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ADB Draft Energy Policy Could Leave Door Open for up to 78% of Bank's Gas Finance

Fossil Free ADB Analysis of ADB Draft Energy Policy

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Background

The Asian Development Bank (ADB) is currently revising its energy policy for the first time since 2009. A draft of the policy was released on May 9th 2021 and is now available for public comment.

The review comes at a time of unprecedented momentum to end public finance for fossil fuels. The European Union, UK, US, and the European Investment Bank have all made commitments this year to stop public financing of fossil fuel projects. The International Energy Agency and United Nations Secretary General have all provided important signals in the same direction, calling for governments to end finance for new fossil fuel projects and phase out fossil fuels — including gas — if we are to limit warming to 1.5C.

In a review of its existing 2009 energy policy, the ADB noted the policy "is no longer adequately aligned with the global consensus on climate change, recent changes in the energy sector of DMCs, the ongoing transformation of the energy sector globally, and ADB's new Strategy 2030."

The new draft energy policy has some key improvements, but still falls far short of what is needed for climate leadership as it leaves space for continued large-scale gas investments. The draft provides broad conditions for continued gas finance that include few details. If these conditions are applied liberally, they could allow for as much as 78% of the ADB's gas finance since Paris to continue. This would be out of sync with climate science and the recent net-zero energy scenario published by the IEA.

Continued support for long-lived carbon-intensive gas infrastructure threatens to impede a just transition to renewable energy. The IPCC's landmark 1.5°C report states that, "[s]ince the electricity sector is completely decarbonized by mid-century in 1.5°C pathways, electrification is the primary means to decarbonize energy end-use sectors." This means that both coal and gas must be phased out of the power sector. Building gas power plants instead of coal plants today, will not cut emissions by nearly enough. With the falling costs of renewables, investment in gas infrastructure risks burdening governments with stranded assets, higher energy costs and dependence on imports.

Since the Paris Agreement, the ADB has financed at least $4.9 billion in fossil fuels, almost all of which (96%) has gone to gas. The ADB cannot be a climate leader without a clear end to gas finance.

Further, since the release of the ADB draft energy policy last month, the ADB has failed to meaningfully consult with civil society groups from across Asia and beyond. The ADB has not disclosed information about the timeline for consultations nor the process for considering input.

This analysis outlines key elements of the policy, concerns and specific recommendations for the ADB as it revises the draft energy policy.

What does the policy say?

(a) On fossil fuels

Rules out direct support for coal

The ADB's last direct coal support was in 2013 but this is a long overdue assurance that it will not resume this finance. However, as discussed below it leaves the door open for coal finance through financial intermediaries. This is significant given the ADB's long support for dirty coal plants and the impacts on communities. See NGO Forum's press reaction to the Draft Energy Policy for quotes on this.

Rules out direct support for oil and gas extraction

In the 2009 Energy Policy, only exploration for these sectors was barred. Since 2016, oil and gas extraction made up 22% of the ADB's fossil fuel finance — almost all for one transaction for the Shah Deniz Gas Field in Azerbaijan.

This move is aligned with a key takeaway from the IEA's new net zero scenario, which is that limiting warming to 1.5C means investment in new fields should end in 2021.

Allows for continued direct support for gas under 5 broad conditions — while keeping the details of these conditions out of the consultation.

ADB has said it will continue to consider finance for gas pipelines, LNG terminals, storage facilities, power plants, and heating and cooking when five conditions are met. These are that projects must: improve or add access to energy services; pass a least cost of energy test with a social cost of carbon applied (starting at $36.60 per ton of CO2); use best available technology; reduce the net grid-emission factor for power generation, for example, by replacing a higher-emissions fuel; and demonstrate alignment with a net-zero by 2050 plan (see endnotes for full text).[1]

However, the energy policy has not given details on how these 5 conditions will be applied, stating a separate staff guidance note will be issued. This is a major transparency issue — without the full text of the guidance note on gas being included in the policy, these conditions are not meaningful.

Without the details being made public and the possibility for these conditions to be interpreted liberally, we have to assume the new policy would allow for as much as **78%** of their recent gas finance (based on the ADB's finance since Paris) to go ahead — that is, all of its past gas finance except for the gas extraction which is now clearly excluded. This would total more than **$700 million** a year.

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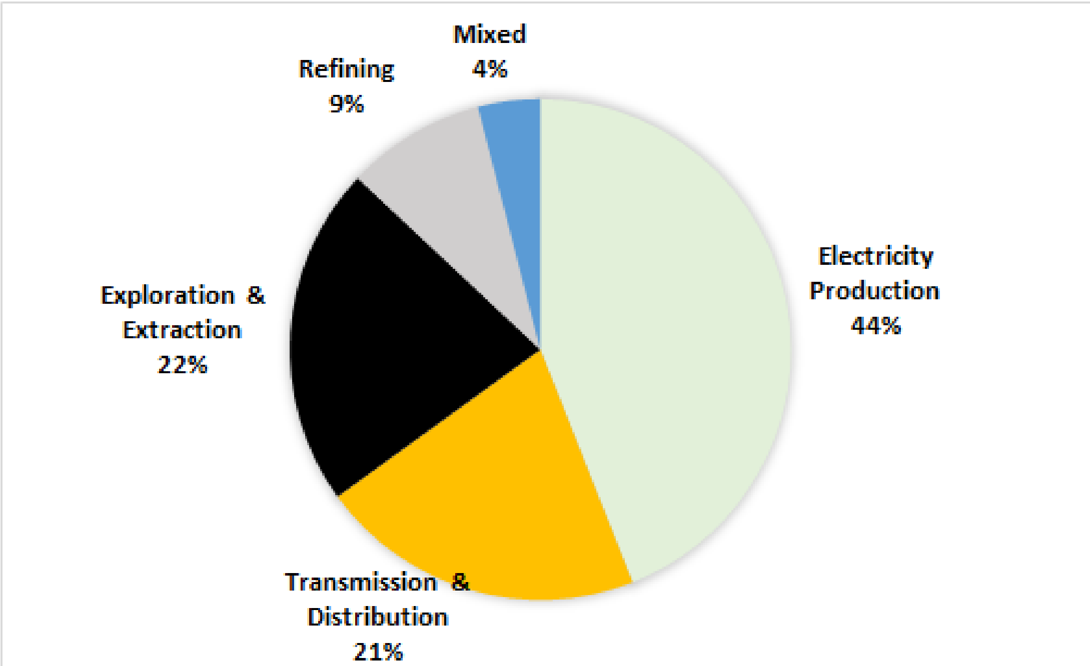
[1] Para 87 of the ADB's draft energy policy: "ADB may finance natural gas projects (including gas transmission and distribution pipelines, LNG terminals, storage facilities, gas-fired power plants, natural gas for heating and cooking) when the following conditions are all met: (i) provides energy services to those who currently are without said energy service or will provide a more modern means of providing the same energy service (e.g., natural gas stoves to replace traditional biomass stoves or natural gas power to provide last-mile electricity); ii) demonstrates that no other technology can provide the same energy service at an equivalent economic cost that considers the social cost of carbon (i.e., natural gas power would be compared to renewables plus storage to provide the same level of service); iii) uses high-efficiency and internationally best available technologies for new plants, retrofit or fuel switching, replacement, energy efficiency improvement, or heating projects; (iv) for natural gas power generation, will result in a net reduction in grid emission factor (e.g., natural gas or replacing diesel or coal power); and v) demonstrates alignment with targets to achieve carbon neutrality by mid-century, avoiding long-term lock-in into carbon infrastructure and significant risk of creating stranded assets."

ADB Gas Finance by Stage (2016-2020)



Source: Oil Change International's Shift the Subsidies Database. See the data behind this figure here.

While renewable energy alternatives are already more cost-effective than gas in many scenarios even without a social cost of carbon applied, there are still ways the conditions in the draft could be applied to allow for the ADB to continue similar levels of funding for downstream and midstream gas projects as before. For example, a high discount rate and poor definition of 'same energy service' could mean the least-cost test (condition 2) is formulated to favour gas. Similarly, using a risky net-zero by 2050 pathway that is heavily reliant on CCUS and offsets for condition 5 would leave room to justify continued increases in gas consumption. Conditions 1, 3, and 4 may improve the social outcomes or efficiency of gas projects but are not formulated to limit gas finance.

With the gas conditions as written, they are not stringent enough nor aligned with recent peer policy updates — development banks should not be funding ANY new gas.

Even before taking into account methane emissions along the gas supply chain — which can make gas more climate-damaging than coal — further expansion of infrastructure that locks-in gas consumption is inconsistent with the climate goals in the Paris Agreement. Recent IISD research shows the majority of gas consumption is associated with uses that already have cost-competitive clean alternatives in most countries and circumstances. For other uses, costs of alternative new technologies are falling, with competitiveness expected to be achieved in the 2020s or 2030s.

A development bank like the ADB — with a mission to promote sustainability and equality — should be using its public finance for energy for a just transition to renewable energy rather than locking-in risky gas. However, instead the ADB is playing a critical role in laying the groundwork for gas infrastructure development and expansion in Asia through its technical assistance program. The ADB approved $11.1 million in technical assistance grants from 2016-2020 to help governments prepare to build out gas pipelines, power plants and LNG terminals across Asia. For more background on the impact of ADB's gas finance, see Fossil Free ADB's earlier briefing.

Many recent energy policies from other public international finance institutions public finance policies exclude much more gas than the ADB's, by using some combination of the following:

a) A stronger climate test that requires showing alternatives to gas are not *viable* rather than just more expensive (e.g. UK and the Dutch development bank (FMO))
b) Strict emissions standards (e.g. EIB has a power generation standard for all projects of less than 250 grammes of CO_2 per kilowatt-hour), and/or
c) A shadow cost of carbon aligned with the upper end of the High-Level Commission on Carbon Prices (e.g. EIB currently employs a shadow cost of carbon of 97 USD, set to rise rapidly). This is what is consistent with a 1.5°C goal. See OCI briefing with further recommendations for MDBs and shadow carbon pricing here.

The ADB draft's overall framing on gas is also concerning. Where the above peers state gas would only be funded in clearly-defined rare exceptions, the ADB refers to gas as a "transitional" fuel and provides few details. The Bank also mentions the re-engineering of coal plants to use fossil gas (par. 86), promotion of investment in fossil gas network infrastructure (par. 45), and five conditions for financing gas projects (par. 87).

On energy access, the focus should be on greatly increasing concessional finance for distributed renewable energy (see below) rather than gas. There is increasing recognition that support for fossil fuels is not improving energy access: last year, the UN Sustainable Energy for All Initiative recommended that "financing of fossil fuel projects as a means of closing the energy access gap should be terminated."

The ADB states that it "will support carbon capture, utilization and storage investments for power plants and industries" and work to identify and remove hurdles to the development and commercialization of this technology. This is an unproven technology that is much more expensive than alternatives — because of this, no gas-fired power plants with CCUS exist yet. ADB support should prioritize finance for fossil-free alternatives instead.

No restrictions on fossil fuel finance via financial intermediaries or associated projects:

The draft energy policy does not add any details on whether it will prevent fossil fuel finance when this is provided through financial intermediaries (FIs) or associated facilities. This is concerning as many of the ADB's peers, including the World Bank Group and European Investment Bank, have started to limit these forms of lending for some or all fossil fuels.

ADB's indirect lending to financial intermediaries (FIs) is growing rapidly, increasing tenfold in just a decade. At the same time, an internal ADB evaluation points to problems with environmental and social protections, stating "projects implemented through FIs have remained the weakest performers on safeguards." FIs are banks, infrastructure funds and private equity funds, which effectively 'outsource' decisions to a third party, which in turn invests in sub-projects or sub-clients. The draft policy focuses on using FI lending to support energy efficiency and energy access, which is welcome as FIs can act as aggregators, bundling smaller subprojects. However, the risk of FI investments leaking to fossil fuel projects remains if exclusions are not explicitly applied — this was seen with the World Bank when it ended direct coal financing in 2013. Furthermore, although the draft policy promises enhanced transparency, there is currently little to no public disclosure of which sub projects are supported via ADB FI investments. Without transparency, it will be impossible to track and monitor ADB's commitments with regard to fossil fuels in its FI lending portfolio.

The draft energy policy also does not rule out indirect support for new fossil fuel projects through associated facilities like transmission lines, roads, and ports.

(b) On just transition, energy access, and climate goals

Promises finance and policy advice for just transition, but remains vague and limited to coal

There are welcome and important commitments in the policy to support a just energy transition including technical support for DMCs to undertake transparent and inclusive planning and policies. Although there are stated commitments to consult with "all relevant stakeholders and affected groups," the process for doing so in a way which would avert reprisals for those who raise questions or provide critical input remains left unanswered, and overall provides no concrete reference to ensure affected peoples' concerns are duly addressed and accounted for.

In addition, most references to just transition in the ADB energy policy focus on support for DMCs to phase out only coal — rather than oil and gas as well. For example, there is a welcome commitment to support for planning for early retirement of coal power plants and decommissioning of coal power plants, but no mention of similar processes for oil and gas. There are also no timelines or financial targets for the promised support for just transition.

The just transition clauses must also include a recognition of workers and their unions as a key party which must be included in all stages, in full respect of core ILO conventions.

Promises finance and policy advice for energy access and distributed renewable energy, but remains vague:

There are no timelines or financial targets for the promised support for energy access, which makes the language difficult to evaluate. This is concerning given that since 2016, the ADB has spent only about 4% of its total energy finance on renewable energy aimed at expanding energy access.[2]

The draft mentions only private sector and market-based approaches to address energy access which raises questions about affordability and reach for the low-income communities lacking electricity and clean cooking access.

Does not commit to a 1.5°C goal

It is important to specify Paris-alignment to the 1.5°C Goal because warming of more than 1.5°C can save millions of people from joblessness, poverty, hunger, and disasters. The draft policy's language does not specify which temperature goal it is aligning to.

Waste-to-energy

The draft policy allows for continued support for waste-to-energy investment (which includes waste incineration). It also states that waste is a source of renewable energy while ignoring that plastics are a fossil-based material with significant carbon emissions. Waste-to-energy projects also have concerning human rights, health, and environmental impacts.

(c) On public participation and public benefits

Unclear consultation process

The deadline and process for public consultation is unclear, with no timeline or process listed and an email portal without an option to submit documents for evidence. There is no public outreach strategy to ensure civil society organizations in Developing Member Countries have adequate and meaningful opportunities to shape the final policy. Furthermore, there is no clarity on how consultations are being rolled out at a regional level (North America, Europe, Asia), the timelines for their execution and the way that invites are being disseminated. Nor is there clarity on how different stakeholder input will be weighed, taken into account and reflected in revisions to the draft language.

Privatization

The policy actively supports the privatization of state owned electricity systems through unbundling vertically integrated utilities, corporatization of utility functions, securitisation, asset recycling and full privatization of public enterprises (see para 109). The draft Energy Policy also states an aim to increase private sector lending to make it a third of ADB's lending by 2025, more than 50% of its current value (par. 37). Such an approach places all the risk on the public sector while privatising profits.

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[2] Based on Oil Change International's Shift the Subsidies Database, which relies on the ADB's own project reporting for ADB data.

Energy privatization has widened inequality and delayed the urgent transition to renewable energy globally. The International Monetary Fund has increasingly recognized this risk and suggests that while “in the short term, PPPs may appear cheaper than traditional public investment, over time they can turn out to be more expensive and undermine fiscal sustainability.” The UN Special Rapporteur on extreme poverty and human rights criticized the extent to which the World Bank, the International Monetary Fund, and even the UN itself have aggressively promoted widespread privatisation of basic services through the PPP model, without regard to the human rights implications or the consequences for the poor; “While privatisation's proponents insist that it saves money, enhances efficiency, and improves services, the real-world evidence very often challenges or contradicts these claims. Privatising the provision of criminal justice, social protection, prisons, education, basic healthcare and other essential public goods cannot be done at the expense of throwing rights protections out of the window.”

As an example, in the Philippines, ADB in fact assisted the government in restructuring and privatizing the power industry through the enactment of the Electric Power Industry Reform Act of 2001 (EPIRA). After 20 years of EPIRA, 5 corporations own at least 73% of the total installed capacity in the country. Supply is not reliable, legislators have been ineffective at holding companies accountable and electricity rates in the country have increased. According to the Global Retail Electricity Tariff Survey conducted by the International Energy Consultants, the Philippines ranked 2nd in Asia, and 24th globally in terms of expensive electricity prices. Furthermore, the 37th EPIRA Implementation Status Report revealed that the country’s average electricity rate in 2020 is its highest in the last 3 years.

Recommendations

The ADB’s Energy Policy must **end all direct and indirect fossil fuel finance**, including for gas.

- The ADB should amend the draft policy to exclude midstream and downstream gas financing and support, including through technical assistance grants, associated facilities, and policy advice. This means removing conditions that would allow further fossil gas financing.
- Climate provisions that apply in the energy policy to direct investments must also be extended to apply to indirect investments through financial intermediaries or other financial instruments.This should include a commitment and plan to screen and limit fossil fuel finance through financial intermediaries to the Energy Policy. To enable tracking and monitoring, ADB must disclose the name, sector and location of high risk sub-projects, including any that involve fossil fuels.
- The ADB’s fossil fuel exclusions should extend to fossil fuel projects utilizing carbon capture and storage given these rely on unproven and expensive technologies and divert public finance away from a just transition to renewable energy. The Bank should reconsider support for these technologies and listen to the many communities and organizations opposing these projects on the ground.

- If the Bank does not update the draft to end financing of gas projects and other carbon-intensive projects, a more stringent shadow carbon price will be needed. In line with the High Level Commission on Carbon Prices recommendations for 1.5°C, the ADB should impose a shadow carbon price of at least 100USD/tCO_2, coupled with a faster and higher rate of increase than their currently proposed 2% per year increase.

The ADB's Energy Policy process must be **transparent and participatory.**

- The ADB must run a full public consultation on the draft energy policy with a clear process and timelines that are easily accessible on the ADB's website. This should include details on how the ADB will collect and integrate feedback.
- The ADB should organize dedicated consultations to collect input from impacted communities and civil society organizations based in the region with translation available and clear public information on how to participate . At a minimum, accessible and participatory online civil society input sessions should be scheduled for groups within Central, South and South East Asia as well as the Pacific.
- To ensure full participation for civil society groups that may risk reprisals for giving input, submissions via a digitally encrypted platform should be enabled on the ADB's website.
- The ADB must publish its gas guidance note as part of the energy policy review. It is not possible for stakeholders to assess the policy meaningfully if we are missing key details on how it will be applied including considerations and standards for selecting projects and assurances that mechanisms will be in place to avert reprisals against affected communities.
- The ADB should commit to reviewing the energy policy by 2023.

The ADB's Energy Policy needs clear timelines, metrics, and targets for **just transition, energy access, and alignment with the 1.5°C goal of the Paris Agreement**.

- While the draft energy policy includes commitments to support just transition and energy access, these need timelines, targets for financing, and metrics to help ensure equitable outcomes.
- The commitment to the Paris Agreement should include a process for aligning all ADB energy lending and operations with a high-probability and equitable pathway that limits warming to well below 1.5°C before 2023.
- Support for just transition must not be limited to coal, the ADB should include support for communities and workers dependent on oil and gas production as well.
- For energy access, the ADB should include specific financing targets for community and publicly-owned distributed renewable energy, and metrics to ensure these projects promote decent work and affordable energy.
- The policy must make direct grants and concessional finance available for DMC governments to directly own and operate integrated renewable energy systems.

ADB must **include ADB-funded coal projects in the rapid and planned coal phase-out** in DMCs.

- Since the Bank commits to support the early retirement and decommissioning of coal power plants (par. 86), we recommend that it starts with ADB-funded coal projects. Given the Bank's familiarity with these projects and proponents, the Bank can more easily encourage and assist in the early retirement or decommissioning.
- Withdrawing financing from coal should extend to existing ADB coal projects, including the Jamshoro coal plant, which is still an active loan project.

ADB must **uphold human rights** and ensure its energy lending does not worsen inequality.

- ADB must ensure full free, prior, and informed consent for communities impacted by the energy projects it finances.
- ADB's energy lending policy should allow for locally-tailored approaches to the climate crisis, based on a DMC's fair and equitable share to the global climate response.
- ADB must not support the liberalization, unbundling and privatization of electricity systems in its technical assistance and must support and assist DMCs in assessing the long-term impacts of privatization and deregulation in their energy sectors.

This analysis was produced with input from the members of the Fossil Free ADB coalition, including Center for Energy, Ecology and Development, Coastal Livelihood and Environmental Action Network, GAIA, E3G, Indian Social Action Forum, NGO Forum on the ADB, Oil Change International, Oyu Tolgoi Watch, Public Services International and Recourse. Full list of coalition members is available at www.fossilfreeadb.org.