CEE Bankwatch Network

CEE Bankwatch Network position on the AIIB's Energy Sector Strategy Update

15 July 2022

CEE Bankwatch expresses its deep disappointment in the Asian Infrastructure Investment Bank's (AIIB) call for public consultation on its Energy Sector Strategy Update.[1] In coalition with other civil society organisations, we have raised concerns on numerous occasions that the AIIB's consultation process is neither inclusive nor meaningful. Unfortunately, scheduling virtual meetings and extending the initial timeline in response to the repeated requests of civil society does not change the 'tokenistic'[2] nature of the AIIB's current approach.

Therefore, we urge the Bank, before finalising its Energy Sector Strategy Update,[3] to ensure that comments from civil society and experts are published alongside responses from AIIB senior management. In line with best practices of international financial institutions, the AIIB should release a revised draft of its Energy Sector Strategy Update in the months ahead, which should remain open for a period of public comment before approval by the Board of Directors.

Therefore, once again we call on the AIIB, as an international financial institution with a development mandate, to:

- increase the transparency of its policy revision processes and project-related matters, including financial intermediary facilities and capital market investments;
- ensure meaningful and inclusive public participation; and
- be accountable and responsive to the concerns of communities affected by its projects and broader civil society actors across the Bank's membership.

AIIB's Energy Sector Strategy commitments

According to AIIB's consultation draft, its Energy Sector Strategy now 'embraces and is informed by the principles underpinning the 2030 Agenda for Sustainable Development, particularly Sustainable Development Goal 7 (SDG 7, 'affordable and clean energy'), and the Paris Agreement'. However, we believe

[1] Asian Infrastructure Investment Bank, Call for public consultation: AIIB's Energy Sector Strategy update, *Asian Infrastructure Investment Bank*, June 2022.
[2] Office of the High Commissioner for Human Rights, High-level side event: participation, human rights and the governance challenge ahead, *Office of the High Commissioner for Human Rights*, 25 September 2020.
[3] Asian Infrastructure Investment Bank, Energy Sector Strategy, *Asian Infrastructure Investment Bank*, June 2022.

this commitment is insufficient. In order to reduce the carbon intensity of energy supply, deliver on SDG 7 on universal access to affordable, reliable and sustainable modern energy, and promote a low carbon energy transition that 'leaves no-one behind', the Bank should commit to developing a binding climate action and energy policy. The AIIB also needs to bring its strategy more in line with the UN's development policies and poverty reduction aims. Large-scale energy infrastructure projects lead to reallocations and distortions in public finance budgets in other sectors. For example, nuclear energy production, in addition to its environmental risks and waste disposal problems, depends on a very expensive, highly secured and controlled centralisation model. And while safety enhancements and upgrades extend the life of this costly energy source, they also impede objective access to energy for the poor.

The AIIB's commitment to align with the Paris Agreement sounds promising on paper. But questions remain about how the Bank will reach that mark and evaluate its own success, particularly given that its updated draft Energy Sector Strategy extends support for fossil fuel financing with only limited conditions attached to new fossil fuel projects.

The AIIB's Energy Sector Strategy Update does not acknowledge the United Nations Guiding Principles on Business and Human Rights[4] or the principle that zero emissions must be achieved in tandem with zero human rights abuses, as advocated by Amnesty International in its recommendations for governments and corporations involved in energy transformation.[5]

The Bank should commit to following the UN Guiding Principles on Business and Human Rights and build its own human rights policy, one that refuses to tolerate any human rights violations by its borrowers. The creation of such a policy should also result in meaningful consultation processes with communities and workers engaged on many important issues, including human rights due diligence, benefit-sharing schemes and fundamental labour conventions. It should also safeguard the rights of local communities and indigenous peoples (including their land rights) by upholding free, prior and informed consent across the lifespan of each AIIB-financed project and maintaining effective access to grievance mechanisms.[6]

The Bank should acknowledge that the public, especially affected communities and marginalised groups, has the right to participate and design future energy systems based on their own needs and demands. The AIIB can play an important role in mobilising resources for the infrastructure required to develop distributed, decentralised renewable energy systems owned and directly operated by local communities.

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[4] United Nations Human Rights, Guiding Principles on Business and Human Rights, *United Nations Human Rights*, 16 June 2011.

[5] Amnesty International, Stop burning our rights! What governments and corporations must do to protect humanity from the climate crisis, *Amnesty International*, 7 June 2021.

[6] The AIIB's Environmental and Social Framework, Project-affected People's Mechanism (PPM) and updated Energy Sector Strategy do not together constitute a comprehensive, precise and reliable environmental and social safeguard policy for the Bank's energy projects. The AIIB still has no robust set of environmental and social guidelines that clearly commits to excluding fossil fuels and projects with large social and environmental impacts, such as large dams. Moreover, AIIB's obligations to address social and environmental impacts on gender equality, the rights of indigenous peoples and the PPM should be reinforced in the future.

Concerns regarding AIIB commitments on fossil fuels

CEE Bankwatch Network appreciates the AIIB's commitment to exclude financing for new coal- fired power plants and coal-related projects, including associated facilities. We also appreciate that the Bank has recognised the 'risks of long-term carbon lock-in' and decided to rule out investments in upstream fossil gas projects.

However, the Bank must stop supporting all fossil fuels, including gas. Since its establishment in 2016, the AIIB has spent twice as much on fossil fuels, primarily on fossil gas, as it has on renewable energy. The Bank has invested more than USD 2 billion in fossil gas projects, representing almost half of its energy portfolio. But the Bank's actual investment in fossil gas is probably even greater, as the above figure excludes indirect financing through undocumented financial intermediaries. If the Bank is serious about its 'green credentials' and commitment to energy transition, it must significantly strengthen its energy and climate policies. That would send a signal to private markets that clean energy investments are the only option. The Bank needs to scale up its climate investments in the energy sector so that fossil fuel lending decreases steeply from its current unsustainable levels.

Worryingly, the AIIB's updated Energy Sector Strategy considers natural gas a transitional fuel: 'The increased use of natural gas instead of oil and coal has helped many developed economies reduce carbon emissions and air pollution. It is expected that natural gas will also play an essential role in the transition strategies for many developing countries in the region, especially in hard-to-abate sectors. In addition, natural gas potentially contributes favourably to members' energy security, particularly when the resource is domestic.'

The AIIB should be keenly aware that gas, not coal, has been the primary driver of the global increase in carbon dioxide emissions since 2013, and that methane, the main component of fossil gas, is a highly potent greenhouse gas and the second most significant driver of climate change. The 1.5°C-compatible mitigation pathways evaluated by the Intergovernmental Panel on Climate Change (IPCC) advocate a significant decrease in gas use across energy systems by 2035 in advanced economies and by 2040 in developing and emerging countries, as well as a rapid decline in the carbon intensity of electricity and increased electrification of end uses up to 2050.

There is also the issue of financial viability. For instance, investments made today in a new gas infrastructure with a life expectancy of over 20 years (plus a significant period of at least five years necessary for planning and construction) would likely become stranded assets long before the end of the project's anticipated economic lifespan. Another distinct possibility is that new gas projects will aggravate the existing fossil fuel lock-in faced by countries in which the Bank operates to the detriment of necessary investments in renewables and energy efficiency measures.

The World Energy Outlook 2022 report by the International Energy Agency (IEA) reveals that the path to net-zero emissions is narrowing.[7] Staying on it requires the immediate and massive deployment of all available clean and efficient energy technologies combined with a huge decline in the use of fossil fuels. The IEA reiterates the key role reserved for international public finances, which are so critical to energy transitions,

[7] International Energy Agency, World Energy Outlook 2022, *International Energy Agency*, November 2022.

especially in developing economies. International financial institutions, including the AIIB, should take all measures to ensure successful and affordable clean energy transitions for all.

In its Energy Sector Strategy Update, the AIIB states: 'Reliance on fossil fuel imports subjects many to the risks of supply chain disturbances and price volatility. Renewable energy is domestic and less exposed to global risks.' But considering that the energy mix in countries where the AIIB operates is predominately based on coal and gas and that the deployment of renewables has thus far been limited, the potential issues with balancing renewables do not represent a threat to the energy systems in these countries. The Bank goes on to claim: 'Gas-fired power offers flexibility for balancing the variability of renewable energy and can thus enable a higher share of renewables in the generation mix.' However, as an argument in favour of financing gas facilities, it is hardly convincing.

Furthermore, domestic fossil gas production in the AIIB's countries of operation, including those in Asia, has been steadily declining over the last decade and there are no market signals that this might change in the future. If we are to stay in alignment with IPCC's 1.5°C-compatible mitigation pathways and IEA recommendations, no new gas extraction should occur, as recognised by the Bank's decision to exclude financing for upstream gas projects.

The latest assessments of pledges by countries around the world, including nationally determined contributions (NDC) and long-term strategies (LTS), have shown that countries will significantly overshoot trajectories necessary to keep warming below even 2°C-compatible mitigation pathways based on a 2070 to 2100 timeline. Therefore, the Bank's Energy Sector Strategy Update must address the credibility of its claim that its future fossil fuel investments align with the Paris Agreement.

According to the Energy Sector Strategy Update, the Bank's intention to lend 'support to natural gas mid-stream infrastructure (LNG terminals, storage, and transmission pipelines), natural gas-fired power generation and downstream (distribution and end-use) facilities is conditional on the investments credibly replacing higher carbon fuels, inefficient technologies, or oil- and coal-fired energy facilities, thus reducing the carbon intensity of the energy sector immediately or over time'.

The justification for public support and Paris alignment of the midstream pipelines is non-existent. Also, the risks of significant lock-in and transition call into question the feasibility of repurposing low-carbon gases in the future. According to a 2021 report by the International Institute for Sustainable Development, liquefied fossil gas infrastructure is especially harmful to the climate because of the associated fugitive emissions and high-energy demands for liquefaction, marine transport and regasification. Lifecycle emissions can be twice as high as those of domestic gas production.[8]

[8] International Institute for Sustainable Development, Step off the gas: international public finance, natural gas, and clean alternatives in the global south, *International Institute for Sustainable Development*, June 2021.

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The AIIB needs to make a blanket commitment to sustainable energy

The Bank should develop a transition strategy that focuses on low-carbon energy and infrastructure to (i) scale up decentralised, distributed renewable energy systems, (ii) move to grid technologies to ensure uptake of variable renewable energy, and (iii) adopt precautionary, no-go principles when planning infrastructure. These measures are necessary to protect people, biodiversity and the environment.

The Bank claims that it will support 'members to develop variable renewable energy— hydropower, wind, solar, and other sources—to reduce fossil fuel consumption and increase access to modern energy through decentralised generation and mini- and micro-grids'. However, the Bank lacks the specific conditionalities for the category of renewables from the outset (excluding large-scale hydropower dams, waste-to-energy incineration, etc.).

Encouragingly, the AIIB has already explicitly excluded the financing of large hydropower projects via financial intermediaries in some on-lending agreements. But more needs to be done. The AIIB should move beyond this limited commitment and fully reconsider its overarching support for hydropower infrastructure, including unconditionally identifying it as renewable energy. Specifically, investments in the construction of new impoundment, pumped-storage and run-of-river hydropower dams and associated facilities should no longer be considered part of the AIIB's 'low-carbon' portfolio. As has been consistently shown, hydroelectric dams of varying scale, whether built on mainstream or tributary rivers, cause incalculable damage to people and ecosystems upstream, downstream, and in the vicinity, of project sites. Therefore, hydropower should not be considered part of an economically, socially or environmentally sound strategy aimed at transitioning away from fossil fuel dependency.

The AIIB should review and withdraw its proposals for investments in future dams, given the related social, economic, environmental, climate and reputational risks already flagged by civil society groups in the respective member countries.[9]

Worryingly, the AIIB's support for 'innovative and transformative projects' may include floating solar power infrastructure, large-scale wind farms and green hydrogen pilot production facilities. However, it has become increasingly clear that these projects lead to unsustainable extraction of ground and surface water, cause irreparable harm to surrounding ecosystems (including the ecosystem of migratory birds) and reduce access to land, territories and resources which local communities rely on to survive.

The Bank should incorporate precautionary principles that explicitly elaborate aims to avoid complicity with, or exacerbate, conflicts; gross human rights violations; biodiversity degradation; and the grabbing of land, resources and territories from Indigenous Peoples and local communities. Also, a transboundary impact assessment of large wind and sun farms should be carried out to define their potential impacts on biodiversity.

The AIIB should develop a comprehensive no-go policy for critical habitats under local, national and international protection as well as for areas with endemic species, free-flowing rivers, protected or at-risk

[9] CEE Bankwatch Network, Neskra hydropower project: update, *CEE Bankwatch Network*, 29 January 2021.

marine and coastland ecosystems, pristine forests, Indigenous People's territories and sacred lands.[10] This policy should be reflected in its Environmental and Social Exclusion List and accordingly referenced in its Energy Sector Strategy. This will increase the likelihood of minimising harmful impacts on biodiversity, the environment and people.

The concerns raised here are just some of many we have with AIIB's updated Energy Sector Strategy. We hope further revisions to the consultation draft will result in a more thoughtful, meaningful and inclusive process that fully considers the diversity of communities across the regions in which the AIIB operates.

Sincerely,

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[10] A joint statement by the NGO Forum on ABD, an Asian-led civil society organisation, contends: 'Critical habitat should include not only habitat of Endangered and Critically Endangered species but also habitat of Vulnerable species as defined by the IUCN Red List of Threatened Species or as defined in any national legislation. Vulnerable species are likely to become endangered unless the circumstances that are threatening their survival and reproduction improve.'