

AfDB – Second opinion

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Summary and conclusion

CICERO - Center for International Climate and Environmental Research, Oslo, has considered the framework for the Green project portfolio of the African Development Bank (AfDB) with respect to their likely impact on climate change.

The documents provided by AfDB give the impression of an institution that is very aware of environmental concerns including the challenges associated with climate change. Being mainly at an early stage of development and industrialization, it is very important that Africa is choosing a low carbon development path that avoids 'lock in' investments in infrastructure which later will make it very difficult and costly to abide by future climate requirements. It is therefore of the outmost importance that institutions like AfDB are taking the following points into account:

- Avoid investments in projects that have the potential of creating 'lock in' that in turn will make a transition to a low carbon society difficult in the not too distant future.
- While investments that lead to emission reductions are good, small reductions are not enough for the longer term, even for Africa. Thus, one should avoid investing in projects that only leads to 'small' reductions over time and that may stand in the way of the more radical shift in technologies that are needed for the longer term. Such 'blind alley' projects are not 'green'. An example could be retrofitting a coal fired power plant.
- Thus, in general the projects area of influence should considered to be wide both in space and time when assessing projects.

"Eligible projects" for the Bank's Green Bonds Portfolio is defined by the Bank as a pool of projects that have been selected firstly based on the Bank's methodology for tracking climate change mitigation and adaptation finance and secondly based on additional criteria to be applied for the specific purpose of the Bank's Green Bonds Portfolio.

The tracking methodology has been developed in cooperation with other multilateral development banks, and the additional criteria are principle based and secure in our opinion that selected projects are in accordance with good climate governance.

The standards are transparent and reasonably simple to apply. The rules and procedures will be made publicly available on a dedicated internet site of the bank.

In conclusion, we find the rules and procedures employed by AfDB to select projects for its Green Bonds Portfolio to be sound and in accordance with good climate governance.

Introduction and documents received

As an independent research institute, CICERO - Center for International Climate and Environmental Research, Oslo, elaborates second opinions on institutions' framework and guidance for assessing and selecting eligible projects for green bond investments, here defined as investments in projects that will or may have effects on the mitigation of, or adaptation to, anthropogenic climate change.

These second opinions are normally restricted to an evaluation of the mechanisms or framework for selecting eligible projects at a general level. CICERO does not validate or certify the climate effects of single projects, and, thus, has no conflict of interest in regard to single projects. CICERO is not responsible for how the framework or mechanisms are implemented and followed up by the institutions.

Typical issues that we look into during the formulation of our second opinion include:

- Are the procedures for internal assessment sound seen from a general level?
- Do the projects deemed to be 'green' according to the rules and procedures have a high probability of being climate 'sound'?
- What is the room for subjective assessments within the framework?
- Are the procedures standardized, transparent and reasonably simple to apply?
- Are the procedures and rules publicly available?
- Are the potential for rebound effects from actions related to the projects included in the assessment?
- Are the potential for technological lock ins that may hinder future climate friendly solutions considered?
- How are external effects of 'green' projects taken into account in the assessment procedure?
- Are there routines for monitoring of projects and verification of results and impacts?

Our opinion with a conclusion and details on why we have concluded the way we do is written in a brief draft report. This is then discussed with the client before we produce a final second opinion.

The final report typically points out:

- Weak and strong points of the rules and procedures (the framework).
- What types of projects will be fairly assessed as green by the existing rules and procedures.
- What types of projects could potentially have problems related to climate change even though assessed as 'green' by the existing rules and procedures. What are the problematic issues?
- Ideas for improving the rules and procedures.

The second opinion is based on documentation of rules and frameworks provided by the institutions themselves (the client) and information gathered during meetings and e-mail correspondence with the client.

CICERO has been asked by SEB to provide a Second Opinion on the rules and regulations employed by the African Development Bank (AfDB) for its Green Project Portfolio (GPP) selection procedures.

Documents received

Documents received and forming the basis for this second opinion were contained in the following files:

Document No.	File name
1	AfDB Green Bond Framework.doc
2	2 Environment Policy (selected pages).pdf
3	3 Environmental review for private sector operations (full document).pdf
4	4 Environmental review procedures for public sector operations (full document).doc
5	5 DRAFT African Development Bank Group's Integrated Safeguards System (selected pages).pdf
6	6 Energy Policy (selected pages).pdf
7	7 AfDB Strategy for 2013–2022.pdf
8	8 - Private sector development strategy 2013-2017.pdf
9	9a Joint MDB Mitigation Finance Tracking Approach & 2012 report (full document).pdf
10	9b Joint MDB Adaptation Finance Tracking Approach & 2012 report (full document).pdf
11	10 AfDB climate finance tracking methodologies EN final (full document).pdf
12	AfDB Green Bond Framework_August_2013.doc

Discussion

Documents 1-11 were in the initial package received from AfDB. After the discussions with the Bank, the revised document no. 12 was produced.

Quite a number of the documents are concerned with general bank strategies and policies, in addition to rules for tracking climate related financing (financing of mitigation as well as adaptation related projects). This tracking is done within the framework of a broader international effort to establish a common practice among the multilateral development banks (MDB), but with some variations for individual MDBs. The main difference being that the Joint MDB mitigation methodology follows a restricted positive list of eligible mitigation activities (to be counted as climate related) while AfDB, like IBRD, IFC and IADB, follows a wider illustrative list of activities. We note that the annexes are missing from document no. 3 and 4. Otherwise there is a fair amount of overlap between the different documents.

Document 5 describes the bank's Integrated Safeguard System. The objectives of the safeguards are to avoid, or when avoidance is not possible, to minimize and mitigate negative impacts of projects on the environment and affected people.

The Integrated Safeguard System consists of four interrelated components:

1. The Integrated Safeguard Policy Statement, which describes common objectives of the Bank's safeguards, lays out policy principles, and outlines the delivery process for the safeguard policy.
2. Operational Safeguards,
3. Environmental and Social Assessment Procedures (ESAP),
4. Integrated Environmental and Social Impact Assessment (IESIA),

The Operational Safeguards cover themes like: Environmental and social assessment, involuntary resettlement, biodiversity and ecosystem services, pollution prevention and control, greenhouse gases, hazardous materials and resource efficiency, and labour conditions, health and safety.

The overall impression from the initially received documents (no. 1-11) is that of an institution which takes environmental and sustainability concerns seriously, seen in the light of the development mandate of AfDB. For instance is 'energy for all' a primary objective, with environmental concerns coming as a strong priority backed by an underlying Environmental Policy which need to be enforced through all activities. The documents describing the approach to classifying projects are comprehensive. The AfDB has through document no. 12 committed to provide investors easy access to relevant documents through a homepage dedicated to their Green Bonds. The administrative responsibilities are described and assigned in the original documentation, but with relatively little details on the 'algorithm' for which department or section is reporting to whom. This was improved in document 12.

When it comes to the selection of 'green projects', we initially found document no. 1 and no. 11, supported by no. 9 and 10 most useful. We had some critical remarks in particular to some specific elements in document no. 1, which after discussions was updated to document no. 12. In this new document the eligibility criteria and administrative procedures for selection of green projects was much clarified. The list is now as follows:

1. Greenfield Renewable Energy Generation (e.g. solar, wind, geothermal and ocean power)
2. Demand-side Brownfield and Greenfield Energy Efficiency (e.g. energy efficiency improvements in lighting and equipment; retrofit of transmission lines, substations or distribution systems to reduce technical losses)
3. Vehicle energy efficiency fleet retrofit or urban transport modal change
4. Biosphere conservation projects (reduce emissions from deforestation and degradation of ecosystems)
5. Solid Waste Management (e.g. incineration of waste, landfill gas capture and landfill gas combustion)
6. Industrial Processes (reduce GHG emissions from industrial processes improvements and cleaner production)

7. Fugitive emissions and carbon capture (e.g. carbon capture and storage, reduction of gas flaring or methane fugitive emissions in the oil and gas industry, coal mine methane capture)
8. Urban Development (e.g. rehabilitation and upgrade of urban water drainage systems in areas vulnerable to frequency and/or severity of flash floods and storm surges brought by climate change)
9. Water Supply and Access (e.g. water saving measures such as introduction of less water intensive crops or preservation of soil moisture and fertility)

Document 9-11 give brief descriptions of the climate finance tracking methodology which is a sound methodology (based on a no-project baseline) seen from a climate perspective.

Strength (clear areas)

The environmental (including climate) awareness of the bank seems from the documents provided, to be high. In particular, we note from document no. 4 the description of the Environmental and Social Assessment Procedures (ESAP). Here it is written:

“External impacts: A sectoral or regional ESA shall be carried out to evaluate the likely environmental and social consequences of a proposed sector-wide or region-wide plan or program. The plan or program may be related to a sector such as water and sanitation, energy, transport, etc. or it might be related to a geographical area or region. The main benefit of a sectoral or regional ESA is that it allows for the consideration of more far-ranging and cumulative impacts and broader types of alternatives than provided by a project-specific ESA.”

This awareness of far-ranging and cumulative impacts is key in making a proper assessment of the climate impacts of projects.

The illustrative list above contains types of projects that most likely are without or with only minor problems when it comes to likely climate impacts.

Weakness (unclear areas, too broad/subjectivity)

We find no obvious weaknesses in the AfDB framework as it now stands.

Pitfalls

A common pitfall is to invest in projects that may improve the climate impacts from the activity today, but may lead to a postponement for even more climate benign projects. This will always be difficult to assess in an objective manner, but should nevertheless be part of the project appraisals. The long term goal of low carbon societies will eventually require a near phase out of fossil fuels, and marginal climate improvements ‘today’ should not come in the way of more future oriented solutions that eventually will be required. One should avoid investments in projects that lead down ‘blind alleys’.

A somewhat related pitfall is associated with the so-called rebound effect. This may occur in projects that aims at improving the efficiency for a single unit activity, but which then in turn may lead to a higher overall activity level. Thus, for instance investments in transport infrastructure may make every trip more climate efficient (lower emissions), but may invite to a larger number of trips.

We include these issues here because they are recurrent themes that come up times and again in discussion with many financial institutions, and are not particularly related to AfDB. To be climate conscious requires a focus also on this aspect of investments. We feel ensured by the provided documentation that AfDB have these aspects in mind when selecting projects for the Green Bonds.

Overall assessment

The documents provided by the bank give a clear impression of an institution that are well aware of the challenges posed by climate change as well as other environmental and social concerns that may be associated with investments projects. In particular we are pleased with the consciousness shown towards the external impacts of projects both across space and time.

The eligibility criteria used for ‘green projects’ are now described as follows in document no. 12:

“The selection of eligible projects will be done in two phases:

- Phase 1: the Energy, Environment and Climate Change Department will identify and categorize among all projects approved in any given fiscal year the climate change projects using the Joint MDB and AfDB’s climate finance tracking methodologies.
- Phase 2: the Energy, Environment and Climate Change Department will apply the additional selection criteria under the AfDB’s Green Bonds Program and categorize the projects that can be part of the that program. The final list of projects to be part of the portfolio for any Green Bonds issuance will be agreed upon jointly by the Bank’s Energy, Environment and Climate Change Department and Treasury Department based on the proposed list by the former.”

Furthermore:

“Additional selection criteria to be applied for the specific purpose of the Bank’s Green Bonds Portfolio include:

- Projects that are eligible for financing under the African Development Bank. Projects eligible for financing under the African Development Fund and Nigerian Trust Fund will be excluded.
- Projects whose financing by the Bank can be qualified in full as promoting either low-carbon or climate resilient development. Projects whose financing by the Bank can be qualified only partially as promoting either low-carbon or climate resilient development will be excluded.
- Projects that will lead to significant accumulated GHG emissions reduction over the lifetime of the asset.”

We find these procedures and criteria sufficient to safeguard the climate integrity of selected project to a reasonable degree. The standards seem to be transparent and reasonably simple to apply. The rules and procedures will be made publicly available on a dedicated internet site. Thus, the revised document 12 says about monitoring the following:

“To enable investors to follow the implementation of the AfDB’s Green Bonds Program, the Bank will establish a dedicated website which will include, among other things:

- 1) key documents related to the AfDB Green Bonds Program and links to other relevant Bank documents such as the Long-Term Strategy or the Environment Policy;
- 2) Key information about the AfDB’s Green Bond Program and Framework, including project selection criteria;
- 3) progress status report on the selection and implementation of the projects which are part of the Green Bonds portfolio (e.g. information on implementation status, disbursement status and other relevant indicators as they are collected as part of the Bank’s project monitoring procedures).

In addition, the Bank will produce an annual newsletter for investors which will include a summary of the information under points 2) and 3) above.”