

## SUBMISSION: ENERGY SECTOR STRATEGY UPDATE

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### Introduction

Recourse welcomes this opportunity to provide input to the Asian Infrastructure Investment Bank's (AIIB's) draft updated Energy Sector Strategy (ESS). [Recourse](#) is a Netherlands-based civil society organisation, working for a world where people and planet are at the heart of development. We campaign to redirect international financial flows away from dirty, harmful investments, towards greener and more inclusive development, working with partners around the world to hold financial institutions accountable.

**Recourse strongly encourages AIIB to fully refresh its ESS to consider a number of advances and commitments in the past two years, in climate science, international commitments and technological innovations** (see box on page 2).

The first iteration of AIIB's ESS, approved in 2017, was a disappointment. Despite AIIB being a post-Paris multilateral development bank (MDB) with a mission to be 'green', and in contrast to other MDBs burdened with decades of unsustainable policies, the ESS lacked restrictions on fossil fuel investments and provided little impetus for borrowers to shift towards low carbon alternatives. The results are telling. For every \$1 AIIB spends on renewable energy options, it spends almost double on fossil fuels.<sup>1</sup>

In October 2021, AIIB announced a new target to become Paris aligned by July 2023. A year earlier it announced a target for 50% of all approved financing to be directed towards climate finance by 2025. Moreover, AIIB shareholders have increased their individual and collective action on climate change, such as the UK's new Export Finance policy, committing the UK not to provide any further support for the fossil fuel energy sector overseas. This commitment also determines the UK's engagement at MDB board level.<sup>2</sup> At COP26, AIIB shareholders representing nearly a quarter of AIIB's voting power committed to end direct international public finance for unabated coal, oil, and gas by the end of 2022 and to prioritise clean energy finance.<sup>3</sup> Other MDBs have also raised the bar by strengthening their policies, including the ADB's exclusion of financing for coal power in its new Energy Policy (however, not for other fossil fuels, such as gas).<sup>4</sup>

In this submission, Recourse provides a summary overview of key concerns followed by further recommendations on how to strengthen the strategy and raise its ambition. We call on AIIB to play a leadership role in shifting the trajectory towards a more sustainable path, building on efforts to align with the Paris Agreement and its 1.5°C aspiration, by ensuring the revised ESS is fossil free and climate proof, and in line with the Sustainable Development Goals (SDGs).

## The urgency of 1.5°C and net zero commitments

In the past two years there has been an enhanced international focus on keeping global temperature rise under 1.5°C, in line with the Intergovernmental Panel on Climate Change (IPCC) internationally endorsed special report on 1.5°C.

- The IPCC 6<sup>th</sup> Annual Assessment, agreed between 195 member countries, raised the threat of catastrophic impacts of climate change in coming decades further, if rapid decarbonisation does not take place, in particular in the energy sector: “limiting warming to around 1.5°C (2.7°F) requires global greenhouse gas emissions to peak before 2025 at the latest, and be reduced by 43% by 2030” and to achieve “net zero carbon dioxide emissions globally in the early 2050s”. This leaves no room for emissions growth.
- The report was fully endorsed at the United Nations Framework Convention on Climate Change (UNFCCC) Conference of Parties (COP) 26 in 2021. The Glasgow Climate Pact, a decision of parties to the Paris climate agreement, states that it “resolves to pursue efforts to limit the temperature increase to 1.5°C.”
- In response to the science and growing international support for net zero emissions, the International Energy Agency (IEA) stated: “The path to net-zero emissions is narrow: staying on it requires immediate and massive deployment of all available clean and efficient energy technologies.”
- According to IEA: “Net zero means a huge decline in the use of fossil fuels ... Beyond projects already committed as of 2021, there are no new oil and gas fields approved for development in our [net zero] pathway, and no new coal mines or mine extensions are required”.
- In the past two years many countries have enhanced their Nationally Determined Contributions (NDCs) under the Paris Agreement and set Long Term Strategies (LTs) for net zero by mid-century. These commitments, if fully implemented, will still take the world to about 2.7°C of warming and many low-income countries need funding to deliver their commitments. These at a minimum should set the basis for energy investment by Multilateral Development Banks (MDBs), and it is essential that the NDC commitment period to 2030 prepares the ground for rapid low-carbon development in the 2040s, not locking in high carbon infrastructure which could hinder net zero targets.
- Further technological advances are not only making the price of renewable energy technology competitive with the fossil fuel alternatives, the advances in storage and energy management are making them increasingly viable as the major viable source of energy. According to the IPCC’s Working Group III report on mitigation (2022): “From 2010–2019, there have been sustained decreases in the unit costs of solar energy (85%), wind energy (55%), and lithium-ion batteries (85%).” In line with IEA, it argues that clean energy investments must triple to limit the global temperature rise to 1.5°C.

References: <https://www.ipcc.ch/2022/04/04/ipcc-ar6-wgiii-pressrelease/>,  
[https://unfccc.int/sites/default/files/resource/cop26\\_auv\\_2f\\_cover\\_decision.pdf](https://unfccc.int/sites/default/files/resource/cop26_auv_2f_cover_decision.pdf),  
<https://www.unep.org/resources/emissions-gap-report-2021>,  
<https://www.ipcc.ch/report/ar6/wg3/>

## Summary of key concerns

### Downplaying the climate threat

To be Paris compliant AIIB should include Paris climate trajectories, put targets in place to ensure the scale of transition is sufficient, avoid lock-in beyond 2030 to high carbon fossil fuel infrastructure (including gas), and commit to a pro-active scale up of renewable energy and energy efficiency. It is concerning that despite AIIB's commitment to the Paris Agreement, the scale of the threat posed by climate change is downplayed throughout the draft ESS. For example, in the first paragraph of the section, Global Energy Landscape (para 6), climate change is mentioned last and with reference to "global commitments to climate change", rather than highlighting the significant risks in continuing 'business as usual'. Climate change is not discussed in its own right until the last paragraph in this section (para 10). This para refers to the energy sector as "the largest contributor to anthropogenic climate change", however, this message should be front and centre – not left in the periphery. Moreover, the ESS refers to the Paris Agreement 2°C target (para 20, 43), again underplaying the urgency of addressing climate change and despite the growing consensus on 1.5°C as a priority goal, including by all parties to the 'Glasgow Climate Change Pact' at COP26 (see box on page 2).

### Continued emphasis on fossil gas

The ESS should include a clear plan for transition out of all fossil fuels, moving from lock in to phase out, coupled with clear trajectories and time frames (in line with the Paris Agreement and the Glasgow Pact). The draft updated ESS commits to some positive steps; significantly AIIB's long-anticipated exclusion of funding for coal power. Yet, fossil fuels still feature strongly in the draft, sending mixed signals about AIIB's priorities. Significantly, the draft puts a strong emphasis on gas as a transition fuel with few restrictions, leaving giant loopholes for unabated support for gas to continue. Meanwhile, references to renewable energy are weak and often associated with outdated assumptions. Overall, the draft lacks ambition and targets, including few meaningful changes to the Results Monitoring Framework, also undermining accountability.

### Supply focus undermines attention to energy access and efficiency benefits

The ESS starts with a discussion of energy access and energy services delivery, however, overall it is focused on power and fuel supply and demand. Instead of a supply driven approach, the ESS should focus on supporting countries across the energy system, ensuring the energy services and sectors are provided with the service they need. This approach would mean working with sectors and stakeholders to deliver the energy service in the most effective and efficient way, managing energy demand and improving overall economic and development results. This also allows for the energy supply to be matched more effectively to the service required, including off-grid and mini-grid renewable energy systems. Sectoral economies of scale can ensure financial efficiency is built in.

### Adaptation cut from new draft

Wording in the 2017 ESS to support adaptation projects is absent in the new draft ESS, despite commitments in the recently updated Environmental and Social Framework (ESF) for clients to assess proposed projects with respect to climate change mitigation and adaptation. This commitment is referenced in para 56, yet the examples are solely focused on mitigation, despite the importance of adaptation in reducing vulnerability to climate change impacts. Energy access and

sustainable renewable energy, including distributed renewable energy, are important parts of adaptive measures. This dropping of any mention of adaptation sends troubling signals.<sup>5</sup>

#### Lacking international focus

The draft ESS sends mixed message regarding AIIB's priorities as an increasingly international MDB. It focuses on analysis and experiences from Asia throughout, yet AIIB's international footprint has grown significantly in recent years, including new members and projects in MENA, Sub-Saharan Africa, Europe/Eurasia and most recently in Latin America. It is concerning that the analysis does not include any references to this growing proportion of AIIB's portfolio and membership.

#### No Climate Change Action Plan undermines systemic approach

AIIB has to date rejected calls for an institutional Climate Change Action Plan, which could introduce a systemic approach to addressing climate change, including through the energy sector. The World Bank Climate Change Action Plan takes a systemic approach including, for example, a commitment to increase support to cities, including to "decarbonise urban energy systems"<sup>6</sup> A Climate Change Action Plan would also provide a dedicated space to outline AIIB's Paris alignment priorities, pathways and targets.

#### Robust consultation needed to build an effective energy strategy

Finally, this submission should be read in conjunction with other inputs, in particular from civil society and indigenous peoples' organisations in borrowing countries. We would further like to reiterate our disappointment with the consultation's weak format, including lack of timely outreach in Asia and beyond and the fact that it was conducted solely in English. These concerns were outlined in a letter to AIIB signed by almost 60 organisations.<sup>7</sup> Recourse and partners repeatedly raised these issues verbally and in correspondence with AIIB and shareholders in advance of the consultation launch, yet our calls for best practice went unheard. The CSO letter also called for AIIB to make available the CEIU's Early Learning Assessment of energy projects and other background documentation. There are several references to "lessons learned" throughout the document, but without any further qualification or authoritative references. The majority of CSOs' concerns were not addressed by AIIB. We strongly encourage all of these points to be rectified as a matter of urgency.

## Analysis – 10 Essentials for AIIB’s new Energy Strategy

In anticipation of the ESS review, Recourse together with NGO Forum on ADB and the Big Shift Global coalition released a short brief outlining ten essentials for the revised strategy. In this submission, we elaborate on these ‘essentials’, by updating priorities based on the ESS draft, providing further context and more detailed recommendations.

1. [STOP FUNDING COAL](#)
2. [IMMEDIATELY START PHASING OUT SUPPORT FOR OIL AND GAS](#)
3. [CLOSE FOSSIL FUEL LOOPHOLES](#)
4. [RAMP UP SUPPORT FOR SUSTAINABLE RENEWABLES](#)
5. [PRIORITISE ENERGY ACCESS FOR ALL](#)
6. [NO FALSE SOLUTIONS](#)
7. [PUT GENDER EQUALITY FRONT AND CENTRE](#)
8. [ENSURE A RIGHTS-BASED APPROACH AND MEANINGFUL PARTICIPATION](#)
9. [SUPPORT A JUST TRANSITION](#)
10. [SET AMBITIOUS, TRANSPARENT AND ACCOUNTABLE TARGETS](#)

### 1) EXTEND COAL POWER BAN TO ALL USES OF COAL

*“Fossil fuels are a dead end – environmentally and economically. The only sustainable future is a renewable one. The good news is that the lifeline is right in front of us. Wind and solar are readily available and, in most cases, cheaper than coal and other fossil fuels. If we act together, the renewable energy transformation can be the peace project of the 21st century.”*

*António Guterres, UN Secretary General, May 2022<sup>1</sup>*

Ever since the 2017 approval of the ESS, leaving AIIB open to funding all types of fossil fuels, AIIB’s President has repeatedly emphasised that AIIB will not finance coal in practice.<sup>8</sup> Recourse therefore welcome that, in line with the President’s verbal commitments, the updated ESS confirms that “AIIB will not finance new coal-fired power and heating plants or projects that are functionally related to coal” and further clarifies that this means “associated facilities enabling coal use such as roads or transmission lines serving coal-based facilities directly and materially, or industrial plants drawing their energy from dedicated coal-based facilities” (para 47).

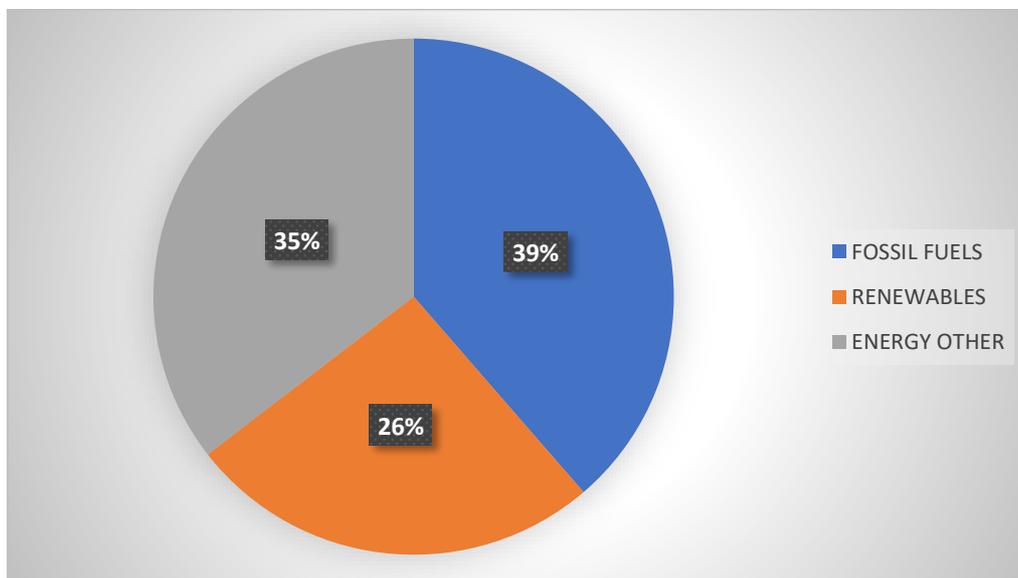
The reference to exclusion of coal fuelled industrial plants is particularly welcome. This is aligned with ADB, which while not specifying industrial plants does not mention any limitations related to its ban on support for coal-fired power generation. ADB also commits to support decarbonisation of industrial processes. According to the IPCC, GHG emissions derived from industrial processes, such as steel and cement, accounted for over a fifth of direct global GHG emissions in 2010 and is growing.<sup>9</sup> Alternative methods are increasingly available and it is important that public finance supports, and does not undermine, these efforts.<sup>10</sup> AIIB, however, stops short of excluding industrial use of coal for other purposes than captive power. For example, in 2017, AIIB made a \$150m equity investment in IFC Emerging Asia Fund, which in turn invested \$20m in Shwe Taung Cement in Myanmar for expansion of a cement plant.<sup>11</sup> Coal is used in the production process, which would still be allowed under the revised ESS.

The shift from coal power and other fossil fuels to clean energy will require clear plans for just transition (see point 9) and investment in companies looking to develop processes which use renewable energy alternatives. It should not allow loopholes for speculative carbon capture use and storage (CCUS) - an unproven and costly option which would hinder the development of sustainable energy systems. See section 6 below.

**RECOMMENDATIONS:**

- ⇒ The ESS coal exclusion should explicitly cover all forms of AIIB support, both direct and indirect, including financing through financial intermediaries. For example, the EIB’s Energy Policy says: “this policy applies not only to direct investment loans but also to all intermediated operations of the Bank, including those carried out through commercial banks and investment funds.”<sup>12</sup> It should also exclude support for transmission and distribution lines serving coal power plants.
- ⇒ AIIB should clarify and strengthen its position in the ESS on exclusion of coal and phasing out of industrial use of fossil fuels, including a commitment to support development of sustainable renewable energy alternatives that are not relying on unproven and costly technologies. For example, EIB commits to “intensify its continuing efforts to support accelerated investment in areas that require large volumes of long term and low-cost capital – including ... deployment of low carbon technologies by industry.”<sup>13</sup>

**AIIB’s energy portfolio, end June 2022**



Source: [AIIB project data](#)

## 2) IMMEDIATELY START PHASING OUT SUPPORT FOR OIL AND GAS

*“If we build out a huge infrastructure for gas now and continue to use it as the bridge fuel, when we haven’t really exhausted the other possibilities, we’re gonna be stuck with stranded assets in 10 or 20 or 30 years”*

*John Kerry, US Presidential Climate Envoy, 2021*

To date, AIIB has invested over \$2 billion in gas projects, excluding indirect finance. Recourse welcomes a commitment to not finance upstream activities “because of their risk of long-term carbon lock-in”. However, the ramped up narrative on support for mid-stream and downstream gas is disappointing, including a misleading narrative on the future of gas and its role as a so-called ‘transition fuel’ and that gas is needed to create a baseload for renewable energy technology to enter the grid. Both assumptions are now outdated. AIIB again places itself behind the curve and goes counter to a growing body of evidence of what is needed to counter climate change.

For example, the ESS claims that “The increased use of natural gas instead of oil and coal has helped many developed economies reduce carbon emissions and air pollution” (para 49), neglecting to acknowledge that gas is in fact driving the rise in carbon emissions<sup>14</sup> and locks in emissions for decades to come. Further, the draft ESS claims that “it is expected that natural gas will also play an essential role in the transition strategies for many developing countries in the region”. Moreover, the draft refers to gas as important for “energy security” in several places (para 19, 23, 49), disregarding the impact of the war in Ukraine on Liquefied Natural Gas (LNG) supply which demonstrates that importing gas and LNG reliance has significantly increased energy insecurity, and caused extreme price volatility and supply problems.

Further support for gas directly conflicts with IEA’s 1.5°C net-zero pathway, under which unabated fossil gas-fired generation must peak by 2030 and be 90% lower by 2040, compared to 2020 levels.<sup>15</sup> Research by IISD reveals that in most countries and cases the majority of gas consumption is associated with uses that already have cost-competitive clean alternatives.<sup>16</sup> So gas is not a ‘transition fuel’ - it has become a blocker for the shift to renewables. The continued support for gas, including LNG, is not only locking countries into a high-carbon and polluting energy model, but it also drains investments that could be used for a renewable energy transformation. The process of creating and regasifying LNG is particularly energy intensive and is driving growth in emissions. In fact, gas, rather than coal, is the main driver of the global increase in CO2 emissions since 2013.<sup>17</sup>

The draft ESS introduces some cautions in paragraph 49-50, referencing that “the transitional role of gas will evolve over time” and thus must be assessed in the context of the Paris Agreement. AIIB will therefore focus on “members’ energy and climate objectives and decarbonisation trajectories.” However, the restrictions introduced here are full of loopholes and unlikely to help borrowers shift their priorities away from fossil fuels. The ESS references several ways AIIB is prepared to support fossil gas, including “mid-stream infrastructure (LNG terminals, storage, and transmission pipelines), natural gas-fired power generation and downstream (distribution and end-use) facilities”, with the condition that the investments are “credibly replacing higher carbon fuels, inefficient technologies, or oil- and coal-fired energy facilities”. But there is no clear explanation on how “credible” will be

assessed, apart from AIIB committing to “consider each member’s LTS, NDC, and other such plans and scenarios”. It is also essential not just to deliver the NDC targets by 2030, but to ensure that investments in the 2020s set up for effective and rapid emissions decline in the 2040s.

Studies have illustrated how methane and CO2 emissions from existing gas infrastructure alone are compromising the climate goals.<sup>18</sup> Moreover, planned gas projects are likely to become unbankable. A recent report by the German Government’s Clean Affordable and Secure Energy for Southeast Asia (CASE) project confirms these concerns: “Switching from coal to gas brings additional complexities and new economic risks, especially due to potential lock-in. ... As the world decarbonises, some of today’s investments in gas infrastructure are likely to become stranded assets.”<sup>19</sup> The CASE report further explains that comparisons to the US and Europe are unhelpful, since the gas networks were built in a different context: “Given the urgency of climate constraints, the falling cost of renewables and energy storage, and the centrality of flexible generation in the electricity sector, developing a similar network ... could expose regional economies to a number of risks.”<sup>20</sup> It warns that continuing to invest in gas infrastructure “could crowd out renewable energy from future investment portfolios.”<sup>21</sup>

This heavy bias towards gas is already present in AIIB’s portfolio. For example, a 2019 report by Recourse, CLEAN and NGO Forum on ADB analysed the first four AIIB projects in Bangladesh, all in the energy sector, including a greenfield gas power plant. But despite Bangladesh being an extremely climate vulnerable country none of the projects supported renewable energy.<sup>22</sup> This stands till today, including a new greenfield gas power plant in the project pipeline, Unique Meghnaghat.<sup>23</sup>

### **The trouble with gas**

It is now widely accepted that gas cannot be considered a ‘transition’ fuel to cleaner energy systems, but rather another carbon intensive high emitting fossil fuel, similar to coal, potentially diverting funds to cleaner renewable alternatives. Therefore, plans to expand gas infrastructure pose one of the greatest threats to meeting the goals of the Paris Agreement and averting the most catastrophic impacts of the climate crisis. Fossil gas is harmful because:

- There is significant leakage of methane from the processing, transport, regasification and consumption of gas. Methane is 83 to 86 times stronger over 20 years than carbon dioxide (CO2) as a greenhouse gas.
- Fossil gas affects air quality and hazardous air pollutants have harmful effects on health and the environment.
- Fossil gas infrastructure, including pipelines, leaks harmful chemicals into the environment and water supplies.

References: <https://www.iisd.org/articles/gas-bridge-fuel>;  
<https://www.ucsusa.org/resources/environmental-impacts-natural-gas>

Other IFIs are increasingly taking a stricter approach to gas. For example, the EIB committed to ending support for unabated fossil fuels, including gas, by end of 2021.<sup>24</sup> Other restrictions include:

- “(a) a stronger climate test that requires showing alternatives to gas are not *viable* rather than just more expensive (e.g. UK and FMO, the Dutch development bank)<sup>25</sup>
- (b) strict emissions standards (e.g. EIB has a power generation standard for all projects of less than 250 grammes of CO2 per kilowatt-hour<sup>26</sup>), and/or
- (c) a shadow cost of carbon aligned with the upper end of the High-Level Commission on Carbon Prices (e.g. EIB currently employs a shadow cost of carbon of €80, set to rise rapidly<sup>27</sup>).”<sup>28</sup>

#### **RECOMMENDATIONS:**

- ⇒ AIIB should commit to phasing out support for gas and LNG by end of 2022, in line with the Glasgow Statement and G7 commitments. This should include direct and indirect financing, such as financing through financial intermediaries.
- ⇒ There should be a total ban on any gas or oil developments, including pipelines and import/export terminals, because these will lock in high emissions beyond the 2025 ‘emissions peak’ after which rapid carbon emissions reductions will be needed towards net zero.
- ⇒ The phase out should extend to midstream and downstream gas financing and support, as well as associated facilities.

### 3) CLOSE FOSSIL FUEL LOOPHOLES

Investing through financial intermediaries (FIs) is an important and growing portion of AIIB’s overall portfolio (at approximately one quarter of projects). AIIB also uses FIs as a vehicle for support to the energy sector. The ESS being explicit that it applies both to direct and indirect financing has several advantages. It simplifies matters for AIIB’s investment officers, makes AIIB’s expectations clear to stakeholders, and avoids creating unintended loopholes that allow projects to be financed indirectly that AIIB would not usually support directly. An example is the Shwe Taung Cement project in Myanmar, funded by AIIB through the IFC Emerging Asia Fund, which required increased extraction from a coal mine, tripling its output.<sup>29</sup>

ADB recently fulfilled this recommendation in its revised 2021 Energy Policy: “This proposed policy applies to all of ADB’s sovereign and non- sovereign operations, including project loans, sector loans, policy-based loans, results-based loans, financial intermediary loans, equity participation, and technical assistance.”<sup>30</sup>

AIIB has made significant changes to its requirements for FI lending in its updated ESF, including welcome improvements to the degree of disclosure of sub-projects funded via intermediaries. It is important that this strong commitment to transparency is repeated in the ESS, to underline AIIB’s commitment to being accountable for its energy sector commitments.

The potential benefits of using FIs to bundle together smaller energy access or clean energy projects, or to achieve portfolio-level shifts in client financing from fossil fuels to clean, are significant.<sup>31</sup> We welcome new language in the ESS that highlights the potential of FIs in “directing additional financial resources particularly to sub sectors needing smaller scale financing” (para 23). At the same time, the risks of FI lending, which Recourse has explored in publications such as [Risky Venture: The AIIB’s hands of approach to funding infrastructure in India](#) or [Do no harm: New recommendations for AIIB’s ESF review](#), should be acknowledged in this ESS, following important reforms to the ESF.

However, while investing in FIs can help to mobilise funds and attract private capital for economic development, this form of third-party or ‘hands-off’ lending also comes with significant risks. The ESS does not address the risk that some of AIIB’s FI financing may pave the way for fossil fuel expansion. For instance, AIIB recently approved \$200 million loan to Infrastructure Development Co. Ltd. (IDCOL) in Bangladesh, a public aggregators with a significant track record in supporting small-scale renewable energy projects, such as rooftop solar. But it has also supported gas and this investment may end up backing two gas power plants (Unique Meghnaghat and FeniPower) under IDCOL’s project pipeline, which could lock in emissions for up to 30 years.<sup>32</sup>

Other risks refer to clients’ adherence to E&S safeguards. In recent years, IFC - whose FI investment portfolio is over 50 per cent of - has been forced to acknowledge these risks and has taken some steps to address them. Following critical findings from both IFC’s own watchdog, and from civil society groups, IFC has reduced high-risk lending through FIs, no longer provides general-purpose loans, and has developed a ‘Green Equity Approach’ to help to transform not only its own lending but that of its FI equity clients, to phase out coal to zero by 2030.

The ESS review is also a timely opportunity for AIIB to chart a path to Paris alignment for its indirect lending portfolio. AIIB is a member of the Joint MDB Working Group on Paris Alignment, which produced an overarching framework for development finance institutions (DFIs) to align their indirect financing – leaving it up to individual DFIs to customise how they will adopt the framework in their contexts. AIIB should use the opportunity of the ESS review to signal how it will take advantage of the potential benefits of FI investing to catalyse a shift from dirty to clean energy, while defining how it will avoid the significant risks.

In 2019, AIIB began to invest in capital markets projects, aimed at attracting institutional investors to finance infrastructure development in Asia. These operations delegate portfolios to a third-party asset manager, which makes decisions about investments in securities traded through capital markets. The draft ESS states: “The provisions of the ESF, as updated in 2021, will continue to guide implementation of the Strategy” (para 55). However, the ESF does not apply to capital market projects. Rather than applying AIIB’s Environmental and Social Framework, these projects use ‘ESG Frameworks’ to guide their investments. They are also not subject to the AIIB’s standard disclosure policies and it has declined to provide any information on the contents of the project portfolios. This represents a blind spot in the draft ESS. As with standard FI investments, it is vital that the terms of the new ESS apply to capital market projects in order to guarantee AIIB funds do not end up indirectly supporting fossil fuel projects it would not support directly.

## RECOMMENDATIONS:

- ⇒ The ESS must explicitly state that its requirements apply BOTH to direct and indirect finance, including financial intermediary investing and capital markets projects, to ensure coherence and deliver economy-wide commitment to the Paris aligned goals.
- ⇒ The ESS must explicitly commit AIIB to publishing the name, sector and location of all high and medium risk projects it supports through FIs, to enable public tracking and assessment of AIIB's fossil fuel commitments.
- ⇒ The ESS should commit FIs to track their contribution towards delivering Paris aligned investments, including support for NDCs.
- ⇒ The ESS should be explicit that its support for aggregators will aim to invest in renewable energy projects, rather than financing fossil fuel expansion, such as fossil gas.

As noted, there has been significant improvement in terms of the requirements applied by AIIB to its FI clients in recent years. In both policy (the revised ESF) and practice (individual projects), AIIB has taken important steps to minimise risk and increase the beneficial impacts of its investing through FIs.

For the last two years or so, AIIB has begun to be explicit in contracts with FI clients about which type of sub projects it will and won't support, especially in terms of energy-related investments. For example, AIIB's 2021 \$150 million investment in GIP emerging markets fund 1 specifies that "Coal mining, coal transportation and coal-fired power plants, as well as infrastructure exclusively dedicated to support any of these activities will be excluded from eligibility for financing under the Project." The same investment also rules out "portfolio companies' Category A or high-risk Category B subprojects."<sup>33</sup> In the same year, AIIB invested \$100 million equity in Keppel Pierfront, stipulating that its private credit fund must "avoid high risk projects which may have, (i) significant adverse impacts to community health and safety as a result of construction/operation of the assets, (ii) significant number of serious injuries and/or fatal accidents during construction and/or operation of the assets, (iii) involuntary resettlement of people and (iv) impacts on critical habitat, Indigenous Peoples and cultural resources. These sensitive activities are either to be avoided or managed in accordance with AIIB's ESP, including applicable ESSs. The Fund shall not invest in coal-related activities."<sup>34</sup>

AIIB's \$100 million support to TCB Bank in Georgia in 2021 goes yet further, excluding not only "all Category A sub-projects and Category B sub-projects inducing higher environmental and social ("ES") risks" and coal projects, but also stipulating that "large dams will also be excluded".<sup>35</sup> The newly-proposed Everbright Infrastructure Investment Fund stipulates that, as well as coal, "gas-related subprojects will also be excluded."<sup>36</sup>

Since greenfield gas projects are regarded by AIIB as either Category A (Sirdarya 1,500MW CGGT power plant in Uzbekistan for example)<sup>37</sup> or Category B (Bhola IPP in Bangladesh)<sup>38</sup>, exclusions of Cat A and higher risk Cat B projects in numerous recent FI investments have de facto ensured that AIIB does not finance fossil fuels through intermediaries. This ad hoc approach should be codified in the ESS, to ensure a uniform application across FI investments.

The ESS should also go further in promoting the potential of FI investments to have a transformational effect on clients in terms of shifting private finance out of fossil fuels and towards clean energy. One example is AIIB's investment in the IFC's Emerging Asia Fund, which in 2021 took a stake in India's Federal Bank. As a result of the IFC's Green Equity Approach, this equity investment resulted in Federal Bank – till now, one of the most important financiers of coal in India – committing to exclude all coal projects in future.<sup>39</sup> This catalytic potential to effect transformative shifts in FI clients should be highlighted in the new ESS, especially given such leverage will be key to ensuring AIIB succeeds in aligning both its direct and indirect investments with the goals of the Paris Agreement on Climate Change. It is vital that exclusions and targets be included in contracts between AIIB's FI clients and sub project developers or financiers, to ensure that commitments reach down to project level.

#### RECOMMENDATIONS:

- ⇒ The ESS should clarify that FI clients lending to the energy sector should exclude all high risk lending (Cat A and B subprojects), which would de facto cover coal, gas, oil and large-scale hydropower projects. Such commitments must be enshrined in contracts between AIIB's FI clients and sub project developers or financiers.
- ⇒ The ESS should detail how AIIB will use FI lending to effect transformation among its FI clients, to help shift private financial flows out of dirty, polluting fossil fuels and into sustainable renewable energy.

#### 4) RAMP UP SUPPORT FOR SUSTAINABLE RENEWABLES

*"If we had invested much more seriously in the last 10, 20 years in renewable energy, we would not be dependent on the permanent fluctuations in the markets in relation to fossil fuels. The fact that countries have not enough renewable energy, which is based on self-reliance, makes them much more dependent on markets, and markets have always been extremely volatile."*

*António Guterres, UN Secretary General, April 2022<sup>40</sup>*

According to the International Energy Agency, "renewables are set to become the foundation of electricity systems around the world."<sup>41</sup> As fossil fuel investment declines, the investment in a renewable future should increase to match and give countries confidence in moving to a sustainable renewable energy economy.

The draft ESS rightly acknowledges that "achieving a smooth and just energy transition will require significant efforts to redirect capital flows toward clean and sustainable energy investment", including "investments in the electricity infrastructure" (para 20), also noting "the sharp fall in the cost of renewable energy" (para 9). Moreover, the draft recognises that the domestic nature of renewable energy makes it "less exposed to global risks" (para 19). The war in Ukraine has led to extreme and volatile global fuel pricing trends and supply failures. This has made fossil fuel supply unstable and has rendered energy and economic planning for most countries extremely challenging, driving them further into debt and energy insecurity. A move to sustainable, renewable energy

systems, such as wind and solar, would improve energy security and remove supply uncertainty and price volatility. For example, Sustainable Energy For All (SEforALL) concluded that renewable energy fared better during the Covid-19 pandemic, proving “flexible, cost-effective, and resilient in the face of the 2020 health and economic crisis.”<sup>42</sup>

Despite these and many other references to the importance of the big shift towards renewable energy, the draft fails to draw obvious conclusions for AIIB’s role and how it could play a key part in the transition to renewable energy. This lack of leadership is evident in AIIB’s current energy portfolio. The draft points to the size of the energy portfolio (though erroneously claims that the figure includes FI lending), but fails to acknowledge that almost half of this is exclusively for fossil fuel, renewable energy representing just a quarter. This proportion has grown in recent years, yet despite commitments to increase climate finance and be Paris aligned it is still far from a priority. This is unacceptable for a post Paris Agreement bank, which should aim to scale down fossil investment dramatically and put commensurate investments into a renewable energy and energy efficient economy.

Support should focus on sustainable renewable options, that avoid harm to people and the environment. While solar and wind power are considered the most sustainable renewable options, large scale developments will have to be reviewed for environmental sustainability and be subject to local consultation. Large hydro power and industrial scale biofuels are not considered as sustainable renewable energy due to their huge impact on land, nature and people, including displacing food production (see section 6). It is essential that renewable energy technology be compliant with the stringent social and environmental scrutiny that should be applied to all MDB investments.

Overall, the draft ESS takes an extremely cautious approach towards renewables, building on largely outdated arguments. For example, in para 20 it outlines a number of ‘risks’ (largely based on outdated claims), claiming that these “warrant the need for transition fuels that can quickly lower the carbon intensity of energy supply” – rather than seeing an opportunity for AIIB to fill the void with increased investment in renewables that could move the agenda forward.

One caution is that “variable renewable energy plants do not supply a consistent flow of electricity the way conventional energy sources do and require other types of resources to balance generation” (para 19). This is a common argument focusing on the necessity of fossil fuels as key providers of so called baseload energy. However, this argument is no longer valid with current technology, with research showing that all countries have the capacity to move to 100% renewable energy grids, with ten countries already running electric grids without fossil fuel or nuclear power<sup>43</sup>. Research by Agora Energiewende and CASE shows how variable renewables can form the core of a flexible system, with “generators, storage and demand-sectors that can rapidly adjust operations according to system needs [and] maintain system stability and reliability.” MDBs like AIIB could play a key part in financing this shift, including to support “modern and interconnected transmission and distribution grids [to] widen the area in which resources are shared.”<sup>44</sup>

Previously fossil fuel dependent countries are moving to decarbonising the power sector (by 2035 in the UK)<sup>45</sup> as the power sector has the greatest possibility to go zero carbon quickly given current technology. This will allow time for research and development in other sectors which are harder to

decarbonise, but will have to become net zero by 2050. According to the IEA: “Clean electrification is the dominant theme in the early phases of the transformation of the global energy economy together with the quest for improvements in efficiency. Over time, however, continued rapid deployment in these areas needs to be accompanied by clean energy innovation and the widespread use of technologies that are not yet readily available on the market.”<sup>46</sup>

Moreover, taking a sectoral approach (as opposed to an energy supply model) to delivering energy services will allow for much greater opportunity to address and manage the whole energy system, to optimise efficiency of sectors, manage energy demand and develop the most effective energy solutions, including on and off grid, passive heating and cooling and service delivery alternatives. City or sector scale (including transport, industry, public services or household) can provide the economy of scale to implement such an approach. IEA World Energy Outlook calls this the “new energy economy”.<sup>47</sup>

The section on Power T&D recognises that “substantial investments” are required to achieve SDG7 and “allow for smooth renewable energy integration into power systems”. This recognition is welcome and should be a priority to support the big shift towards making renewable energy accessible on a large scale. Strong collaboration is needed to build renewable powered grids, such as the Renewable Grids Initiative in Europe, which recognises grid development as an essential precondition for substantive renewable energy integration from both decentralised and utility scale installations. This challenge is met with an “energy transition ecosystem-of-actors” in order to promote fair, transparent, sustainable grid development to enable the growth of renewables to achieve full decarbonisation in line with the Paris Agreement.<sup>48</sup> Yet, nowhere is this element further developed in the draft ESS to provide clear incentives, instead other mentions of T&D references gas specifically (para 19, 34). The RMF indicator is only focused on km of lines and pipelines, again missing the opportunity of directing financing specifically towards renewable energy.

#### **RECOMMENDATIONS:**

- ⇒ The ESS must provide clear incentives for sustainable renewable energy and energy efficiency support, building on latest science and economic analysis, including support for distributed renewable energy
- ⇒ The ESS should adopt effective sectoral approaches for innovations in energy service provision and managing energy systems for sectors such as cities, housing, transport and industry.
- ⇒ The AIIB should provide innovation funding to accelerate infrastructure to maximise renewable energy uptake and to stabilise a grid for higher renewable uptake, including grid and demand management, and energy storage.
- ⇒ The ESS should include targets for renewable energy and energy efficiency to deliver SDG7 and the Paris agreement should be included the RMF, and drive increasing investment across all financing mechanisms, including direct and indirect finance.

## 5) PRIORITISE ENERGY ACCESS FOR ALL

*“Continued reliance on fossil fuels means forgoing the economic opportunity of localised, renewable energy systems, which create jobs and boost developing countries’ GDP ... Financing of fossil fuel projects as a means of closing the energy access gap should be terminated.”*

Sustainable Energy for All, 2020

Access to energy continues to be a challenge for communities around the world. Globally, almost 800 million people lack electricity and 2.8 billion need clean cooking solutions, figures that are likely to increase due to the impacts of the Covid-19 pandemic.<sup>49</sup> It is therefore welcome that the draft ESS identifies SDG 7 as a priority, recognising that globally progress “falls far short of the pace required to achieve universal energy access to affordable and reliable modern energy services by 2030” (para 7). It includes other welcome elements, such as reference to affordability, quality and safety (para 32).

Public financing can and should play an important role in supporting SDG 7. The revised ESS must set out a plan with ambitious targets and timelines for actioning SDG 7 on universal access to affordable, reliable, sustainable, and modern energy, which should include efforts to reach the “last-mile” households. This support should not come through fossil fuels, but through clean sustainable renewable solutions, while ensuring gender equality and a rights based approach.

Directing finance towards energy access, clean cooking and decentralised energy systems may be challenging for multilateral investors, but it is an essential remit for delivery of the SDGs and should be a marker for success. Overcoming the scourge of energy poverty should be a central driver of AIIB’s energy strategy, requiring clear targets for delivering energy access and clean cooking, which will drive more innovative financing mechanisms.

Business as usual approaches to electricity access, focussed on generation, transmission and distribution investments in centralised grids, are not connecting enough people fast enough to reach SDG 7. For electricity-poor households and communities living in rural areas, far from the grid, distributed stand-alone and mini-grid solutions powered by renewables such as wind and solar PV can be deployed more quickly and are the most viable and affordable option for connecting most new households. These distributed solutions powered by renewable energy (DRE) could connect 51% of energy poor people by 2030 and 77% in rural areas.<sup>50</sup>

The draft identifies “decentralised generation and mini- and micro grids” as a priority (para 45). This is welcome, however, this commitment was made already in the 2017 iteration of the ESS without any impact on AIIB’s project portfolio. One reason for this is the lack of targets. This mistake is again repeated in the draft ESS. Concerningly, the draft downplays AIIB’s role in supporting last-mile electrification and “basic human needs” (para 32) – thus diverting from the core of SDG 7 to secure energy access for all.<sup>51</sup> Instead, the draft points to the need to “meet the standards required by sophisticated equipment and the connectivity needs of households and businesses” (para 14), with Principle 2 focusing on “higher service levels of access” instead. This is also replicated in the draft RMF, which has added improved access to energy to the earlier language on increased access. While

an important aspect, basic needs and last mile access must come first. SEforALL's 2020 analysis found that finance for grid-connected renewables and for mini-grids and off-grid solutions remained low, undermining progress on "gender equality, economic opportunity, climate change, and protection of land and forests." Public finance could play an important role here.

Clean cooking is the most neglected but highly urgent part of the energy sector and the delivery of SDG7. The number of families who cook on dirty, polluting fuels such as wood, dung and charcoal remain stubbornly high and over 2.7 million, and 3.4 million people die prematurely because of indoor air pollution predominantly from these cookstoves.<sup>52</sup> But cooking solutions receive by far the least investment, with only about 1.6 of MDB energy finance invested in clean cooking.<sup>53</sup> MDBs need to find a way to invest in clean cooking solutions for a fossil free world, and ensure these solutions are accessible and affordable to the most vulnerable families.

It is also deeply concerning that the draft leaves the door open to address energy access by supporting fossil fuels, including coal: "AIIB may support investments in and efficiency improvements of power and heat distribution networks to improve energy access irrespective of the supply-side energy mix" (para 47). This is a risky strategy that runs counter to the goals of the Paris Agreement. A review of 27 countries in Africa and Asia by SEforALL found that much of the increase in commitments to fund universal energy access was for fossil fuel technologies "which will lock those [countries] into decades of carbon emissions and dependence on imported coal", as well as risk becoming stranded assets.<sup>54</sup> Again, this is where public finance could play a role to ensure financing is available to secure energy access without resorting to fossil fuel options.

## **RECOMMENDATIONS:**

- ⇒ The ESS should include a priority focus on energy access for all, including basic needs and last-mile connectivity and access to clean cooking. This could include working with partners to develop innovative financing models, bundling smaller-scale projects using financial intermediaries or aggregators.
- ⇒ The ESS must specify clear targets and timelines for its contribution to achieving energy access for all, including sub-targets for gender and vulnerable groups, including in the RMF. AIIB should communicate and report on these targets in an open and transparent manner.
- ⇒ Energy access investments should not be treated as an 'add-on' to the core energy portfolio, but must fully integrated into its national and regional support. Programmes should be designed to proactively focus on reaching the 'last mile', while ensuring these have sufficient resourcing and skilled staff.
- ⇒ The Special Fund on Project Preparation could be used to pilot and demonstrate innovative investments that target hardest-to-reach groups that, if successful, could be replicated or scaled-up by other IFIs, investors or client governments.
- ⇒ The option to support energy access through fossil fuels should be removed. Energy access should focus on investments in clean, renewable energy, and not lock countries into decades of carbon emissions, dependence on imports of coal and other fossil fuels, as well as stranded asset risks. Importantly clean cooking needs particular attention to deliver affordable, accessible clean solution.

⇒ The RMF should include appropriate and impact-focussed energy access goals and metrics, with indicators that are fit for purpose and focused on ensuring energy access investments result in affordable, reliable, safe and sustainable services for poor and vulnerable groups. We recommend basing the assessment of energy access on the on the ESMAP Multi-tiered Framework<sup>55</sup> for energy access which evaluates the progression up the energy ladder, with the aim to get all people with not just a connection but adequate access to clean energy for a decent life.

## 6) NO FALSE SOLUTIONS

The draft ESS opens up for continued support of fossil fuels in combination with “emerging technologies like blue hydrogen (from fossil gas) and CCUS [carbon capture, use and storage] in decarbonisation” (para 46). Equally under renewable energy (para 45) it commits to support the development of “innovative and transformative projects”, including “low- or zero-carbon hydrogen”, however, without safeguarding against risky and fossil fuel based technologies.

This reliance on largely unproven and costly technologies as viable options is a dangerous strategy, that also risks displacing investments urgently needed in the shift away from fossil fuels to renewable energy. A growing body of evidence questions support for CCUS and blue hydrogen produced using fossil fuels, including their technical and economic viability. For example, a 2021 report by the Tyndall Centre for Climate Change Research demonstrates that CCUS perpetuates the use of fossil fuels.<sup>56</sup> Resources are far better targeted at sustainable renewable energy solutions, which are technically proven and dropping in cost continually.

Concerningly, the draft also promotes public-private partnerships (PPPs) referencing MDB experiences: “Innovative approaches have ... been initiated using grants and concessional financing to reduce the cost of electricity generated under [PPPs] or to improve risk sharing in PPP ventures” (para 36). However, this statement runs counter to AIIB’s own experiences. For example, in 2016 AIIB invested \$20 million in Myanmar’s Myingyan greenfield gas power plant, a Category A project and the first PPP in the country. Myingyan’s Power Purchase Agreement is not publicly available, making it hard to determine the terms of the contract and the tariff fees. This is not uncommon, most PPP projects suffer from poor transparency, including secrecy around the contracts and the use of non-disclosure agreements.<sup>57</sup>

It is also important that the draft ESS provides clear definitions and priorities in terms of what types of renewable energy to prioritise (see section 4). According to the ESS, the renewable energy portion of the current portfolio consists of “various types of renewable energy and supporting infrastructure, including solar, wind, geothermal, hydropower, and energy storage.” However, it does not address the risks of some of these technologies and how to safeguard against these.

For example, with regards to hydro power, the draft refers to the ESF for guidance, however, the ESF does not exclude large scale hydro, despite the significant risks. This goes against recent guidance, such as a statement by UN Rapporteurs noting the devastating impacts on rivers and riverside communities and calling for “governments, the power generation industry and financial institutions

to halt planned new large hydropower dams”. Instead they call for “the development of other renewable energies with lower social and environmental impacts.”<sup>58</sup> AIIB has taken steps to exclude large dams from one FI project (see section 3). This is welcome and should be institutionalised in the updated ESS. A move in this direction would require AIIB to remove controversial projects from its pipeline, such as the proposed Nenskra Hydropower project in Georgia.<sup>59</sup>

The draft ESS also commits to support development of biofuels (para 45). It is essential that rigorous safeguards are in place. Industrial scale biofuels can compete with food production and undermine land rights of indigenous communities. Extreme caution should be taken in developing biofuels at scale.

## RECOMMENDATIONS

- ⇒ The ESS should exclude fossil fuel projects or sub-projects utilising unproven, risky and expensive technologies, such as carbon capture and storage, which can divert public finance away from a just transition to renewable energy.
- ⇒ The ESS should not promote risky financing models, such as PPPs, without ensuring value for money, disclosure of contracts terms and tariffs, and accountability.
- ⇒ The ESS should exclude support for environmentally damaging renewable energy technologies, such as greenfield hydropower and greenfield projects reliant on construction of new large dams and industrial scale biofuels.

## 7) PUT GENDER EQUALITY FRONT AND CENTRE

*Sustainable Development Goals (SDGs) 5 and 7 are inextricably linked, as a lack of energy access disproportionately affects women and girls in the form of health, productivity, unpaid labour, and employment burdens.*

*Sustainable Energy for All, 2020<sup>60</sup>*

It is welcome that the draft ESS has an explicit focus on promoting gender equality (para 68), rather than just “taking gender into account” in the 2017 version (para 45). Women and children are particularly badly impacted by lack of access to clean fuels, causing health and development risks.<sup>61</sup> Furthermore, the draft ESS concludes that “traditional fuels ... extends gender inequality and prolongs exposure to health risks”, which points to the importance of combining SDG 7 with SDG 5 on gender equality.

The draft refers to “measures” that will be “supported to include women in project consultations, and to address women’s priorities and needs so as to increase opportunities for enhanced livelihood and economic benefits as well as improved health outcomes” (para 58). This is in line with the revised ESF, which also includes gender equality language, but puts the main impetus on the client, with AIIB’s support. In the ESS context, however, it is not clear what the exact ‘measures’ are that AIIB intends to support, which undermines this commitment. To date there is little accountability for AIIB’s commitments to gender equality, which partly stems from AIIB’s reluctance to develop an

institutional gender policy, setting out clear and accountable parameters and targets. It is particularly concerning that this commitment is not reflected in the RMF, which fails to call for any kind of gender disaggregated data or targets.

This is a missed opportunity which should be rectified in the final updated ESS. Achieving SDG 5 on gender equality must be a key priority in the revised ESS. The impacts of climate change often hit women first and hardest, due to systemic inequities, including women's important role in, for example, small scale agriculture and as main providers of water for the family in rural, remote and informal communities. From irrigation to agro-processing machines, food storage, lighting and refrigeration, access to energy can transform how women use their time, labour, income and productivity. For example, access to energy can lessen the time and energy women spend on tasks such as fuel wood and water collection, leaving more time for education and income generation activities.<sup>62</sup>

This can have a positive effect on a community's ability to bounce back from unexpected climate shocks and enable them to adapt to the changing climate.<sup>63</sup> It is therefore also concerning that the draft ESS, rather than expanding on commitments around adaptation, instead has cut them out bar one mention. Moreover, where it is mentioned in relation to ESF commitments, it is not linked to any specific example. Given the specific impacts of climate change on women and the urgent need for support to adapt, such as access to sustainable renewable energy, it is very concerning that these links are not made in the ESS.

Distributed renewable energy has the additional benefit of reaching the so called last mile communities, which are often the poorest, while not relying on fossil intensive climate inducing technologies. This also protects these communities from fossil fuel price variability and shocks, likely to become more prevalent in the future, and strengthens their ability to adapt to a changing climate.<sup>64</sup> Women have a critical role to play in facilitating the shift to renewables, in particular off-grid renewable energy solutions, and as such must be meaningfully included in determining project plans and development models, as well as have access to gender-sensitive and responsive grievance mechanisms.<sup>65</sup>

## **RECOMMENDATIONS**

- ⇒ The ESS should clarify exactly what measures AIIB is committing to address the gender gaps with respect to energy access, which should be ambitious and accountable.
- ⇒ The RMF should include gender disaggregated targets for all energy investment, including on energy access.
- ⇒ The ESS should reintroduce language on adaptation and commit to support for adaptive measures, with a particular focus on women and girls

## **8) ENSURE A RIGHTS-BASED APPROACH AND MEANINGFUL PARTICIPATION**

Energy projects can have detrimental impacts on indigenous peoples and vulnerable groups, undermining their right to land and livelihoods, while not serving their needs. The draft ESS acknowledges that: "Energy system impacts include not only climate change and air pollution, but

also impacts on human settlements, land use, and livelihoods, as well as on water bodies, landscapes, ecosystems, and biodiversity” (para 18).

Comprehensive and meaningful consultations are essential for ensuring energy projects and programmes are well targeted and sustainable in all senses of the term. The ESS must have a right based approach, to ensure projects respect and protect communities’ rights. This includes ensuring Free Prior and Informed Consent (FPIC) for indigenous peoples. In developing suitable energy solutions, all stakeholders must be involved to ensure vulnerable group’s rights are prioritised. These principles should also apply to the ESS consultation, which must include public engagement, prioritising outreach to project affected communities.

The “commitment to social sustainability and inclusiveness” is encouraging, including “inclusive access to project benefits to all citizens – irrespective of age, gender, location, ethnicity, and other socio-economic characteristics – and particularly for groups which are often marginalised, vulnerable, or excluded from access to services” (para 58). It singles out “promoting gender equality” and “taking disability into account” specifically, however, fails to make a single reference to indigenous peoples here or at any other place in the ESS.

Given indigenous peoples particularly vulnerable situation, this is a serious omission. Although accounting for only about five percent of the world’s population, indigenous peoples effectively manage an estimated 20-25 per cent of the Earth’s land surface. This also makes them particularly vulnerable to climate change and to intrusive projects, including energy projects, which encroach on their lands and resources. For example, large scale projects need to deliver the energy needs of affected communities who are often by-passed by energy infrastructure that impacts on them. This also relates to renewable energy projects, which can put indigenous peoples at risk without mandatory requirements for their active participation in any project development and monitoring and for their rights to be thoroughly considered, including FPIC (see section 4 and 6).<sup>66 67</sup>

To fully address the implications of the energy sector, including securing the rights of vulnerable communities and ecosystems, the ESS must therefore take further steps. This include measures such as adopting the Banks and Biodiversity No Go Policy, which “prohibits any direct or indirect financing related to unsustainable, extractive, industrial, environmentally, and/or socially harmful activities in or which may potentially impact” a number of areas, including:

- ecologically sensitive areas as designated by international agreements, conventions and institutions (e.g. UNESCO, FAO, IUCN);
- free flowing rivers;
- intact forests;
- areas protected by national or subnational laws and regulations;
- protected or at risk marine or coastland ecosystems;
- Indigenous Peoples’ and Community Conserved Territories and Areas (ICCAs) and areas where FPIC of Indigenous and Local Communities have not been obtained.<sup>68</sup>

## RECOMMENDATIONS

- ⇒ The ESS should require an energy access options analysis, with clear guidelines, to ensure the needs of vulnerable groups and 'last-mile' communities are prioritised. Financing mechanisms should focus on affordability and reach for those most vulnerable, rather than a bias for private sector and market-based options.
- ⇒ The ESS should include requirements to meaningfully consult and actively involve vulnerable groups, including Indigenous Peoples, in project and programme development and monitoring, whilst respecting their right to free, prior and informed consent. Community participation should be compulsory when determining prioritisation of end-uses of grid systems and for organising the system.
- ⇒ The ESS should include a Zero Tolerance provision on reprisals linked to AIIB funded energy projects, building on the ESF commitments to address retaliations

## Consultation process

The consultation process for ESS review is not in line with best practice, including a prohibition to submit input in other languages than English. AIIB has committed to provide a summary of collated responses, which is welcome, but there are no provisions for groups to submit comments confidentially. This is concerning, as affected communities and local civil society are unlikely to be able to engage fully and contribute with vital input, for example, on their priorities for energy access. Moreover, AIIB has not made publicly available background documents, vital for understanding lessons learned incorporated into the updated draft.

## RECOMMENDATIONS:

- ⇒ AIIB should post translated draft texts of the proposed ESS in major languages of regional and non-regional members and enable options for submissions to be received in all languages.
- ⇒ AIIB should permit comments on the draft to be submitted anonymously.
- ⇒ AIIB should disclose any approach or background paper on the Energy Sector Strategy Update that is informing the revisions proposed (e.g. CEIU's Early Learning Assessments on energy projects) at the earliest possible date, i.e. during (rather than following) the public consultation period.
- ⇒ AIIB should schedule interactive discussion based sessions (non-webinar format) held in different time zones and languages to accommodate regional and non-regional members, and times for meetings to discuss sub-sector concerns. These sessions should be notified well in advance and include translation options in major relevant languages.
- ⇒ To ensure full participation for civil society groups that may risk reprisals for giving input, submissions via a digitally encrypted platform should be enabled on AIIB's website.

## 9) SUPPORT A JUST TRANSITION

*"The purpose of the transformation of the energy sector is to improve lives and livelihoods. Alongside the benefits of avoiding the worst of climate change, this means enabling citizens to seize the opportunities and navigate the disruptions caused by the shift to clean energy technologies. It means eradicating energy poverty: no system is sustainable if it continues to exclude large parts of the global population from access to modern energy. And it means putting considerations of employment, equity, inclusion, affordability, access and sustainable economic development at the centre of the process."*

*International Energy Agency, World Energy Outlook 2021<sup>69</sup>*

The urgent and rapid phase out of all fossil fuels must be complemented by support for a gender responsive Just Transition, ensuring no one is left behind in the shift to a clean sustainable energy pathway. It is welcome that the ESS introduces some language on the Just Transition, primarily referring to the 2021 MDB principles for a Just Transition.<sup>70</sup> It also includes references to how AIIB will "support and accelerate its member's respective transitions toward low-carbon energy mixes through investments in", for example, "associated efforts to mitigate adverse social impacts of energy transition and facilitate a just transition" (para 31).

However, there is no further clarification of what this means in practice. It is further concerning that Just Transition is referenced in the context of 'low carbon' rather than 'zero carbon', in particular given the strong focus on gas throughout the text. There is some language that points towards the renewable energy sector instead, eg para 20, which acknowledges the "substantial new employment opportunities" expected in the clean energy sector, outpacing "job losses in the conventional energy sectors". These elements should be further expanded and directly linked to Just Transition.

The references to Just Transition also fails to include specific mentions and links to issues regarding gender equality and specific rights for vulnerable communities. Green, just and inclusive transitions should be grounded in the different contexts and realities of affected communities across the countries where AIIB operates, and must uphold all human rights conventions, including but not limited to ILO Conventions and frameworks. AIIB should focus on securing people's access to energy, prioritising public supported decentralised solutions with meaningful decision-making structures, including local communities. The ESS must also address Just Transition for communities already displaced and affected by already funded projects, such as the Bholra IPP.

### RECOMMENDATIONS

- ⇒ The ESS should include commitments to promote and implement measures to support a gender responsive Just Transition, which is green and inclusive and grounded in the different contexts and realities of affected communities. This should include commitments towards communities already negatively impacted by AIIB projects.
- ⇒ Just Transition in the ESS should focus on securing people's access to energy, prioritising public supported decentralised solutions with meaningful decision-making structures, including local communities.

## 10) SET AMBITIOUS, TRANSPARENT AND ACCOUNTABLE TARGETS

The new ESS should include ambitious targets, including on GHG emissions reductions, sustainable renewable energy support, energy access for all and gender equity, which align with the Paris Agreement and the SDGs. It is concerning that the draft updated ESS makes the same mistakes as its earlier 2017 iteration. It continues to outline priorities and intentions, to 'promote' or 'support', but without any clear requirements, guidelines or targets. Judging from experience, this means that very few of these 'commitments' will be reflected in AIIB's actual energy portfolio. For example, AIIB commits to prioritise both renewable energy and distributed generation in the 2017 iteration, yet the evidence from the portfolio reveals that very little of this took place in reality.

The Results Monitoring Framework (RMF, Annex 1) is an important part of the strategy, which should incentivise, make accountable and drive investments to key priorities in the strategy. It should also track impact and ensure over-arching goals of keeping the temperature increase to 1.5 degrees in line with the Paris Agreement and delivering Agenda 2030, especially SDG7, are being met. Already weak in the 2018 iteration, it remains disappointing, with few amendments to the previous version of any significance. It does not help setting the vision for clients, nor will it help understanding AIIB's progress towards "sustainable energy for tomorrow". Instead some targets are even weaker. For example, greenhouse gas "reduction" has been replaced with "avoidance" and "number of households with increased access to electricity" is now "number of households with increased/improved access to energy". Moreover, none of these indicators have any baseline nor target, instead AIIB refers to "investment amount", making the exercise unaccountable and with little incentives to improve outcomes. Given that AIIB has not made the lessons learned report publicly available, it is not possible to review the assessment of the original RMF.

While we welcome the references to the ESF regarding greenhouse gas (GHG) reporting (para 57), new language on climate change risk assessment (para 46) and a commitment to conduct project-level assessments to align them with the Paris agreement (para 40), these commitments lack in detail, including whether they are applicable to FI and capital markets investments as well. For example, the commitment to GHG accounting in the ESF is weak and conditional on the "client's request", and also to respond to national commitments rather than AIIB and ESF requirements. As there are no spelled-out AIIB targets or caps on GHG emissions, nor any clear requirement for GHG accounting, AIIB's ESF fails to provide clients with any encouragement to put forward carbon neutral projects. These omissions should be rectified in the ESS.

Other MDBs, such as the IFC and ADB, usefully define projects expected to cause 'significant GHG emissions'. This enables the banks to ensure that projects estimated to have significant emissions according to a specified threshold receive specific attention, and must abide by provisions, including being required to measure and reduce annual emissions. AIIB should adopt this approach in line with best practice, for example at the IFC. This should include direct and indirect emissions.

Moreover, despite the considerable criticism of the original ESS and despite a commitment to review the strategy regularly, this first 'review' has been downgraded to an 'update'. This is disappointing, not the least since the ESS requires far more thorough revisions than currently conducted, as can be

seen from this submission and in light of the urgency of the climate crisis, in which the energy sector plays a fundamental part.

## RECOMMENDATIONS

- ⇒ The Results Monitoring Framework should include ambitious and measurable targets, aligning with or going beyond MDB best practice and delivering Paris Alignment, and include gender disaggregated data.
- ⇒ The ESS should introduce specific emissions targets, with a requirement for GHG assessments (including direct and indirect emissions) of all projects expected to emit above a specified GHG benchmark, in line with best practice. There should be a specific threshold for projects with significant emissions, with a requirement to measure and report emissions reductions on an annual basis.
- ⇒ The ESS should include clear and specific language to ensure GHG reporting and climate change risk assessments cover all projects, including FI investments, especially higher risk sub-projects.
- ⇒ The ESS should be subject to regular reviews, including public consultations. Background documentation, including lessons learned assessments, should be available.

**JULY 2022**

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<sup>1</sup> <https://www.re-course.org/wp-content/uploads/2021/10/Ten-AIIB-ESS-Essentials-1021-FINAL-v2.pdf>

<sup>2</sup> <https://www.gov.uk/government/consultations/aligning-uk-international-support-for-the-clean-energy-transition>

<sup>3</sup> <https://bigshiftglobal.org/multilateral-development-banks-absent-glasgow-pact-shift-fossil-finance-renewables-signed-major>

<sup>4</sup> <https://www.adb.org/what-we-do/energy-policy>

<sup>5</sup> <https://practicalaction.org/news-media/2022/02/04/links-between-energy-access-climate-adaptation/>

<sup>6</sup> <https://openknowledge.worldbank.org/handle/10986/35799>

<sup>7</sup> <https://www.re-course.org/news/call-for-a-transparent-and-inclusive-consultation-on-aiibs-revised-energy-sector-strategy/>

<sup>8</sup> See for example <https://www.climatechangenews.com/2020/09/11/asian-multilateral-bank-promises-end-coal-related-financing/>

<sup>9</sup> [https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc\\_wg3\\_ar5\\_chapter10.pdf](https://www.ipcc.ch/site/assets/uploads/2018/02/ipcc_wg3_ar5_chapter10.pdf)

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