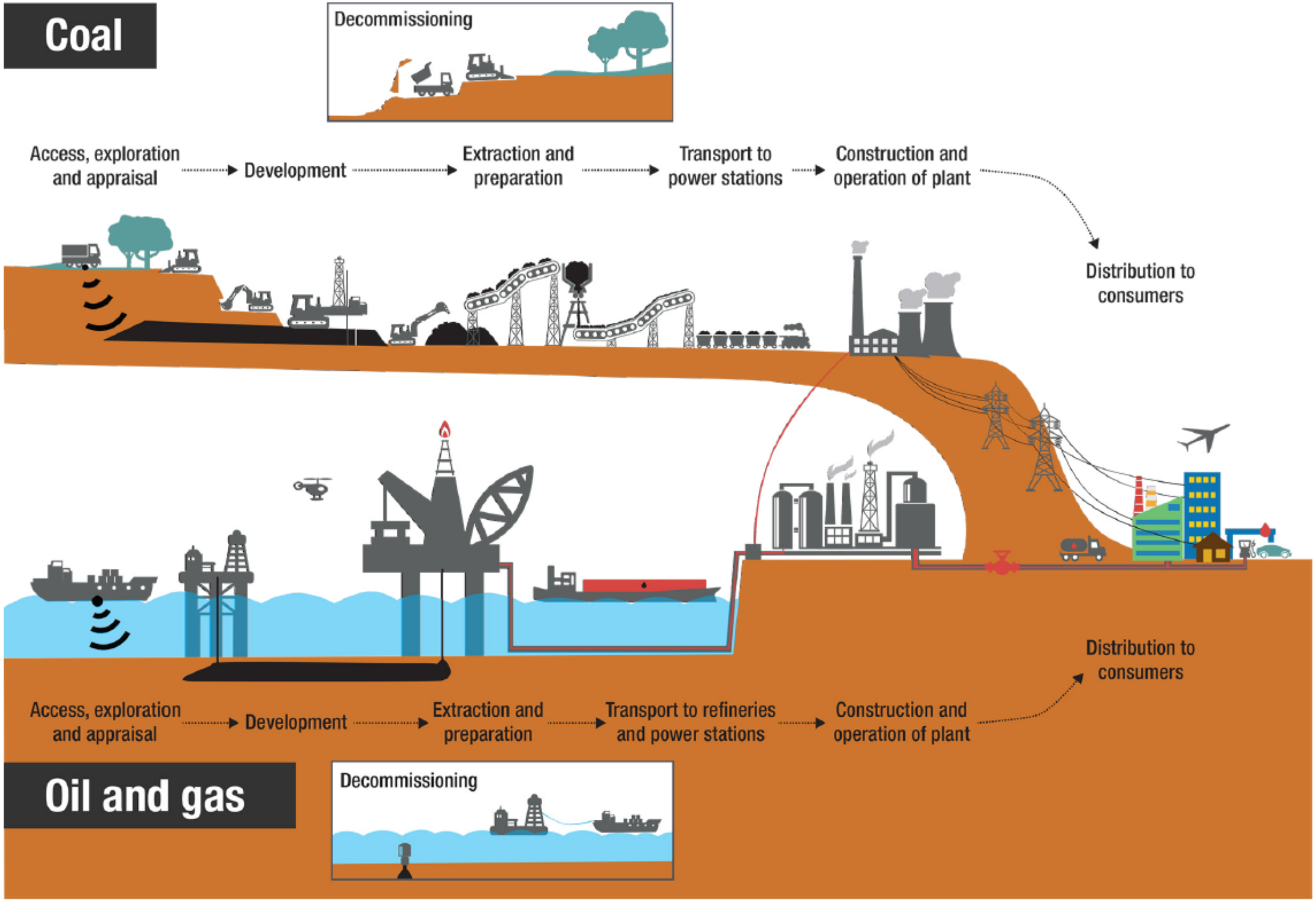
Tax breaks
(OECD)

Public finance
(%)

Support to state-owned enterprise
(%)

Failure to price externalities
(IMF)

Figure 1: Stages of fossil fuel production



Source: authors, 2015.

G20 (and G7) public finance for fossil fuel production

- Collectively, the G20 countries hold between 36% and 75% of the shares of the major multilateral development banks (MDBs) – including AfDB, ADB, EBRD, EIB, IaDB, World Bank Group, IBRD, IDA, IFC, MIGA.

- **Through all MDBs the G20 provided $5.5 billion a year in public finance for fossil fuel production in 2013 and 2014 ($4.6 billion of which was from the G7)**

Table 5. Average annual public finance for fossil fuel production 2013-2014 ($ million)

Country	Financial institutions included in the calculation of average annual public finance (excepting list of MDBs – see Table 6)	Sub-sectors included in the calculation of average annual public finance (by order of contribution)	Average annual domestic public finance	Average annual international public finance	Average annual financing via shares in MDBs	Average annual public finance (2013-14) ($ million)
Canada	EDC	Upstream oil and gas; Oil and gas pipelines; power plants and refineries; Coal-fired power	447	2,088	176	2,711
France	COFACE, Proparco	Oil and gas pipelines, power plants and refineries; Upstream oil and gas; Coal-fired power; Coal mining	–	570	812	1,382
Germany	KfW IPEX, KfW Entwicklungsbank, DEG, Euler Hermes	Oil and gas pipelines, power plants and refineries; Coal-fired power; Upstream oil and gas; Multiple or unspecified fossil fuels; Coal mining	43	1,704	848	2,595

Country	Financial institutions included in the calculation of average annual public finance (excepting list of MDBs – see Table 6)	Sub-sectors included in the calculation of average annual public finance (by order of contribution)	Average annual domestic public finance	Average annual international public finance	Average annual financing via shares in MDBs	Average annual public finance (2013-14) ($ million)
Italy	SACE, CDP	Oil and gas pipelines power plants and refineries; Upstream oil and gas; Coal mining	–	1,510	757	2,267
Japan	JBIC, NEXI, JOGMEC, JICA, DBJ	Oil and gas pipelines, power plants and refineries; Upstream oil and gas; Coal-fired power; Coal mining	351	18,238	440	19,029
United Kingdom	RBS, UKEF, DFID, CDC, BIS	Multiple or unspecified fossil fuels; Upstream oil and gas; Oil and gas pipelines, power plants and refineries; Coal-fired power; Coal mining	72	4,626	817	5,515
United States	USExIm, OPIC	Upstream oil and gas; Oil and gas pipelines, power plants and refineries; Coal-fired power; Coal mining	–	2,992	743	3,735

Options for international support: technical and financial support for subsidy reform

Volumtary ---- Mandatory

- Ensure that development and export finance for fossil fuels is shifted to supporting reform and low-carbon energy
- Linking existing technical and financial support for 'complementary measures' with subsidy reform processes
- Ensure climate finance is not used to support fossil fuels
- Incorporate reform of fossil fuel subsidies in the mechanisms of the UNFCCC through INDCs and NAMAs, and with support from climate finance
- Increase funding of existing subsidy reform initiatives

Ambition

New Climate Economy, 2015

Economic, social and environmental impacts of FF subsidies

- Creating a significant **burden on government budgets**, and reducing resources that could be used more efficiently and sustainably (**ie. for health, education, security, public transportation etc.**)
- **Perpetuating inequality** and limiting access to affordable energy, benefiting the rich and failing to meet the needs of the poorest in society
- **Compromising energy security** (compared to alternatives such as subsidizing renewables and energy efficiency)
- **Decreasing the competitiveness** of key industries, including **low-carbon businesses**, skewing the playing field for investment in clean technologies and energy efficiency
- Damaging **public health** by increasing air pollution
- **Increasing the risk of stranded assets**
- **Negating carbon price signals**

Key G20 asks from over 200 civil society organizations, insurers and investors with $3.5 trillion in AUM.

- Set a clear timeline for the full and equitable phase-out by all G20 members of all fossil fuel subsidies by 2020, starting with the elimination of all subsidies for fossil fuel exploration and coal production.

Leading insurers tell G20 to stop funding fossil fuels by 2020

Aviva, Aegon and Amlin issue joint statement urging leaders to build on previous commitments and end subsidies within four years, reports Climate Home

- Set a clear timeline for the phase out of domestic and international public finance for oil, gas and coal production by 2020.

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Investors press G20 to ratify Paris Agreement swiftly & expand Low Carbon / Green Investment

As leaders of the world's largest economies prepare to attend the upcoming G20 meeting in Hangzhou, China, 130 investors (with over $13 Trillion AUM) from a coalition of six organisations have written to the G20 heads of state urging them to ratify the Paris Climate Agreement this year and call on G20 nations to double global investment in clean energy, tighten up climate disclosure mandates, develop carbon pricing and phase out fossil fuel subsidies.

- Commit all G20 members to complete fossil fuel subsidy peer reviews by the end of 2018, building on the leadership of China and the United States in 2016.

How to use innovations in development finance to expand climate investment:

1

Increase multilateral development bank loan to capital ratios

Read more:
odi.org/new-finance-climate

How to use innovations in development finance to expand climate investment:

2

Expand development finance institutions' use of guarantees

Read more:
odi.org/new-finance-climate

How to use innovations in development finance to expand climate investment:

3

Encourage development finance institutions to invest in clean technology deployment

Read more:
odi.org/new-finance-climate

How to use innovations in development finance to expand climate investment:

4

Strengthen multilateral development bank support of national financial intermediaries

Read more:
odi.org/new-finance-climate

How to use innovations in development finance to expand climate investment:

5

Scope a Global Green Cities Bank

Read more:
odi.org/new-finance-climate

How to use innovations in development finance to expand climate investment:

6

Deliver green debt reimbursement

Read more:
odi.org/new-finance-climate

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