

KYOTO PROTOCOL DAY

New opportunities for investing in cleaner development

Kyoto Protocol Day

The landmark **Kyoto Protocol** sets binding targets on industrialized countries for the reduction of greenhouse gas (GHG) emissions and for lowering the risk of **global climate change**. Created in 1997 in Kyoto, Japan, the agreement comes into force and becomes legally binding on **16 February 2005**, after recent ratification by Russia made that possible. A majority of Asian Development Bank (ADB) member countries have ratified and are official parties to the Kyoto Protocol. Events around the world will mark the day, including events hosted by the Government of the Philippines, the Government of Japan (in Kyoto), the European Parliament, and the United Nations.

Relevance to the Development Community

Of most relevance to the development community, the Kyoto Protocol establishes the **Clean Development Mechanism (CDM)**, a market-based financial instrument allowing industrialized countries to invest in developing-country projects and acquire GHG emission reduction "credits" they can then use to meet their GHG reduction targets under the Protocol. For the investor country, this means an opportunity for offsetting emissions at a



An example of a clean energy project

The CDM Facility

The Clean Development Mechanism (CDM) Facility at the Asian Development Bank (ADB) aims to provide parallel assistance to projects that can qualify as CDM, and to facilitate agreements between sellers and buyers of carbon credits. Sellers will include public and private entities in ADB's developing member countries (DMCs), and buyers will typically come from ADB's developed members.

Additional costs associated with CDM, commonly known as 'transaction costs,' can be a significant barrier to the processing of projects. To help boost DMC involvement in this important emerging market, the ADB CDM Facility proposes to cover all transaction costs for selected projects in ADB's lending portfolio. Costs incurred by the CDM Facility would only be recovered, on a direct-cost basis, if the project were successful in signing a transaction agreement. It is a risk-free service provided on top of ADB's lending services.

From the buyer's perspective, the underlying project-finance risk is lowered significantly if the ADB operations departments act as the project sponsor and provide debt finance to the project. ADB's involvement will also make it easier for project developers to access other sources of finance, such as commercial banks. ADB already has excellent working relationships with Asian governments, which will help mitigate the host country approval risk.

The CDM Facility is developing project documentation and discussing/screening additional projects in the technical assistance portfolio. It is also seeking interest from potential buyers. Detailed project information will be presented to interested parties as it becomes available (see *Fuxin Project*). The project portfolio is gaining momentum, and will continue to do so as further partnerships develop.

fraction of the cost of reducing GHGs domestically since most developing countries still use very inefficient and inexpensive technology. For example, lowering carbon dioxide emissions by 1 ton in an industrialized country typically costs anywhere from \$50 to \$400, but only \$0.5 to \$20 in a developing country today. The CDM is a 'win-win' for all: (1) it will mobilize additional financial resources for developing countries to implement projects that reduce GHGs and promote sustainable development (e.g. clean energy, sustainable agriculture, forestry, urban waste management); and (2) it will generate emission reduction credits that can help industrialized countries meet commitments to the international community.

ADB's role

ADB is one of few international institutions providing underlying finance to projects that can produce tradable emission reduction credits. Two ADB-financed projects in the People's Republic of China have already contracted credit buyers (including the World Bank's Prototype Carbon Fund), and two more projects are coming up in the portfolio this year (see *Fuxin Project*). As a premier project developer and financier in Asia, ADB can use the CDM to expand the project pipeline and contribute to sustainable growth, social development, and environmental management. The ADB CDM Facility was set up in 2003 to provide technical and administrative assistance in parallel with ADB loans for projects that may qualify as CDM (see *The CDM Facility*). For selected projects, the Facility shoulders the upfront cost of CDM due diligence and regulatory requirements, until a carbon transaction is successful. Associated capacity building and project development initiatives are supported by trust funds from Canada, Denmark, and the Netherlands, administered by ADB, under the Renewable Energy, Energy Efficiency, and Climate Change (REACH) Program. New initiatives to leverage both public and private lending programs are being developed. ADB is also seeking government partners interested in jointly developing CDM projects.



An example of a sustainable forestry project

Fuxin Project

The Fuxin Coalmine Methane/Coal bed Methane Project is a subcomponent of the Liaoning Environmental Improvement Project, for which ADB approved a loan in November 2004. The project will improve coalmine methane and coal bed methane extraction and distribution in Fuxin, improving safety conditions in the mining area and enabling methane to be supplied as a clean fuel to residents, industry, and electricity-generation schemes.

The project will reduce GHG emissions by capturing and using methane that would otherwise be released to the atmosphere, and by displacing electricity and/or other fossil fuels that would otherwise be used. As a GHG, methane is 21 times more potent than carbon dioxide. The CDM market can, therefore, leverage significant additional capital to capture and use this much cleaner fuel. From a buyer's perspective, methane-capture projects are among the most cost-effective in producing tradable emission reduction credits and are, therefore, very attractive. The project is expected to produce more than 500,000 units of tradable carbon credits in the first few years and up to 800,000 units after the fourth year, worth about \$2.5 million–\$4.0 million per year.

ADB will help the project find a buyer and facilitate the transaction process in 2005. For more information on the Fuxin Project, contact the CDM Facility.

For more information on the Kyoto Protocol and ADB's initiatives, e-mail the CDM Facility at adbcdm@adb.org, or visit www.adb.org/reach; www.adb.org/cdmf