ARO
AMAZON REGIONAL OBSERVATORY

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Amazon Cooperation Treaty Organization

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DEVELOPMENT BANK OF LATIN AMERICA AND THE CARIBBEAN

User Guide

Financial Planning and Prioritization Tool for Climate Action Projects

Financial Planning and Prioritization Tool for Climate Action Projects

Strengthening and expansion of the Amazon Regional Observatory (ORA) in the areas of climate change, forests and biodiversity and climate change

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Content

Glossary

GEI	Greenhouse Gases
COP	Conference of the Parties
COP21	Twenty-first conference of the parties
CAF	Andean Development Corporation
ODS	Sustainable Development Goals
CND	Nationally Determined Contributions
AP	Paris Agreement
PNA	National Adaptation Plan
UN	United Nations

Introduction

Climate financing primarily aims to support countries and regions in achieving their climate goals by promoting transformative projects that challenge existing paradigms.

This type of financing focuses on mitigating and adapting to climate change caused by human activities while fostering stronger links with the Sustainable Development Goals (SDGs) established in the Paris Agreement.

Specifically, its objective is to keep the global temperature increase below 2°C above pre-industrial levels, with an additional target of limiting the increase to 1.5°C. Mitigation and adaptation to climate change in each of the five-greenhouse gas (GHG) emission sectors have their unique paradigm shifts and barriers to overcome. **For example:**

Agriculture

- Promote resilient agroecology with improved and climate-resilient plant varieties, innovative adaptation practices and technologies, crop diversification, and improved land and water management.
- Facilitate risk management services and climate-informed advisory services, addressing future climate risks and strategies to face or manage them.
- Reconfigure food systems with interventions covering the entire chain, from planting to the final consumer.

Cambio de uso de suelos

- Protect forests and natural landscapes.
- Restore degraded forests and landscapes.
- Manage productive forest landscapes sustainably.

Energy Access

- Generate low-emission energy and electricity from renewable sources.
- Improve energy transmission, distribution, and storage efficiently and reliably.
- Promote access to modern renewable energy in isolated systems and small grids.

To change these paradigms, barriers must be overcome by ensuring access to favorable and flexible financing conditions for regions, governments, and the private sector.

This type of financing, referred to as climate financing, requires an assessment of a project's efficiency and effectiveness. This involves determining whether the project is independently profitable, whether it requires subsidies, and whether it is eligible for co-financing from other climate financiers.

Purpose of the Guide

This guide aims to complement the work of project financial analysts by providing an initial tool to determine the profitability of a project through a preliminary evaluation.

Financial Decision Criteria

Bajo el término de financiamiento climático se entiende el apoyo financiero para la lucha contra el cambio climático.

Under the term climate financing, we understand financial support aimed at combating climate change. The United Nations Framework Convention on Climate Change (UNFCCC) defines climate financing as financial support for measures to prevent or reduce greenhouse gas (GHG) emissions ("mitigation") and for measures to adapt to global warming ("adaptation"). It primarily refers to funds made available by industrialized countries to developing nations.

In a broader sense, the term also includes all financial flows directed toward climate action, whether private investments or public funds, regardless of their origin or location of use. Recently, the term has been expanded to include financial resources aimed at addressing or compensating for unavoidable damage and losses resulting from climate change. In this context, climate financing encompasses the three pillars of action under the Paris Agreement: mitigation, adaptation, and loss and damage.

Climate financing is intended to help achieve the goals of the Paris Agreement, including the aim of limiting global warming to less than 2°C, preferably to a maximum of 1.5°C above pre-industrial levels. It also seeks to reallocate funds toward low-carbon and climate-resilient development.

In general, this type of financing is channeled through existing bilateral development cooperation mechanisms. Additionally, there are several multilateral climate funds, such as the Green Climate Fund and the Global Environment Facility, which are primarily financed through contributions from industrialized countries.

Multilateral development banks also fund climate programs in developing nations. Moreover, numerous initiatives, institutions, and funds are dedicated to attracting private investment in countries with limited resources.

Conceptualization of Climate Change

By addressing the question: What is climate change? What are mitigation and adaptation? What is climate financing? What is the Paris Agreement? What is climate action? and Who are climate financiers? We can understand the importance and relevance of this topic for vulnerable populations living in the Amazon and the planet.

- **Climate Change:**
  According to the United Nations Framework Convention on Climate Change (UNFCCC), climate change refers to a change in climate attributed directly or indirectly to human activity that alters the composition of the global atmosphere and is additional to natural climate variability observed over comparable time periods (UNFCCC, 1992). The Intergovernmental Panel on Climate Change (IPCC) defines climate change as any change in climate over time, whether due to natural variability or because of human activity (IPCC, 2021).

- **Mitigation:**
  The UNFCCC defines mitigation as the implementation of policies and actions aimed at reducing emissions from sources or enhancing sinks of greenhouse gases and greenhouse gas compounds. This process includes both the reduction of emissions and the increase in the absorption of these gases (UNFCCC, 1992). The IPCC describes climate change mitigation as human interventions to reduce sources or enhance sinks of greenhouse gases (IPCC, 2021).

- **Adaptation:**
  According to the UNFCCC, adaptation involves adjustments in human or natural systems in response to projected or actual climatic stimuli or their effects. These measures can moderate damage or exploit beneficial opportunities from climatic changes (UNFCCC, 1992). The IPCC defines adaptation as the process of adjustment to current or expected climate and its effects. In human systems, adaptation seeks to moderate or avoid harm or exploit beneficial opportunities. In natural systems, human intervention can facilitate adjustment to expected climate and its effects (IPCC, 2021).

- **Degradation and Desertification:**
  Within the framework of the United Nations Convention to Combat Desertification (UNCCD), desertification is defined as the degradation of land in arid, semi-arid, and dry sub-humid areas resulting from various factors, including climatic variations and human activities. Degradation includes loss of soil productivity due to erosion, salinization, and loss of vegetation cover (UNCCD, 1994).

- **Climate Financing:**
  According to the UNFCCC, climate financing refers to financial resources aimed at supporting actions to reduce greenhouse gas emissions, enhance carbon sinks, reduce vulnerability, and increase the resilience of human and ecological systems to the impacts of climate change (UNFCCC, 2011). The IPCC describes climate financing as funds intended to support mitigation and adaptation actions for climate change (IPCC, 2021).

- **Paris Agreement:**
  The Paris Agreement is an international treaty legally binding on climate change. Adopted by 196 Parties at COP21 in Paris on December 12, 2015, and effective from November 4, 2016, its goal is to limit global warming to below 2 degrees Celsius above pre-industrial levels, preferably to 1.5 degrees. To achieve this goal, countries must reach peak greenhouse gas emissions as soon as possible to achieve a climate-neutral planet by mid-century (UNFCCC, 2015).

- **Climate Action:**
  Any policy, measure, or program aimed at reducing greenhouse gas emissions, increasing climate resilience, or supporting and financing actions related to the Sustainable Development Goals (SDGs), the Paris Agreement, Nationally Determined Contributions (NDCs), and other related initiatives (UNFCCC, 2015).

- **Climate Financiers:**
  Financial entities or institutions that channel economic resources to support actions related to climate change. This includes both private investments and public funds aimed at mitigating greenhouse gas emissions, adapting to climate change impacts, and compensating for losses and damages associated with these phenomena. Climate financing encompasses the three pillars of action established in the Paris Agreement: mitigation, adaptation, and loss and damage (UNFCCC, 2015).

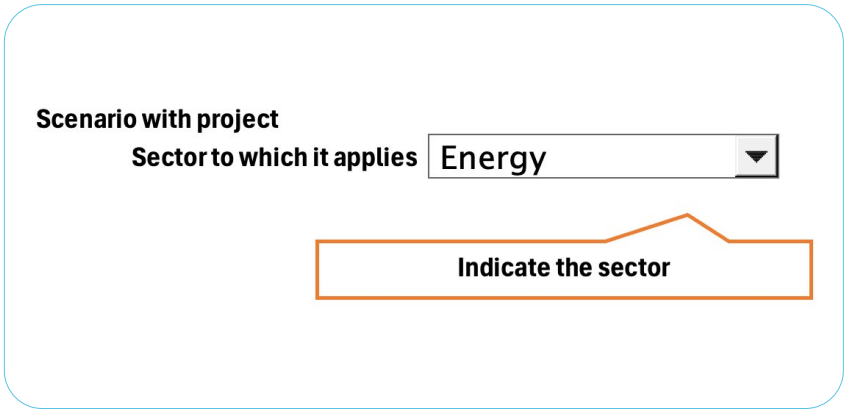
Tool Usage

For the use of the tool, it is recommended to have estimated annual revenues and costs, including the amount of annual income from products and/or services and the associated annual variable or direct and fixed or indirect costs.

Step 1:

Select the sector to which the project is directed

These can be Energy, Agriculture, Land-use change, Industrial processes, or Waste.



Step 2:

Describe the project scenario and baseline

Describe the scenario under which the project would operate and the current situation without the project. This ensures clarity on how the project creates paradigm shifts.

Step 3:

Select the currency, taxes, and discount rate

Indicate the currency of the country or region that applies, as most countries require the use of their local currency (reals, US dollars, bolivianos, soles, etc.).

Specify the income tax (applicable profits), as these differ in each country.

Provide a discount rate (the minimum expected return the funds would generate if invested in another project or venture, such as the bank's passive interest rate).

Analysis Currency	Surinamese Dollar
Income tax (%)	
NPV Discount Rate (%)	

Step 4:

Specify the financing conditions

Initially, to verify whether the project is profitable and capable of obtaining financing in the local market.

Subsequently, you can adjust the parameters to achieve the minimum profitability required for the project's execution.

This exercise will allow you to determine the project's efficiency and effectiveness and whether climate financing is necessary.

PROJECT ACTIVITIES DATA		
Investments to be made	Surinamese Dollar	
Useful life of assets	Years	
Percentage of Financing	%	
Financing Term	Years	
Financing Rate	% annual	

Step 5:

Revenues and costs

Indicate the expected total annual revenues, as well as the variable or direct and fixed or indirect costs associated with the project's activities.

Expected Annual Data (without VAT)		Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Revenues	Surinamese Dollar										
Expected Costs/Expenditures											
Variable or Direct Costs	Surinamese Dollar										
Fixed or Indirect Costs	Surinamese Dollar										

Step 6:

Evaluation results

With all the data, the tool will deliver the investment results, which include:

Financial Results

Activity/Project	NPV With Project Surinamese Dollar	IRR With Project %	Repayment Investment With Project Years
	0	0%	> to 10 years

Conclusions

The financial viability of a project is determined through an analysis of financial indicators, which provide an evaluation of its feasibility. If a project is not viable with the available local financing, it is necessary to explore alternative financing sources offering more favorable conditions, such as lower interest rates and longer terms.

This tool allows you to estimate these values. With the minimum required rates and terms, along with the project's initial viability, it becomes possible to initiate negotiations with financial organizations that provide this type of credit.

The financial evaluation indicators established in this guide are:

Internal Rate of Return (IRR): Decision criterion: The alternative is profitable if the IRR exceeds the proponent's discount rate (expected return).

Payback or Investment Recovery Period: Decision criterion: The alternative is feasible only if the recovery period is shorter than the planned debt term.

Net Present Value (NPV): Decision criterion: The alternative is feasible only if the present value is greater than zero.

In general, climate projects may face difficulties in being viable under the current financing conditions in the local markets of OTCA member countries. However, by improving these conditions, we could foster a greater number of quality projects that challenge this paradigm and address mitigation and adaptation to climate change.

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Financial Tool
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Prepared by libélula