AFAC

African Financial Alliance on Climate Change

AFRICAN FINANCIAL ALLIANCE ON CLIMATE CHANGE

AFRICA'S FINANCIAL INDUSTRY ACCELERATING CLIMATE ACTION

AFRICAN DEVELOPMENT BANK GROUP


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"Africa's financial actors need to work together creatively to mobilise global financial resources at scale that can support local innovation, that drives climate-resilient and low-carbon development on the continent. Having been short-changed by climate change, Africa must not be short-changed by climate finance."

AKINWUMI ADESINA
President
African Development Bank Group



Climate Change Risks and Opportunities

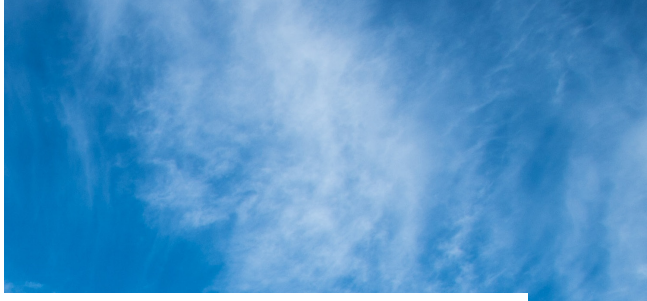
Africa is the **most vulnerable** continent to climate change and will remain highly impacted under all climate change scenarios above 1.5°C.

Food Insecurity	Crop Failures	Livestock	Humanitarian Aid
31% population	9.3 million ton deficit	643,000 dead	40 million people

The effects of the 2015 drought in Southern Africa

7 out of 10 countries considered the most vulnerable are in Africa, despite the continent having contributed the least to global warming and having the lowest emissions. The financial and structural constraints to manage climate impacts further compound the threat posed by climate change.

> " The impacts of 1.5°C would disproportionately affect disadvantaged and vulnerable populations through food insecurity, higher food prices, income losses, lost livelihood opportunities, adverse health impacts, and population displacements. Some of the worst impacts on sustainable development are expected to be felt among agricultural and coastal dependent livelihoods, indigenous people, children and the elderly, poor labourers, poor urban dwellers in African cities, and people and ecosystems in the Arctic and Small Island Developing States."
>
> Source: Intergovernmental Panel on Climate Change Special Report (2018): Global Warming of 1.5 °C



Nevertheless, climate change presents a **US $3 trillion investment opportunity in Africa.**

Africa offers tremendous greenfield investment opportunities to support climate action across key economic sectors offering high returns for investors. These opportunities are underpinned by Africa's young workforce, largest global percentage of untapped arable land, abundant natural resources for renewable energy generation, rare-earth metals and mineral wealth.

Africa's commitments to the Paris Agreement presents a US $3 trillion investment opportunity by 2030. 75% of the investment is expected to come from the private sector to complement the public sector financing. This calls for innovative approaches to attract, and steer financial flows consistent with a pathway towards low-carbon and climate-resilient development.



The urgency to address climate change in Africa warrants global support that also involves Africa's private sector and financial institutions.

Africa will continue to experience residual loss and damage under all climate change scenarios, **posing grave threats to livelihoods and survivability.**

Africa needs to **"urgently take the lead"** in fast-tracking its climate resilience to minimise these losses.

An increase in average global temperature of 2°C will trigger a normal occurrence of heat waves that are classified as unusual today. These longer, hotter and more frequent heat waves will have a damaging effect on crop production and life expectancy in Africa.

Even if the warming stays below 2°C, Africa's under-nourished would increase 25-90%.

Africa's under-nourished are projected to increase 25-90% and adaptation costs will still hover around US $35 billion per annum until the 2040s and US $200 billion per annum by the 2070s.

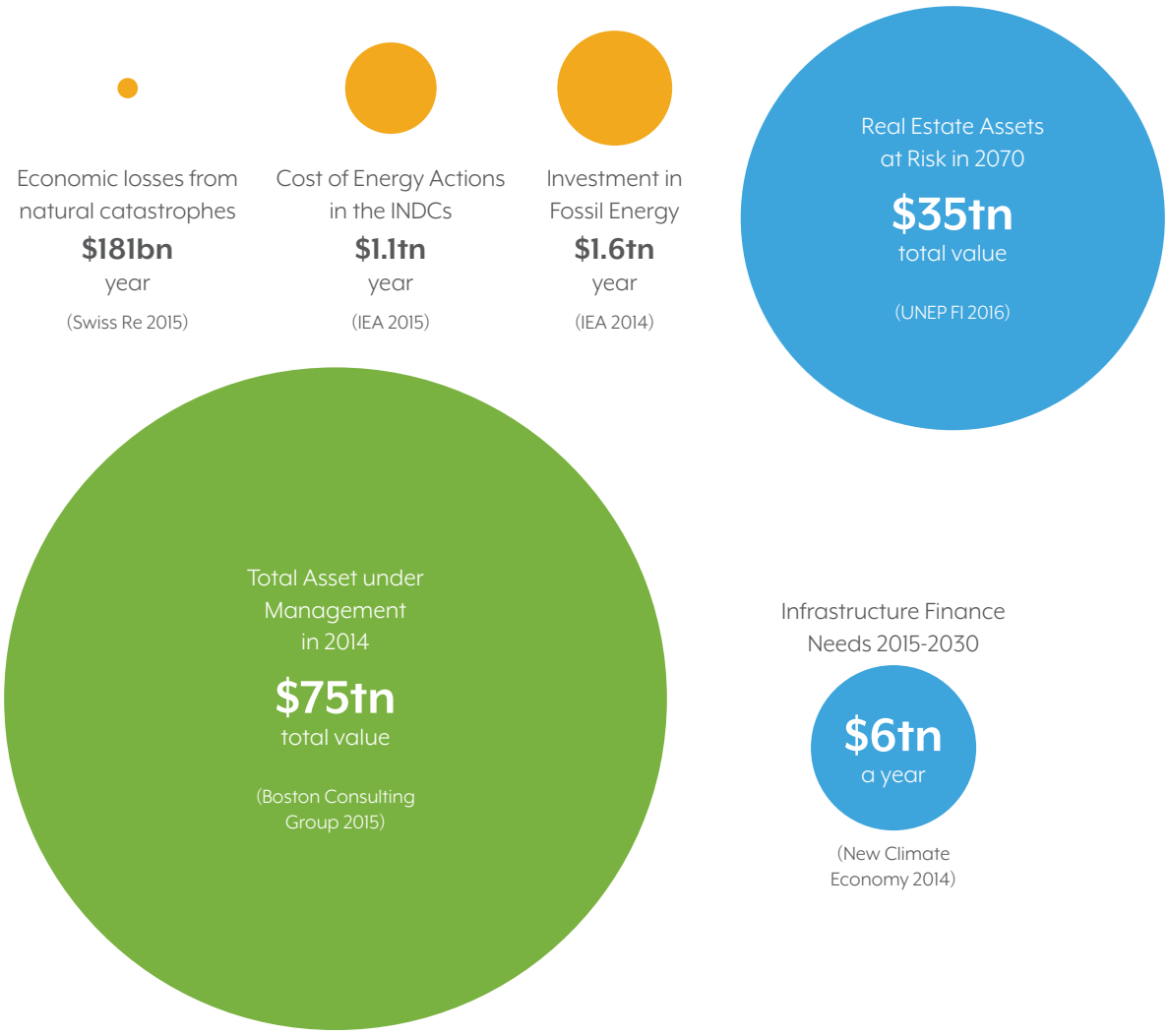
Less than 20%	**GLOBAL share of Land, Population and Disasters**
72%	**VICTIM share against 18% of global disasters**
US $150-350BN	**investments needed for ADAPTATION** by 2030
US $3TN	investments required for **NATIONALLY DETERMINED CONTRIBUTIONS (NDCs)** by 2030

Climate vulnerability has cost developing countries **US $62 billion** in higher interest payments across the public and private sectors.

Additional interest payments attributable to climate vulnerability are expected to increase to **US $146 – 168 billion** over the next decade, further exacerbating the financial indebtedness of developing countries and threatening future investments.

Source: UNEP Report - Climate Change and the Cost of Capital in Developing Countries

Fig.2.2. Global climate risk - financial exposure



Source: UNFCCC Standing Committee on Finance - 2016 Biennial Assessment and Overview of Climate Finance Flows Report

Climate change is being acknowledged as a real long-term investment risk for many investors. Financial Institutions, globally, have called on governments to scale up climate action and introduce mechanisms, including financial reporting, to help them better manage climate related risks. Inadequate risk information can lead to a mispricing of assets and a misallocation of capital. Since markets will typically make abrupt corrections, these risks become even more unmanageable. Hence, there is an urgent need to develop appropriate mechanisms to assess the climate impact of financial assets and investments.

3. DRIVING CHANGE: OPPORTUNITIES FOR INVESTMENTS

INVESTMENT
Brownfield

GLOBAL ASSETS UNDER MANAGEMENT FACING CLIMATE RISKS

$110 - $200TN

2014

INVESTMENT
Greenfield

AFRICA NATIONALLY DETERMINED CONTRIBUTIONS (NDCs)

$3TN

BY 2030

ADDITIONAL INFRASTRUCTURE INVESTMENTS REQUIRED

$6TN

PER ANNUM TO 2030

GLOBAL
CLIMATE FINANCE

$383BN

INVESTED IN 2016

STRANDED ASSETS **$1-4TN**

MANAGE SUBSIDY REFORMS AND ON-GOING OPERATIONAL EXPENSES

RE-DIRECT ALLOCATIONS FOR NEW INVESTMENTS

CHALLENGES IN FINANCING FOSSIL FUELS

$ = US Dollars

Climate Financing Opportunities

Africa offers the highest returns compared to most emerging market economies. For the last two decades the continent has seen steady economic growth underpinned by commodity exports, growing market demand, and strengthened structural elements. For example, African's demographics are dominated by a young work-force, increased urbanisation and consumer base and an acceleration in digital developments. With around 30% of global mineral reserves and 60% of the world's uncultivated arable land, the investment potential offered across the energy and agriculture sectors amongst others remains huge.

However, investors face significant challenges in assessing opportunities and mitigating risks. These include:

1. Lack of clarity, and transparency on risk-reward profiles and asset pricing
2. Small size of the projects
3. High development and transaction costs
4. Lack of aggregate financing vehicles.

Only about 0.1% of assets by global investors would be enough to bridge the annual US $108 billion infrastructure gap on the continent.

Within Africa, the Assets Under Management (AUM) of the institutional investors are expected to rise by 50% to US $1.8 trillion by 2020 from US $1.2 trillion in 2017.

DEMOGRAPHICS

Africa will have 2 billion people by 2050 - one fifth of the global population, the largest and youngest workforce by 2025 and over 500 million people in the labour market. **Millennials are more inclined towards environmental, social and governance values.**

Successfully absorbing this workforce in labour-intensive and highly productive activities/sectors (e.g. manufacturing) holds the key to creating Africa's demographic dividend.



URBANISATION

Africa has the highest urbanisation rate in the world. About 40% of the population already live in urban areas and the 20 largest African cities are expected to grow by 50% in the next 10 years.

This provides opportunities for resilient cities and green infrastructure.



GROWING INTERNAL MARKETS AND THE MIDDLE CLASS

With growing populations and rapid urbanisation have come the rise of a middle class, a figure that is expected to reach 210 million in 2020 and rise to 490 million by 2040. The rise of the middle class has caused a shift in consumption patterns with its members preferring consumer goods.

This is a market worth US $250bn that is set to grow at an annual rate of 5% over the next 8 years. **The increase in demand for climate-friendly products and services can be supported through initiatives like African Continental Free Trade Area (AfCFTA) Agreements.**



DIGITAL AND TECHNOLOGICAL DEVELOPMENTS

In 2016, mobile technologies and services generated US $110 billion of economic value in Sub-Saharan Africa, equivalent to 7.7% of GDP. It is expected to rise to US $42 billion or 8.6% of GDP by 2020 as countries benefit from improvements in productivity and efficiency brought about by increased take-up of mobile services. **Digital and technological developments offer potential to overcome barriers across payments, information flows, etc.**

The mobile ecosystem accounted for approximately 3.5 million jobs in Sub-Saharan Africa in 2016. The number of mobile broadband connections will reach half a billion by 2020.



Industrialisation

The African industry potential can be at or even surpass Latin America at US $2,500 or East Asia at US $3,400 of GDP per capita from current US $700, by leveraging its structural strength and other natural advantages.

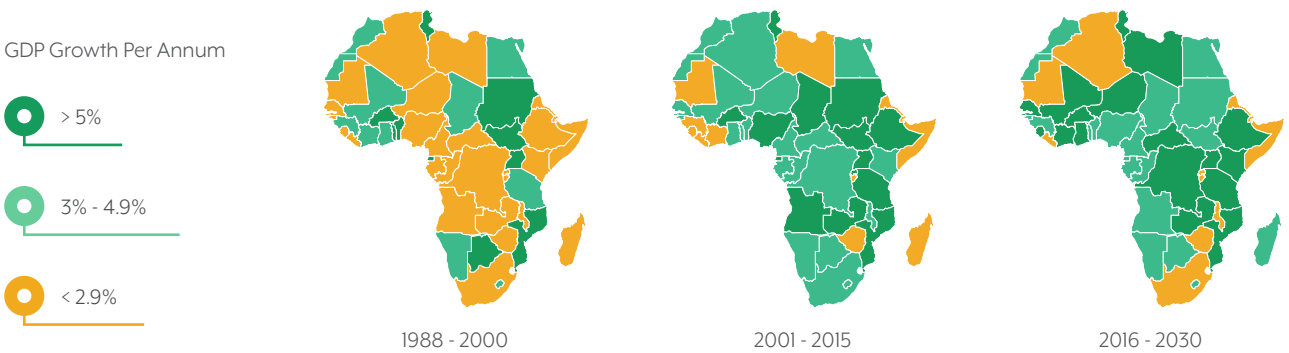
Africa's economic growth is accelerating and this is fueled by a growing internal market and external in-flows. Africa is the second largest foreign direct investment (FDI) destination after the Asia-Pacific region.
FDI inflows to Africa have risen from approximately US $10 billion in 2000 to over US $55 billion in 2015.

Intra-African FDI is also on the rise. Financial services alone accounted for about 50 percent of intra-Africa greenfield investment projects between 2003 and 2014.

Successful transition towards a green industrialization requires huge financial investments by public and private investors.

Strengthening capacities for domestic resource mobilization and re-invigorating the manufacturing sectors will be key to enlarging Africa's fiscal envelope.

Fig.3.1. Emerging internal market



Source: EY Attractiveness Program Africa, May 2017 / Oxford Economics

Energy

US $32 billion per annum renewable energy investment potential by 2030.

1000 GW Solar. **350GW** Hydro-electric. **110GW** Wind. **15GW** Geothermal.

Africa's renewable energy options would open up potential investment opportunities up to US $32 billion per annum by 2030.

Renewables are playing a critical role in reducing carbon emissions as well as supporting economic growth and energy access in Africa.

They can also meet almost two thirds of the continent's new energy demand in the short term.

Harnessing these resources to their full potential to upscale renewable energy in the African power sector requires dedicated efforts including adequate financing.

Fig. 3.2. Cumulative investment needs between 2015 and 2030

	Investment in billion USD (2015 – 2030)			
Region	**All generations**	**Large hydro**	**Other renewable**	**T&A**
North Africa	342	2	218	186
West Africa	89	36	31	52
Central Africa	32	13	17	14
East Africa	72	36	21	49
South Africa	145	18	94	74
Total	**681**	**106**	**381**	**375**

Source: IRENA database, accessed in April 2018



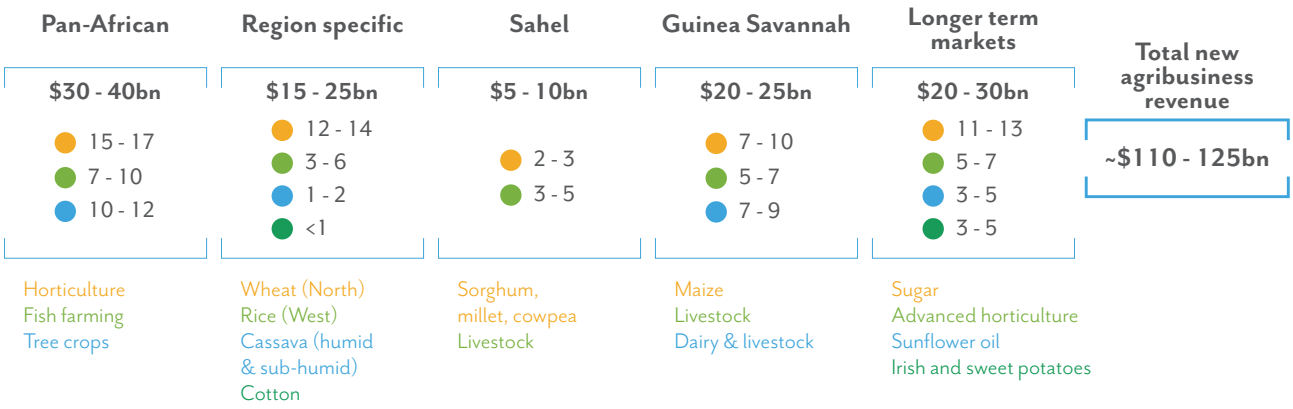
Agriculture

60% of the world's uncultivated arable land is found in Africa yet, US $35 billion worth of food is imported into the continent each year.

Agriculture is an integral part of the African economy. It accounts for over 51 percent of jobs across the continent. Despite its central role, the agricultural sector represents only a quarter of African GDP due to the low productivity of the sector.

Private sector infrastructure, beyond production, remains relatively underdeveloped. A well-functioning, vibrant and competitive private sector that can manage and allocate skills and capital to scale is key to drive long-term sustainable agribusiness growth.

Fig. 3.3. Potential agriculture and agribusiness markets by incremental revenue opportunities



Source: African Development Bank

Notes: (1) Market is valued at import parity prices, which can be taken as a proxy for the wholesale market value of these products ; (2) Additional focus areas for future consideration post first 5 years of execution of the transformation strategy; (3) involves application of high-productivity horticulture methods to substantially increase Africa's share of horticulture export markets. Source: CGIAR; FAOstat; Dalberg analysis.



4. THE ROLE OF THE FINANCIAL SECTOR

Placing the African financial sector at the heart of climate action is an innovative solution to drive continent-wide sustainable transformation.

Financial risks and opportunities stemming from underlying economic, technological, transition, and social climate-related drivers directly impact the financial sector and institutions in the sector's value chain. The degree and nature of impact is contingent on the position of the institution in the value-chain and economy. Financial institutions should proactively drive transformational climate action through both domestic and international financial flows by providing critical information on climate-related risks and investments. For example, across asset classes, financial institutions could be supported to:

1. Measure and manage climate investments and risks
2. Disclose climate-related information to enable investors make informed choices
3. Develop risk-reward mechanisms to influence systemic behavioural changes

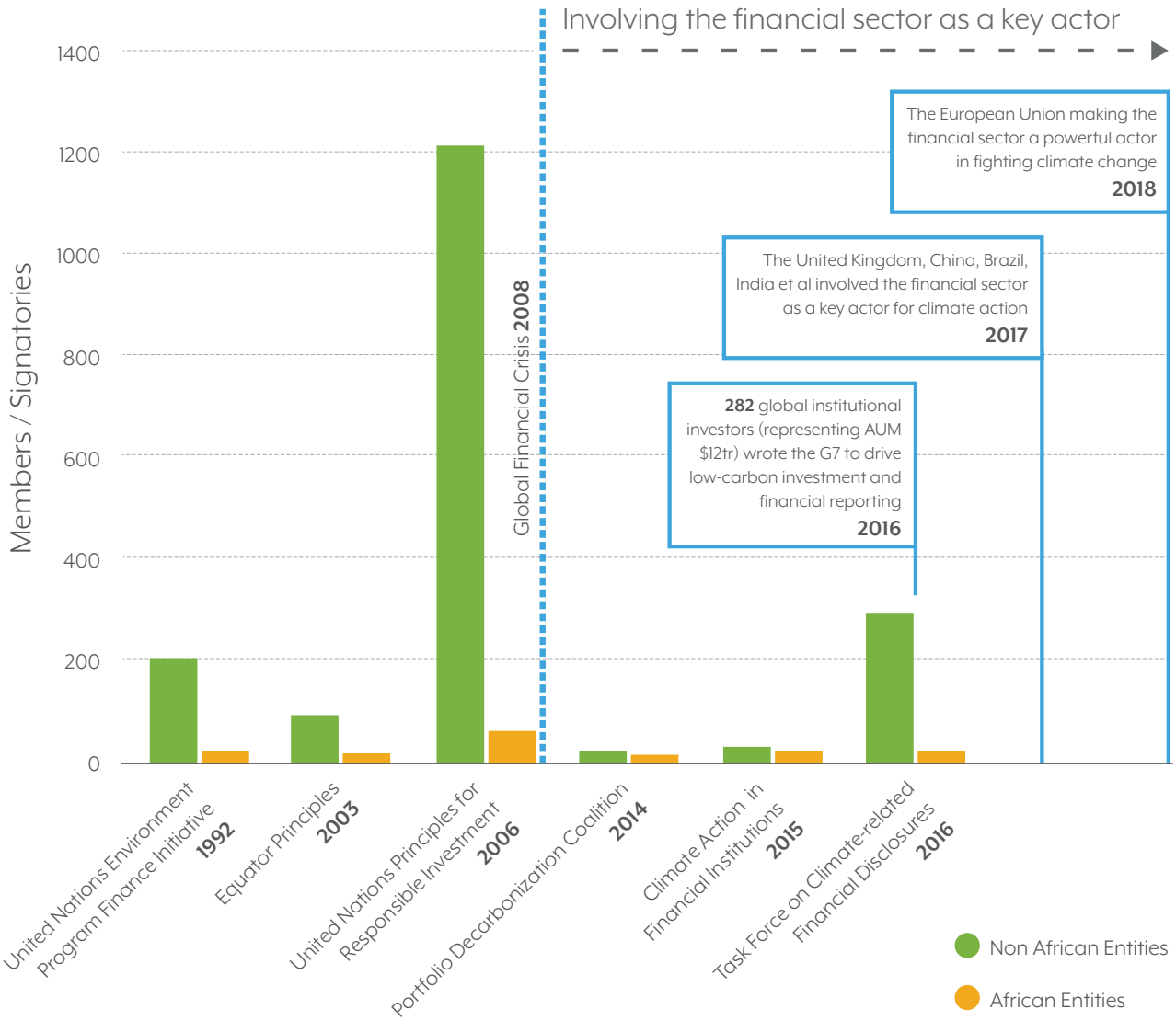


Involving financial sector actors will help leverage opportunities to leap-frog to a climate-friendly trajectory. Financial institutions, globally, are driving and developing low-carbon and climate-resilient investment regimes, asking governments for support through enabling market policies and mechanisms.

For the past few decades, several leading climate-change initiatives have been launched, globally. However, African members/signatories are significantly underrepresented in almost all of these global climate-action initiatives. After the global financial crisis, the focus has been to involve financial institutions as key actors in driving climate-action. African financial institutions are under-represented here too.

There is a compelling proposition for Africa financial institutions to also get engaged in driving climate action especially given the risks and opportunities offered by the continent. AFAC seeks to increase their effective participation.

Fig.4.1. Leading finance initiatives on climate action



Source: AfAC Secretariat



5. THE AFRICAN FINANCIAL ALLIANCE ON CLIMATE CHANGE (AFAC)

The objective of AFAC is to bring together the main financial sector owners and purveyors of capital **to support the mobilization and deployment of climate finance in Africa** for climate action.

"As a continent most vulnerable to climate change, we can only thrive if we set our economies on a low-carbon and climate-resilient development trajectory. The smart choice is to rethink how we deploy capital in a changing environment. An engaged financial sector is essential. AFAC will be instrumental in defining pathways which direct financial flows towards Africa's NDCs and SDGs."

AFAC Steering Committee Co-Chair
DR. UZZIEL NDAGIJIMANA
Minister of Finance and Economic Planning,
The Republic of Rwanda

"Improved understanding of climate-related risks and opportunities is essential if investors are to be in a position to manage risks and make the investments necessary for delivery on the Paris COP 21 Agreement. Failure to reach the Paris targets would be deeply damaging for the world as a whole and especially for Africa. Thus the African Financial Alliance on Climate Change is a very important initiative for engaging Africa's financial sector to drive climate action. AFAC forms a building block for climate-related governance, strategy, and risk-reward metrics towards low-carbon and climate-resilient investments."

AFAC Steering Committee Co-Chair
LORD NICHOLAS STERN
IG Patel Professor of Economics & Government,
Chair, Grantham Research Institute on Climate Change and the Environment,
The London School of Economics and Political Science

The African Financial Alliance on Climate Change

The African Financial Alliance on Climate Change (AFAC) aims to put the financial sector at the centre of climate action in Africa. It brings together Africa's key financial institutions, including central banks, insurance companies, sovereign wealth and pension funds, stock exchanges, as well as commercial and development banks, to mobilise private capital flows towards continent wide low-carbon and climate resilient development.

AFAC primarily intends to foster climate action by promoting: **knowledge sharing, climate risk mitigating financial instruments, climate risk disclosure, and climate finance flows.**

AFAC is unique as this is the first time that key actors in financial value chain are taking a leading role in driving climate action for the continent. The Alliance will work with key financial institutions along the financial value chain to help identify mechanisms for climate-resilient and low-carbon development.

African financial institutions not only need to engage early on but also need to act in parallel alongside their global peers to co-create mechanisms that are fit-for-purpose for the still evolving and developing African financial ecosystem and markets.



The Alliance positions African financial actors as key stakeholders in the evolving global climate finance architecture, helping design solutions and mobilising private capital for enhanced climate action.

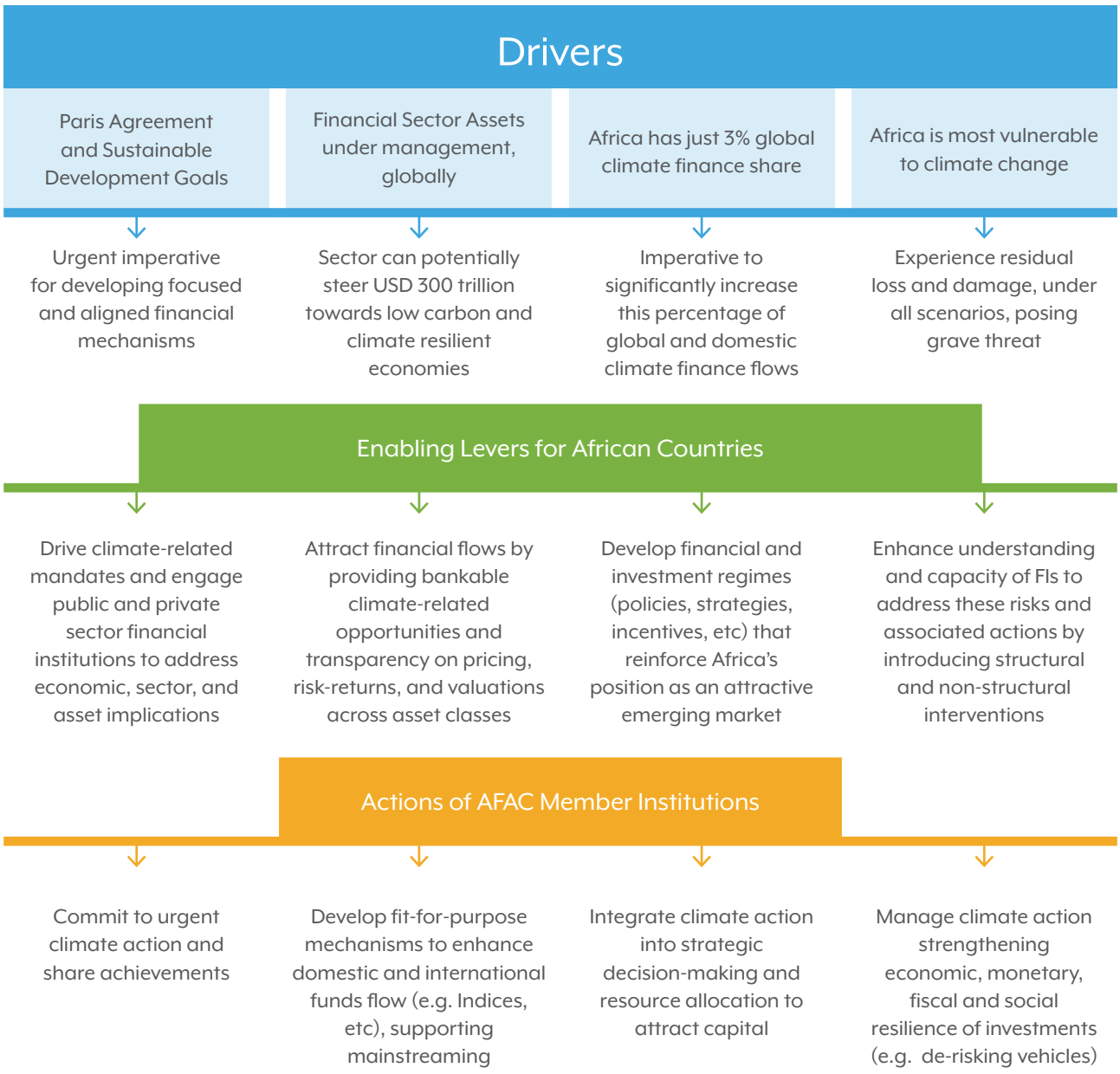
AFAC complements other global and regional initiatives being launched by the G20 for their respective countries/ regions. AFAC will leverage and complement other global initiates on climate change to ensure seamless alignment across governance, policies, standards, procedures and instruments.

In addition to addressing both climate-related risks and opportunities, the Alliance will also be customised to the African financial ecosystem ensuring inclusiveness and wider appeal.

AFAC to mobilise investment for climate action in Africa



Fig.5.1. Driving action



AFAC: The Benefits

Attracting private sector financing is fundamental to mobilising climate finance at scale. AFAC becomes a key building block for attracting investors and future-proofing their investments by;

1. Enabling information on and understanding of **risk-returns profile**, pricing and opportunities across asset classes
2. Assuring **business continuity and reduced volatility** by capturing impacts across investment portfolios
3. Lowering **financial and reputational risks** through better public disclosure and management of climate-related risks
4. Capitalising opportunities to attract **global climate finance and 'stranded capital'** by offering transparency on low-carbon portfolios
5. Upscaling to **deploy innovative technologies** supporting the low-carbon and climate-resilient transition

Ultimately, capitalising on these benefits sets Africa on a transformational sustainable development trajectory where African institutional investors and asset managers:

- Engage and **re-allocate capital** on the basis of companies' climate action strategies, **providing a strong incentive** for those companies to re-channel their own investments towards climate friendly activities, assets and technologies
- Proactively **redirect capital** from particularly carbon intensive companies, projects and technologies in each sector, and **reinvest this capital** into green companies, projects and technologies of the same sector.





Membership

Membership is voluntary and open to financial institutions as well as owners and purveyors of capital in Africa.

Representatives from these institutions should be interested in, have subject matter expertise, and have the ability to influence the internal strategy of their organisation/association.

This includes but not limited to the following entities:

- Multilateral Development Banks
- Central Banks
- National and Regional Development Banks
- Commercial Banks
- Institutional Investors
- Stock Exchanges
- Insurance Companies
- Ministries of Finance

For enquiries on how to become a member, contact the AFAC Secretariat: **afac_secretariat@afdb.org**

Governance

The Africa Financial Alliance on Climate Change (AFAC) is led by a Steering Committee comprised of experts and leaders in the African financial industry. The Steering Committee is supported by a Secretariat hosted at the African Development Bank.

Fig.5.3. Indicative actions by AFAC institutions

Institutions	Indicative Actions
Multilateral Development Banks	Lead the Alliance and coordinate with relevant actors such as international donors, development financial institutions, philanthropic organisations for example Provide lending, investments and co-financing Provide guarantees and other de-risking instruments for commercial and regional development banks, and institutional investors Provide concessional lines of credit dedicated to climate change related projects to commercial and regional development banks Provide grant funding for first loss and project preparation Provide knowledge sharing platforms related to climate change mainstreaming
Central Banks	Develop policies and procedures to incentivise commercial banks to finance more climate change related projects Set up preferential local currency facilities and lines of credit dedicated to climate change related projects for commercial banks
National and Regional Development Banks	Provide lending, investments and co-financing Provide guarantees and other de-risking instruments for commercial and institutional investors Provide lines of credit dedicated to climate change projects to commercial banks
Commercial Banks	Provide lending, investments and co-financing Provide lines of credit dedicated to climate change projects
Institutional Investors (sovereign funds, pension funds, private equity funds, asset managers)	Invest directly in de-risked projects, projects which demonstrate they are managing their climate related risks, and in financial instruments dedicated to climate change projects and issued by other financial institutions of the Alliance or by other sponsors
Stock Exchanges	Offer preferential listing fees and modalities to companies and institutions promoting climate change related projects and assets Bring together issuers and investors, and drive the development of sustainable market-based solutions
Insurance Companies	Insurers and re-insurers to continue the review of their exposure in view of climate-related risks and adjust their cover accordingly Re-evaluation of climate-related risks held by the clients to influence the cost of capital
Ministries of Finance	Develop policies, directives and instruments across financial sector to support climate change (e.g. taxation, subsidies, tariffs, incentives, capital markets, carbon pricing, etc) Work with domestic and international stakeholders to manage climate risks and increase climate investments Promote the sustainability of the finance sector leverage economic and monetary mechanisms to enable transition to a low-carbon economy

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