

**REPORTING
FRAMEWORK**

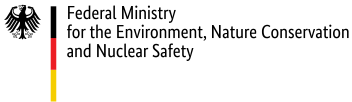
Climate-consistent finance flows in the agriculture, forest and other land use sector:

A framework for reporting on Article 2.1(c) of the Paris Agreement





On behalf of:



of the Federal Republic of Germany

Climate-consistent finance flows in the agriculture, forest and other land use sector: A framework for reporting on Article 2.1(c) of the Paris Agreement

For Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH (GIZ)

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Author: Charlene Watson

ODI
203 Blackfriars Road
London SE1 8NJ
UK

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About the project

This report was developed in the context of a broader project on the practical policy challenges for 'Shifting finance towards sustainable land use' with five parallel workstreams. All project outputs are available on the web platform of the Food, Environment, Land and Development (FELD) Action Tracker, at www.feldactiontracker.org. The website also includes a dedicated section on "Shifting Finance" with a direct link through www.greytogreenfinance.org and an opportunity for individual download of the following five project reports:

- A: Shifting finance towards sustainable land use: Aligning public incentives with the goals of the Paris Agreement
- B: Climate-consistent finance flows in the agriculture, forest and other land use sector: A framework for reporting on Article 2.1(c) of the Paris Agreement
- C: Shifting finance towards sustainable land use: Repurposing public support to agriculture

The focused analysis undertaken under this project and towards a proposed reporting framework were supported and complemented by two case studies for a closer look at the policy instruments employed in the land sector. These also include specific examples to illustrate the opportunities for policymakers to redirect existing finance flows to become more consistent and supportive of the Paris Goals.

- D: Shifting finance towards sustainable land use: A case study from Colombia
- E: Shifting finance towards sustainable land use: A case study on the European Union

Project partners

Climate Focus is a pioneering international advisory company and think tank that provides advice to governments and multilateral organizations, non-governmental and philanthropic organizations, and to companies across the globe. We support our clients in shaping and navigating through international and domestic climate policies, accessing climate finance and evaluating climate policy and investments.

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The Food, Environment, Land and Development (FELD) Action Tracker is a strategic initiative under the Food and Land Use Coalition (FOLU), led by SDSN in cooperation with other partners, to support countries in their transformation toward sustainable food systems and land use.

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Executive summary

Accord De Paris c'est fait

Agriculture, Forestry and Other Land Use (AFOLU) finance flows are complex and lacking transparency. The majority of finance arises from private sources, presenting challenges to tracking and quantification. Public finance flows are a relatively smaller but essential part of the landscape. Despite this, it is well understood that there remains room to make all finance flows to the AFOLU sector more climate-compatible. Globally, the sector contributes over one-fifth of greenhouse-gas emissions; half are attributed to agricultural expansion and half to agricultural production. Shifting the incentives that guide finance flows can have two effects: support emissions reduction by, for example, increasing carbon sequestration or reducing the emission-intensity of consumption; and support the climate-resilience of households, corporations and institutions engaged with and reliant on the AFOLU sector by, for example, embedding climate risks in borrowing decision-making or encouraging livelihood diversification.

In its long-term goal to make finance flows consistent with low-emission, climate-resilient development pathways, the Paris Agreement recognizes the need for coordinated shifts and reforms to ensure climate change is considered during financial decision-making. Embedded within this Article 2.1(c) is that we need not only to increase finance flows towards climate-positive actions, but also to reduce and redirect the finance flows that are high-emission or that create more climate-change vulnerability. Furthermore, it acknowledges that changes are needed in the institutions and systems that govern these financial flows.

The first global stocktake of the Paris Agreement, set to occur in 2023, represents a key opportunity to incorporate reporting towards Article 2.1(c). The global stocktake obliges a collective assessment of progress toward climate-consistency at five-year intervals. Yet, a common understanding is lacking, and the United Nations Framework Convention on Climate Change (UNFCCC) has offered no guidance to countries on what such climate-consistency of finance flows looks like, how to get there and what role each constituent country should play.

This paper addresses this gap by outlining a framework that would allow state and non-state actors alike to report on the climate-consistency of finance flows in the AFOLU sector. Four broad government levers are identified as relevant in the pursuit of the climate-consistency of AFOLU finance flows (Table 1). These levers and sub-levers, if applied in combination at a range of scales and for particular commodities or across groups of actors, have the potential to provide strong and credible signals to

AFOLU investors and financiers towards more climate-aligned practices.

Using this framework to develop a nationally-appropriate set of indicators on climate-consistency of AFOLU finance flows will support the identification of the actions already being taken that are climate-consistent. It can also highlight opportunities to fill gaps. In light of the self-determination embodied by the Paris Agreement, the framework is not intended to be prescriptive, but flexible. It allows for nationally driven indicators to be selected and designed in light of a country's climate-change objectives, the degree to which the AFOLU sector is relevant to their climate objectives, as well as their wider economic and market context. The paper further highlights the need for countries to consider a just transition away from climate-inconsistent finance flows. This necessitates the consideration of the socio-economic impacts of incentive reform options, and of political economy factors, that have long challenged efforts to pursue sustainable forest and land use.

The wide application of this reporting framework could progress global best practice in the pursuit of climate-consistency in AFOLU finance flows. The lack of UNFCCC guidance or global consensus on a broad and loosely defined concept hinders the forward momentum needed to face the climate emergency. The first global stocktake in 2023 will be the only space in climate negotiations under which to discuss progress towards the long-term goal of the consistency of finance flows with low-emission, climate-resilient development pathways. As such, an opportunity presents itself to use this framework to learn lessons and develop best practices on progress towards climate-consistency of finance flows, particularly when submitted as part of information inputs to the official global stocktake process.

TABLE 1. Framework of levers for supporting the consistency of finance flows in the AFOLU sector


Framework of public policy levers

For a fully detailed table of the framework, please see the comprehensive tables 2, 3, 4 and 5 in the body of this document

FINANCIAL POLICY AND REGULATION		FISCAL POLICY LEVERS	PUBLIC FINANCE	SOFT LAW	
Public policy lever	Sub-lever	Possible indicators	Role in making AFOLU finance flows more climate-consistent		
FINANCIAL POLICY AND REGULATION	Finance strategies, institutional arrangements, taxonomies, standards and guidelines	Adoption of strategies and institutional accountability	Indicates a level of political will and awareness of climate change and wider environmental impacts.		
		Development and adoption of taxonomy	Increases investor confidence, prevents greenwashing and facilitates market development.		
		Creation of standards and guidelines	Reduce greenwashing and accelerate green market development.		
	Enhancement of supervisory review	Mandated disclosure of risks	Shift capital allocation away from carbon-intensive assets with high transition risks or that are maladaptive.		
		Mandated disclosure of environmental, social and governance risks	Shift capital allocation away from activities with high-deforestation risk, or areas with high biodiversity risk or risks of adverse social impacts.		
		Conducting of stress-testing	Identify financial institutions exposed to emission-intensive assets or highly climate-vulnerable assets.		
	Adjustment of capital and liquidity requirements	Adjusting liquidity requirements	Reducing the amount that financial institutions have to hold against green lending.		
		Adjusting lending limits and credit caps and floors	Set targets or limit exposure to emission-intensive investments or those that are not resilient to climate impacts.		
	Public policy lever	Sub-lever	Possible indicators	Role in making AFOLU finance flows more climate-consistent	
	FISCAL POLICY LEVERS	Direct transfers	Reform of production payments	Reduce and decouple payments to reduce emissions or the inefficiency of production.	
Conditionality of production support			Conditionality to avoid environmentally harmful practices or to adopt less environmentally harmful practices.		
Introduction of conservation payments			Production retirement (land or livestock) for carbon sequestration and other environmental benefits.		
Goods and services		Rules for public procurement	Public authorities required to choose 'green' goods and services.		
		Development of general services	Advisory services minimizing the misuse of emission-intensive inputs. Research and development improving yields, drought resistance.		
Foregone revenues		Preferential tax treatment on inputs- and outputs	Reform tax concessions to increase high-emission inputs and decrease or remove low-emission activities.		
		Special tax rates on farm income	Place environmental conditionalities on tax concessions.		
		Special treatment for depreciation			
Market price support		Preferential property tax rates	Reduction and removal of market price supports on high greenhouse gas (GHG)-emitting commodities.		
		Reforms of trade barriers (e.g., tariffs), price floors and public stockholding			

FINANCIAL POLICY AND REGULATION		FISCAL POLICY LEVERS	PUBLIC FINANCE	SOFT LAW
Public policy level	Sub-lever	Possible indicators	Role in making AFOLU finance flows more climate-consistent	
PUBLIC FINANCE	Upstream policy	Development of mandates, strategies and operations	Climate change integrated into overarching strategy, and climate integrated into sectoral strategies.	
			Climate change embedded in institutional structures and leadership in climate change response.	
			Negative/ black-listing of Paris-misaligned investments.	
			Institutional- or portfolio-level tracking and accountability.	
	Downstream policy	Adoption of decision making and evaluation processes	Adopt risk screening methodologies, tools and scenarios.	
			Introduce lending limits (caps and floors) for particular sectors, targets and incentives.	
		Development of de-risking tools and instruments to support climate-aligned finance flows.		
		Transparency in and the monitoring, reporting and verification of impact of finance flows.		

FINANCIAL POLICY AND REGULATION		FISCAL POLICY LEVERS	PUBLIC FINANCE	SOFT LAW
Public policy level	Sub-lever	Possible indicators	Role in making AFOLU finance flows more climate-consistent	
SOFT-LAW	Commitments and pledges	Making commitments and pledges	Signals to public and private sector actors future policy directions in the AFOLU sector.	
	Learning networks, associations and institutions	Developing learning networks, associations and institutions	Promote awareness, information and tools at both national or international level.	
	Adopting standards, certification and labelling	Adopting standards, certification and labelling	Prevent greenwashing, increase quality and credibility and create green markets.	



CHAPTER 1
Making finance
flows in the
agriculture,
forestry and other
land use sector
climate-consistent

The finance landscape for the Agriculture, Forestry and Other Land Use (AFOLU) sector is complex and lacking in transparency. The majority of finance in the sector is private, including from households, small-holder farmers, timber, agribusiness and extractive companies, through to financial institutions and institutional investors. These private finance flows are hard to quantify (Falconer, 2016), in part because of the length and sophistication of supply chains, their overlaps with other economic sectors such as transportation and industry, and the fact that many upstream agricultural and forestry companies are not publicly listed. The cyclical nature of international commodity markets also leads to volatility in finance flows, further complicating quantification.

Public finance flows are a smaller – but essential – component of the finance landscape for AFOLU, and are key to influencing and directing private spending (Parker and Watson, 2018). Public agricultural financial support is estimated at over USD 600 billion per year (OECD, 2019a; Bellmann, 2019). Private farm investment is understood to exceed these levels of public agriculture support by some way (see Galt et al., 2021 for a full review of the AFOLU financing landscape).

There is room to make finance flows to the AFOLU sector more climate-compatible. The sector is responsible for over 20 percent of greenhouse gas (GHG) emissions globally, and up to 80 percent in some developing countries (IPCC, 2019; WRI nd). Around half of these emissions are attributed to agricultural production, and half to agricultural expansion (Searchinger et al., 2020). In a 2019 report, the Intergovernmental Panel on Climate Change (IPCC) makes clear that significant opportunities for GHG-mitigation solutions exist in the land-use sector. Shifting the incentives that guide finance flows to the AFOLU sector can, therefore, support the reduction of GHG emissions through, for example, increasing carbon sequestration or reducing the emissions intensity of consumption (Galt et al., 2021; Locke and Lowe, 2021).

The AFOLU sector is highly vulnerable to the impacts of climate change. Geographical shifts in food production and weather variation, for example, will be experienced by the world's poor through agricultural and food security challenges (World Bank, 2018; FAO, 2018). The disruption of supply chains, production and operations, and changing demand for products and services will lead to changes in resource and input prices. This will affect business models and debt repayment, with knock-on impacts on tax revenues. These real economy impacts – be it through industry, corporations, enterprises, and consumers – then

have cascading implications for the financial system (see Bolton et al. 2020; Voß et al, 2020; NGFS, 2019). There is, therefore, a need for land-use sector actors to adapt to climate change. Shifting the incentives that guide finance flows can, therefore, support the resilience of households, companies and institutions engaged in the AFOLU sector. This can be done by necessitating consideration of physical climate risks in agricultural infrastructure when borrowing capital, making lending to fishing communities conditional on concurrent mangrove restoration activities, or encouraging forest-livelihood diversification through reduced interest rates for lending to diversified portfolios, for example.

The need to increase the coherence of finance flows with climate change objectives is reflected in the third long-term goal of the Paris Agreement, Article 2.1(c). It calls for *'making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development'* (UNFCCC, 2015). This goal of the Paris Agreement is important, as it recognizes not only the need to increase climate-consistent finance flows, but also the need to reform climate inconsistent finance flows. In the AFOLU sector, the pursuit of the climate-consistency of finance flows speaks to a re-examination of and shifts in the underlying incentives that drive land use activities.

The most promising forum under which to explore action and progress towards Article 2.1(c) of the Paris Agreement in the UNFCCC process is the global stocktake (GST). Article 14 of the Paris Agreement obliges Parties to assess collective progress toward the purpose and long-term goals of the Paris Agreement every five years, with the first of these global stocktakes to be completed in 2023 (UNFCCC, 2015). At the 24th Conference of the Parties to the United Nations Framework Convention on Climate Change (COP24) in Katowice, 2018, paragraph 36(d) of the Decision states that the GST will consider information at a collective level on 'The finance flows, including the information referred to in Article 2, paragraph 1(c), and means of implementation and support and mobilization and provision of support...'¹

¹ Katowice Decision 19, Matters relating to Article 14 of the Paris Agreement, 2019. Available at: https://unfccc.int/sites/default/files/resource/CMA2018_03a02E.pdf

There are, however, challenges in assessing and reporting on the climate-consistency of finance flows:

- **Article 2.1(c) is a goal of the Paris Agreement, not individual Parties.** There is no common understanding of how to operationalize Article 2.1(c), and no UNFCCC guidance to countries on what consistency of finance flows with the Paris Agreement looks like, how to get there and what each constituent country's role should be.

Few forums exist under the UNFCCC to explore how to achieve the long-term goal of Article 2.1(c). In 2018, the COP gave an official mandate to the Standing Committee on Finance to map available information on the consistency of finance flows as part of the Biennial Assessment, every four years (decision 4/CP.24, paragraph 10).² The Biennial Assessment, however, is a product of a body designed only to fulfil mandates from the COP. To date, it has only been asked to consider data and metrics that might be relevant to climate-consistency; it has not been asked to further conceptually develop the concept of the consistency of finance flows.

- **Unifying approaches to reporting on climate-consistency of finance flows is hindered by nationally driven reporting.** The 2015 Paris Agreement shifted multilateral climate negotiations towards a country-driven, bottom-up, target-setting approach rather than a top-down, target-setting approach. Thus, while the Paris Agreement sets global goals,³ countries themselves define their own pathway to low-emission, climate-resilient economies (Cochran and Pauthier, 2019).

Parties' near-term mitigation goals (over the next decade) are articulated in Nationally Determined Contributions (NDCs) (Article 3, UNFCCC, 2015). Parties are also invited to provide longer-term strategies (LTS) extending through 2050 (Article 4.19, UNFCCC, 2015). The Paris Agreement further includes a ratchet mechanism whereby Parties assess, review and improve on their NDCs every five years. This is an attempt to ensure a progression in climate ambition over time (the aggregate impact of the first round of NDCs was found not to limit warming to within 2°C above pre-industrial levels, UNFCCC, 2016a) (Figure 1).

- **Countries are not obliged to report on progress towards making finance flows consistent with low-emission, climate-resilient development pathways.**

This is despite information on finance being included to varying degrees in many country-level reporting frameworks including biennial reporting, national communications and NDCs. There is only an indirect reference to the Enhanced Transparency Framework (ETF) – which builds on and enhances the existing monitoring, reporting and verification arrangements of the UNFCCC and will come into force in 2024. That indirect reference requests that developed countries include information on how developed countries will 'ensure that support provided and mobilized through public interventions is in line with the long-term goals of the Paris Agreement'.⁴

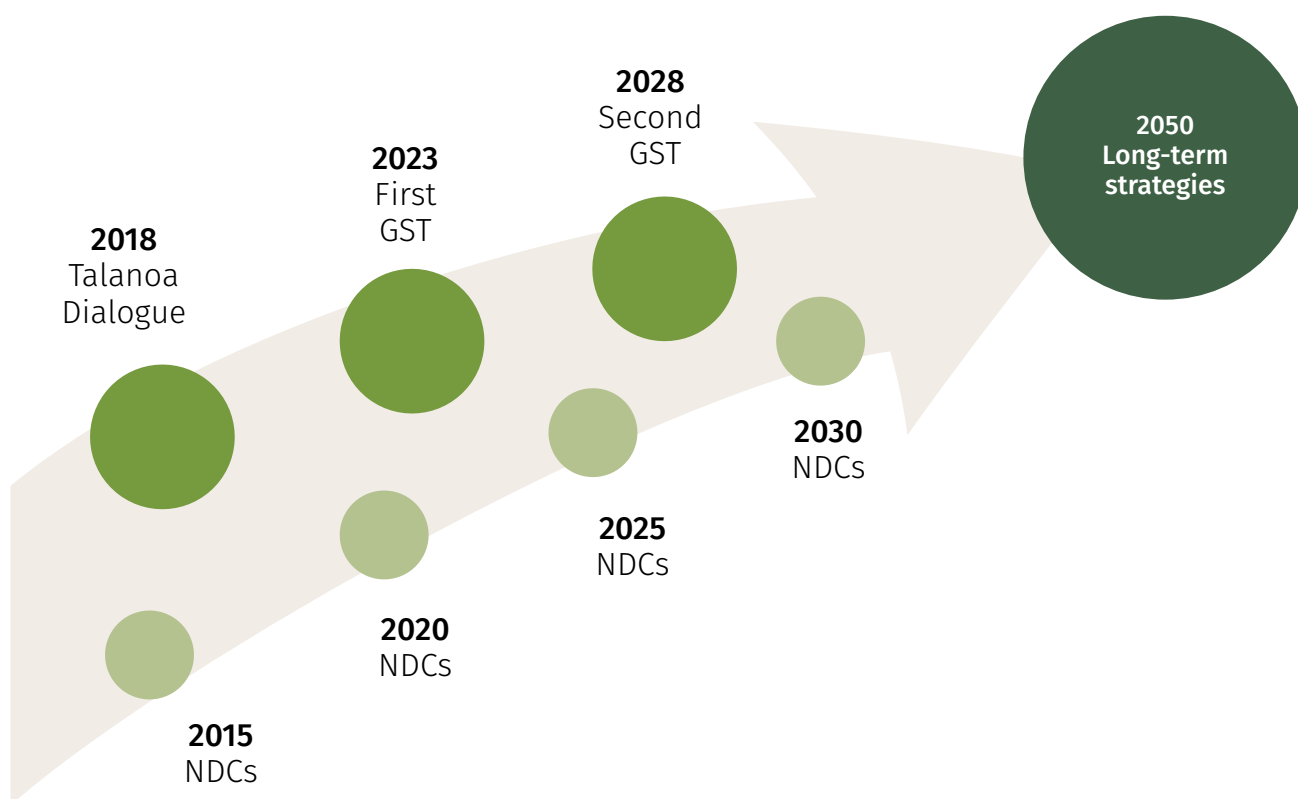
Furthermore, the GST is a collective exercise. As currently articulated the process will not publicly review or appraise country reports and performance. Obergassel et al. (2019), however, highlight that without accurate and sufficiently granular data, it will be impossible to determine whether and to what extent goals are being achieved. While Parties to the Paris Agreement are unlikely to rapidly converge around a single quantitative measure of the consistency of finance flows - it is unlikely that a single data point can even capture the breadth of progress towards the consistency of finance flows with low-emission, climate-resilient development (Whitley et al., 2018) – a common reporting framework would allow countries to share information and advance best practices in making finance flows consistent with low-emission, climate-resilient development pathways, even if executed on a voluntary basis.

2 The SCF dedicated a portion of each of its three chapters of the 2018 Biennial Assessment and Overview of Climate Finance Flows to this topic, covering methods and metrics, datasets that may be relevant to tracking consistency in insurance, lending, and investment decision-making processes, and in assessing how regulatory instruments, economic instruments, and information instruments could be taken into consideration to this end (UNFCCC, 2018). The forthcoming 2020 publication, delayed in light of the COVID-19 pandemic, will dedicate a whole chapter to Article 2.1(c).

3 In addition to the long-term goal of climate consistency, the two further long-term goals are limiting the increase in average temperatures to well-below 2°C above pre-industrial levels while simultaneously pursuing efforts to limit that increase to 1.5°C; and increasing the ability to adapt to the adverse impacts of climate change.

4 Decision 18/CMA.1, Annex, paragraphs 121.(q) and 132.(b)


FIGURE 1. Process of ratcheting climate ambition through nationally determined contributions, global stocktakes and long-term strategies



Source: author's own.

This paper outlines a framework within which Parties to the Paris Agreement can develop reporting processes to take stock of progress towards the climate-consistency of finance flows in their AFOLU sector. This chapter outlines the purpose of such a framework. A result of both desk review and key stakeholder consultations, chapter 2 proposes four government-led levers that can be employed or re-examined, to promote greater climate-consistency in the AFOLU sector. The four levers are defined, their role in supporting climate-consistency of finance flows in the AFOLU sectors described, and examples provided as to how each lever can be implemented. The framework is intended to be flexible, not prescriptive, with chapter 3 exploring how indicators can be selected and designed based on the framework in light of a country's climate-change objectives, the degree to which the AFOLU sector is relevant to their climate objectives, as well as their wider economic and market context. Chapter 4 makes considerations for a just transition away from climate-inconsistent finance flows

in the AFOLU sector, and chapter 5 offers a conclusion. This paper allows state and non-state actors alike to report on the climate-consistency of finance flows in the AFOLU sector, allowing them to take stock of progress to implement such actions and opportunities to fill gaps as well as contribute to the collective assessment of progress towards the third long-term goal of the Paris Agreement, Article 2.1(c).



CHAPTER 2
**A framework for
consistency of
finance flows
in the
AFOLU sector**

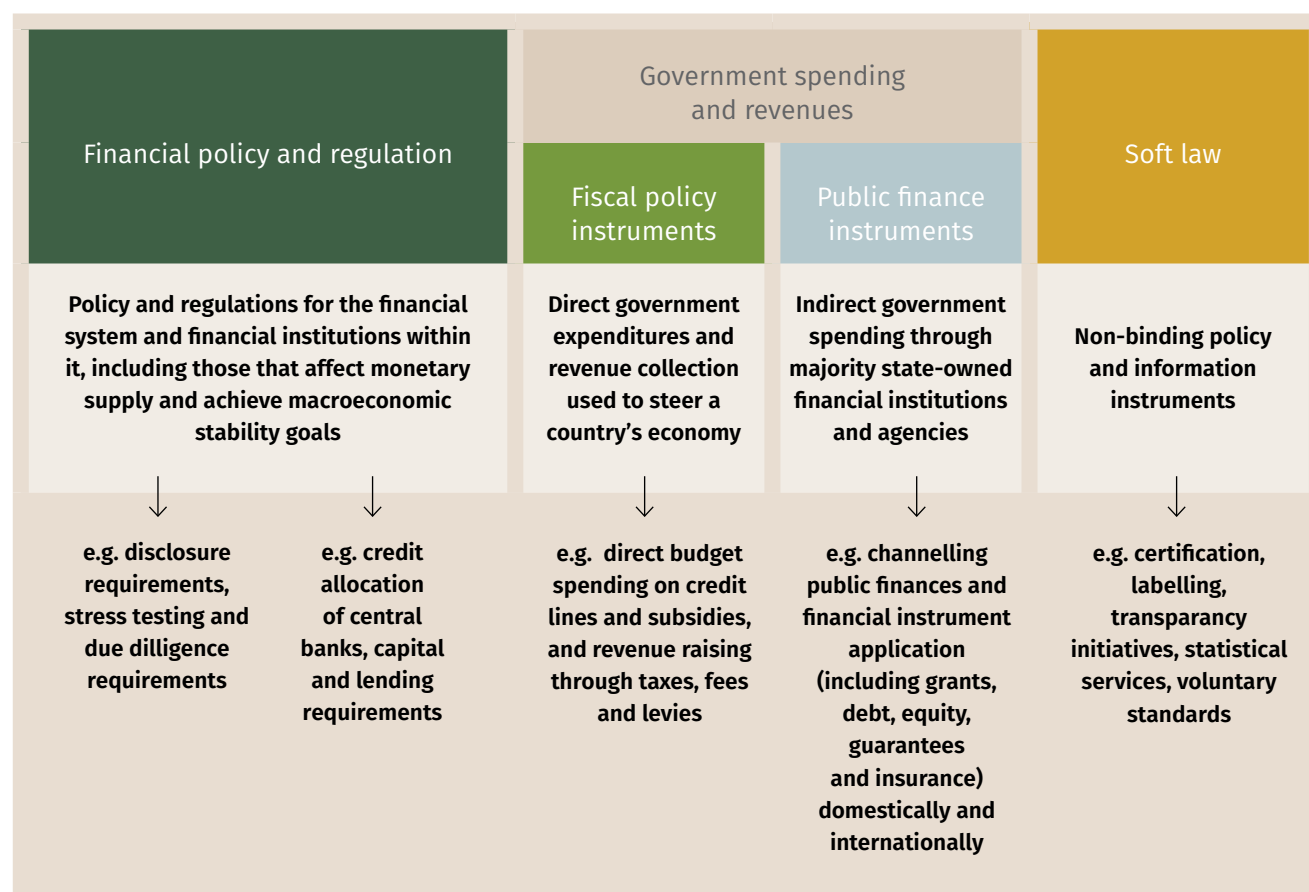
Governments have at their disposal a number of policy levers that influence the complex system of financial flows. These levers both directly and indirectly change the allocation and impact of financial flows. A framework of government levers, incentivizing and disincentivizing finance flows, relevant to operationalizing Article 2.1(c), is proposed by Whitley et al. (2018). Building on this framework, four levers for making finance flows climate-consistent in the AFOLU sector are proposed. These are financial policy and regulation, fiscal policy, public finance and soft law instruments (Figure 2).

2.1. Financial policy and regulation levers for consistency in the AFOLU sector

Financial policy and regulation refer to the regulation, supervision and oversight of financial and payment systems, including markets and institutions. Financial

policies and regulations are largely driven by ministries of finance, central banks and other financial regulatory authorities (Watson and Schindler, 2017) and are largely focused on promoting financial stability, in addition to improving market efficiency, increasing credit access and protecting investors (Labonte, 2020; Park and Kim, 2020). The focus here is not on wider climate-related policies and regulations, though these do impact investment decision-making in the real economy (Fankhauser et al., 2018), but specifically on those that influence the financial sector, implying the policy and regulation developed to shift and mobilize finance to low-emission and climate-resilient development in the AFOLU sector by influencing asset owners, asset managers, banks and corporations.

FIGURE 2. Government policy levers for redirecting finance



Source: Based on Whitley et al., 2018.

Table 2 details the three groupings of levers and sub-levers that are particularly salient for financial policy and regulation:

1. Finance strategies, institutional arrangements, taxonomies, standards and guidelines:

Growing awareness in the financial sector of the materiality of climate change has led to action from government and quasi-government financial sector actors. This action varies from statements of intent to financial system roadmaps and systemic plans, and a number of countries are working to enhance the ability of the financial system to mobilize capital towards climate objectives and away from climate-inconsistent objectives (World Bank Group, 2020; UNEP Inquiry, 2017). Sustainable and green finance taxonomies, in particular, are growing rapidly. These are tools to help investors understand if an activity is environmentally sustainable or ‘consistent’ with climate objectives. The EU, for example, is in the process of developing a green taxonomy while other taxonomies and green principles exist in China, Japan, France and the Netherlands (EUTEG 2020a; OECD, 2020a).

Guidance for green or sustainable investments for AFOLU can also emerge for particular markets or instruments. Green bond guidance and principles, for example, have emerged in Japan and China (UNEP Inquiry, 2017). This guidance allows for standardization of products and can, in turn, drive up their quality and value while avoiding ‘green washing’ - in which a product is labelled green but offers little environmental benefit. In some cases, these efforts are accompanied by the creation of high-level expert groups and in-country permanent bodies for green or sustainable finance.

2. Enhancement of supervisory review:

There has been a rapid growth in the disclosure of climate-related risks in financial decision-making. This has been spurred by the Task Force on Climate-Related Financial Disclosures (TCFD). Established in 2015 by the Financial Stability Board, TCFD has provided a platform and popularized the physical, transitional and liability-related risks of climate change, developing voluntary climate-related financial disclosures such that companies can provide information to lenders, insurers and investors from which (investment) decision-making can take better account of climate-related risks and regulators can better monitor financial activities (Feridun and Gungor, 2020; TCFD, 2017). While the TCFD recommendations have received many endorsements, countries are slower to mandate climate-related

financial disclosures that could not only highlight the emissions potential of AFOLU investment but also the physical risks of climate change that AFOLU sector actors will face.

The disclosure of climate risk builds on a long-standing body of work on the disclosure of environmental, social and governance (ESG) risks that are driven by corporate policies and commitments to achieve ethical commodity production and trade (CDP, 2020). Such commitments have significant climate-change mitigation potential. One-quarter of the global forest loss in the last 20 years has been commodity-driven including through palm oil, soybean, cattle, cocoa, coffee and wood pulp production (GFW, 2020; TFA, 2019).

To date, much disclosure of ESG risks is voluntary rather than mandatory (or comply or explain). To be effective, ESG risk disclosure must either be widely applied or applied to the most relevant investors. For example, they can be applied to banks and credit providers, asset manager and institutional investors or companies. Galt et al. (2021) highlight that, over the past two decades, improvements in agricultural finance have attracted an increasing number of institutional investors, including pension funds, hedge funds and high net-worth individuals. This suggest such disclosure tools could play an increased role in AFOLU investment.

3. Adjustment of capital and liquidity requirements:

Central banks and financial regulatory authorities can go further to influence the consistency of finance flows with low-emission, climate-resilient development pathways by influencing credit allocation policies and requirements for banks in their macroprudential role. They can, for example, set criteria for pension and sovereign wealth funds (though often managed privately). Tools also include enhancing capital and liquidity requirements, lowering liquidity requirements for green sectors to encourage green investment and setting lending limits that can limit the exposure to emission-intensive investments or create floors for green-activity lending. These tools are nascent in their application to promote consistency in finance flows, and many remain to be tested for their effectiveness and efficacy, measures that likely will be dependent on country contexts as well as on the perceived mandate of the regulators (Moessa et al., 2020).

TABLE 2. Overview of levers supporting the consistency of finance flows for financial policy and regulation in the AFOLU sector

FINANCIAL POLICY AND REGULATION			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
1. Finance strategies, institutional arrangements, taxonomies standards and guidelines			
Adoption of strategies and institutional accountability	Strategies and institutions with forward-looking intentions at a sectoral or target level, applied across the whole economy, or component parts of it.	The creation of a sustainable or green finance strategy/ roadmap/ action plan and/or related institutions and expert groups indicates a level of political will and awareness of climate change and wider environmental impacts and risks as well as the need for aligning prudential and climate-change objectives in the national financial architecture.	<p>The People's Bank of China has published 'Guidelines for Establishing the Green Financial System', providing a clear signal on future direction including some AFOLU relevant plans (e.g. insurance) (People's Bank of China, 2016).</p> <p>The Indonesia Financial Services Authority (IFSA) launched a Sustainable Finance Roadmap in December 2014. In 2017, Otoritas Jasa Keuangan (OJK), the regulator for the financial sector, released the Sustainable Finance Umbrella Policy to provide guidance to the whole financial system in Indonesia.</p>
Development and adoption of taxonomy	A classification system of economic activities.	Clarity on what can be considered 'green' or 'sustainable', or the identification of the activities that are Paris-aligned, increase investor confidence, prevent greenwashing and facilitate market development through increased demand and visibility in the market.	<p>The EU Technical Expert Group has created a green taxonomy with technical annexes outlining screening criteria for agriculture and forestry activities and their contribution to adaptation and mitigation (EUTEG, 2020b). Eventually, mandatory disclosure of the EU financial sector, using this taxonomy, will be required.</p> <p>Colombia's banking regulator (Superintendencia Financiera de Colombia) has a regulatory roadmap to develop a sustainable taxonomy – as a result of a study by the banking regulator on environmental and social risks in banks – that will cover loans and investments to spur market development (CCADI, 2020).</p>
Creation of standards and guidelines	Government-produced or endorsed standards and guidelines for the use and application of financial instruments and tools.	These increase the credibility of instruments, such as green bonds or green loans, to reduce greenwashing and can also work to accelerate market development.	<p>Indonesia's financial sector regulator – Otoritas Jasa Keuangan (OJK) – issued Technical Guidelines for Banks in 2017 on what are sustainable activities and how to implement environmental and social impact management, for example.</p> <p>In 2020, Japan's MoE published updated Green Bond Guidelines, with extended scope to cover green loan and sustainability-linked loans.</p>

FINANCIAL POLICY AND REGULATION			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
2. Enhancement of supervisory review			
Mandated disclosure of risks	Requires financial reporting to include information on particular risks that allows for more efficient capital allocation.	Where there is more transparency on the physical and transitional climate-risks (as a result of changes to policy in support of climate change, for example) to which specific financial institutions are exposed, it can shift capital allocation away from carbon-intensive assets that have high transition risks, for example, or those that are maladaptive.	<p>The Securities and Exchange Board of India (SEBI) requires detailed disclosure for the issuance and listing of green bonds and has expanded its requirement for 'responsibility reports' from the top 100 to 500 businesses in the country.</p> <p>France has developed specific requirements for climate-risk reporting attached to French law (Article 173 of the law on energy transition and green growth).</p> <p>In 2019, Japan held its first summit with its Consortium of the Task Force on Climate-Related Financial Disclosures (TCFD). An emerging focus area was the integration of climate into governance processes for businesses and the disclosure of their carbon targets to capital markets.</p> <p>The UK and the EU are planning to introduce mandatory climate-risk disclosures in 2021. These would prevent the import of commodities linked to deforestation and forest degradation (European Central Bank, 2020).</p>
Mandated disclosure of environmental, social and governance risks	Requires financial reporting to include information on particular risks that allows for more efficient capital allocation.	Where transparency is increased on the environmental, social and governance risks to which specific financial institutions are exposed, it can shift capital allocation away from activities with high-deforestation risk, or areas with high biodiversity risk or risks of adverse social impacts.	<p>Colombia's banking association (Asobancaria) also has a green protocol that is working to manage ESG risks (Asobancaria, 2017).</p> <p>Peru's regulator Superintendencia de Banca, Seguros y AFP, issued regulation for social and environmental risk management in financial institutions in 2015.</p> <p>Indonesia's Sustainable Finance Regulation requires all financial actors to annually report on their sustainability impacts, but also that institutional investors, in particular, develop an action plan on how to incorporate environmental and social considerations into their activities.</p> <p>In 2017, the Federal State of Berlin introduced a sustainability index to reallocate its pension fund investments.</p>
Conducting stress-testing	A supervisory level evaluation of the resilience of the financial system to adverse shocks.	Climate stress-testing can lead to the identification of financial institutions exposed to emission-intensive assets or highly climate-vulnerable assets, thus improving information and capital allocation.	Australia's Prudential Regulation Authority (APRA), will increase the intensity of its supervisory activities to assess the effectiveness of risk identification, measurement and mitigation strategies adopted by APRA-regulated entities.

FINANCIAL POLICY AND REGULATION			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
3. Adjustment of capital and liquidity requirements			
Adjusting liquidity requirements	Such requirements ensure financial institutions have enough assets available – and not too much tied up in particular types of assets – should market conditions shift.	Lowering liquidity requirements for green sectors encourages green investment by reducing the amount that financial institutions have to hold against lending.	<p>Indonesia's Sustainable Finance Regulation requires banks to scale up their financing of green sectors, including land use activities. The Reserve Bank of India in April 2015 issued a circular of Priority Sector Lending – Targets and Classification which explicitly target renewable energy and agriculture. The latter provides additional and subsidized liquidity to banks for lending to environmentally friendly projects (as well as imposing minimum credit floor).</p> <p>The Brazilian Circular on Internal Process of Capital Adequacy Assessment (No. 3,547/2011) includes a requirement for banks to demonstrate how they evaluate the risk arising from exposure to social and environmental damage caused by their activities when assessing how much capital is needed to cover a range of operational and financial risks.</p>
Adjusting lending limits and credit caps and floors	These manage bank exposure to certain type of sectors' activities and loan categories by setting maximum and minimum amounts for particular activities or sectors.	Adjusting lending limits, credit caps and floors can be used to limit exposure to emission-intensive investments or those that are not resilient to climate impacts; set targets for flows towards green activities; or set caps on climate misaligned activities.	<p>Brazil's banking regulator, Banco Central do Brasil (BCB) prohibits lending to farms violating sustainability-related laws and regulations. There are also regulations on rural loans that provide positive impacts through productivity increases in crops or livestock through the ABC programme (though the programme has now been discontinued).</p> <p>In 2014, the People's Bank of China (PoC) complemented the Green Credit Guidelines by introducing a Green Credit Monitoring and Evaluation mechanism and a key Performance Indicators Checklist. The China Banking Regulatory Commission (CBRC) launched the Green Credit Statistics System in 2014. Green credit loans are classified into 12 categories with sub-categories.</p>

Sources: Authors own, plus analysis based on a revised version of data presented in D'Orazio and Popoyan, 2019a,b; and Moessa, et al., 2020.

2.2. Fiscal policy levers for consistency in the AFOLU sector

Fiscal policy levers are those that shift private investment decisions and consumer behaviours through prices. Finance ministries, in particular, can use direct public budget allocations, taxes and subsidies that can be implemented through sectoral ministries, state-owned enterprises and other public authorities. Common fiscal policy levers that have been employed in pursuit of climate action include environmental levies and carbon pricing – both highly relevant for the AFOLU sector – as well as renewable energy subsidies and the phase-out of inefficient fossil fuel subsidies (Climate Transparency, 2020; Watson and Schindler, 2017).

Table 3 outlines the four groupings of fiscal policy levers that may be particularly salient in a country's efforts towards making finance flows consistent with climate objectives in the agriculture sector:

4. Direct transfers:

Focusing on agricultural support to producers, direct transfers include production payments and conservation payments. Farm-level production payments have been favoured in many countries over agricultural research and development, for example. This is despite the danger that production support results in excess use of fertilizer, over-pumping of groundwater and inefficient use of water (with low-priced electricity or under-priced water) and monocultural production systems that can lead to adverse climate outcomes and environmental pollution (World Bank, 2018).

Adjusting public agricultural support – in particular, production payments – in order to contribute to climate change mitigation should retain a focus on increasing efficiency. This can be efficiency in the use of land, in animal rearing, in the use of water and application of chemicals. Emission reductions can be delivered, therefore, from shifts in production processes and the avoidance of agricultural land expansion, as well as through improving animal feed quality, reducing food loss, and changing agricultural management practices (such as separating manure solids from liquids).

Attaching climate conditionalities to producer support and conservation payments is discussed in the literature. These levers allow access to production payments or pay farmers directly to avoid environmentally harmful actions, or these levers pay

farmers to start using practices that are considered less harmful to the environment (Mamun et al., 2019; Searchinger, 2020).

5. Goods and services:

This captures government spending towards the provision of public goods, such as research and advisory services, public infrastructure, and food and safety standards. Such spending does not necessarily alter producer costs/revenues, though it can work to increase productivity, boost farmer income and may reduce consumer prices. Although currently a tiny proportion of overall support in most countries, research and development investment can yield high returns (World Bank, 2018). Such research could support adaptation, for example, in the face of increased droughts and changing growing seasons. If designed and communicated in a way that considers the needs of different producers and farming systems, government spending on goods and services can also contribute to wider economic and social goals (Bellman, 2019).

6. Forgone revenues:

As applied to the agriculture sector, exemption from tax obligations may include preferential treatment on taxes on inputs – including fossil fuels – and outputs such as Value Added Tax (VAT); special tax rates on farm income that allow for averaging across volatile income years; special treatment for depreciation to encourage investment; and, preferential property tax rates applied when transferring a farm to new owners to avoid disruption to production (OECD, 2020b).

7. Market price support:

This includes tariffs and price floors that keep domestic prices for specific products higher than world market prices (and so are distortionary). Plausible mechanisms to reform market price support for climate change mitigation are challenging to find (Searchinger et al., 2020). Some suggest they could increase emissions (Laborde et al., 2020). However, much market price support is linked to income and food security and, while it has so far failed to support the poorest and most-vulnerable, redirection or reform of market price support could play a role in adaptation to climate change.

The AFOLU sector and its relevant fiscal policy extends far beyond agricultural support. It is noted that this chapter has not fully addressed fiscal policy for forestry, nor biomass and biofuels, soil protection, water supply and distribution, all of which will need to be explored

in the pursuit of consistency of finance flows with climate objectives in the AFOLU sector. As AFOLU is an energy- and transport-intensive sector, fiscal policies of these sectors should be considered too. Fossil fuels are used in many production activities involving trucks, machinery, pumps, heating and cooling, as well as in fertilizer and pesticide manufacture (FAO, 2018). As such, carbon pricing or other environmental levies will also have a role to play.

Fiscal policy as an adaptation tool is a nascent area in which more research is needed. Canales Trujillo et al., (2015) and Norman et al., (2016) suggest introducing tariffs and exemptions for water supply, tax breaks for geographical diversification of farming, and exemptions from land-use fees for road and rail infrastructure could build resilience to climate change. Fiscal policy

for resilience is further likely to include the better integration of climate risks into planning and budgeting cycles. This would include contingency planning – government finances and a country's debt sustainability are exposed to fiscal risks from climate-related weather events (Volz et al., 2020a) – for spending on climate-related event relief and recovery. It would also include any necessary bailouts for public or private corporations, including state-owned enterprises, as a result of these events, that can be considered contingent liabilities (IMF, 2019). In this context, fiscal tools available to increase liquidity and reduce debt default include contingency and reserve funds, ex-ante contingent credit and ex post borrowing; and risk transfer and pooling, such as multi-country sovereign disaster insurance, insurance of public assets and catastrophe bonds (Watson et al., 2020; Pigato, 2019).

TABLE 3. Overview of fiscal policy levers supporting climate-consistency of finance flows in the AFOLU sector

FISCAL POLICY LEVERS			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
4. Direct transfers			
Reform of production payments	This includes production support; farm income support (including public procurement of farm outputs); and input subsidies (including financial subsidies such as lowered interest rates on agricultural credit or loan guarantees).	Reduce and decouple payments based on inputs or outputs, in order to reduce emissions or the inefficiency of production being introduced by coupled subsidies.	In 1984, New Zealand enacted wide-ranging reforms to eliminate agricultural subsidies, a unique policy among developed economies that has broadly positive effects on the environment – for example reducing pesticide and fertilizer use and improving water quality (Vitalis, 2007). China has recently phased out its nitrogen (fertilizer) subsidies, in addition to increasing public agricultural support for reforestation and regenerating grasslands.
Conditionality of production support	Placing mandatory conditions on agricultural public payments such as compliance with certain activities.	Conditionality incentivizes farmers not to undertake environmentally harmful practices or pays them to start using practices that are considered less harmful to the environment.	US farmers must not drain or have not drained wetlands since 1985 to be eligible for most farm payments. Brazilian eligibility requirements for government-sponsored, low-interest agricultural loans include compliance with the Forest Code, which restricts the amount of forest land that farmers can clear. Between 2014-20 the EU Common Agricultural Policy provided direct, decoupled payments (per hectare) to farmers on top of a basic payment if they made use of climate and environmentally friendly farming practices (including, crop diversification, maintaining grassland, buffer strips, and nitrogen-fixing crops) (European Parliament 2020). ⁵

⁵ The EU CAP (2021-27) has proposed 'enhanced conditionality' that acts to increase the scope of mandatory activities required so that producers can receive direct payments (including requirements to maintain permanent grassland and protect wetlands and peat-land). It also proposes new voluntary, 'eco-schemes' – optional environmental and climate rules that qualify farmers to receive a certain amount of annual area-based direct payments to be determined by Member States (Lotz et al., 2019).

FISCAL POLICY LEVERS			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
4. Direct transfers			
Introduction of conservation payments	Such payments link productivity gains with protection of natural lands. This can involve taking land out of production (retirement) or putting it into conservation of existing natural landscapes.	Production retirement (land or livestock), particularly for less-productive assets, can lead to carbon sequestration and other environmental benefits.	<p>The Conservation Reserve Program in the US provides temporary land retirement through 10-year contracts on highly erodible and environmentally sensitive lands.</p> <p>China's Grain for Green programme controls the expansion of agricultural land on natural grasslands and improves production efficiency through water and soil improvements.</p>
		Conservation and restoration of land (including grasslands, peat-lands and wetlands).	<p>The Conservation Reserve Enhancement Program in the US allowed states to submit plans for coordinated restoration, protecting buffer zones and wetlands, where farmers that enrolled lands received special incentives.</p> <p>China makes payments to avoid cattle grazing on severely degraded grassland</p> <p>Executed by the Fondo Nacional de Financiamiento Forestal (FONAFIFO) and funded by a fuel tax and water charge, landowners in Costa Rica receive direct payments for the environmental services delivered through sustainable land-use and forest management. Agreements are adaptable and differentiated according to the strategic importance of the environmental service provided (FONAFIDO, 2021).</p>

FISCAL POLICY LEVERS			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
5. Goods and services			
Rules for public procurement	The purchase of government- and state-owned enterprises of goods, services and works, accounting for a portion of taxpayers' money.	Public authorities, as major consumers of goods and services – in construction, catering, vehicles and transport – can be required to choose 'green' over other goods and services.	<p>The European Commission is actively considering green public procurement in its member states to tackle the EU's impact on global deforestation. The EU public procurement directive includes legality as a criterion based on the EU Timber Regulation that prohibits the placing on the EU market of illegally harvested timber (and its products) (EU, 2018a, b).</p> <p>The European FLEGT Action Plan includes support to timber-producing countries to develop national timber procurement policies. Voluntary Partnership Agreements can also be made as part of a scheme to ensure only legally harvested timber is imported into the EU from countries agreeing to take part (timber producing countries voluntarily enter into negotiations but once signed, the VPAs become part of the trade agreement).</p> <p>In New York, Mayor Bill de Blasio announced that all New York City public schools will have 'Meatless Mondays' beginning in the 2019-2020 school year providing all-vegetarian breakfast and lunch menus every Monday, with the aim to reduce greenhouse gas emissions and improve health (NYC, 2019).</p>
Development of general services	These capture the spending on the provision of public goods, such as research and advisory services, public infrastructure, and food and safety standards.	<p>Advisory services might work towards minimizing the misuse of emission-intensive inputs e.g., fertilizer.</p> <p>Research and development might work to improve yields, drought resistance, reduce transportation losses.</p> <p>The development of public infrastructure should take into account climate risks, both transitional and physical.</p>	<p>Agromet advisory services assist Indian farmers in making tactical decisions on which crops to plant and when, when to undertake fieldwork, apply fertilizer and pesticides, and when to harvest.</p> <p>The National Hydrological and Meteorological Service of Cuba (INSMET) has created a Fire Danger Index to assist farmers and foresters in planned burns and policymakers to move firefighting resources to areas of high risk.</p> <p>China has increased support for research towards farm practices to help reduce emissions in recent years, and the effort is ongoing.</p>

FISCAL POLICY LEVERS			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
6. Foregone revenues			
Preferential tax treatment on inputs– and outputs	These exempt a sector or activity from tax obligations and can be considered forgone revenues and an indirect subsidy.	Reform tax concessions so as to decrease or remove on high emissions inputs and increase on low-emission activities	Kenya has lowered the tax concessions on fertilizer, though motivations are not climate-linked (Light et al., 2019).
Special tax rates on farm income			In Sweden, farm buildings, farmland and forested land are exempted from all property taxes, including annual land taxes.
Special treatment for depreciation		Place environmental conditionalities on tax concessions.	Costa Rican farmers who practice soil conservation are eligible for a 40 % reduction on annual property taxes.
Preferential property tax rates			In Japan, the registration tax rate on transfers of land managed for conservation purposes is 0.4 %, compared to a registration tax rate of 2 % for other land use types. Hungary, in a bid to promote continuity in farmland management, offers a further 25% reduction on inheritance tax for farmland if the heir is a registered farmer. In Japan, inheritance tax waivers are in place for sole heirs of agricultural land to prevent the subdivision of farmland.
7. Market price support			
Reforms of trade barriers (e.g. tariffs), price floors and public stockholding	Transfers from consumers and taxpayers to agricultural producers from policy measures that create a gap between domestic market prices and the border prices of a specific commodity.	Reduction and removal of market price support on high GHG-emitting commodities (such as rice, beef, veal and dairy) could improve their GHG efficiency, while there is a need to further explore options to improve climate-change resilience by market price support reform.	Market price support has largely declined in countries such as the US and in the EU. China has substantial market price support, though it has discontinued price support for cotton, soybeans, rapeseed and maize.

Sources: Galt et al., 2021; Locke and Lowe, 2021; Searchinger et al., 2020; OECD, 2020b; WMO, 2019.

2.3. Public finance levers for consistency in the AFOLU sector

There are multiple institutional arrangements through which public finance is channelled, as captured in this framework element. This understanding of public finance excludes the expenditures through fiscal policy and public budgets in the chapter above. It therefore focuses on expenditure from majority government-owned financial institutions.⁶ Public finance is employed domestically and internationally. The latter notably is used in the climate space through developed country obligations to provide climate finance to developing countries. Public finance flows include those motivated not by development objectives but by commercial and foreign policy objectives, including export credits through export credit agencies.

Table 4 outlines the two groupings of levers that are particularly important in the climate-compatibility of finance flows from majority-owned public finance institutions:

8. Upstream policy:

These focus on the steps taken within the governance and institutional arrangements of institutions programming public finance. Increasing numbers of public finance institutions are pledging alignment with the Paris Agreement (EDFI, 2020; MDBs, 2019; AfDB, 2017). Such upstream policies would work to embed such pledges into mandates, strategies and operations, the objective being to build coherence and eliminate conflicts between funding objectives, as well as to build the leadership and capacity to adequately address climate change in a public finance institution.

9. Downstream policy:

These focus on the steps taken towards the development and application of methodologies, tools and financial instruments in public finance institutions and during the monitoring of their impact. Tools to screen for climate risks and to develop temperature scenarios that can guide portfolio spending are increasingly available. Longer-standing tools like GHG accounting and shadow carbon pricing are already in existence, and they can direct investment decisions to more climate-aligned actions. Furthermore, similar to in the case of regulatory authorities mandating lending limits (caps and floors) to direct finance towards or away from particular sectors and activities, public finance institutions can adopt their own, internal capital and liquidity requirements.

Public finance can shift investment decisions and raise capital for low-emission, climate-resilient investments by influencing the real and perceived risks and costs of capital. The financial instruments and structures through which public finance institutions can encourage climate-aligned finance – and the associated barriers that necessitate them – have received much attention (for example, see: UNCCD and FAO, 2015; Guarnaschelli et al., 2018; Castren et al., 2014; Limketkai et al., nd). The MDBs, for example, have faced criticism for continued lending to the high GHG-emitting, intensive livestock sector. The International Finance Corporation (IFC) – the commercial lending arm of the World Bank – and the European Bank for Reconstruction and Development (EBRD) have together provided \$2.6 billion for pig, poultry and beef farming, as well as dairy and meat processing, in the past 10 years (Guardian, 2020).

⁶ Following Whitely et al. (2018), this implies that while the public resources used to establish or capitalize a public fund or institution would be captured under fiscal policy, the grants, loans or guarantees disbursed by those public funds or institutions (and the rules governing that disbursement) would be captured here, under the category of public finance.

TABLE 4. Overview of public finance levers supporting climate-consistency of finance flows in the AFOLU sector

PUBLIC FINANCE			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
8. Upstream policy			
Development of mandates, strategies and operations	Policies that embed themes or topics into the mandates, strategies and operations of public finance institutions can build coherence and eliminate conflicts between funding objectives, as well as referring to adjustments in leadership and capacity.	Climate change integrated into overarching strategy and climate integrated into sectoral strategies.	Development Bank of Southern Africa (DBSA) has created a Climate Finance Unit that operates as a green bank-like institution within an institution (Coalition for Green Capital, 2017).
		Climate change embedded in institutional structures and leadership in climate-change response.	The Netherlands Development Finance Company (FMO) has an exclusion list (e.g. coal) as well as screening for ESG risks and a green label to be applied to investments that reduce GHG emissions and support adaptation, corresponding with internal annual spending targets.
		Negative/ black-listing of Paris misaligned investments.	French Development Agency (AFD group) decided in 2013 to formally exclude the financing of coal power plants without an effective carbon capture and storage (CCS) system in place.
		Institutional or portfolio-level tracking and accountability.	The Netherlands Development Finance Company (FMO) compares the annual emissions footprint of its finance against the point where it should be along a pathway towards limiting global temperature rise to 1.5°C (FMO, 2018).

PUBLIC FINANCE			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
9. Downstream policy			
Adoption of decision-making and evaluation processes	Public finance institutions' development and application of methodologies, tools and financial instruments and the monitoring of their impact.	Adopt risk-screening methodologies, tools and scenarios.	<p>The French Development Agency has created a sustainable development analysis mechanism including transition to a low-carbon pathway and climate-change resilience. The agency also defines the scope of climate action at country level using NDCs (AFD, 2018)</p> <p>The EIB uses shadow carbon pricing to assess its investments and has an emissions-performance standard requiring electricity generation projects to meet a minimum GHG emissions threshold.</p>
		Introduce lending limits (caps and floors) for particular sectors, targets and incentives.	The Development Bank of Japan introduced the Environmental Rating Loan programme in 2004 that offers preferential interest rates determined by eco-ratings on a company's environmental management.
		Development of de-risking tools and instruments to support climate-aligned finance flows.	<p>The Global Agriculture and Food Security Programme Private Sector Window, managed by the International Finance Corporation (IFC), invests alongside IFC's commercial funding across the food supply chain for agribusiness and agro-based products. The fund is supported by Australia, Canada, Japan, the Netherlands, the UK and the US through grants and risk guarantees.</p> <p>The German development bank KfW, through its InsuResilience Fund, and the UK's FCDO support the Africa and Asian Resilience Disaster Insurance Scheme to help smallholder farmers below the poverty line recover after drought through access to small loans on special terms (early stage funding also engaged the Rockefeller Foundation and FMO, the Dutch Development Bank).</p> <p>The Council on Smallholder Agricultural Finance, together with the Global Development Incubator, have created Aceli Africa, a grant-funded facility that will provide financial incentives for lenders paired with technical assistance for small- and medium-enterprises (SMEs) to mobilize high-impact loans in East Africa. The initiative is supported by development cooperation agencies.</p>
		Transparency in and the monitoring, reporting and verification of impact of finance flows.	TRASE initiative, backed by Norway, is a tool to trace deforestation risks in key deforestation sectors such as soy and palm oil, allowing financial institutions to improve the sustainability of their portfolios.

2.4. Soft law levers for consistency in the AFOLU sector

Information instruments are a category of government levers that act by raising awareness, promoting learning, shifting behaviour and business development. Including learning platforms, industry associations, voluntary standards and reporting initiatives, they can be used by governments and non-state actors alike (Whitely et al., 2018).

Table 5 outlines the three groups of soft-law levers that may be particularly salient for climate-consistency in the AFOLU sector including:

10. Commitments and pledges:

The Paris Agreement and the signatory governments' commitment to it, can be considered an information instrument in itself. Within the Paris Agreement, countries – to varying degrees – are committed to producing plans, strategies and protocols to monitor and report on their progress towards climate objectives; and civil society, particularly youth groups, are mobilizing behind these government commitments. Many countries have made a wealth of further commitments and pledges around the AFOLU sector. These serve to provide signals to public and private sector actors of future policy directions (that can identify where, for example, transition risks might lie).

Commitments and pledges can act as precursors to wider action – and even mandated action. Within the AFOLU sector, there is a general increase in the attention paid to halting deforestation in commodity supply chains. This is in part due to rising consumer awareness, and can also be prompted by companies experiencing physical disruptions to supply chains.

11. Learning networks, associations and institutions:

Coalitions of non-state actors, or of state and non-state actors, have also worked well to promote awareness of the climate crises and climate change in the AFOLU sector. Institutions have also developed around particular commodities that drive land-use change. There is the Round Table for Sustainable Palm Oil and Round Table for Responsible Soy, for example.⁷ There are a variety of structures; but, in general, such groups work to promote awareness, information and tools at both national or international level.

12. Voluntary standards and guidelines:

Standards, certifications and labelling guidelines that allow consumers to make more informed choices, as well as generate a price premium for products. These can be at a national or international level and driven by a theme – such as climate or forestry – or a commodity – such as palm oil. For example, Indonesia and Malaysia both have a Sustainable Palm Oil (ISPO) scheme and, together, the two countries produce close to 80 percent of the global supply of palm oil (Galt et al., 2021). Rainforest Alliance and Fair Trade are well-known organizations internationally and commonplace now in supermarkets, for example.⁸

⁷ See: <https://rspo.org> and <https://responsiblesoy.org/?lang=en>

⁸ See: <https://www.rainforest-alliance.org> and <https://www.fairtrade.net>

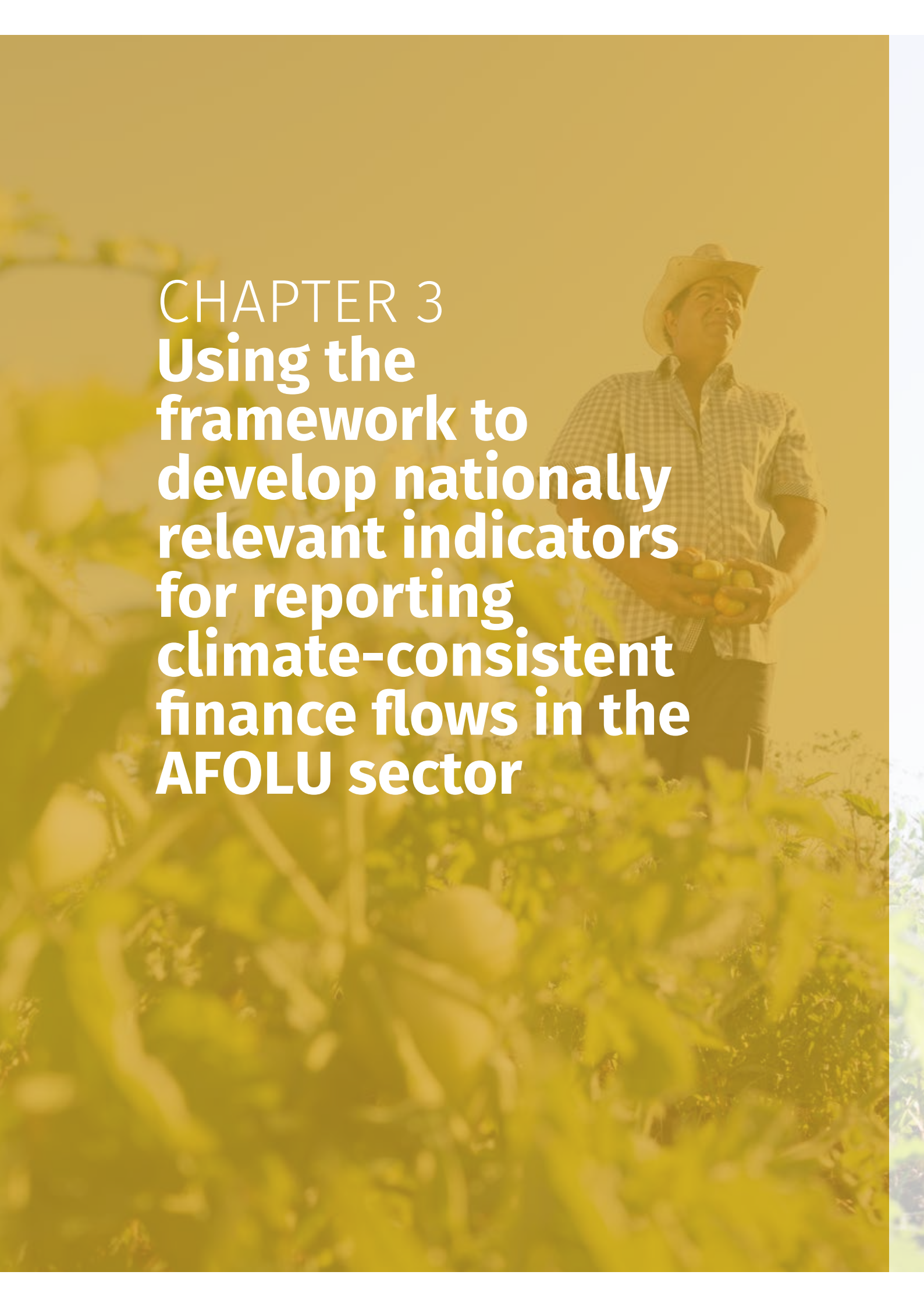
TABLE 5. Overview of soft law levers supporting climate-consistency of finance flows in the AFOLU sector

SOFT LAW			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
10. Commitments and pledges			
Making commitments and pledges	Legally non-binding international and national intentions towards action.	These serve to provide signals to public and private sector actors of future policy directions in the AFOLU sector. This can support the identification of where, for example, transition risks might lie. They can also act as precursors to wider action and even mandated action.	<p>The Paris Agreement is an international treaty on climate change adopted by 196 Parties in 2015 and in force since November 2016.</p> <p>The New York Declaration on Forests is a voluntary and non-legally binding international declaration to act to halt global deforestation.</p> <p>The Bonn Challenge is a global goal to restore degraded and deforested landscapes.</p> <p>In November 2018 the French government published an action plan to deal with imported deforestation, including proposals to stop importing products linked to deforestation and unsustainable agriculture by 2030, to help companies meet their own deforestation goals and to encourage financiers to take environmental and social issues into account for investment decisions (Ministere de la Transition Ecologique et Solidaire, 2018).</p> <p>The Brazilian Vegetable Oil Industry Association and Brazilian Grain Exporters Association and their member countries pledged not to trade and finance soy produced after 2016 from deforested areas within the Amazon Biome.</p>

SOFT LAW			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
11. Learning networks, associations and institutions			
Developing learning networks, associations and institutions	Organizations of various structures to facilitate learning, sharing of ideas and collective action.	These networks, associations and institutions can be organized around a theme – such as climate or forestry – or a commodity – such as palm oil. They promote awareness, information and tools at both national or international level.	<p>The Task Force on Climate-Related Financial Disclosures (TCFD) led by the Financial Stability Board consists of over 30 members from G20 countries who develop recommendations for more effective climate-related disclosures.</p> <p>The Network of Central Banks and Supervisors for Greening the Financial System works to share best practices on climate risk management in the financial sector. As of the end of 2020, there were 83 members and 13 observers of the network.</p> <p>The Institutional Investors Group on Climate Change is a collaboration of businesses, policymakers and investors who mobilize capital for the low-carbon transition and to ensure resilience.</p> <p>The Accountability Framework initiative is an umbrella coalition of interested institutions. It considers the elimination of deforestation and ecosystem conversion in commodity supply chains. It also considers human rights abuses in agricultural and forestry supply chains. It includes supply chain goals and effective implementation systems, including traceability, certification and monitoring and verification for timber, palm oil, soy, cattle, rubber and a category to capture other commodities (CDP, 2020).</p> <p>FAIRR is a collaborative investor network made up of investors with collective assets of over USD 29 trillion that raises awareness of the environmental, social and governance (ESG) risks and opportunities brought about by intensive animal agriculture (FAIRR, 2020).</p>

SOFT LAW			
Levers	Definition	Role in making AFOLU finance flows more climate-consistent	Examples
12. Voluntary standards and guidelines			
Adopting standards, certification and labelling	Including standards, certification and labelling, these allow consumers to make more informed choices, as well as generate a price premium for products.	Akin to the standards and guidelines developed by government stakeholders, these work to prevent greenwashing, increase quality and credibility and create green markets when adopted by large-scale purchasers and consumers.	<p>The Climate Bonds Initiative has established a Climate Bonds Standard and Certification Scheme to label bonds, loans and other debt instruments. These include sectoral criteria for agriculture, forestry, land conservation and restoration, for example (CBI, 2019b).</p> <p>CICERO Shades of Green AS provides research-based evaluations of green bond investment frameworks to determine environmental robustness.</p> <p>The International Organisation for Standardization (ISO) – an independent body – launched standard ISO14097 to provide a common framework for governments and businesses to assess and report on investments and financing to climate change (ISO, 2018).</p>

Sources: Author's own, additional links <https://www.fsb-tcfd.org/about/>; <https://www.iigcc.org>; <https://www.ngfs.net/en>; <https://cicero.green>

A photograph of a farmer wearing a cowboy hat and a checkered shirt, holding a basket of lemons. The background is a field of green plants, possibly lemons, under a bright sky. The entire image has a yellowish tint.

CHAPTER 3
**Using the
framework to
develop nationally
relevant indicators
for reporting
climate-consistent
finance flows in the
AFOLU sector**

The four framework elements for climate-consistency of finance flows in the AFOLU sector can be developed to create nationally appropriate indicators. Reporting on a nationally appropriate set of indicators on climate-consistency of AFOLU finance flows support the identification of the actions already being taken in the AFOLU sector that are climate-consistent. Such indicators can be developed and applied by state and non-state actors alike, though a process of engaging and involving cross-government stakeholders can help identify the levers that are most relevant both technically and politically. A with-government approach is also more likely to ensure ownership and engagement in the results, particularly if an expert group is established within existing government structures.

There are opportunities for parties and non-party stakeholders to make submissions of progress towards these indicators into the information collection phase of the GST. Implementing guidelines for the GST were elaborated in Katowice, identifying that there would be a three-step process of information collection and preparation, technical assessment and political assessment. Though as of yet, the transparency of the input process is not clear. Should the underlying framework be developed into indicators and applied in multiple countries and submitted into the GST process, it could support a collective understanding of progress towards this long-term goal. Repeated reporting on indicators can also indicate progress made over time; the second GST is currently planned for 2028.

Beyond the collective-level reporting on the Paris Agreement's long-term goal, the process of developing indicators and reporting on them can also support countries in understanding the role that these levers can play in the development of sustainable finance strategies and scenarios, and support countries in better articulating the role of the AFOLU sector in their national climate policies, actions and measures.⁹

The indicators for climate-consistent finance flows are unlikely to be the same in all countries. Three areas of consideration will support the selection of the most nationally appropriate indicators. Consideration of each will guide the selection of nationally relevant levers from chapter 2 around which indicators, and subsequent progress reporting, should concentrate:

a) The nature and relevance of the AFOLU sector:

This area of consideration speaks both to the AFOLU sector's contribution to the economy (and so the scales of finance flows), as well as the sector's climate change impacts (GHG emissions) and climate change mitigation and adaptation potential.

Agricultural emissions are highly concentrated by commodity, for example. Beef, dairy and rice together account for over 80 percent of agricultural GHG emissions from cultivation practices, while emissions arising from deforestation are focused on beef, palm oil and soybean production (Mamun et al., 2019). As a result, countries that are significant producers of these commodities may wish to focus indicators on the specific landscape of fiscal policies that drive production in these commodities. Countries that are significant consumers, or are home to capital providers to these commodities, may wish to focus on indicators of financial disclosures of risk. Similarly, countries whose agricultural sectors will face increased variability in rainfall, drought and other weather extremes may include more indicators for the disclosure of physical climate risks and the development of indicators for fiscal policy for resilience, than would be included in countries that do not frequently experience frequent climate-related weather events.

b) The end-point objectives in the AFOLU sector:

As noted above, Nationally Determined Contributions and longer-term strategies propel the country-driven approach of the Paris Agreement. In most countries, additional national targets will engage the AFOLU sector. These would include national and sub-national development strategies, medium-term development plans, sectoral strategies, biodiversity and forest protection policies and plans.

Forests are found to be a key sector in a number of first NDC submissions (IUCN and Climate Focus, 2018). These NDCs, however, are found to largely underestimate the potential for forest solutions or lack the specificity needed to implement them (Sato et al., 2019). Few contain forest sector-specific quantitative targets and

⁹ It has been suggested that countries could voluntarily choose to report on Article 2.1.c through the ETF, in particular through their NDCs, whereby the inclusion of policies, actions and measures around climate-consistency would then trigger reporting on progress towards this in their biennial reporting (Whitely et al., 2018).

a number actively exclude the sector from mitigation commitments (IUCN and Climate Focus 2018). Where these targets can be identified, indicators can be developed that are directly relevant to national land use change drivers. For example, indicators might be focused on the main commodity driving deforestation in the country, or on conditional payments that require deforestation or forest restoration. A cacao-producing country, with strong exports, may wish to focus on indicators around taxonomies and disclosures, linking domestic efforts with those of its trade partners.

Not all high-level commitments are mainstreamed in government policies. Not all countries have reached consensus on the drivers of deforestation. As such, the process of creating indicators for this framework can also support countries in better articulating their AFOLU targets in their NDCs (and LTS) and in highlighting opportunities to further create incentives towards meeting these goals or identifying trade-offs.

c) The enabling environment within which to make finance flows consistent with climate objectives:

This relates to broad factors such as governance, aspects of the ease-of-doing-business, market structures, and the ability and capacity to employ certain government levers of this framework.

The AFOLU sector, forestry in particular, has long been characterized by governance and law enforcement weaknesses and challenges that result and perpetuate illegal activities like logging, forest clearing and export (Brack, 2019). These weaknesses and challenges in the AFOLU sector often stem from unclear land tenure, resource ownership and use rights, and policy incoherence; but other important impacts include the degree of stakeholder participation in policy-making and failures in enforcement that can be linked to corruption. Unpredictable regulatory and political environments, combined with macroeconomic risks (especially exchange rate movements) and poor infrastructure in some developing countries, deter or create barriers to the deployment of private finance in the land-use sector (Castren et al., 2014). In addition to which, small-holders and rural communities may have little access to financial markets to overcome often high-upfront costs of sustainable land uses (AGF, 2012). SMEs also play an enormous role in supporting sustainable land use but lack significant access to finance (see e.g., Aceli, 2020).

Indicators need to be realistically embedded into the country context in which finance flows, cognizant of the

challenges and opportunities of a country. A national development bank with low capacity may be unable to implement upstream levers to make public finance flows climate consistent, making these indicators redundant in such a country. In a country highly fiscally constrained, there may be no scope for an indicator on tax concessions. Or a country with poor credit ratings will likely be unable to issue a sovereign green bond, making an indicator on the existence of green bond guidance redundant. Such countries may instead focus on indicators around general services, in particular the role of this form of government spending in validating technologies and providing technologies to farmers.

The further design of the indicators will likely consider both quantitative and qualitative aspects of climate consistency. Quantitative efforts are likely to suffer from poor data availability and comparability issues, necessitating more qualitative, action-based indicators. It is also important to recognize that the presence of a policy or regulation does not necessarily mean it is being implemented, nor that the extent of its action is aligned with a country's NDC or LTS, both supporting the effectiveness of the lever. In some countries, for example, environmental levies can be the first to be waived in times of hardship. Bingle et al. (2021) suggest not only recording the presence or absence of a policy lever, but also subcomponents that consider implementation status, climate ambition and data availability. Table 6 takes a subsection of indicators developed to track progress towards climate-consistency of finance flows in Switzerland.

Developing and applying a framework for reporting on Article 2.1(c) in the AFOLU sector, as outlined in this paper, can also establish a baseline from which repeated assessment could show progress or regression against making finance-flows climate-consistent. While each country or actor may apply the framework differently, every application must be clear and transparent regarding indicator selection and development; this will allow scrutiny of each country's interpretation of 'consistency' and add legitimacy and rigour to the reporting.

This framework, focused on government-led action, does not imply that private-sector led actions are not relevant. Instead, it is intended to highlight the responsibilities and accountabilities government actors have under their Paris commitment. There is a growing appreciation that climate change presents material risks to economic activity and the financial system, which is leading to the growth of both public- and private-led commitments to

aligning investments and portfolios with climate targets, as well as increasing disclosure of climate risks. Initiatives such as the FAIRR Initiative¹⁰ benchmark companies across the food system on their climate disclosures and relevant targets (FAIRR, 2020). Further development of this framework could incorporate private-led actions towards

climate-consistency in the AFOLU sector. These could be surveyed on a voluntary basis. Where indicators of private-led action can be designed appropriately, they can also feed into an understanding of effective policy outcomes, given the role of these levers in shifting predominantly private finance flows.

¹⁰ The FAIRR (Farm Animal Investment Risk & Return) Initiative is a collaborative investor network made up of investors with collective assets of over USD 29 trillion that raises awareness of the material ESG risks in animal agriculture.

TABLE 6. An exemplary template for reporting on indicators and their implementation status, ambition and data availability

Measure	Implementation status			Paris alignment			Data availability		
	0	1	2	0	1	2	0	1	2
Financial Policy and Regulation									
Disclosure requirements on climate risks		2		0				1	
Disclosure requirements on climate impacts		.		.				1	
Climate impact analysis principles defined and disclosure templates standardized		.		.				1	
Macroprudential supervision considers climate risks		2		0				.	
Microprudential supervision considers climate risks		2		0				.	
Fiscal Policy									
Carbon Pricing		2		1				2	
Climate misaligned tax incentives and subsidies phase-out plan		.		.				.	
Other activities: CO2 compensation obligation for petrol & diesel importers		2		1				2	
Public budget and spending climate alignment plan		1		2				0	
Sovereign green bonds issuance		0		.				.	
Sub-national entities green bonds issuance		2		1				1	
Public Finance									
Provision of international support		2		1				2	
Public climate finance fund		2		1				1	
Climate bank or public Bank with climate-aligned portfolio, investment and financing activities		.		.				.	
Public export credit agency exclusively supports climate-aligned activities		.		.				1	
State DFI has climate-aligned investment portfolio and focuses on climate-aligned development strategies		1		1				1	
Public pension funds follow climate-aligned investment approach		1		0				1	

Legend

	Implementation status	Paris alignment	Data availability to assess consistency status quo and progress
2	Implemented or to be implemented	In line with scientific 1.5° / <2° scenario or Climate Action Tracker fair-share target	Government-provided data
1	Under discussion by government	Progress in right direction, but not sufficient	Data partially available, high search costs
0	Rejected or disregarded by government	Misaligned without considerable progress towards alignment	Data not publicly available or search costs prohibitively high
.	Measure not yet on governmental agenda	Measure not yet on governmental agenda	Data probably available once measure would be implemented

Source: Bingler et al., 2021.

CHAPTER 4
**Considerations for a
just transition towards
the consistency of
finance flows
in the AFOLU sector**



Economic cost-benefit analyses suggest that the benefits of early climate action outweigh the costs of inaction (OECD, 2017). Yet barriers remain to these actions and to funding the costs of transitioning to low-emission, climate-resilient development pathways. The Paris Agreement embeds the concept of equity in climate action. It recognizes both the historic responsibility for climate change and the respective capabilities of countries to respond to that change (Article 3) along with an obligation for developed countries to provide funding to support developing countries' response efforts (Article 4). Equity is also considered one of two overarching principles of the global stocktake (GST) (UNFCCC, 2015, Article 14). Given the collective nature of the goal of consistency of finance flows with climate objectives and a lack of common understanding on the need to operationalize consistency at the national level, no discussion on when countries must achieve their consistency commitment has been initiated. Nor has a discussion begun on if, or how, this will differ with respect to common-but-differentiated responsibilities.

Countries will face differing challenges and barriers in reaching pathways that are consistent. For example, the financial sector is not as developed in all countries; credit ratings may not be sufficient to access some pools of finance; debt markets may not be deep enough to issue green or forest bonds; or adding more sovereign debt might be unsustainable. Many developing countries have a large informal economy to consider. Small-holder farmers may be excluded from revenue raising or subsidy schemes. The AFOLU sector may be characterised by SMEs that face challenges in financial access. All of these factors would lessen the effectiveness of some government levers towards the operationalization of consistency.

Political economy factors have long challenged efforts to pursue sustainable forest and land use. Daugbjerg and Feindt (2017) highlight domestic land use policy landscapes characterized by high entry barriers and high opposition to policy reform.¹¹ The recent protests in India as a result of agricultural reforms illustrate this well. It is notable that public agricultural support tends to be clustered around a small number of crops important to food security or to the incomes of politically influential groups within society. Three-quarters of total global support goes to just six products: rice, maize, pig, beef, veal and milk (Bellmann, 2019; OECD, 2020b). Aligning finance flows in the AFOLU sector with climate objectives is a complex undertaking that will need to consider sectoral and policy interlinkages – from national to subnational level – that lead to and interact with the political economy.

The IPCC (2019) has also highlighted possible trade-offs between adaptation and mitigation options, as well as the pursuit of climate action versus the pursuit of sustainable development goals. DeBoe (2020) found that long-term rice field abandonment generally reduced GHG emissions and improved water quality but had a negative impact on biodiversity, especially if the land was previously used for livestock production. Any policy supporting land retirement would, therefore, need to combine this with the restoration of native habitats (Searchinger et al., 2020). Policymakers are aiming to achieve a combination of goals with their support of producers with food security a core goal that can be perceived as a trade-off in pursuit of climate outcomes (Bellmann, 2019; World Bank, 2018). At the same time, opportunities exist that can address multiple Sustainable Development Goals and contribute to a just transition: for example, as recently highlighted by the Inter-American Development Bank (IADB) and the International Labour Organisation (ILO), shifting to healthier and more sustainable diets in Latin America would create millions of jobs and simultaneously reduce pressure on the region's unique biodiversity (IADB, 2020).

It is clear that the deep transformations that are required to mitigate and adapt to climate change will create costs and benefits, winners and losers. Reflecting this, both public and private actors are increasingly exploring how socio-economic impacts of low-emission, climate-resilient development pathways on workers and communities can be accounted for and managed. This is often called a 'just transition' (Robins et al., 2018). Principles that seek to ensure an environmentally effective, economically efficient and socially inclusive just transition have emerged (e.g. ILO, 2016; UNFCCC, 2016b), and progressive governments are developing strategic initiatives to guide action. With a vision to transform land use systems by 2030, the Food and Land Use Coalition launched the initiative 'A Just Rural Transition' during the United Nations Climate Action Summit in 2019.¹²

Several developing countries' targets for climate action in the AFOLU sector, predominantly for forestry, are conditional on the receipt of international financial assistance (Brack, 2019). It stands to reason, therefore, that resources committed to supporting developing countries' climate action (under Article 9 of the Paris Agreement) could extend to supporting efforts to operationalize commitments to the consistency of finance flows with low-emission, climate-resilient pathways (Article 2.1(c)).

¹¹ <https://www.bbc.co.uk/news/world-asia-india-55817628>

¹² See: <https://www.foodandlandusecoalition.org/global-initiatives/jrt/>



CHAPTER 5

Conclusion:

**The opportunity of the
global stocktake to
advance green finance
in the AFOLU sector**

This paper demonstrates that four broad government levers are relevant to making finance flows in the AFOLU sector consistent with climate change mitigation and adaptation objectives. State and non-state actors alike can use these four levers to develop a framework for reporting on the climate consistency of finance flows in the AFOLU sector. Constructing this framework would necessitate a systematic and critical look across the various incentives and disincentives that have resulted from policies and regulations. Once built, this framework can help countries understand the role the levers can play in the development of sustainable finance strategies and scenarios and in the better articulation of the AFOLU sector in their respective national climate policies, actions and measures.

The next steps towards climate-consistency of AFOLU finance flows will not be the same in all countries. This framework could be adapted to create relevant, bottom-up indicators of progress. These indicators will need to reflect the role and importance of the AFOLU sector, for example focusing efforts on key commodities, the degree to which the AFOLU sector is relevant to their climate objectives for example leaning to avoided deforestation, as well as their wider economic and market context – and political economy – to develop climate-consistency indicators of progress. Efforts to consider the effectiveness of measures can also be built into the indicators, such as implementation and ambition, with repeated assessment over time supporting progress tracking.

At a global level, the application of this reporting framework will progress global best practice in the pursuit of climate consistency in AFOLU finance flows. The first global stocktake in 2023 is the only space in climate negotiations under which to discuss progress towards the long-term goal of the consistency of finance flows with low-emission, climate-resilient development pathways. To share learning and best-practice, and to build ambition for future climate-consistency milestones and targets, state and non-state actors can use this framework to provide information inputs to the official GST process. Without such a uniting framework, an opportunity could be missed to take stock of collective progress and so to progress the discourse on Article 2.1(c) in the AFOLU sector and more broadly.

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