

'Second Opinion' on ADB's Green Bond framework

Contents

Summary 2

1. Introduction and background 2

2. Brief description of ADB and the Green Bond framework 3

Environmental policies that guide ADB 4

Eligible projects 5

3. Assessment of ADB's Green Bond framework and environmental policies 6

Strengths 7

Weaknesses 8

Pitfalls 8

Transparency, monitoring, reporting and verification 8

Summary

Asia and the Pacific have fast growing dynamic economies, but also the fastest growth in greenhouse gas emissions. At the same time climate change has severe impacts in the region, in particular for the most vulnerable countries. Hence the Asian Development Bank (ADB) considers climate change as a high priority. This is well incorporated in the Banks strategy and operational directions.

ADB's green bond framework and environmental policies provide a sound framework for climate-friendly investments. The bank has adopted an integrated approach to climate change, addressing both mitigation and adaptation. Fossil fuel energy investments will be excluded from the green bond framework. To maintain a conservative approach to project eligibility ADB has informed us that the same applies for road projects (new and rehabilitation).

Specialists in the area of energy, climate change, transport and environment identify eligible projects. ADB has in place good procedures for monitoring and reporting of the implementation of projects. Newsletters and environmental and safeguard documents will be provided. CICERO encourages ADB to include in these documents or the newsletter appropriate environmental impact reporting. Impact reporting is an important tool to enhance transparency in regard to the projects economic risk from climate change and the environmental effectiveness of the projects.

1. Introduction and background

As an independent, not-for-profit, research institute, CICERO (Center for International Climate and Environmental Research - Oslo) provides second opinions on institutions' framework and guidance for assessing and selecting eligible projects for green bond investments, and assesses the framework's robustness in meeting the institutions' environmental objectives. The second opinion is based on documentation of rules and frameworks provided by the institutions themselves (the client) and information gathered during meetings, teleconferences and e-mail correspondence with the client.

CICERO has established the global Expert Network on Second Opinions (ENSO), a network of independent non-profit research institutions on climate change and other environmental issues, to broaden the technical expertise and regional experience for second opinions. CICERO works confidentially with other members in the network to enhance the links to climate and environmental science, building upon the CICERO model for second opinions. In addition to CICERO, ENSO members include Basque Center for Climate Change (BC3), International Institute for Sustainable Development (IISD), Stockholm Environment Institute (SEI), and Tsinghua University 's Institute of Energy, Environment and Economy.

CICERO encourages the client to make this Second Opinion publically available. If any part of the Second Opinion is quoted, the full report must be made available.

CICERO's 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 neither responsible for how the framework or mechanisms are implemented and followed up by the institutions, nor for the outcome of investments in eligible projects.

This note provides a Second Opinion of ADB's Green Bond Framework and policies for considering the environmental impacts of their projects. The aim is to assess ADB's Green Bond Framework as to its ability to support ADB's stated objective of low-carbon and climate resilient growth.

Climate change will have a significant impact on economic development, both from the perspectives of sustainable future development pathways and from the perspective of adapting to changing circumstances. The recently released Intergovernmental Panel on Climate Change report (IPCC, 2014) on the physical science of climate change highlighted the seriousness of human-induced climate effects. The report can be viewed as an immediate call to action on the challenge of reducing greenhouse gas (GHG) emissions. The 195 countries that have ratified the United Nations Framework Convention on Climate Change (UNFCCC) have agreed to reduce GHG emissions to limit global temperature increase to below 2°C above pre-industrial level. Reaching this target requires shifting development pathways towards low- or zero-emitting economies without delay, and avoiding locking-in high-emitting capital.

CICERO takes a long-term view on activities that support a low-carbon climate resilient society. In some cases, activities or technologies that reduce near-term emissions result in net emissions or prolonged use of high-emitting infrastructure in the long-run. CICERO strives to avoid locking-in of emissions through careful infrastructure investments, and moving towards low- or zero-emitting infrastructure in the long run.

2. Brief description of ADB and the Green Bond framework

The Asian Development Bank (ADB) is a regional development bank established in 1966. The Bank now has 67 member countries. The region has fast growing dynamic economies, but also the fastest growth in greenhouse gas emissions. At the same time climate change has severe impacts in the region, in particular for the most vulnerable countries. Hence the Asian Development Bank (ADB) considers climate change as a high priority. This is well incorporated in the Banks strategy and operational directions.

Climate change has been on the agenda of ADB since the beginning of the 1990s. Efforts have been undertaken to better understand the region's greenhouse gas emissions and how these could be mitigated. In ADBs long-term strategies environmental sustainable growth is one of three strategic agendas together with economic growth and regional integration.

The Bank has adopted an integrated approach to climate change, addressing both mitigation and adaptation. The Bank's climate change program highlights five areas. These are 1) scaling up clean energy, 2) promoting sustainable transport and urban development, 3) managing land use and forests for carbon sequestration, 4) building climate resilience and 5) strengthening related policies, governance and institutions.

The aim of the ADB Green Bond program is to support climate change actions in developing member countries to deliver an environmental sustainable growth to help reduce poverty and improve the quality of life of their people.

Table 1 Documents received from ADB

Ref. nr.	File name
	Policies and guidelines
1	ADB Green Bond Framework
2	a) Joint MDB Mitigation Finance Tracking Approach & 2012 report b) Joint MDB Adaptation Finance Tracking Approach & 2012 report
3	ADB Strategy 2020
4	Environmental Operational Directions 2013-2020
5	ADB Climate Change Program
6	Safeguard Policy Statement June 2009
7	IFI Framework for Harmonized Approach to Greenhouse Gas Accounting
8	Energy Policy 2009
9	Water Operational Plan 2011-2020
10	Sustainable Transport Initiative
11	Urban Operational Plan 2012-2020
12	Project Classification System
13	Operations manual overview http://www.adb.org/documents/operations-manual
14	Mid-term review on Strategy 2020 http://www.adb.org/about/strategy-2020-mid-term-review
15	ADB Sustainability Report 2013
16	Public Communications Policy 2011
17	Accountability mechanism policy 2012
18	Social Protection

Environmental policies that guide ADB

In the context of its long-term strategies ADB prepared a report on its operational directions on Environment from 2013–2020 (document 4). By preparing this report ADB provides a

coherent overview of its environment operations and articulates how to step up efforts to help the region to achieve a transition to environmentally sustainable growth.

It is stated in this paper that these environmental operational directives are aligned with key elements of relevant ADB sector and thematic operational plans, particularly for sectors where environmental sustainability is a priority. These include the Sustainable transport Initiative Operational Plan, the Urban Operational Plan, the Water Operational Plan, the Energy Policy, and the Sustainable Food Security Plan, as well as the Climate Change Strategic Priorities. CICERO has had a look at these documents, except the Sustainable Food Security Plan, since it is not directly applicable to the green bond. Environmental concerns and climate change issues are well incorporated in all these operational documents.

It is mentioned in the green bond framework that in addition to addressing trans-boundary concerns, eligible projects will deliver natural resource conservation, urban environment improvement, eco-efficiency, environmental policy and legislation, or disaster risk management.

ADB achieved ISO 50001 certification (an energy management system) for its headquarters in December 2012. In 2003, ADB was the first multilateral development bank to achieve ISO 14001 and OHSAS 18001 certification. And in 2012, ADB's Energy, Environment, Health, and Safety Management Systems were recertified under international standards ISO 50001, ISO 14001, and OHSAS 1801 ADB is focusing on reducing their carbon footprint. Emissions from the ADB headquarters are reported in the banks sustainability report.

Eligible projects

It is stated in the framework that ADB's climate change program adopts an integrated approach to addressing climate change mitigation and adaptation across five priority areas, namely, (i) scaling up clean energy; (ii) promoting sustainable transport and urban development; (iii) managing land use and forests for carbon sequestration; (iv) building climate resilience; and (v) strengthening related policies, governance, and institutions.

The ADB green bond framework defines climate change mitigation projects as eligible for green bond financing if they target a reduction of GHG emissions into the atmosphere, or the sequestration (removal) of GHGs from the atmosphere. GHG reductions are measured against the GHG emissions that would have occurred in absence of the project ("business as usual").

Climate change adaptation projects are defined as those which target the reduction of vulnerability of human or natural systems to the consequences of climate change and enhance resilience and adaptive capacity.

Transparency and reporting

According to the framework detailed information about ADB projects and green bond issuance is available on the ADB website. Green Bond newsletters will provide highlights of eligible projects.

3. Assessment of ADB’s Green Bond framework and environmental policies

Overall, ADB’s green bond framework and environmental policies provide a sound framework for climate-friendly investments.

Table 2: Eligible project categories

Primary objective	Eligible project categories	Likelihood of meeting objectives - concerns
Renewable energy	Solar	Good – Consider lifecycle pollution.
	Wind	Good - Consider negative impacts on wildlife, nature
	Geothermal	Good – Potential for heavy metal pollution
	Small hydro	Good – Consider negative impacts on wildlife and nature
Energy Efficiency	Demand side energy efficiency, such as street lighting	Good – consider potential rebound effects
	Supply side energy efficiency, such as smart metering	
Sustainable transport	Urban transport projects (Bus Rapid Transit and Metro Rail Transit)	Good/medium depending on the fuel type (biofuel or fossil fuel)
	Non-urban railway projects	Good
	Non-motorized transport	Good
Adaptation	Energy projects that help improve energy security (no fossil fuel)	Good – see renewable energy concerns above
	Improve water security and livelihoods of vulnerable urban populations	Good – consider possible negative impacts on wildlife and nature
	Reduce vulnerability of transport infrastructure such as rerouting vulnerable stretches, increasing the embankment heights and bridge clearances and improving storm water drainage	Good

Strengths

CICERO takes a long-term view on climate change, and thus recommends excluding projects that support prolonged use of fossil fuel-based infrastructure that will contribute to GHGs in the long run. Efficiency improvements in existing thermal plants has been seen as prolonging the lifetime of the power plant, and hence possible increasing accumulated GHG emissions from the plant. Also the greenness of switching from coal to natural gas is not guaranteed.

ADB has informed us that fossil fuel projects in the energy sector will be excluded from the green bond framework. CICERO is encouraged by this clarification. Eligible ADB projects will focus on renewable energy (such as solar, wind, small hydro) or demand-side energy efficiency (such as efficient lighting). The framework explicitly states that fossil fuel energy efficiency projects and fossil fuel energy adaptation projects are excluded.

ADB sustainable transport projects under the green bond framework will focus on (a) urban public transport projects (Bus Rapid Transit and Metro Rail Transit); and (b) non-urban railway projects. ADB has informed us that they generally considers the impact of (road) transport projects to personal vehicle and truck miles travelled as such information informs the economic analysis of the project. Based on such analyses, ADB believes there is a robust rationale to suggest that in the transport sector, the largest amount of carbon savings come from the (a) shift of passengers/goods from very inefficient modes of transport (e.g. private cars) to mass transit; or (b) avoidance of travel altogether through smart planning. Typically, the introduction of such forms of mass transport allows movement of people at 1/4 of CO₂ per passenger kilometers/ton kilometers or even much less, compared to private cars and trucks. ADB has informed us that the busses mainly will run on diesel or natural gas. CICERO agrees that public transportation projects are important in order to bring us on a low carbon development pathway, even if the busses run on fossil fuels. It is however important to aim at reducing emissions from these busses running on fossil fuels in Asia, i.e. by choosing the most efficient fleet, and also move towards alternative fuels where that is economically feasible.

ADB has informed us that to maintain a conservative approach to project eligibility for green bond issuance, road projects (new and rehabilitation) will be excluded from the green bond framework.

In the process of identifying eligible projects the framework ensures that competent ADB staff takes part in the process. ADB energy, climate change, transport, and environmental specialists identify eligible projects on a continuous basis. The joint MDB approach, as described in documents 2 a) and b), for tracking and reporting of climate change mitigation and adaptation finance is taken as a starting point. Then the project's classification as a means of identifying "green" projects that deliver environmentally sustainable growth, and compliance with environmental and social safeguards are examined.

According to ADBs' safeguard policy Statement (document 6) the Bank uses a screening process for each proposed project, as early as possible, to determine the appropriate extent and type of environmental assessment so that appropriate studies are undertaken,

commensurate with the significance of potential impacts and risks. ADB has informed us that the result of these screening processes will be made available for investors.

Weaknesses

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

Pitfalls

A macro-level concern is the potential for rebound effects. For example, energy efficiency improvements that lower energy costs, inducing more energy use and partially offsetting energy savings. This can have the end result of lower reduction in GHG emissions than anticipated.

While these effects can never be entirely avoided, it is recommended to be aware of possible rebound effects and avoid investing in projects where the risk of such effects is particularly high. 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 particular related to ADB. To be climate conscious requires a focus also on this aspect of investments. We feel ensured by the provided documentation that ADB have these aspects in mind when selecting projects for Green Bonds.

Due to the complexity of how socio-economic activities impact the climate, a specific project is likely to have interactions with the broader community beyond the project borders. These interactions may or may not be climate-friendly, and thus need to be considered with regards to the net impact of climate-related investments.

It is stated in document 8 “IFI Framework for Harmonized Approach to Greenhouse Gas Accounting” that the project boundary for GHG Accounting should include all activities, facilities or infrastructure that the IFI is financing. It is further stated that gross emissions from construction may be included in the assessment. We expect ADB to include such emissions from their supply chain. Significant emission sources from the project, regardless of ownership should be included.

Transparency, monitoring, reporting and verification

Transparency, reporting and verification are key in order to enable investors to follow the implementation of the ADB Green Bond Program. Without becoming too burdensome impact reporting enhances transparency in regard to the projects economic risk from climate change and the environmental effectiveness of the projects.

ADB will provide newsletters with highlights of eligible projects. Each eligible green project loan will also have applicable environmental and social safeguard documents which will be publicly available on ADB’s website. ADB will provide a list of green projects related to the bond issuance on ADB's website as well as annual newsletters to the green bond investors. CICERO encourages ADB to include in these documents or the newsletter appropriate environmental impact reporting.

ADB has in place good procedures for monitoring and reporting of projects. The framework includes supervision and monitoring at project level to ensure that safeguard and other requirements are complied with during project preparation and implementation. ADB has informed us that in a given year, at least 75% of all ADB project completion reports (including green bonds projects) are either validated or subject to an in-depth performance evaluation of development effectiveness by ADB's Independent Evaluation Department. Project-affected people can also directly submit complaints to the accountability mechanism