

POLICY PAPER

Multilateral Development Banks’ Paris Alignment Methodologies

Best Practice and Suggestions for Improvement

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Imprint

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Abbreviations

ADB	Asian Development Bank
AfDB	African Development Bank
AIIB	Asian Infrastructure Investment Bank
BB	Building block of the joint MDB framework to align with the Paris goals
CEB	Council of Europe Development Bank
COP	Conference of the Parties to the United Nations Framework Convention on Climate Change
EBRD	European Bank for Reconstruction and Development
EIB	European Investment Bank
ESF	Environmental and Social Framework
ESPF	Environmental and Social Policy Framework
FI	Financial Intermediary
GHG	Greenhouse Gas
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IsDB	Islamic Development Bank
LTS	Long-Term Strategy
MDB	Multilateral Development Bank
MIGA	Multilateral Investment Guarantee Agency
NAP	National Adaptation Plan
NDB	New Development Bank
NDC	Nationally Determined Contribution
PAIA	Paris Alignment Implementation Approach
PBF	Policy-based Finance
UNFCCC	United Nations Framework Convention on Climate Change

Executive Summary

MDBs and Paris alignment

The Multilateral Development Banks (MDBs) play a substantial role in the transition to low-carbon, climate-resilient economies and societies. In 2017, they collectively committed to supporting countries' implementation of the Paris Agreement goals. In 2018, they launched a joint framework for aligning their operations with the goals. The year 2023 was then critical in the MDBs' progress, as several of them, forming part of a joint MDB working group on Paris alignment, reached self-appointed deadlines for achieving this alignment for new operations. In the context of this commitment, in June 2023, the joint MDB working group published the Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment. These principles set out a common basis for defining and assessing new MDB operations' Paris alignment. Also in 2023, four MDBs – the European Bank for Reconstruction and Development (EBRD), Inter-American Development Bank (IDB), World Bank, and Asian Infrastructure and Investment Bank (AIIB) – published individual versions of the joint principles. These versions interpret, adapt, and concretise the principles' provisions and complement them with information and guidance on methods, sectors, regions, and individual institutional processes.

MDBs should urgently pursue the highest standards in their Paris-alignment approaches, as they channel an annual average of over USD 100 billion in development finance to client countries and play a pioneering role in the financial sector. Other financial institutions, companies, and governments also often follow the MDBs in setting standards. It is, therefore, critical to closely examine how the MDBs aim to put Paris alignment into practice.










Purpose and scope of the analysis

This analysis aims to highlight both shortcomings and best practice in designing the joint MDB methodological principles, and the specific Paris-alignment methodologies of the World Bank, EBRD, IDB, and AIIB. It does this with a particular view to providing constructive input for upcoming reviews and revisions of those methodologies. The assessment of the joint principles is especially important because this document serves as a main reference for developing further methodologies for individual MDBs and allows comparison of the MDBs' Paris-alignment approaches with their joint basis. The analysis is mainly informed by a desk review of the joint principles and the abovementioned four methodologies. It covers only the publicly available methodological documents' content and not their operationalisation. Therefore, it only provides information about the MDBs' theoretical alignment approach, not about the practical application. The analysis also does not cover further MDB policy documents, such as environmental and social policies, as any relevant correlation to those policy documents should be mentioned by the Paris-alignment methodologies.

This executive summary highlights the main results for each assessment category, focusing on where the authors see scope for improvement.

Assessment categories

The analytical framework applied covers a set of indicators for each overarching category, which the paper's authors identified as essential for the MDBs' Paris alignment. The categories cover:

-  the scope of MDB operations and actions the methodology covers
-  a 1.5°C compatibility test (including the use of low-emission pathways, considerations of indirect impacts on emissions, low-emission design and technology alternatives, and carbon lock-in risks)
-  adaptation and resilience goals (including climate risk and vulnerability assessments and respective response measures, and avoidance of operations that increase vulnerabilities)
-  consistency with national climate strategies and policies
-  the extent to which climate action opportunities are proactively sought
-  consideration of human rights-related obligations under the Paris Agreement
-  provision of additional sector specific guidance
-  considerations of a just transition; management of transition risks, such as stranded assets
-  financial intermediaries and corporate counterparties
-  transparency of and participation in Paris-alignment assessments; a review of the methodology

These categories and their respective indicators collectively assess the steps taken for ensuring the MDBs' alignment with the Paris goals.

Assessment category results



Scope of the methodology

This section addresses the MDB methodologies' applicability to the spectrum of MDB operations and the consideration of elements relevant for Paris alignment that go beyond the project level.



SCOPE FOR IMPROVEMENT

- Most MDBs do not specifically include technical assistance operations in their Paris-alignment approaches. Some also specify that they apply their Paris-alignment methodologies only to operations that pass a funding amount-related threshold. However, the MDBs' methodologies should cover all types of finance and all financial instruments, independently of the funding amount.
- The application of the Universally Aligned List is highly problematic, as it might lead to a major share of operations not being specifically assessed for Paris alignment, although those operations may support non-aligned activities.
- It might additionally lead to MDB operations not being systematically screened for climate action opportunities.
- The Universally Aligned List's preface on fossil fuels should be revised because an investment might still encourage the use of fossil fuels even if its economic feasibility does not depend on such fuels.
- The joint Universally Non-Aligned List does not cover new investments in expansion of upstream and midstream fossil gas or oil. The MDBs should progressively expand their joint exclusion list to align with long-term net-zero scenarios.



1.5°C compatibility test

This section looks at a range of criteria that MDBs need to fulfil to ensure that their operations are compatible with the Paris 1.5°C goal. The criteria include: (1) the use of low-emissions pathways to assess operations' alignment with 1.5°C; (2) consideration of potential indirect impacts on emissions (particularly for policy-based lending), (3) consideration of low-emissions alternatives in an operation's design, and (4) the assessment and management of potential lock-in risks.



SCOPE FOR IMPROVEMENT

- The joint methodological principles' use of a 1.5°C or 2°C temperature goal for assessing an operation's Paris alignment is unclear. Most MDBs refer more generally to the Paris goal(s). Only the EBRD clearly commits to 1.5°C. All MDBs should clearly commit to 1.5°C and, respectively, align their operations.
- Particularly for policy-based lending operations, MDBs should better incorporate a requirement for assessing potential low-emissions design alternatives.

- The joint MDB methodology and most MDBs' individual methodologies do not examine their MDB operations' potential indirect impacts on countries' mitigation pathways (e.g. unintended overall emissions increases)
- While all MDBs require an assessment of lock-in risks in their Paris-alignment methodolo-

gies, neither the joint principles nor the specific MDB methodologies establish a clear threshold for acceptable 'low' lock-in risks. This omission leaves scope for interpretation that may lead to operations with considerable lock-in risks still being considered aligned.



Adaptation and resilience goals

This section examines three main considerations that MDBs should ensure for aligning their operations with a climate-resilient development pathway. It analyses how MDBs: (1) assess risks from climate hazards and respective vulnerabilities for their operations, (2) define response measures for previously identified climate risks, and (3) avoid operations that potentially increase climate vulnerabilities, independently of whether the operation itself faces climate hazard-related risks.



SCOPE FOR IMPROVEMENT

- The joint methodological principles do define the boundaries of an MDB's operation relatively broadly when assessing climate hazard-related risks. However, they lack clarity on the emissions scenarios (and respective temperature scenarios) used when assessing physical climate risks and use vague timeframe formulations. The AIIB, EBRD, and World Bank specifically require consideration of different emissions scenarios.
- The joint principles require that MDBs identify and assess only physical climate risks. They do not mention intangible climate risks, such as potential loss of cultural artefacts and places, or the loss of sense of identity and security.
- The MDBs do not systematically promote opportunities for enhancing climate resilience, as project staff are not required to identify potential resilience building measures for operations with 'low' and/or 'immaterial' risks from physical climate hazards. Moreover, there is no clearly defined threshold for such risks, which leaves scope for interpretation and may lead to MDB operations not being aligned with the Paris adaptation and resilience goals. The lack of well-defined thresholds also creates ambiguity about the extent to which previously identified climate hazard-related risks should be remedied.
- The joint methodological principles have no specific requirement that only operations that do not exacerbate existing vulnerabilities be considered Paris-aligned. The principles refer to this important step only vaguely in their approach for policy-based lending operations. Only the EBRD methodology requires that, for it to be considered Paris-aligned, an operation may not undermine resilience in the context in which it operates.



Consideration of national climate strategies and policies

This section analyses the extent to which the MDBs' Paris-alignment methodologies assess consistency with a country's Nationally Determined Contribution (NDC) and with other national climate strategies and policies, such as National Adaptation Plans (NAPs). However, these strategies often remain insufficient for achieving the Paris mitigation goals, while their contribution to building resilience may be difficult to assess. Therefore, this section also assesses whether the methodologies anticipate the MDBs providing support to countries for improving on insufficient national climate strategies and policies.



SCOPE FOR IMPROVEMENT

- The joint methodological principles and all individual Paris-alignment methodologies assess consistency with national climate strategies and policies. However, MDBs' methodologies also should include processes to systematically consider support options in the case of a non-aligned NDC or LTS, and support for developing and enhancing NAPs.



Proactively seeking climate action opportunities

MDBs should use their Paris-alignment methodologies to direct as much of their portfolios as possible to generating positive and transformative climate impacts. In that light, this section examines the extent to which MDBs, in their alignment methodologies, go beyond a do-no-harm approach and toward 'doing good' and advancing the Paris goals.



SCOPE FOR IMPROVEMENT

- The joint MDB principles do not include any guidance on proactively seeking opportunities for climate action in operations design. The IDB, in turn, includes guidance for proactively seeking climate action opportunities as part of its upstream dialogue with clients, but the methodology still lacks clear steps to do so.
- All MDBs should include steps to proactively seek opportunities to support the Paris goals in all operations and thereby surpass mere due diligence and a do-no-harm approach, instead moving to doing good and advancing with the goals.



Human rights-related obligations

The Paris Agreement preamble acknowledges that action to address climate change must respect, consider, and promote human rights obligations. Human rights violations related to climate change can occur in various ways, such as through the absence of climate-related actions or implementation of inadequate or disproportionate climate mitigation or adaptation actions. The wind and solar sectors have been particularly associated with human rights violations. Therefore, this section analyses the extent to which the MDBs' Paris-alignment methodologies provide specific guidance on human rights-related risks from the climate crisis itself and from MDB operations' climate mitigation and adaptation actions.



SCOPE FOR IMPROVEMENT

- Neither the joint principles nor MDBs' individual Paris alignment methodologies refer to any type of human rights obligations. The MDBs' environmental and social safeguards usually cover human rights considerations, but they do not always cover all Paris-Agreement-related human rights obligations.
- MDBs' Paris-alignment methodologies should refer to human rights obligations under the Paris Agreement.
- In their annexed sector notes (that complement most such methodologies), MDBs should include further guidance and examples of potential human rights implications from physical climate hazards as well as from MDB operations' climate mitigation and adaptation actions.



Additional sector-specific guidance

Additional sectoral guidance is vital for ensuring MDB personnel's consistent implementation of Paris alignment, given that the joint methodological principles are formulated rather generally and that decarbonisation pathways and adaptation needs vary considerably by sector. Therefore, this section assesses the scope, detail, and practical applicability of the sectoral guidance notes that complement the MDBs' methodologies.



SCOPE FOR IMPROVEMENT

- All individual MDB methodologies reviewed have additional sectoral guidance. However, the guidance varies substantially in scope, detail, and practical applicability, sometimes even within the same bank. A more consistent approach to sectoral guidance within MDBs would ensure the sectoral assessments' quality and effectiveness. The World Bank's sector-specific guidance stands out in that it covers a broad range of sectors.
- More detailed sectoral guidance is needed, especially for adaptation alignment. The sectoral guidance notes would, for instance, benefit from further guidance and examples of operations that could potentially increase or decrease (existing) vulnerabilities. Most MDBs need to further develop their approaches for adaptation alignment across all sectors.
- MDBs should also include sector-specific guidance and examples for a range of aspects considered in this paper (e.g. examples for maladaptation, transition risks, and potential human rights violations for Paris-aligned activities in a sector).



Considerations of just transition elements and transition risks

This section analyses two main components of transition risks: (1) the extent to which the MDB Paris-alignment methodologies consider just transition elements in their assessments, including concrete operational steps to assess a just transition, and (2) whether the alignment methodologies foresee concrete steps to assess MDB operations' transition risks, including stranded assets, and whether MDBs are required to manage identified risks.



SCOPE FOR IMPROVEMENT

- Though the MDBs jointly committed to supporting a just transition and agreed on the MDB Just Transition High-Level Principles, the joint Paris alignment principles make no reference to a just transition as part of their transition risk requirements. Only the EBRD and IDB require considerations of a just transition as a principle in their Paris-alignment methodologies. Of those two, only the EBRD gives further details on how just transition considerations will be concretely applied.
- The joint principles include a step for assessing transition risks for direct lending operations. They also mention shadow carbon prices as a tool for assessing such risks. However, no information is provided on how to manage these risks once they have been assessed. Moreover, the joint methodological principles do not require assessment of transition risks for policy-based lending operations.
- While the IDB clearly states the need to include strategies for managing climate transition risks, only the World Bank and EBRD provide concrete tools and guidance for assessing transition risks. Only the World Bank provides some guidance on how to manage identified transition risks.
- All MDBs should integrate considerations of a just transition in their Paris-alignment approaches, and these should surpass mere principles and include operational steps for assessing that transition.



Financial intermediaries and corporate counterparties

Some MDBs channel substantial portions of their finance to financial intermediaries (FIs), especially for private-sector clients. However, they also lend directly to corporate counterparties. This means that for MDB finance to be aligned with the Paris goals, MDBs should ensure that finance flowing to financial intermediaries and corporate counterparties is also aligned. Therefore, this section looks at criteria related to counterparty alignment, covering whether: (1) the methodologies require assessment of the counterparties' commitments to Paris alignment in the entire portfolio, (2) financial support is excluded for counterparties not committed to Paris alignment, (3) alignment commitments and respective transition plans by counterparties are required to be time-bound (with transitioning as soon as possible but, at least, before 2030), (4) the methodologies anticipate the opportunity for MDBs to support and assist counterparties in their Paris-alignment efforts, (5) safeguards to avoid financing non-aligned investments are in place during counterparties' transition periods toward alignment, and (6) the methodologies expect the MDBs' stopping of financial support for counterparties if the counterparties fail to fulfil their alignment commitments in the agreed time period for transition.



SCOPE FOR IMPROVEMENT

- In the joint MDB principles and most of the current individual MDBs' methodologies, the counterparty-based approach is only applied if ringfencing of investments through the transaction-based approach is not possible. Thus far, only the EBRD requires all its FIs to commit to Paris alignment.
- All alignment methodologies should ensure they apply a combination of the counterparty- and transaction-based approaches, since complementarity is needed to ensure full Paris alignment of MDBs' investments.
- MDBs' applying only the transaction-based approach may lead to MDB finance indirectly supporting non-aligned FI investments by bolstering the FIs' balance sheets. Thus, in addition to restricting proceed use to Paris-aligned activities, the counterparty approach should be applied to all FIs to prevent MDB finance from indirectly supporting counterparties' climate-problematic activities. Thus far, only the EBRD requires all its FIs to commit to Paris alignment.
- Whenever the use of proceeds is known, the transaction-based approach should complement the counterparty-based approach. The transaction-based approach should include a full test for 1.5°C compatibility and for responsiveness to climate vulnerabilities, as suggested in previous sections.
- If the use of proceeds is not known and only the counterparty approach in its current form is applied, MDBs may not be able to verify their investments' Paris alignment during the counterparties' transition period. Therefore, as part of the counterparty approach, an immediate stoppage of the most climate-damaging investment types (e.g. exploration and extraction of coal, oil, and gas) should be a required precondition for counterparties to receive MDB finance.
- Most alignment methodologies establish no clear means of monitoring counterparties' implementation of their Paris-alignment commitments and do not anticipate stopping support if counterparties fail to keep their commitments. Only the EBRD will annually monitor progress in FIs' development and implementation of transition plans, up to stopping further engagement with the FI if the FI does not fulfil its commitment. All MDBs should ensure that monitoring occurs and that this results in clear negative consequences when there is non-compliance.



Transparency, review of the methodology, and participation

Regarding transparency, this section analyses whether the Paris-alignment methodologies: (1) include a clear commitment to public availability of Paris-alignment assessments of individual MDB operations, and (2) require the inclusion of alignment considerations in the monitoring and reporting processes (such as intermediate and ex-post evaluations) of individual MDB operations.

This section also looks at whether the MDBs' Paris-alignment methodologies have clear commitments to regularly reviewing and updating those same methodological documents, including lessons learned, new international developments, and the latest science. Additionally, in this context, this section examines whether there are clear commitments to setting up participatory processes, including consultations with different stakeholders, for the Paris-alignment methodologies' planned reviews and updates.

Regarding participation, this section also analyses whether the methodologies anticipate a process to obtain input from a range of stakeholders when conducting alignment assessments of a particular MDB operation in the planning stage. This section also examines the possibility of recourse on the grounds of an MDB operation's non-alignment, such as through existing redress or complaint mechanisms.



SCOPE FOR IMPROVEMENT

- Neither the joint methodological principles nor the MDB Paris-alignment methodologies include a commitment to making the full Paris-alignment assessment of their individual operations (including details on applying certain assessment tools) public. In practice, the IDB, for example, does disclose a full climate change annex for most of its new operations, including information on the assessment.
- Neither the joint methodological principles nor the individual Paris-alignment methodologies require the inclusion of alignment considerations in their operations' intermediate and final reports and ex-post evaluations.
- While all MDBs commit to reviewing and updating their Paris-alignment methodologies, only the EBRD commits to an annual review, with updates as required. All MDBs should further specify the process of reviewing and updating their methodologies in terms of regular timelines for review and collecting feedback from a range of stakeholders, including civil society. Though the EBRD and AIIB methodologies specifically refer to public consultation and the inclusion of feedback from a range of stakeholders, their methodological documents do not clarify how specific processes are defined. Some banks do not refer to such consultative processes in their methodological documents but still announce them on their website.
- None of the MDBs' Paris-alignment methodologies foresee the possibility of recourse on the grounds of a project's Paris non-alignment (e.g. through redress or complaint mechanisms).
- The Paris-alignment methodologies also do not require MDB personnel to contact or consult with relevant national stakeholders and other actors, including civil society, to obtain pertinent information for assessing an MDB operation's alignment.
- A full commitment is required by all MDBs to full transparency of Paris alignment assessments, regular participatory reviews of the methodologies, stakeholder participation in project assessments, and recourse options on the basis of a project's non-alignment.

Brief conclusions

No single MDB scores notably well or poorly across all categories assessed in this paper. The paper identifies good practices and scope for improvement for all the Paris-alignment methodologies assessed. However, there are a few assessment categories that are insufficiently addressed by all these methodologies, including the joint methodological principles. These categories include the methodologies' coverage of all potentially misaligned operations, transparency of alignment assessments of individual operations, as well as participatory processes, when assessing operations' alignment, considerations of indirect impacts on countries' mitigation pathways (e.g. unintended overall emissions increases), and considerations of intangible risks from climate hazards.

Notably, the EBRD's methodology contains a range of good practices that could provide guidance for strengthening the joint methodological principles and other MDBs' individual methodologies. This includes its clear commitment to the 1.5°C goal, its explicit requirement that its operations do not undermine resilience in the context in which they operate, its requirement for all its FIs to commit to Paris alignment and provision of respective steps to monitor progress on FIs' transition plans, and its detail on how just transition considerations will be applied. However, the methodologies of all MDBs assessed, including the EBRD's, require further improvement and strengthening.

A good theoretical methodological approach for Paris alignment does not necessarily lead to Paris-aligned MDB operations in practice. Their practical application requires additional analysis to generate insights on the MDBs' progress toward their self-set Paris-alignment commitments. One such mismatch between theory and practice is how, in April 2024, the EBRD approved a controversial North Macedonia gas project (PN 51747), which experts from civil society consider to cause carbon lock-in. The EBRD's methodology, however, theoretically requires carbon lock-in risks to be assessed and, if identified, reduced. This also underscores the need for all Paris-alignment assessments of MDB operations to be transparent and publicly available.

The imprecise language used in methodologies (e.g. 'technically feasible' and 'financially viable'; 'low' or 'material' risks from climate hazards or lock-in risks) and the lack of clearly defined thresholds leave scope for interpretation in the MDBs' methodologies. This opens loopholes that could lead to approval of non-aligned operations.

The joint methodological principles for Paris alignment greatly need review and further strengthening based on the scope for improvement identified in this paper. However, given that the principles are only a lowest common denominator of the joint MDB group in their alignment process, individual MDBs also should go beyond them and close existing loopholes in their individual Paris-alignment approaches.

1 Introduction

1.1 MDBs and Paris alignment

The multilateral development banks (MDBs) play a considerable role in climate transition. As of 2017, MDBs collectively had already committed to supporting countries in implementing the Paris Agreement. In 2018, at the 24th Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP24) in Katowice, Poland, the MDBs announced a joint framework for aligning their activities with the Paris goals.¹

The framework consists of six 'building blocks' (BBs): (1) alignment with mitigation goals, (2) adaptation and climate-resilient operations, (3) accelerated contribution to the transition through climate finance, (4) engagement and policy development support, (5) reporting, and (6) alignment of internal activities. A joint MDB working group was convened to develop methods and tools to operationalise these efforts under each BB, and at each subsequent COP, the MDBs have presented updates on their alignment framework.²

At both COP27 and COP28, Parties to the United Nations Framework Convention on Climate Change (UNFCCC) called on the MDBs to substantially step up their climate change-related actions. The COP28 Global Stocktake text 'calls on multilateral development banks and other financial institutions to further scale up investments in climate action and calls for a continued increase in the scale, and effectiveness of, and simplified access to, climate finance, including in the form of grants and other highly concessional forms of finance.' In June 2023, the G20 Independent Expert Group also recommended that MDBs adopt a triple mandate of eliminating extreme poverty, boosting shared prosperity, and contributing to global public goods, including climate, and that they triple sustainable lending levels by 2030. MDBs' ambitious implementation of their Paris alignment commitments is imperative toward their ability to respond to these calls.

The year 2023 was critical in the MDBs' progress on Paris alignment, as several banks of the joint MDB working group on Paris alignment reached their self-set deadline for achieving alignment of new operations: the European Bank for Reconstruction and Development (EBRD) and Inter-American Development Bank (IDB) by 1 January 2023, and the Asian Infrastructure Investment Bank (AIIB), Asian Development Bank (ADB), and World Bank by 1 July 2023 (with the limitation that for non-sovereign operations of the latter two, only 85% of new operations would be aligned by that date, while the remaining 15% were to follow by July 2025). The African Development Bank (AfDB) has committed to aligning new operations with building blocks 1, 2, and 3 by December 2023, and to complete alignment by December 2025. The European Investment Bank (EIB) claims to have already been Paris-aligned as of 1 January 2021. The Council of Europe Development Bank (CEB) and Islamic Development Bank (IsDB) aimed to be fully Paris-aligned by 1 January 2024, while the New Development Bank (NDB) committed to alignment by the end of 2026.

1 World Bank, 2018, *The MDBs' alignment approach to the objective of the Paris Agreement: working together to catalyse low-emissions and climate-resilient development* (accessed 16 January 2024). As of the first statement, the MDB group comprised the African Development Bank Group, Asian Development Bank, Asian Infrastructure Investment Bank, European Bank for Reconstruction and Development, European Investment Bank, Inter-American Development Bank Group, Islamic Development Bank, New Development Bank, and World Bank Group.

2 European Bank for Reconstruction and Development, 2023, *Joint MDB Event: MDB Paris Alignment Progress Update* (accessed 20 March 2024).

Paris alignment dates	Bank
1 January 2021	EIB
1 January 2023	EBRD, IDB, CEB (direct financing)
1 July 2023	ADB (non-sovereign operations: 85%), AIIB, World Bank Group (except IFC and MIGA)
1 December 2023	AfDB (for BB 1, 2, and 3)
1 January 2024	IsDB, CEB (full alignment)
1 July 2025	ADB (full alignment), World Bank Group (full alignment)
1 December 2025	AfDB (full alignment)
31 December 2026	NDB

Table 1: Multilateral Development Banks' Paris alignment dates³

1.2 MDBs and their methodologies

Following their commitment, the group⁴ of MDBs published the Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment⁵ in June 2023. These laid out a common basis for defining Paris alignment for operations and conducting respective assessments. Additionally, in 2023, four MDBs – the EBRD⁶, IDB⁷, World Bank⁸ and AIIB⁹ – published adapted versions of that joint methodology. These individual versions interpret, adapt, and concretise the joint methodology's provisions and complement them with information and guidance on methods, sectors, regions, and individual institutional processes.

Adopted the Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment	Published individual methodologies based on the Joint Principles
ADB, AfDB, AIIB, CEB, EBRD, EIB, IDB Group, IsDB, NDB, World Bank Group	AIIB, EBRD, IDB Group, World Bank Group

Table 2: Multilateral Development Bank-authored Paris alignment methodologies as of March 2023

- ³ European Bank for Reconstruction and Development, 2023, *Joint MDB Event: MDB Paris Alignment Progress Update* (accessed 20 March 2024); African Development Bank Group, n.d., *Climate Change and Green Growth Strategic Framework* (accessed 20 March 2024).
- ⁴ Table 2 contains the list of MDBs that form part of that group.
- ⁵ World Bank, n.d., *Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment* (accessed 20 March 2024); by then, the group of MDBs was joined by the Council of Europe Development Bank (CEB).
- ⁶ European Bank for Reconstruction and Development, n.d., *EBRD Activities and Paris Alignment* (accessed 20 March 2024).
- ⁷ Inter-American Development Bank, n.d., *Paris Alignment: Aligning Financial Flows to the Goals of the Paris Agreement* (accessed 20 March 2024).
- ⁸ World Bank, n.d., *The World Bank Group and Paris Alignment: Instrument Methods* (accessed 20 March 2024); World Bank, n.d., *The World Bank Group and Paris Alignment: World Bank Group Sector Notes* (accessed 20 March 2024).
- ⁹ Asian Infrastructure Investment Bank, 2023, *Methodology for Assessing the Alignment of AIIB Investment Operations with the Paris Agreement* (accessed 20 March 2024).

The MDBs emphasise that presented methodologies do not cover the entire MDB Paris alignment framework. Mainly they cover BB 1 (alignment with mitigation goals) and 2 (adaptation and climate-resilient operations). They also relate to BB 5 (reporting). The other BBs and themes are, according to the MDBs, addressed separately through joint and individual bank strategies and facilities. The MDBs also emphasise that these methodologies are not intended to increase climate finance, which they claim is covered by the separate BB 3 and separate commitments. They also do not intend to mainstream climate considerations in wider MDB processes, which the MDBs argue is covered under their climate strategies. The presented Paris alignment methodologies are, thus, mainly due diligence and risk mitigation instruments for individual operations, based primarily on a do-no-harm approach. However, the assessment framework developed for this paper is based on the underlying conviction that the different Paris alignment BBs that MDBs identified are strongly linked and cannot be considered in isolation.

The MDB joint methodological principles cover direct investment lending operations, policy-based lending operations, intermediated financing, and general corporate purpose finance in separate documents. The World Bank's methodology consists of multiple documents on separate approaches for different financial instruments. The AIIB, EBRD, and IDB have published their methodology in one document. All methodologies include annexes specifying details on Paris alignment tests for different sectors.

Bank	Methodological documents
MDBs jointly	<p>Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment of New Operations, consisting of:</p> <ul style="list-style-type: none"> • Direct investment lending operations • Intermediated financing • General corporate purpose financing • Policy-based lending operations • Direct investment lending operations – List of Activities Considered Universally Aligned with the Paris Agreement's Mitigation Goals or Not Aligned with the Mitigation Goals
AIIB	<p>Methodology for Assessing the Alignment of AIIB Investment Operations with the Paris Agreement – Covering direct investment operations and intermediated investment operations, and including annexes on: joint MDB universally aligned or non-aligned lists, sector-specific approach for investment (BB1), sector-specific approach for direct investment operations (BB2), and Suggested Outline for Paris Alignment Action Plan</p>
EBRD	<p>Methodology to determine EBRD investments' Paris Agreement alignment, covering directly financed EBRD investments, indirectly financed EBRD investments, other financial instruments used by the EBRD, and including annexes on: links between the EBRD's Paris alignment methodology and other processes, joint MDB 'aligned' and 'not aligned' project lists, economic assessment of EBRD projects with high greenhouse gas emissions, determining the Paris Agreement alignment of EBRD investments – sectoral application, and high-emitting sectors</p>
IDB Group	<p>IDB Group Paris Alignment Implementation Approach: Principles, Methodology, and Technical Guidance, covering investment loans, policy-based loans, guarantees, equity, long-term corporate finance, and investment grants, including dedicated conclusions on enabling conditions for successful implementation, and including annexes on activities considered universally aligned and not aligned with the Paris mitigation goals</p>

World Bank

The World Bank Instrument Methods for Paris Alignment, consisting of:

- World Bank Paris Alignment Method for Investment Project Financing
- World Bank Paris Alignment Method for Development Policy Financing
- World Bank Paris Alignment Method for Investment Project Financing
- World Bank Paris Alignment Method for Program for Results
- Agriculture and Food – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Digital Development – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Education – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Energy and Extractives – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Environment, Natural Resources and Blue Economy - Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Health, Nutrition and Population – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Social Protection and Jobs – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Social Sustainability and Inclusion – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Transport – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Urban, Resilience, Disaster Risk Management, and Land – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods
- Water – Sector Note on Applying the World Bank Group Paris Alignment Assessment Methods

Table 3: The Multilateral Development Banks' joint principles for Paris alignment and related individual bank methodologies – Overview of related documents¹⁰

Not all MDBs have published dedicated Paris alignment methodologies. The ADB, for example, uses the joint MDB principles and has internal guidance for implementation, but it has not published its own methodology. The International Finance Corporation (IFC), the World Bank Group's private sector arm, also uses the joint MDB principles but has not published its own methodology. The alignment methodologies the World Bank has published do not cover the IFC or Multilateral Investment Guarantee Agency (MIGA) operations. Therefore, any reference to the World Bank herein excludes the IFC and MIGA. The IDB Group's Paris alignment implementation approach applies to both the IDB and IDB Invest (the IDB Group's private sector arm).

The EIB presents its overall approach to Paris alignment of operations in a dedicated chapter of its Climate Bank Roadmap¹¹ and specifies some aspects for financial intermediaries (FIs) and corporates in its PATH

¹⁰ Asian Infrastructure Investment Bank, 2023, *Methodology for Assessing the Alignment of AIIB Investment Operations with the Paris Agreement* (accessed 20 March 2024); European Bank for Reconstruction and Development, n.d., *EBRD Activities and Paris Alignment* (accessed 20 March 2024); Inter-American Development Bank, n.d., *Paris Alignment: Aligning Financial Flows to the Goals of the Paris Agreement* (accessed 20 March 2024); World Bank, n.d., *Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment* (accessed 20 March 2024); World Bank, n.d., *The World Bank Group and Paris Alignment: Instrument Methods* (accessed 20 March 2024); World Bank, n.d., *The World Bank Group and Paris Alignment: World Bank Group Sector Notes* (accessed 20 March 2024).

¹¹ European Investment Bank Group, 2020, *EIB Group Climate Bank Roadmap 2021–2025*, (accessed 16 January 2024).

Framework.¹² However, these documents provide comparatively decentralised and scarce methodological information. These aspects might at least partly owe to their being published before the joint MDB principles were finalised and are not based on those principles. This paper, therefore, does not separately analyse the EIB's Paris alignment approach as the approach provides insufficient details to allow for a fair and comprehensive assessment.

1.3 Purpose and scope of this paper

MDBs urgently need to ensure the highest standards in their Paris alignment methodologies. This is because they channel an average of over USD 100 billion annually in development finance to client countries¹³ and play a pioneering role in the financial sector; they are often followed by other financial institutions, companies, and governments in setting standards. Additionally, along with providing direct project finance, MDBs tend to move away from well-defined projects and toward rather loosely defined programs, including special government funds and general corporate finance, budget finance, and trade finance. Many MDBs also conduct policy research, and country and sector diagnostics, offer technical assistance, and provide policy-based and intermediated finance. These can all have a substantial positive (or negative) climate-related impact on the capital stock, policies, laws, and institutions in the countries in which they operate.

This analysis aims to highlight both shortcomings and best practices in the design of current methodologies, with a particular view to providing constructive input for the methodologies' upcoming reviews and revisions.

This paper analyses the MDB Paris alignment methodologies published by the AIIB,¹⁴ EBRD,¹⁵ IDB¹⁶ and World Bank¹⁷ and the joint MDB methodological principles,¹⁸ against a set of stringency, scope, effectiveness, and transparency criteria. The analysis also includes the MDB joint methodological principles, enabling recommendations for improving a document that serves as a main reference for developing further methodologies of particular MDBs. Its inclusion also allows the individual approaches to be compared with their joint basis. The analytical framework includes a criterion examining the sectoral annexes and their contributions to fulfilling other criteria of the analytical framework.

The applied criteria were developed based on work by a research consortium¹⁹ on the MDBs' Paris alignment processes over the years (see section 3.1 [Assessment categories] for details on the indicators). The analysis is mainly informed by a desk review of the joint MDB principles and the four individual methodologies, and by comments and feedback provided by MDB personnel on preliminary results of the analysis, and/or by dedicated discussions with the MDBs. However, note that this paper and its findings are not endorsed by the MDBs and are the sole responsibility of Germanwatch. The analysis concentrates exclusively on the publicly available methodological documents' content and does not cover their operationalisation.

Section 3 gives further details on the analytical framework used and an overview of the analytical categories.

¹² European Investment Bank Group, 2021, *The EIB PATH Framework. Supporting Counterparties on Their Pathways to Align with the Paris Agreement* (accessed 16 January 2024).

¹³ Figures from 2022: Congressional Research Service, 2023, *Multilateral Development Banks: Overview and Issues for Congress* (accessed 16 January 2024).

¹⁴ Asian Infrastructure Investment Bank, 2023, *Methodology for Assessing the Alignment of AIIB Investment Operations with the Paris Agreement* (accessed 20 March 2024).

¹⁵ European Bank for Reconstruction and Development, n.d., *EBRD Activities and Paris Alignment* (accessed 20 March 2024).

¹⁶ Inter-American Development Bank, n.d., *Paris Alignment: Aligning Financial Flows to the Goals of the Paris Agreement* (accessed 20 March 2024).

¹⁷ World Bank, n.d., *The World Bank Group and Paris Alignment: Instrument Methods* (accessed 20 March 2024); World Bank, n.d., *The World Bank Group and Paris Alignment: World Bank Group Sector Notes* (accessed 20 March 2024).

¹⁸ World Bank, n.d., *Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment* (accessed 20 March 2024).

¹⁹ The consortium consists of Germanwatch, the NewClimate Institute, World Resources Institute, and, since 2023, E3G. The German Ministry of Economic Cooperation and Development has funded its work. An overview of related publications can be found at: <https://www.germanwatch.org/en/node/87721>.

ries and criteria. Section 4 presents the results for each analytical category reviewed and includes shorter analyses by MDB. A box highlights each MDB's positive elements and scope for improvement. Section 5 contains the main conclusions and recommendations for the MDBs' future work conducted in the review of their methodologies.

2 Methodology

This section introduces the analytical framework for reviewing the MDBs' joint methodological principles for Paris alignment and their particular alignment methodologies that provide further detail on how to operationalise the joint principles. The first subsection covers the analytical framework's overarching categories, which look at a combination of different elements that MDBs should consider regarding Paris alignment. The elements are based on the Paris Agreement goals and previous work related to MDBs' Paris alignment.²⁰ The indicators break these larger categories down to assess steps needed in each category to ensure Paris alignment. In most cases, alignment requires taking all steps in combination as, individually, they do not ensure fully aligned operations. These indicators are formulated as questions with a 'yes,' 'partially,' or 'no' answer. In section 4, further detail on the specific indicators used in this analysis, which serve to operationalise the criteria, are included as part of the analysis itself.

The categories and their indicators collectively assess the steps taken to ensure alignment with the Paris mitigation and adaptation goals, including, but not limited to, alignment with Nationally Determined Contributions (NDCs) and other national plans, and with other relevant commitments included in the agreement, such as a just transition and human rights obligations. Further categories are added, for example, to ensure alignment of MDBs counterparties, which requires a separate approach. Finally, some are included to ensure that the methods' application follows certain principles of transparency and participation, and that they are applicable to the broadest possible scope of operations. This section's final part covers critical reflections on the assessment's limitations.

2.1 Assessment categories

The applied assessment framework covers key aspects necessary for the methodologies to successfully assess MDB operations for Paris alignment. It encompasses six overarching criteria by which the MDB methodologies are evaluated: scope of the methodology, alignment with national and international climate policies and targets, additional sector-specific guidance, consideration of transition risks, Paris alignment of counterparties, and transparency and participation. Most criteria apply equally to all MDBs' main instruments, whether direct investments, policy-based lending, or programmes for results,²¹ as these criteria and indicators are relevant to all these instruments. Indirect investments are the only exception. As mentioned, assessing the Paris alignment of the MDBs' counterparties requires a different approach, as MDBs have an indirect role in counterparty alignment. In this case, we added a separate criterion looking specifically at this alignment.

The categories and their respective criteria were selected for the following reasons.

20 World Resource Institute, 2018, [Toward Paris Alignment: How the Multilateral Development Banks Can Better Support the Paris Agreement](#) (last accessed on 21/03/2024); Germanwatch & NewClimate Institute, 2018, [Aligning Investments with the Paris Agreement Temperature Goal](#) (last accessed on 21/03/2024); Germanwatch, NewClimate Institute & World Resources Institute, 2020, [Raising the Game on Paris Alignment](#) (last accessed on 21/03/2024); Germanwatch, NewClimate Institute & World Resources Institute, 2021, [Aligning Financial Intermediary Investments with the Paris Agreement](#) (last accessed on 21/03/2024); World Resources Institute, Germanwatch & NewClimate Institute, 2022, [Aligning Policy-Based Finance with the Paris Agreement](#) (last accessed on 21/03/2024).

21 Though not all MDBs use all these instruments, these were assessed for each bank when available.

Scope of the methodology: To generate the transformative impact necessary to align MDB financing with the Paris Agreement, the methodologies should cover a wide range of MDB operations and go beyond individual operations to support adjustment of institutional processes and policies needed to ensure operations' Paris alignment.

Alignment with national and international climate policies and targets: The needs to ensure alignment with 1.5°C-compatible mitigation pathways and responsiveness to risks and vulnerabilities from climate hazards are directly derived from the objectives of the Paris Agreement, the most important binding international climate policy. Notably, consistency with national climate goals and policies should be ensured to take countries' individual and differentiated approaches into account; this also responds to the MDBs' demand-driven way of working with partner countries. Helping countries reach Paris goals also requires transformative efforts that go beyond a do-no-harm approach, which is why we assessed the methodologies for guidance on proactively seeking opportunities for climate action. Finally, the Paris Agreement also points to the importance of complying with human rights obligations when undertaking climate action.

Additional sector-specific guidance: To facilitate and enable operationalisation of the Paris alignment approach in the practice of project teams, additional sector-specific guidance is needed. This guidance breaks down the task of alignment assessment and provides guidance on adequate tools and benchmarks.

Consideration of transition risks: Transitioning to climate neutrality can have substantive negative social and economic impacts. Therefore, considerations of a just transition are needed to avoid detrimental effects on a country's development.

Paris alignment of counterparties: Investments in FIs and corporate counterparties also should be aligned to ensure the alignment of all MDBs' finances.

Transparency and participation: Transparency on Paris alignment assessments' methods and results is necessary for enabling accountability. Making Paris alignment a participatory process can help improve perspectives' quality, comprehensiveness, and inclusiveness. Regular review of the methods is imperative for being able to incorporate lessons MDBs learned and respond to other relevant stakeholders' experiences, criticism, and proposals.

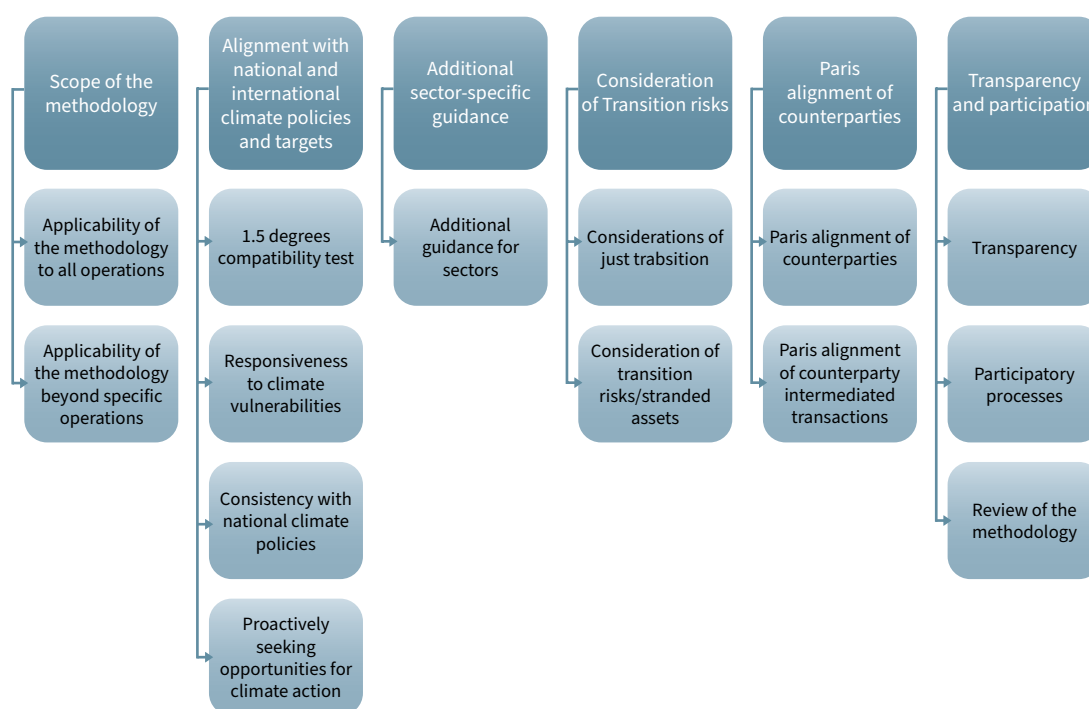


Figure 1: Overview of all assessment categories

2.2 Limitations

While the framework herein aims for a comprehensive analysis of the MDB Paris alignment methodologies, it does not evaluate the quality or appropriateness of specific tools MDBs use to undertake the Paris alignment tests. This includes their sectoral notes or guides, for which the analysis only looks more generally at whether they exist and whether they add information on the indicators, but does not do a detailed analysis of their quality.²² This is partly because (apart from the sector notes) such in-depth information is not always readily available on MDB websites, and partly to limit this paper's focus to a general appraisal of MDBs' Paris alignment methodologies.

A related limitation is that, in evaluating the indicators, we concentrated solely on the methodologies' content. MDBs might have published information separately from the methodologies and that could be relevant to the indicators but was not considered in our analysis, such as the environmental and social frameworks or information disclosure policies. This is also because MDBs' methodologies do not always provide information on which other tools, guidance, or policies are relevant to the analysis of specific aspects of Paris alignment, and in which ways. Most MDB methodologies generally do not establish clear linkages to other existing policies and frameworks relevant to Paris alignment or clearly explain how these other policies and frameworks contribute to alignment. The only exception is the EBRD, whose methodology includes an annex stating links between the Paris alignment methodology and other EBRD processes.

²² For an analysis of the World Bank sector notes, see NewClimate Institute, 2023, [The World Bank's Sector Notes Encourage the Consideration of Transitions, but Lack Sufficient Detail to Ensure Full Alignment with the Paris Agreement](#) (accessed 21 March 2024).

3 Paris Agreement Alignment of MDBs – State of Play

This chapter presents the analysis results. The overall trends across the analysed MDBs are given for each category. Then, the results for the indicators of each category are detailed, tracing differences and best practices among the four MDBs and highlighting opportunities for strengthening approaches.

3.1 Scope of the methodology

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Scope of the Paris alignment methodology	Applicability of the methodology to all MDB operations	Does the methodology foresee a comprehensive Paris alignment assessment of all potentially non-aligned operations?	–	–	–	–	–
	Paris alignment mainstreaming in MDB internal structures and processes more generally beyond certain operations	Does the methodology include assessments of the MDB's policies and internal structures beyond just focusing on specific operations?	–	–	✓	–	–

 Yes
  Partially
  No

Table 4: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Scope of the methodology'

This indicator addresses

- MDB methodologies' applicability to the spectrum of MDB operations
- Consideration of elements relevant for Paris alignment that go beyond the project level

The scope of MDBs' Paris alignment assessments of projects is limited. On the one hand it is limited by the choice of instruments and financing thresholds to which the methodologies are initially applied and on the other by exceptions within the methodologies themselves regarding which operation subcategories the tests are applied to and whether they are applied fully, partially, or not at all.

Regarding the methodology's internal restriction of scope, all methodologies apply a two-phased approach wherein only operations that do not fall under the joint MDB List of Activities Considered Universally Aligned or Not Aligned with the Paris Agreement's Mitigation Goals²³ undergo a specific evaluation for Paris alignment. The application of these lists is discussed below, to address whether it enables a comprehensive Paris Agreement assessment of all potentially non-aligned operations. Apart from this list, there are further exemptions regarding the application of the methodologies' tests to financing directed to FIs and corporate counterparties, as discussed in the respective chapter.

3.1.1 Applicability of the methodology to all financing types and financial instruments

For the first restriction in scope, notably, MDBs do not conduct Paris alignment assessments for all types of projects and instruments.. The IDB specifies that, except for IDB Lab projects, the Paris Alignment Implementation Approach (PAIA; the IDB Group's Paris alignment methodology) starts at an 'approved amount greater than US\$3 million.' Furthermore, and '[c]onsistent with practice at other MDBs, the PAIA does not cover technical assistance or short-term financial instruments and does not apply to credit facilities for natural disasters and public health emergencies, nor to special development loans. Fee-based advisory and knowledge services are also not covered by the PAIA.' Similar limitations apply at other MDBs; for example, most do not specifically refer to technical assistance operations, or activities. While other MDBs may also use similar amount-related thresholds for applying their methodologies, their methodologies do not specify the thresholds. Only the EBRD specifies that 'the methodology covers the full suite of financial instruments and financing types the Bank may use,' also including technical cooperation.

3.1.2 List of activities considered universally aligned with the Paris Agreement's mitigation goals

According to the joint MDB principles,²⁴ '[t]he Universally Aligned List of activities includes those activities that contribute to climate action consistent with the mitigation goals of the Paris Agreement under all circumstances, and those that have no material impact on climate change, as they do not harm countries' transition to long-term low-greenhouse gas (GHG) emissions development pathways and do not lead to lock-in of carbon-intensive patterns.' The list consists of information on 'eligible operation types' by sector, and additional guidance and conditions. Its content decisively determines which activities undergo a Paris alignment assessment for mitigation and which do not.

Most of the assessed methodologies use this Universally Aligned List in the form contained in the joint principles. Applying this list leads to a major share of operations not undergoing a specific Paris alignment assessment, which is problematic.

No exclusion of operations that might indirectly encourage fossil fuel use

Regarding fossil fuels, the list includes a preface stating that all operation types listed to be universally aligned must still go through the specific criteria assessment if any of the following apply:

- economic feasibility depends on external fossil fuel exploitation, processing, and transport activities
- economic feasibility depends on existing fossil fuel subsidies
- significantly rely on the direct use of fossil fuels

²³ World Bank, 2023, *Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment of New Operations: Direct Investment Lending Operations – List of Activities Considered Universally Aligned with the Paris Agreement's Mitigations Goals or Not Aligned* (accessed 16 January 2024).

²⁴ World Bank, 2023, *Joint MDB Methodological Principles for Assessment of Paris Agreement Alignment of New Operations*, p. 4 fn. 4 (accessed 16 January 2024).

While these specifications might be counterintuitive to the spirit of an inclusion list (allegedly for enabling a quick screening to determine cases where no further action is required under any circumstances), they might also leave room for non-aligned activities. Even if an investment's economic feasibility does not depend on fossil fuels, it might still encourage their use, counter to achieving the Paris goals. For example, transmission and port infrastructure could inadvertently support fossil fuels even if not depending on them economically,²⁵ or in building new roads, road upgrading might induce deforestation and substantial emissions increases and lead to illegal roads being built.²⁶

Two main options could be considered for improving the Universally Aligned List of operation types to avoid indirect encouragement of fossil fuel use:

(1) The MDBs could revise the Universally Aligned List's 'preface' on fossil fuels to determine whether operations on the list should undergo a shorter specific assessment, focused on assessing and managing lock-in and transition risks. This should occur if they are related to (a) the expansion of oil and natural gas production, (b) new infrastructure for further processing or transportation of coal, oil, and natural gas (e.g. new gas pipelines or liquefied natural gas export terminals), and (c) activities that increase the demand for natural gas or oil (e.g. new gas-fired power plants not primarily used to meet peak load and stabilise grid frequency, oil for heating, or gas for cooking and heating when renewables combined with electrification are an alternative)²⁷

This measure would allow MDBs to account for country-specific circumstances, in line with the 'common but differentiated responsibilities' principle. MDBs could consider that some countries may need to focus on enhancing their policy frameworks and building the necessary environment to fully transition away from fossil fuels before a full transition can be implemented, while ensuring that short-term investment decisions do not lock these countries into a long-term high-carbon development pathway. In this case, it would be even more relevant for MDBs to play a stronger role in supporting policy development and country policies' alignment with the Paris goals, at all levels, including through their upstream engagement.

(2) Alternatively, the MDBs could remove items from the Universally Aligned List that can indirectly encourage the use of fossil fuels even if not depending on them directly, such as:

- Energy: Electricity transmission and distribution – Transmission infrastructure can inadvertently support coal, oil, or gas power plants.
- Transport: Short-sea shipping of freight ships – Short-sea shipping can include oil, gas, or coal off-lifted from offshore terminals and brought to or from port.
- Transport: Inland waterway freight transport vessels – Freight transport vessels could support coal, oil, or gas transport, especially in countries expanding fossil fuel extraction operations.
- Transport, rail infrastructure – This could benefit new coal, oil, and gas production.
- Transport, port infrastructure (maritime and inland waterways) – Port projects could support the expansion of fossil fuel exports and/or imports.

The second option would be more aligned with the general purpose of an inclusion list to clearly determine cases without further need for action. Items removed must then undergo a specific assessment to check whether they might benefit the use of fossil fuels and rule out this possibility by including respective safe-

25 Urgewald, 2022, *Suriname's Oil Development Made Possible by IMF, IDB and World Bank Public Finance* (accessed 16 January 2024).

26 Reuters, 2020, *Amazon Road-building Could Deforest Millions of Hectares – Report* (accessed 16 January 2024).

27 See International Energy Agency, 2022, *World Energy Outlook 2022* (accessed 23 January 2024); International Institute for Sustainable Development, 2022, *Navigating Energy Transitions: Mapping the road to 1.5°C* (accessed 23 January 2024); Intergovernmental Panel on Climate Change, 2022, *Climate Change 2022: Mitigation of Climate Change* (accessed 23 January 2024); Intergovernmental Panel on Climate Change, 2021, *Climate Change 2021: The Physical Science Basis* (accessed 23 January 2024); NewClimate Institute, Germanwatch, 2022, *German Support for Gas Investments abroad is Mostly not Compatible with the Paris Agreement* (accessed 23 January 2024); NewClimate Institute, 2021, *The Kenyan Cooking Sector – Opportunities for Climate Action and Sustainable Development* (accessed 23 January 2024).

guards in the project design. This would also allow the banks to consider such investments in the context of countries' 'common but differentiated capabilities.'

Unspecific wording and missing thresholds open loopholes

A second, related shortcoming of the Universally Aligned List is that the wording of some eligible operation types leaves scope for interpretation of which projects are covered. Examples of such wordings are terms like 'negligible lifecycle GHG emissions,' 'using significant renewable energy,' and 'non-energy-intensive industry' without specifying respective thresholds. The same is true for the 'preface' on fossil fuels, where it is unclear how 'economic feasibility' is determined and what the threshold is for 'significantly relying on the direct utilization of fossil fuels.'

In this regard, the IDB sector notes should be seen positively, as they concretise many subcategories on the list by adding details on the types of activities included. All MDBs should specify and harmonise thresholds to ensure compatibility with Paris goals and uphold coherent standards for their partner countries.

Missed opportunities to promote further climate benefits

The third limitation with the Universally Aligned List is that the operations considered to have 'no material impact on climate change' (do-no-harm category) will not be systematically screened for opportunities to enhance their climate benefits, and the activities viewed to contribute to climate action will not be evaluated on potentially feasible alternative, even more climate-effective, measures. For example, for forestry, there are substantial qualitative differences between afforestation, reforestation, sustainable forest management, and forest conservation regarding their climate-positive effects. This factor should be considered when using limited MDB financial resources. As another example, electricity transmission lines not directly linked to a single source of generation should include consideration of the future electricity system, which should connect areas of renewable energy potential to demand centres. This consideration is because the location for renewable energy potential could differ substantially from locations of fossil-based electricity generation. Similarly, road upgrading and rehabilitation should be evaluated in the context of a transport sector assessment to ensure the possible prioritisation of rail infrastructure and public transport. To avoid missed opportunities and to promote further climate benefits, the MDBs should still conduct a check on (1) whether an operation and its activities can contribute to climate-related priorities of a country, and (2) instituting some form of alternatives assessment.

3.1.3 List of activities considered universally not aligned with the Paris Agreement's mitigation goals

At the same time, the 'list of activities considered universally not aligned with the Paris Agreement's mitigation goals' (Universally Non-aligned List) is currently limited to mining of thermal coal, electricity generation from coal, peat extraction, and electricity generation from peat. The list does not include new investments in expansion of upstream and midstream fossil gas or oil. Those investments would not be aligned with the Paris Agreement as they risk locking countries into high-emissions development pathways or resulting in stranded assets.²⁸

Banks' individual policies often go beyond the joint Universally Non-aligned List,²⁹ which can be regarded as a least common denominator between the policies of those MDBs. Also, according to MDB governance, the Universally Aligned/Not Aligned Lists as well as the joint MDB methodological principles for Paris alignment are technical documents lacking the legal effect of a policy or strategy. However, the MDBs, as part of their joint commitment to Paris alignment and to do no harm to climate goals, should work on progressively expanding their joint exclusion list to align with long-term net zero scenarios, while ensuring in the short term that their investments do not lock countries into high-emissions development pathways or result in

²⁸ International Energy Agency Net Zero Emissions by 2050 Scenario (NZE).

²⁹ For an overview, see E3G's Public Bank Tracker Matrix, MDB matrix, indicator on mitigation, sub-indicator on 'Fossil fuel exclusion policies'.

stranded assets. The Universally non-aligned list would need to include more guidance and restrictions on operations and activities such as 'road upgrading' to prevent negative climate effects.

3.1.4 Paris alignment mainstreaming in MDB internal structures and processes beyond particular operations

Most MDB methodologies focus exclusively on assessing specific operations and do not include additional evaluation of the MDBs' own policies, processes, capacities, and internal structures. This tendency neglects that the Paris alignment process' intended 100%-aligned operations outcome requires solid mainstreaming of Paris alignment considerations into all operations from the operations' inception. Many steps that happen before an operation's financing contract is signed, and the broader diagnostic and strategic work is undertaken, need to be included, such as country diagnostics, country partner dialogue, formulation of country strategies, sector approaches, country policy and sector diagnostics, detection of technical assistance needs, selection of priority operations with the country, and partner coordination.

Foremost, Paris alignment should be mainstreamed in formulating project objectives and results indicators, and in monitoring and evaluation. Paris alignment considerations should also be included in other policies that MDBs rely on for their assessments, including, most prominently, their environmental and social frameworks. Merely 'adding' Paris alignment considerations to already defined project proposals will limit their effect and create delays that prevent selection of the most transformational and impactful projects to support the Paris goals³⁰, while significant indirect adverse effects might be overlooked.

While MDBs emphasise that their Paris alignment methodologies are solely intended to cover the assessment of operations under BB1 and BB2, they could also suggest processes and measures beyond the design of specific operations to facilitate their alignment under those BBs. This added measure might require effort but it can encourage a systematic approach to such necessary processes and make a convincing case for an MDB's commitment. Such processes and measures should be mentioned and explained in the Paris alignment methodologies if they are already reflected through other existing commitments or policies. Including clear linkages to other MDB policies, frameworks, and commitments related to Paris alignment and mainstreaming could, thus, improve the methodologies' clarity and usefulness. Such linkages would give a comprehensive view of the MDBs' efforts for full alignment with the Paris goals.

The IDB methodology sets a positive example here, as it lays out what the IDB considers necessary for building internal capacities and adding human resources, including in country offices; revising operational procedures; reforming diagnostic, programmatic, and strategic approaches; and engaging with partners and clients to implement Paris alignment at the bank. While this partly gives the methodology the character of a planning document, demonstrating the IDB's comprehensive and ambitious approach to Paris alignment and its commitment to transparency regarding the process has great value.

³⁰ See, for example: Neunuebel, C., et al, 2022, 'Aligning Policy-Based Finance with the Paris Agreement.' Working Paper. Washington, DC: World Resources Institute (accessed 16 January 2024); CPI, I4CE, 2024, *Approaches to Meeting the Paris Agreement Goals* (accessed 16 January 2024).



SCOPE OF IMPROVEMENT

Most MDBs do not specifically include technical assistance operations in their Paris alignment approach. Some MDBs also specify that they apply their Paris alignment methodologies only to operations that pass a funding amount related threshold. Yet, it is important that the MDBs Paris alignment methodologies cover all types of finance and all financial instruments, independently of the funding amount.

The application of the Universally Aligned List is highly problematic as it might lead to a major share of operations not be specifically assessed for Paris Alignment even though those operations might support non-aligned activities.

- The lists preface on fossil fuels should be revised because even if an investment's economic feasibility does not depend on fossil fuels, it might still encourage their use
- Wording in the list that leaves scope for interpretation such as 'significant reliance on the direct use of fossil fuels' or 'negligible lifecycle GHG emissions' need to be specified by referring to concrete thresholds

Even if an operation is fully Paris aligned, by falling under the Universally Aligned List, it will not be systematically screened for opportunities to further enhance climate benefits.

The joint Universally Non-Aligned List does not cover new investments in expansion of upstream and midstream fossil gas or oil. The MDBs need to work on progressively expanding their joint exclusion list to align with long-term net zero scenarios.

Most MDB Paris alignment methodologies focus exclusively on assessing whether specific operations are BB1 and BB2 aligned and do not refer to additional considerations of the MDBs' own policies, processes, capacities, and internal structures. All BBs are systematically linked and MDBs should better reflect this linkage in their Paris alignment methodologies as well as linkages to other Paris alignment relevant MDB processes, policies, and commitments.



BEST PRACTICE

The EBRD Paris alignment methodology covers financial instrument and funding types, including technical assistance operations.

IDB sector notes concretize many subcategories on the Universally Aligned List and add details on types of activities.

The joint Universally Non-Aligned List can be considered a least common denominator and MDBs' individual policies often go beyond the joint Universally Non-aligned List.

The IDB Paris alignment methodology lays out what the IDB considers necessary for building internal capacities and adding human resources, including in country offices; revising operational procedures; reforming diagnostic, programmatic, and strategic approaches; and engaging with partners and clients to implement Paris alignment at the bank.

3.2 Consistency with national and international climate policies and targets

3.2.1 1.5°C compatibility test

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Alignment with national and international climate policies and targets	1.5°C compatibility test	Does the methodology include an assessment requiring the MDB operations' compatibility with the 1.5°C Paris Agreement goal using low-emissions pathways?					
		Does the methodology require an assessment for the MDB operations' indirect impacts on countries' mitigation pathways (particularly for policy-based financing)?					
		Is the method for assessing compatibility with the 1.5°C Paris Agreement goal public and transparent?					
		Does the methodology require an assessment of potential low-GHG design/technology alternatives for operations, including analysis of their feasibility and consideration of national/local context?					
		Is the method for assessing low-GHG alternatives public and transparent?					
		Does the methodology require assessment for MDB operations' lock-in risk?					
		Is the method for assessing lock-in risk public and transparent?					

		Does the methodology require identifying measures for an operation to reduce high lock-in risk? Including clear thresholds for the degree to which lock-in risks have to be reduced to be considered aligned.	✓	✓	✓	✓	✓
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 Yes
  Partially
  No

Table 5: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category '1.5 compatibility test'

The Paris mitigation goal is to hold the 'increase in the global average temperature to well below 2°C above pre-industrial levels and efforts to limit the temperature increase to 1.5°C above pre-industrial levels.' However, considering that limiting warming to 1.5°C will lead to far lower negative impacts than 2°C, the Glasgow Climate Pact included a resolution to pursue efforts for achieving 1.5°C.³¹ MDBs should align their methodologies with this lower temperature goal. This alignment will require that MDBs ensure their operations do not directly or indirectly hinder a country's long-term transition to net zero.

This section looks at a range of criteria that MDBs would need to fulfil to ensure that their operations are compatible with the Paris 1.5°C goal, including:

- The use of low-emissions pathways to assess operations' alignment with 1.5°C
- Consideration of an operation's potential indirect impacts on emissions, including in the short term and particularly for policy-based lending
- Consideration of low-emissions alternatives in an operation's design
- Assessment and management of potential lock-in risks
- Level of detail and transparency in relation to the tools and instruments used in the assessment's different parts

³¹ United Nations Framework Convention on Climate Change, 2022, Report of the Conferences of the Parties Serving as the Meeting of the Parties to the Paris Agreement on its Third Session, Held in Glasgow from 31 October to 13 November 2021, Glasgow Climate Pact on p. 2 (accessed 16 January 2024).

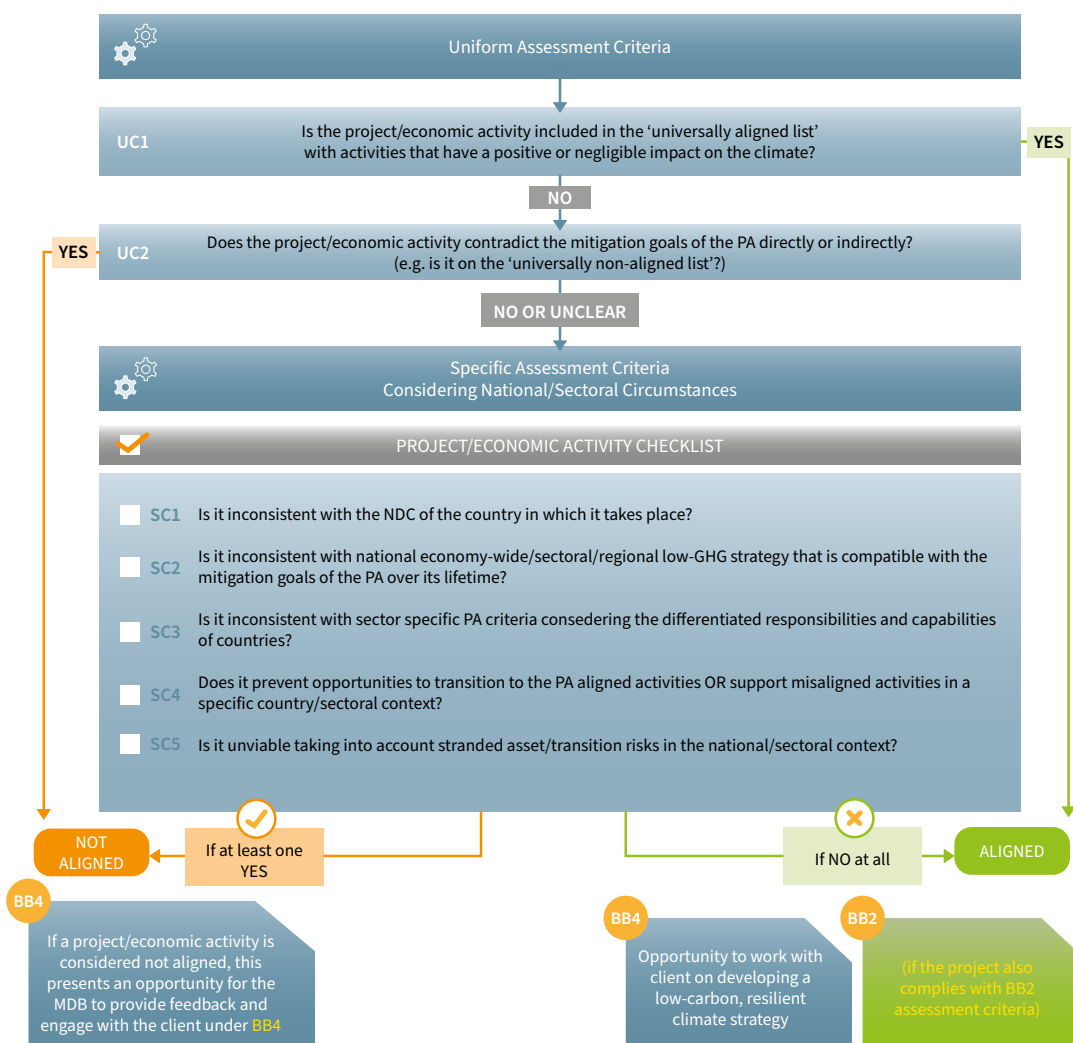


Figure 2: Joint MDB methodological principles; decision-making approach for determining direct investment lending operations' alignment with the Paris Agreement mitigation goals; based on a illustration by the World Bank

3.2.1.1 Use of low-emissions pathways

The joint MDB methodology, and MDBs' individual methodologies, include using low-emissions pathways, such as global and regional, or sectoral decarbonisation pathways, as a tool for assessing an operation or action's Paris compatibility. Yet, the joint principles as well as the particular methodologies from IDB, World Bank and AIIB only refer to the Paris Agreement temperature goal more generally (well below 2°C and pursuing efforts to limit the increase to 1.5°C). Different methodologies also introduce different degrees of flexibility in using these pathways. Even though this flexibility might be necessary, for example, whenever a credible pathway or benchmark is not available, it could also weaken the methodology. This also highlights the importance of transparency when applying the methodologies to particular MDB operations. For example, the EBRD's methodology states that the pathways are not meant to be prescriptive but rather to serve as a guide for evaluating the operations; they include a way of determining suitable for using pathways, and related benchmarks and criteria, to ensure the pathways are credible and aligned with the Paris mitigation goals. The AIIB, however, allows the use of a range of sources, data, and findings in the global literature on sector-specific decarbonisation pathways, including sector roadmaps and sector

scenarios that provide emissions thresholds. For the IDB, based on the recognition that multiple decarbonisation pathways exist, the methodology promotes the application of data and findings relevant to the specific context, while consistent with the best available science. The IDB includes the transaction costs for project preparation as part of the considerations for choosing the appropriate data.

Though the flexible use of low-emissions pathways is needed to allow for MDBs to respond to sector, country, and regional specifics, and for availability of information, MDBs should at least specify a commitment to aligning their operations with the Paris 1.5°C goal and, therefore, to goal-aligned pathways. Flexibility for using different pathways or other information sources, when appropriate, should be complemented with transparent choices of methods and information sources so that others can evaluate the specific tools used when assessing an operation's 1.5°C compatibility.

3.2.1.2 Consideration of indirect impacts

At the same time, the joint MDB methodology and most MDBs' individual methodologies do not look at their MDB operations' potential indirect impacts on countries' mitigation pathways (e.g. unintended overall emissions increases), which is particularly relevant but not limited to policy-based finance (PBF).³² These indirect impacts differ from lock-in risks in that the impacts can be immediate and temporary, and therefore not have a lock-in effect, yet they can result in increased emissions.

The World Bank includes an assessment of the system-level framework or value chain in which the operation will take place, focusing on the project's overall impact, and the policy and regulatory landscape, though only in its Investment Project Financing and Program for Results Paris alignment methodologies. It omits this crucial step in its Development Policy Financing methodology, where these indirect impacts are particularly relevant because they are not necessarily localised in specific areas or sectors, as is most likely true for other operation types, but can have broader macroeconomic, fiscal, and social impacts.³³ The IDB uses 'area of influence' and relevant present and reasonably foreseeable developments associated with an operation in its evaluations, based on its Environmental and Social Policy Framework (ESPF). However, similarly to the World Bank, the 'area of influence' concept often excludes PBF.

3.2.1.3 Assessment of alternatives

The joint MDB methodology and most of the individual MDB methodologies assessed have included an assessment of potential low-emissions design and technology alternatives. This is an important means for avoiding doing harm and for identifying the most transformational options. The joint methodology for direct investment includes a step comparing the operation with lower-emissions alternatives. In its economic viability test, the EBRD contains an assessment of the project against alternatives, using shadow carbon pricing. As part of its method for preventing lock-in emissions incompatible with long-term carbon neutrality, the IDB includes an assessment of alternative lower-emissions solutions that are technically and financially feasible. For its Investment Project Financing and Program for Results methods, the World Bank includes a step for checking whether the same objectives can be reached via means with lower emissions. Yet, the MDBs need to include an assessment of alternatives not only in their methodologies for direct investment lending, but also for intermediated finance and policy based lending.

32 For example, research by Heike Mainhardt from [urgewald](#) traced how policy-based finance and technical assistance can indirectly support fossil fuels: [Urgewald, 2022, Suriname's Oil Development Made Possible by IMF, IDB and World Bank Public Finance](#) (accessed 23 January 2024); [Urgewald, 2021, World Bank Assists Development of Asia's Largest Coal Field](#) (accessed 23 January 2024); [Urgewald, 2021, World Bank Assistance Linked to New Major Oil Investment in Brazil](#) (accessed 23 January 2024); [Urgewald, 2018, \\$10 Billion Dollar of World Bank Finance. Pushing Africa's Fossil-Fueled Development](#) (accessed 23 January 2024); [Urgewald, 2017, World Bank Development Policy Finance Props Up Fossil Fuels And Exacerbates Climate Change: Findings from Peru, Indonesia, Egypt, and Mozambique](#) (accessed 23 January 2024); [Urgewald, n.d., The World Bank Drives Billions into Fossil Fuel Investments](#) (accessed 23 January 2024).

33 World Resources Institute, Germanwatch, and New Climate Institute, 2022, [Aligning Policy-Based Finance with the Paris Agreement](#) (accessed 16 January 2024).

3.2.1.4 Assessment of lock-in risks

All methodologies include a lock-in risk assessment, but it is not always clear how this assessment is performed. Some MDBs include more details on how they perform this step. The EBRD specifically excludes certain operations from undergoing lock-in risk tests, based on characteristics making it unlikely the operation will face such risks. The EBRD also has a list of aspects to consider when assessing potential lock-in risks for the rest of operations, including: (1) commercial arrangements, (2) the sector's market structure, (3) the wider project context, and (4) the assets' cost structure. Based on these elements, specific questions tailored to specific sectors are included as part of a sectoral annex. The IDB also details what lock-in analysis entails, including (1) emissions levels, (2) the operation's expected lifetime, (3) technically and economically feasible alternatives and/or arrangements that may replace it or reduce its emissions to net zero by mid-century, and (4) ways to avoid reinforcing market dynamics that set barriers for the transition.

Responses to operations that have a risk of lock-in also vary among MDBs. Following the MDBs' joint methodology, all the MDBs consider operations with substantial lock-in risks to be non-aligned. This implies that such operations would not proceed and receive MDB financing. However, it is not always clear whether this means the entire operation would be cancelled or if there is a process to redesign the operations to address and reduce these risks. The EBRD and World Bank are two notable exceptions. The World Bank goes the furthest in that its three instrument methods clearly exclude supporting operations for which lock-in risks are not reduced to a low level. The bank requires its teams to introduce risk mitigation measures to adjust the design of operations with considerable risks of lock-in. This measure should reduce the risks to a low level. The bank also lists a series of measures that include technical and other assistance to improve risk management. The EBRD requires the incorporation of features that ensure the risks are low and details different aspects to consider in this case, including whether the project demonstrates low-carbon readiness (meaning it can be readied for low-carbon use with limited additional investments) and whether there is a client commitment to decarbonise at the asset or company level. Nevertheless, in both cases, the definition of 'low' risk is unclear which might lead to MDBs' operations allowing some lock-in risks.

A common feature across most of the assessed MDBs is that the methodologies used for the different parts of the 1.5°C compatibility test category in our analytical framework are not detailed or publicly available. Therefore, it is challenging to assess how the MDBs' teams conduct these tests. A notable exception is the EBRD, which includes explanations on how to conduct a compatibility test with the Paris goals, including examples of benchmarks and criteria for different tools, as illustrated in the different parts of the assessment above.

Overall, all banks address their operations' compatibility with the goal of reducing GHG emissions and avoiding negatively impacting client countries' long-term carbon neutrality (lock-in). However, not all are necessarily in alignment with the Paris temperature goals, and for those that are, it is unclear whether their assessment aims for compatibility with the 1.5°C or 2°C goal and how it is conducted.



SCOPE OF IMPROVEMENT

In the joint MDB methodological principles, it is unclear whether the MDBs will use the 1.5°C or 2°C temperature goal for assessing an operation's Paris alignment. MDBs need to specify a commitment to aligning their operations with the Paris 1.5°C goal and to respective goal-aligned low-emissions pathways. All MDBs need to clearly commit to 1.5°C.

The joint MDB methodology and most MDBs' individual methodologies do not look at their MDB operations' potential indirect impacts on countries' mitigation pathways (e.g. unintended overall emissions increases).

Particularly for policy based lending operations, MDBs need to better incorporate a requirement for assessing potential low-emissions design alternatives.

Neither the joint principles nor the particular MDB alignment methodologies establish a clear threshold for what would be acceptable "low" lock-in risks. This leaves scope for interpretation and might lead to MDBs still approving some operations with considerable lock-in risks.



BEST PRACTICE

Only the EBRD clearly specifies in its methodology that in putting into practice its Paris alignment commitment, the EBRD is guided by the 1.5°C goal.

For direct investment operations, the joint MDB methodological principles require an assessment of potential low-emissions design and technology alternatives.

All MDBs require the assessment of lock-in risks in their Paris alignment methodologies and consider operations with substantial lock-in risks to be non-aligned.

Scope for improvement and best practices identified for the assessment category '1.5°C alignment'

3.2.2 Adaptation and resilience goals

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Alignment with national and international climate policies and targets	Climate risk and vulnerability assessment	Does the methodology require a climate risk and vulnerability assessment for an operation and the relevant wider system that the operation influences or by which it is influenced (including impacts on assets, services the operation aims to provide, the operation's targeted beneficiaries, and associated human and natural systems)?	✓	✓	✓	✓	✓
		Does the methodology require the climate risk and vulnerability assessment for an operation to cover an adequate timeframe (the lifetime of an asset or operation beyond the tenor of the loan)?	✓	–	–	✓	✓
		Does the methodology require the climate risk and vulnerability assessment to include different emissions scenarios and respective temperature scenarios (beyond 1.5°C)?	–	✓	–	✓	✓
		Does the methodology require the climate risk and vulnerability assessment to also include intangible climate risks (non-physical risks such as potential loss of cultural artefacts and places or the loss of identity and security)?	–	–	–	–	–
		Is the method for the climate risk and vulnerability assessment clear and transparent (e.g. website link to publicly available tools to be used)?	–	✓	✓	✓	✓

Alignment with national and international climate policies and targets	Response measures for identified climate risks and vulnerabilities	Does the methodology require response measures for identified climate risks and vulnerabilities?	✓	✓	✓	✓	✓
		Does the methodology also foresee response measures for lower climate risks and vulnerabilities, and general opportunities for enhancing resilience (and not only for 'material' climate risks)?	⚡	✗	✓	✗	✓
		Does the methodology refer to the need for a clear and adequate threshold for response measures to minimise residual climate risks?	✗	✗	✗	✗	⚡
		Does the method require identified response measures to reduce climate vulnerabilities be assessed for maladaptation?	⚡	✗	✗	✗	✓
		Is the method for defining response measures to previously identified climate risks and vulnerabilities clear and transparent?	✗	✗	⚡	⚡	✗
Alignment with national and international climate policies and targets	Avoiding operations that increase climate vulnerabilities	Does the methodology require an assessment ensuring that an operation does not have potential impacts that could substantially increase (existing) vulnerabilities to climate hazards (ensuring that an operation is not expected to impair the wider relevant system's climate resilience)?	⚡	✓	⚡	⚡	⚡
		Is the method for assessing potential impacts that could substantially increase existing vulnerabilities clear and transparent (e.g. link to publicly available tools to be used)?	✗	⚡	⚡	✗	✗

 Yes
  Partially
  No

Table 6: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'adaptation and resilience goals'

Article 2.b of the Paris Agreement refers to the objective of 'increasing the ability to adapt to the adverse impacts of climate change and foster climate resilience [...].' The Paris Agreement also establishes 'the global goal on adaptation of enhancing adaptive capacity, strengthening resilience and reducing vulnerability to climate change, with a view to contributing to sustainable development and ensuring an adequate adaptation response in the context of the [1.5°C] temperature goal.' In 2023, at COP28 in Dubai, parties to the Paris Agreement agreed on a framework for the global goal on adaptation. The framework highlights key areas – such as water, health, and food – requiring adaptation action in all countries. However, as of the date of this publication, parties had not yet agreed on specific and measurable indicators to track progress on the global adaptation goal. Yet this in no way prevents the MDBs from aligning their activities with the overarching Paris adaptation and resilience goals. In fact, under BB2 (Adaptation and Climate Resilient Operations) of the MDB joint methodological framework for Paris alignment, the banks clearly committed to aligning their operations with the Paris goals. Thus, this section analyses the MDBs' approach in their methodologies for aligning with these goals.

The joint MDB methodological principles are a good first step toward the MDBs' commitment to aligning their operations with the Paris adaptation and climate resilience goals. However, the MDB's methodological principles leave considerable room for interpretation in deciding whether an operation aligns with a climate-resilient development pathway. Thus, in applying those principles to their own institutional processes, MDBs should ensure they further define the joint methodological principles to close potential loopholes.

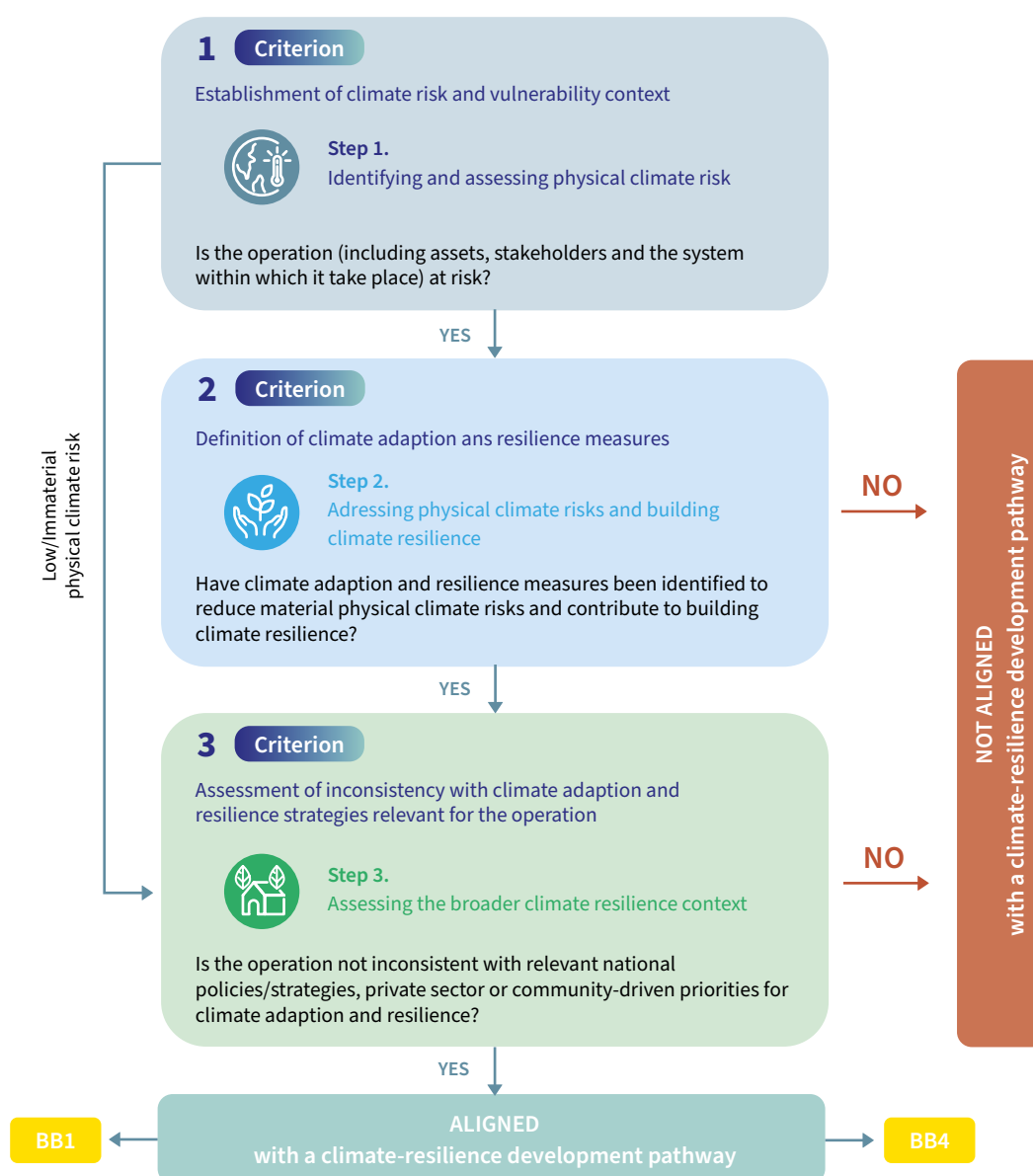


Figure 3: Joint MDB methodological principles; decision-making approach for determining the alignment of direct investment lending operations with the Paris Agreement's adaptation and resilience goals; based on an illustration by the World Bank

MDBs should take three main considerations to ensure alignment with a climate-resilient development pathway: (1) assess risks from climate hazards and respective vulnerabilities for their operations, (2) define response measures for previously identified climate risks, and (3) avoid operations that potentially increase climate vulnerabilities, independently of whether the operation itself faces climate hazard-related risks. The following section looks at these three considerations in more detail.

3.2.2.1 Climate risk and vulnerability assessment

The joint principles ask the MDBs to identify and assess any physical climate risks caused by the climate crisis' negative impacts, such as more frequent and intense storms, heat waves, droughts, sea level rise, glacier melt, and warming oceans. On a positive note, the joint principles refer to the need for defining relatively broad boundaries of an operation and its activities. The joint MDB methodological principles clarify

that physical climate risks to an operation far surpass merely looking at infrastructure and could refer to climate change's adverse impacts on the operation's assets, the services it aims to provide, associated human and natural systems (e.g. ecosystem services), or its targeted beneficiaries.

However, the joint principles lack clarity on the temperature scenarios for such a risk assessment. If MDBs only consider a 1.5°C scenario in their risk assessments, independent of actual emissions pathways (and respective temperature scenarios), they might not identify essential climate risks and present and future climate vulnerabilities and adaptation needs. The AIIB, EBRD, and World Bank close this gap in their methodologies by specifically referring to the need to consider different GHG emissions scenarios.

A thorough climate risk and vulnerability assessment also should consider an adequate timeframe that surpasses the loan's tenor and covers the actual lifetime of the asset or an operation. The joint principles refer to the timeframe for assessing an operation's exposure, sensitivity, and overall vulnerability as a 'relevant time horizon.' The principles further specify that 'suitable time frames' should be based on the nature and lifetime of activities being financed. However, the World Bank, EBRD, and IDB alignment methodologies are quite vague and refer more generally to 'adequate' timeframes or 'relevant' time horizons. They do not specifically require that these should cover the lifetime of operations and activities being financed. The AIIB limits the temporal boundaries only to an asset's 'economic' lifetime. MDBs may fail to identify essential climate risks if they do not consider sufficiently long timeframes in their climate risk assessments.

Moreover, the joint principles call on MDBs to identify and assess only physical climate risks. There is no mention of intangible climate risks (such as potential loss of cultural artefacts and places or the loss of sense of identity and security). The World Bank, AIIB, EBRD, and IDB alignment methodologies do not close this gap. Ideally, MDBs should include the assessment of non-tangible climate risks in their Paris alignment approach.

The World Bank and IDB refer to the use of their own risk assessment tools in their alignment methodology (World Bank Climate and Disaster Risk Screening Tools and the Disaster and Climate Change Risk Assessment Methodology for IDB Projects). The EBRD and AIIB specify no particular tool to be used for climate risk and vulnerability assessment but provide quite detailed explanations on how to proceed for the risk assessment, including, for the AIIB, a reference to tools such as a matrix and questionnaire.

3.2.2.2 Response measures for identified climate risks and vulnerabilities

In a second step, the joint principles request that the MDBs identify and include measures to reduce the previously identified physical climate risks. However, whenever the MDBs consider identified climate risks to be 'low' or 'immaterial,' the joint principles do not require the banks to define potential climate adaptation or resilience-building measures for those risks. Even for climate risks that do not pass the threshold to be categorised as 'material,' there might be straightforward cost-efficient, easy-to-implement response measures that could substantially increase the resilience for, for example, communities forming part of an operation's relevant wider system.

By promoting more general opportunities for enhancing climate resilience, the MDBs could substantially contribute to achieving the Paris adaptation and resilience goals. The joint principles also encourage MDBs to consider opportunities for enhancing overall climate resilience. However, only the AIIB and IDB take this opportunity-driven approach in their alignment methodologies. The AIIB specifies that while the minimum requirement is that the operation itself is made resilient to identified climate risks, '[m]ore ambitious projects may also seek to enhance the resilience of the wider system.'

Nevertheless, the joint principles and particular MDB alignment methodologies would benefit from further methodological guidance on how to consider such opportunities through, for example, resilience-specific sector diagnostics to be systematically mainstreamed into project design.

The joint principles do not define a threshold providing guidance to MDBs on how to assess an identified climate risk as 'material' or 'low/immaterial.' Without further clarification, the threshold of whether climate risks are defined as 'material' may vary substantially and, thus, potentially lead to missed opportunities for resilience-building measures. The alignment methodologies generally tend to define the threshold for risks to be 'material' at quite a high level. The EBRD methodology, for example, considers materiality of risks only for operations with 'high' and 'very high' sensitivity and that are highly likely to face exposure to climate hazards. Thus, operations with medium sensitivity/exposure combination are not considered.

Moreover, notably, the methodologies are extremely clear on the extent to which risks are to be reduced and set a clear bar for adequacy and minimum response to minimise residual risk. The joint principles do not do this and, instead, expect the individual MDBs to undertake 'reasonable measures' to address previously identified climate risks. However, the MDBs also fail to further define a bar for adequacy of response measures for identified risks from climate hazards. Rather, they use vague language referring to terms such as 'acceptable level' or 'appropriate and meaningful' response measures. The World Bank is further opening loopholes in its methodology by stating that an operation is still aligned if there are no 'technically feasible and economically viable' alternatives. Considering there are limits of putting costs on climate hazard-related risks – such as the loss of human life or of a home and sense of security – such an economic cost-benefit approach may not reduce key risks from climate hazards and increase resilience. Individual MDBs, therefore, should set suitable bars for adequate response measures to address identified climate hazard vulnerabilities and risks.

3.2.2.3 Avoiding operations that increase climate vulnerabilities

MDB operations' consistency with national adaptation strategies and priorities is an important topic and is further explored below. However, this national strategy consistency check must not be confused with assessing and ensuring that an MDB operation does not potentially exacerbate (existing) risks and vulnerabilities to climate hazards. MDBs should assess whether any type of operation will impair the relevant wider system's climate vulnerability, independently from an operation's exposure to climate hazards and respective response measures for identified risks and vulnerabilities.



To be aligned with the Paris climate and resilience goals, operations must avoid increasing climate vulnerabilities of potentially affected people and ecosystems. However, only the EBRD specifically refers to this important step within its Paris alignment approach. The EBRD specifically requires that an operation not undermine resilience in the context in which it operates. The World Bank Paris alignment methodology only mentions that project-level impacts that could substantially increase existing vulnerabilities to climate hazards are addressed through the World Bank's Environmental and Social Framework (ESF). However, it is not evident how the ESF precisely addresses this issue. The IDB, for its part, does not refer to avoiding potentially increasing climate vulnerabilities in its Paris alignment approach, but does refer to it in its Environmental and Social Performance Standards 4 for 'community health, safety, and security.' Under this performance standard, it specifically recognises that project activities can increase community exposure to risks and impacts, including those caused by climate change. The IDB's Disaster and Climate Change Risk Assessment Methodology also provides concrete guidance on ways in which project activities and components can potentially intensify climate hazard-related risks. However, the IDB, in its Paris alignment implementation approach, should also acknowledge that avoiding operations that increase climate vulnerabilities is an essential requirement for projects to be Paris-aligned, and it should explain how its environmental and social policy addresses this requirement.

The joint methodological principles and individual MDB alignment methodologies should include an operation's avoidance of existing vulnerabilities as a specific requirement for Paris alignment. This should be required for all operation types, including not only direct investment lending but also intermediated and general corporate purpose lending, as well as policy-based lending. In their methodologies, the MDBs should explain how other policies (such as environmental and social safeguard policies) address the requirement or, if those policies do not address this issue sufficiently, they should opt for a review of those

policies to ensure that the policies effectively address the avoidance of operations that can potentially increase existing risks and vulnerabilities from climate hazards.

The complementarity sectoral guidance that most MDBs provide³⁴ also would benefit from further guidance and examples of operations that could potentially increase (existing) vulnerabilities.

Scope for improvement and best practices identified for the assessment category 'Adaptation and resilience goals'

	
SCOPE OF IMPROVEMENT	BEST PRACTICE
<p>The joint principles lack clarity on using temperature scenarios in assessing climate risks. This aspect could lead to a failure to identify essential future risks, vulnerabilities, and adaptation needs. Further clarity is needed to avoid only focusing on short-term risks and vulnerabilities.</p>	<p>In their methodologies, the AIIB, EBRD, and World Bank include a need for considering different GHG emissions scenarios in their climate risk assessments.</p>
<p>The joint principles do not define a threshold that gives guidance to MDBs on how to assess an identified climate risk as 'material' or 'low/immaterial' or to what extent these should be reduced to be considered acceptable. Further clarity would avoid overlooking critical risks and better manage those identified.</p>	
<p>MDBs do not clearly and systematically promote opportunities for enhancing climate resilience. The methodologies would benefit from further methodological guidance on how to consider such opportunities, using existing tools.</p>	
<p>MDBs should always assess whether any type of operation will impair the relevant wider system's climate vulnerability, to avoid increasing the climate vulnerability of potentially affected people and ecosystems.</p>	<p>The EBRD considers its operations' impacts on the wider system. This bank specifically requires an operation to not undermine resilience in the context in which it operates.</p>

³⁴ Section 3.3 provides further information on complementary sectoral guidance for Paris alignment.

3.2.3 Consistency with national climate strategies and policies (NDCs, LTSs, NAPs)

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Alignment with national and international climate policies and targets	Consistency with national climate policies (NDCs, LTSs, NAPs)	Does the methodology require an operation's consistency with key national climate policies?	✓	✓	✓	✓	✓
		If NDCs, LTSs, etc., are not compatible with 1.5°C pathways, does the methodology foresee engagement with the country to offer support to enhance/improve the NDCs, LTSs, etc., and relevant sectoral policies?	✗	✗	✗	✗	✗

 Yes
  Partially
  No

Table 7: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Consistency with national climate strategies'

As part of the Paris Agreement's bottom-up approach, each country's commitment and contribution to its mitigation and adaptation goals is based on its Nationally Determined Contributions (NDCs) and on other national climate strategies and policies, such as National Adaptation Plans (NAPs). However, these contributions, strategies, and plans often remain insufficient for achieving the Paris mitigation goals, while their contribution to build resilience might be difficult to assess.

Consistency with national mitigations strategies and priorities

Full implementation of the latest NDCs should lead to an increase of 2.1–2.8°C by 2100.³⁵ MDBs should consider their operations' compatibility with nationally determined climate goals and policies. They should do so as they reflect the countries' priorities and realities while exploring any opportunity to help countries enhance their NDCs and national Long-Term Strategies (LTSs), to be fully aligned with the 1.5°C mitigation goal. At the same time, MDBs should continue aligning their portfolios with 1.5°C-compatible pathways.

All MDB methodologies, including the joint methodology, assess an operation's consistency with key national mitigation strategies and policies. However, none include a reference to any type of support MDBs provide for enhancing NDCs' or LTSs' contribution to the Paris goals, such as through dedicated technical assistance.

³⁵ United Nations Framework Convention on Climate Change, 2023, [Nationally Determined Contributions under the Paris Agreement](#) (accessed 16 January 2024).

This does not mean MDBs do not provide such support via other avenues in their client countries.³⁶ Nevertheless, a process for systematically considering support options if there is a non-aligned NDC or LTS could make the methodologies more effective for Paris alignment. It would also allow that consistency test to become more meaningful over time.

Consistency with national adaptation strategies and priorities

The joint methodological principles ask all MDB operations to be consistent with a country's relevant adaptation commitments, policies, strategies, and plans, and with private sector- or community-driven adaptation priorities. However, there are two main limitations here.

First, the consistency check does not assess the completeness, adequacy, or robustness of the country's adaptation strategies and plans, or of respective private sector- and community-driven adaptation priorities. Also, notably, some countries may not yet have comprehensive adaptation strategies. Therefore, for operations in some countries, MDBs might need to refer to the latest scientific data and other available information relevant to the country's NAPs and other national adaptation strategies and priorities.

Second, when relevant information is unavailable in respective strategies, plans, and priorities, the joint methodological principles consider an operation to be consistent and, thus, Paris-aligned. Only for policy-based lending operations, the joint principles acknowledge that NAPs, in particular, are not available in all countries and encourage MDBs to also rely on their own or other publicly available analyses. It may be helpful to apply this principle to all operations. However, in the case of operations' inconsistency with a country's adaptation strategy and policy, the language on expected corrective measures to ensure consistency is quite weak in the joint principles. It only encourages MDBs to continue working on the design of the proposed policy-based lending operation with the respective country's government, without clarifying the extent that such continued work should be performed for the operation to be considered consistent with national adaptation strategies and priorities.

Moreover, the joint methodological principles do not require MDBs to take any further action if the consistency check is inconclusive. Individual MDBs should specify corresponding actions when translating the joint principles into their own Paris alignment processes. These efforts may also include providing support for developing or enhancing NAPs.

Scope for improvement and best practices identified for the assessment category 'Consistency with national climate strategies'



SCOPE OF IMPROVEMENT

In their methodologies, MDBs should include processes to systematically consider support options in the case of a non-aligned NDC or LTS, and support for developing and enhancing NAPs.








BEST PRACTICE

The joint methodological principles and all individual Paris alignment methodologies assess consistency with national climate strategies and policies.

³⁶ Some examples are here: Inter-American Development Bank, 2023, [COP28: Multilateral Development Banks Boost Joint Action on Climate and Development](#) (accessed 16 January 2023); European Investment Bank Group, 2021, [MDB Principles for Long-Term Strategy \(LTS\) Support](#) (accessed 16 January 2024).

3.2.4 Proactively seeking climate action opportunities

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Alignment with national and international climate policies and targets	Proactively seeking opportunities for climate action	Does the methodology include guidance on proactively seeking opportunities for climate action as part of any upstream country dialogue and other country engagement processes?					

 Yes  Partially  No

Table 8: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Proactively seeking climate action opportunities'

Trillions of US dollars in financial support for highly transformative climate action are needed if the world is to seize its last chance to achieve the Paris goals.³⁷ Thus, MDBs should use their Paris alignment methodologies to direct as much of their portfolios as possible to generating positive and transformative climate impacts. In this sense, they should go beyond a do-no-harm approach to 'doing good' and advancing on the Paris goals.

However, of the Paris alignment methodologies covered in this paper, only the IDB's includes any guidance on proactively seeking opportunities for climate action in operations design. Even the IDB's approach stated in its methodology largely focuses on proactively seeking opportunities through upstream engagement. The IDB does not define clear steps for promoting a doing-good approach, including clear guidance on how to integrate an opportunity-driven approach, in its Paris alignment assessment of individual operations.³⁸ The IDB's methodology is expected to be applied to upstream dialogue with client countries, even before Paris alignment assessment, to maximise the positive synergies of climate action with all development needs. Despite there being no further detail on how these engagements will be conducted or lead to identifying and integrating synergies, this does constitute a clear commitment to seeking opportunities for climate action, with client countries, as part of implementing the bank's Paris alignment commitment.

The AIIB, for its part, in its Paris alignment methodology specifically commits to surpassing safeguards or compliance, identifying opportunities where the bank can provide additional value. The plan is to not only assess projects as part of the due diligence for project approval but also to actively select and design operations that are Paris-aligned as an opportunity for developing new businesses. Also, as mentioned, beyond the minimum requirement for alignment with the adaptation and resilience goals, the AIIB's more ambitious operations may seek to strengthen the wider system's resilience. This aspect can also be considered as proactively seeking climate adaptation opportunities.

³⁷ Many different estimates exist, based on different sources and methodologies, but most estimates are in the trillions. Some examples include: UNFCCC, 2021, *First Report on the Determination of the Needs of Developing Country Parties Related to Implementing the Convention and the Paris Agreement* (accessed 27 March 2024). The second report of the Independent High-Level Expert Group on Climate Finance (IHLLEG), also offers estimates in the trillions: Bhattacharya, A., et al., 2023, *A Climate Finance Framework: Decisive Action to Deliver on the Paris Agreement – Summary* (accessed 27 March 2024).

³⁸ This is in line with the joint methodology, which the IDB largely follows.

Scope for improvement and best practices identified for the assessment category 'Proactively seeking climate action opportunities'



SCOPE OF IMPROVEMENT

MDBs should surpass mere due diligence and a do-no-harm approach and move to doing good and advancing on the Paris goals by proactively seeking opportunities to support these goals in all operations.



BEST PRACTICE

The IDB includes guidance for proactively seeking opportunities for climate action in operations design as part of its upstream dialogue with clients.

The AIIB also commits to an opportunity-driven approach, particularly for building the wider system's resilience.

3.2.5 Human rights-related obligations

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Alignment with national and international climate policies and targets	Consideration of human rights-related obligations under the Paris Agreement	Does the methodology include guidance for Paris-aligned operations to actively promote and respect countries' obligations regarding human rights, and the rights of indigenous peoples, local communities, migrants, children, persons with disabilities, and people in vulnerable situations?	—	✓	—	—	—

Yes
 Partially
 No

Table 9: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Human rights-related obligations'

The Paris Agreement emphasises ‘the intrinsic relationship that climate change actions, responses and impacts have with equitable access to sustainable development and eradication of poverty.’³⁹ In its preamble, it also acknowledges that action to address climate change must respect, consider, and promote obligations on human rights:

*Acknowledging that climate change is a common concern of humankind, Parties should, when taking action to address climate change, respect, promote and consider their respective obligations on human rights, the right to health, the rights of indigenous peoples, local communities, migrants, children, persons with disabilities and people in vulnerable situations and the right to development, as well as gender equality, empowerment of women and intergenerational equity [...] (Preamble of the Paris Agreement)*⁴⁰

Human rights violations related to climate change can occur in various ways. They can be due to the absence of climate-related actions or implementation of inadequate or disproportionate climate mitigation or adaptation actions, such as if less invasive measures could have been used to reach the same climate-related goal. Any type of project, irrespective of whether it has climate mitigation or adaptation components, may also exacerbate existing climate risks and vulnerabilities and harm the rights of the most vulnerable.

Human rights considerations are usually covered by the MDBs’ environmental and social safeguards, which ensure that the banks’ operations do not harm the environment or vulnerable social groups, or the MDBs’ mechanisms for addressing complaints from project-affected people. However, these safeguards’ effectiveness and appropriateness are often criticised, especially by civil society.⁴¹ Additionally, while all MDBs have complaint mechanisms, the mechanisms’ effectiveness and neutrality from MDB management also vary considerably.⁴²

Thus, the joint MDB methodological principles for Paris alignment and individual MDBs’ Paris alignment methodologies should specifically refer to those crucial obligations on human rights under the Paris Agreement and ensure their climate actions’ alignment with those obligations. The Paris alignment methodologies should also highlight that the alignment assessments are taking a human rights-based approach and explain how other MDB policies (such as environmental and social safeguard policies) in place address climate-related human rights implications. The MDBs could also consider pointing out potential human rights implications in their sectoral guidance that complements the individual banks’ Paris alignment methodologies.⁴³ For example, renewable energy projects, particularly in wind and solar, have repeatedly been accused of adverse human rights impacts. The renewable energy sector has also often been associated with human rights violations such as land grabbing and other land right violations related to land tenancy, forced displacement, adverse effects on water and food resources, and the destruction of sacred sites, among others. Over 10 years, the Business & Human Rights Resource Centre has recorded more than 200 serious human rights violations related to renewable energy projects.⁴⁴ Thus, in their sectoral guidance, MDBs should raise awareness of specific potential violations frequently associated with climate mitigation and adaptation projects and ensure the safeguard system is appropriate and effective for proactively

39 United Nations Framework Convention on Climate Change (UNFCCC), 2015, *Paris Agreement* (accessed 07 March 2024).

40 Ibid

41 Some of this criticism can be found here: Bankwatch Network, 2019, *Dirty Palms: European Development Banks Need Better Due Diligence and Accountability to Prevent Human Rights Abuses* (accessed 16 January 2024); German Institute for Human Rights, 2016, *New Environmental and Social Standards at the World Bank and the AIIB* (accessed 16 January 2024); Human Rights Watch, 2017, *Human Rights Watch Submission re International Financial Institutions and Human Rights* (accessed 16 January 2024); Tan, C., 2019, *Human Rights and the Bretton Woods Institutions: Moving Beyond Institutional Remedies* (accessed 16 January 2024); The Danish Institute for Human Rights, 2021, *Human Rights at Development Finance Institutions. Connecting the Dots Between Environmental and Social Risk Management and Development Impact* (accessed 16 January 2024).

42 Accountability Counsel, 2021, *How to Compare IAM Policies with the Benchmark Reports Feature* (accessed 16 January 2024); Bissell, R. E., Nannani, S., 2009, *Multilateral Development Bank Accountability Mechanisms: Developments and Challenges* (accessed 16 January 2024); Bretton Woods Project, 2019, *A Complaint by Any Other Name... Good Practice among Independent Accountability Mechanisms* (accessed 16 January 2024).

43 Section 3.3. provides more information on additional sectoral guidance.

44 Business & Human Rights Resource Centre, 2021, *Renewable Energy & Human Rights Benchmark. Key Findings From the Wind & Solar Sectors*, (accessed 07 March 2024).

avoiding such climate change- and climate policy-related violations. This may also imply the need for some MDBs to update their environmental and social safeguard systems to better reflect climate change and climate policy and climate action-related risks to human rights.

Unfortunately, neither the joint principles nor MDBs' individual Paris alignment methodologies refer to any type of human rights obligations. On a positive note, the EBRD Paris alignment methodology requests that all low-carbon pathways that the EBRD uses should include gender-responsive considerations, in line with the enhanced Lima Work Programme on Gender and the UNFCCC Gender Action Plan.



3.3 Additional sector-specific guidance

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Additional sector-specific guidance	Additional sector-specific guidance	Does the methodology include additional sector-specific guidance that provides additional tools, examples, and information on how to apply Paris alignment for specific sectors?	–	✓	✓	✓	✓
		Does the additional sector-specific guidance cover a broad range of sectors and sub-sectors? Including sector-specific guidance for the implementation of a full Paris alignment assessment, including all aspects of climate mitigation (1.5°C alignment) and climate adaptation and resilience, as well as human rights and how to proactively seek opportunities for climate action?	–	⚡	⚡	⚡	⚡

 Yes
  Partially
  No

Table 10: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Additional sector-specific guidance'

Most MDBs have elaborated on additional sector-specific guidance for their Paris alignment assessments in order to facilitate and enable operationalisation of the Paris alignment approach in project teams' work. Given the joint methodological alignment principles' rather general formulation and that decarbonisation pathways and adaptation needs vary considerably by sector, such sectoral guidance is important for making practical implementation consistent and for providing additional detail, guidance, and interpretation for project personnel to determine alignment of sector-specific measures in MDB operations.

All individual MDB methodologies reviewed have additional sectoral guidance. However, such guidance varies substantially in scope, detail, and practical applicability, sometimes even within one bank. This variability can influence sectoral assessments' quality and effectiveness.

Sectoral guidance should cover a range of aspects relevant for Paris alignment assessments. It should complement the MDBs' alignment methodologies and be consistent with the banks' overall Paris alignment approach. The sector notes should not open new loopholes by, for example, introducing exemptions to the methodology; rather, they should close existing gaps. Ideally, this additional technical guidance

should break down the alignment assessment tasks and provide guidance on adequate tools and benchmarks, as well as sector-specific examples of how to apply the assessment. It should cover sector-specific guidance on alignment with the 1.5°C goal and with the Paris adaptation and resilience goals and all respective considerations that this paper's framework and its corresponding sub-indicators cover. It should include guidance and examples for sector-specific lock-in risks or transition risks, sector-specific risks from climate hazards, along with respective response measures, and sector-specific examples for maladaptation practices. It should also include guidance and examples on how an operation's activities in one sector can increase existing vulnerabilities in that operation's relevant wider system, and guidance on potential sector-specific human rights violations for Paris-aligned activities (e.g. for the wind and solar energy sector).

While sectoral guidance is generally helpful, a question remains on how this additional technical guidance for sectors can be applied to multi-sectoral projects. Several MDBs are shifting away from well-defined projects in one sector toward more loosely defined portfolio funds and programmes (also in the case of direct investment operations). MDB personnel, thus, might need to use sector-specific guidance for more than one sector. However, this shift calls into question the true meaningfulness of concrete application of the sectoral guidance and, more generally, the Paris alignment assessment.

The indicator in this chapter looks more generally at the scope of the MDBs' sectoral guidance (coverage of guidance on all relevant steps for assessing mitigation, and adaptation alignment) and the detail, practical applicability, and examples provided. On the whole, there is much more detail and coverage of sectoral considerations for mitigation alignment, while sectoral guidance for adaptation alignment is less extensive. Overall, the World Bank provides the most comprehensive sectoral guidance, covering 11 sectors (Agriculture and Food; Digital Development; Education; Energy and Extractives; Environment, Natural Resources and Blue Economy; Health, Nutrition and Population; Social Protection and Jobs; Social Sustainability and Inclusion; Transport; Urban, Resilience, Disaster Risk Management, and Land; and Water) and further defines sub-sector-specific guidance.

Scope for improvement and best practices identified for the assessment category 'Additional sector-specific guidance'



SCOPE OF IMPROVEMENT

A more consistent approach to sectoral guidance within MDBs is needed to ensure the sectoral assessments' quality and effectiveness.

More detailed sectoral guidance for adaptation alignment is needed. MDBs should further develop their approaches for adaptation alignment across all sectors.

MDBs should include sector-specific guidance and examples for a range of aspects considered in this paper (including, for instance, examples for maladaptation, transition risks, and potential human rights violations for Paris-aligned activities in specific sectors).



BEST PRACTICE

The World Bank's additional sector-specific guidance covers a broad range of sectors.

3.4 Addressing transition risks

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Transition risks	Considerations of a just transition	Does the methodology require an assessment of social risks linked to the operation (considerations of a just transition)?	–	✓	✓	–	–
		Does the methodology require an assessment of transition risks, and/or the risk of an operation's stranded assets?	✓	✓	✓	✓	✓
	Considerations of transition risks/stranded assets	Does the methodology establish a process for appropriately managing transition risks by reducing them to appropriate levels (including clear thresholds)?	–	✓	✓	✓	–
		Does the methodology prevent operations with substantial transition risks if measures to reduce those risks are not identified or available?	✓	–	✓	✓	✓
		Is the method for how to assess transition risks public and transparent, including the method for how to respond to/reduce identified transition risks (clear tools and process)?	–	✓	–	✓	✓

 Yes
  Partially
  No

Table 11: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'transition risks'

Transitioning to a low-carbon economy can entail financial risks to investments because of the measures introduced to drive the transition. Decarbonisation processes can result in stranded assets, which suffer unanticipated or premature write-downs, devaluations, or conversion to liabilities, and which could become systemic risks to financial stability.⁴⁵ The risks depend on the nature, speed, and focus of the policy, legal, technology, and market changes being implemented.⁴⁶

Transitioning to a low-carbon economy can also negatively impact workers, communities, and businesses, and can lead to an unequal distribution of the risks and opportunities that the transition generates, impacting social stability, justice, and welfare. Therefore, transition risks should be managed to avoid potential negative impacts of the transition to a low-carbon and climate-resilient economy, including focusing on a just transition. The Paris Agreement recognised the latter as 'imperative.'

This indicator looks at:

- Consideration of just transition elements
- Assessment and management of transition risks, and risk of stranded assets
- Clarity and transparency of the tools used in this assessment

3.4.1 Just transition considerations

The MDBs' focus on transition risks in their methodologies almost completely excludes mention of a just transition, despite the development of joint MDB Just Transition High-Level Principles,⁴⁷ which could serve as a basis for including a just transition in their Paris alignment methodologies. The methodologies have no focus on the social aspects of transitioning to a low-carbon economy, or any other aspects that might ensure that the type of transition their operations support is just. MDBs already consider their operations' potential social impacts because these aspects are part of their environmental and social frameworks. However, these frameworks' social considerations do not look specifically at the transition's potential negative socio-economic impacts, potential opportunities it brings, and distribution of these costs and opportunities for different stakeholders. Therefore, these frameworks are unlikely to consider how an operation's design influences such costs and opportunities, and how it responds to them.

Only the EBRD concretely mentions a just transition, through its assessment of 'green transition impact,' which is a separate but related EBRD process applied to operations before project signing and as part of monitoring and evaluating operations.⁴⁸ As part of this process, the EBRD assigns projects a higher score for its transition impact rating⁴⁹ if operations contain considerations of a just transition. The IDB includes a just transition as a principle and states that IDB personnel will find models that address aspects such as distribution of the transition's costs and benefits. How and when this process occurs is unclear. The decision tree for assessing mitigation alignment for IDB operations has no step related to a just transition.

3.4.2 Consideration of transition risks and stranded assets

The joint MDB methodological principles include a step for assessing transition and stranded asset risks for direct lending operations, but leave each MDB to apply its own methods and approaches to incorpo-

45 Inter-American Development Bank, 2016, *Stranded Assets: A Climate Risk Challenge* (accessed 16 January 2024).

46 Task Force on Climate-related Financial Disclosures, 2017, *Recommendations of the Task Force on Climate-related Financial Disclosures* (accessed 16 January 2024).

47 Asian Development Bank, 2021, *MDB Just Transition High-Level Principles* (accessed 16 January 2024).

48 This process is included in Annex 1 of the EBRD's Paris alignment methodology, which details the links between the methodology and other processes.

49 European Bank for Reconstruction and Development, n.d., *How We Assess Transition Impact* (accessed 16 January 2024).

rate these risks into their financial and economic analyses. However, the joint principles mention shadow carbon prices as a potential tool for assessing such risks. The principles do not assess transition risks for policy-based lending operations. This might be because these risks are usually seen as directly related to an operation's economic viability. The AIIB follows this exact approach, and only further specifies which shadow carbon price will be used, as part of its sector-specific approach for assessment, which is included as an annex.⁵⁰ The World Bank follows a similar approach, including its guidance for applying shadow carbon prices as one way of capturing transition risks.⁵¹ The World Bank, as part of the economic viability assessment, also includes a comparison of alternatives with lower emissions. The EBRD, however, mentions the need to consider the possibility of stranded assets, but considers this a financial risk and, therefore, does not deal with it in the Paris alignment methodology but rather as part of its banking and risk management considerations. In its annexes, the EBRD further clarifies that its climate-related risk approach focuses on the financial counterparty's impacts, which are considered 'typically beyond the boundaries of the project.'

It is less clear how MDB teams are expected to respond to and manage transition risks. The joint MDB methodological principles contain no guidance on what strategies can be used to manage transition or stranded asset risks beyond stating that the operations are not aligned. Most individual MDB methodologies do not clearly state what measures could be taken to manage risks if material transition risks⁵² are identified. The IDB and World Bank are two exceptions. The IDB clearly states the need to include strategies for managing climate transition risks. However, the IDB methodology includes, as part of its 'key methodological issues that remain unclear,' the need for IDB personnel to further establish criteria for assessing and determining where stranded asset risks are considered material. The World Bank's Paris alignment methodologies for Investment Project Financing and Program for Results clearly state that the operation should not be supported if the risks are not reduced to a low level. However, the World Bank's methodology for Development Policy Financing contains no assessment or management of potential transition risks. Also, the World Bank's Paris alignment methodologies contain no definitions of 'unviability' and 'low risk,' leaving judgment to the project personnel's discretion.⁵³

Regarding the transparency of methods for assessing and managing potential transition risks, only the World Bank and EBRD Paris alignment methodologies clearly state the tools and guidance for assessing these risks. The World Bank also provides some guidance on how to manage those risks.

50 The AIIB will use the shadow carbon price recommended by the High-Level Commission on Carbon Prices.

51 The World Bank recently updated its guidance: World Bank, 2024, [2024 Guidance Note on Shadow Price of Carbon in Economic Analysis](#) (accessed 25 March 2024).

52 In the World Bank's glossary in its instrument methods for Investment Project Financing and Program for Results, this is defined as 'risks that have a moderate, substantial or high risk of failure or unintended consequences, considering the likelihood of the risk materialising and the impact on the desired development outcome'; World Bank, 2023, [World Bank Paris Alignment Method for Program for Results](#), p. 16 (accessed 16 January 2024).

53 Note that MDBs are assessed on whether they assess all operations, including policy-based lending operations, and manage potential risks for these operations. Correspondingly, even MDBs that perform well in terms of assessment and management strategies are rated as 'partially' in the table if they do not include policy-based operations. Here, the AIIB seems to be an exception because it does not provide policy-based finance.



SCOPE OF IMPROVEMENT

Just transition: All MDBs should integrate considerations of a just transition in their Paris alignment approaches.

This integration should surpass only highlighting the importance of a just transition as a principle and should include operation steps required and reference to specific methods/tools used to assess a just transition.

The joint MDB Just Transition High-Level Principles could build a basis to better integrate just transition considerations in their Paris alignment methodologies.

Transition risks, stranded assets: The joint MDB methodological principles include a step for assessing transition and stranded asset risks but they do not require an assessment of transition risks for policy-based lending operations.

The principles do not provide information on how to manage transition risks once they have been assessed.



BEST PRACTICE

Just transition: In their Paris alignment methodologies, the EBRD and IDB both require considerations of a just transition as a principle. The EBRD even provides further details on how just transition considerations will be concretely applied.

Transition risks, stranded assets: The joint MDB methodological principles include a step for assessing transition risks for direct lending operations. They also mention shadow carbon prices as a tool for assessing such risks.

The IDB clearly states the need to also include strategies for managing climate transition risks. The World Bank requires transition risks be reduced to a low level.

The World Bank and EBRD Paris alignment methodologies provide concrete tools and guidance for assessing transition risks. The World Bank also provides some guidance on how to manage those risks.

3.5 Financial intermediaries and corporate counterparties

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Paris alignment of counterparties	Paris alignment of counterparties	Does the methodology require an assessment of all counterparties for Paris alignment in their entire portfolio and their level of alignment (institutional and project level policies and tools, including transparency)?	–	✓	–	–	–
		Does the methodology foresee excluding provision of support to counterparties that have not committed to Paris alignment?	✓	✓	–	–	–
		Does the methodology require non-aligned counterparties that have committed to Paris alignment to commit to a time-bound plan for alignment (as soon as possible but before 2030, depending on their alignment status)?	✓	✓	✓	✓	✓
		For non-aligned counterparties that have committed to Paris alignment, does the methodology, if needed, foresee support for implementing the counterparties' alignment plans?	–	✓	✓	✓	–
		For non-aligned counterparties that have committed to Paris alignment, does the methodology include safeguards for avoiding financing of non-aligned investments until the counterparty's alignment plan is fully implemented?	–	✓	–	–	–

	Paris alignment of counterparty-intermediated transactions	For counterparties that have committed to a plan for Paris alignment, does the methodology include mechanisms for monitoring and stopping support if the plan is not fully implemented within the agreed period?					
		When the use of proceeds or the subprojects being financed is known, does the methodology apply the same 1.5°C compatibility test to the financed activities?					
		When the use of proceeds or the subprojects being financed is known, does the methodology seek to ensure the financed activities' responsiveness to climate vulnerabilities?					

Yes Partially No

Table 12: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Financial intermediaries and corporate counterparties'

Some MDBs channel substantial portions of their finance to FIs, particularly for private sector clients.⁵⁴ However, they also lend directly to corporate counterparties. This means that for MDB finance to be aligned with the Paris goals, MDBs should ensure that the finance flowing to counterparties (i.e. FIs and corporates) is also aligned. Such alignment should include the FIs' entire portfolios and their institutional policies, while for corporates, it should include their entire business model and all business areas as a means of supporting the counterparties' progressive alignment and avoiding indirectly financing non-aligned activities. Many FIs and corporates are less advanced than the MDBs on Paris alignment and have limited capacity for introducing respective processes,⁵⁵ which is why MDB support is needed.

This indicator, therefore, looked at criteria related to counterparty alignment, independent of the financing instrument applied, covering whether:

- the methodology requires an assessment of the counterparties' commitments to Paris alignment in their entire portfolio and their level of Paris alignment.
- support is excluded for counterparties that have not committed to Paris alignment.
- the methodology requires non-aligned counterparties to commit to a time-bound plan for Paris alignment (i.e. as soon as possible but before 2030, depending on their alignment status).

⁵⁴ Germanwatch, New Climate Institute, and World Resources Institute, 2021, [Aligning Financial Intermediary Investments with the Paris Agreement](#) (accessed 16 January 2024).

⁵⁵ Of 18,600 disclosing organisations surveyed by the Climate Disclosure Project, 22% reported that they had developed a 1.5°C-aligned climate transition plan, but only 0.4% reported sufficient detail on the key indicators of a credible plan: Carbon Disclosure Project, 2023, [Are Companies Developing Credible Climate Transition Plans?](#) (accessed 24 January 2024).

- support is provided where necessary to support counterparties in their alignment.
- safeguards to avoid financing non-aligned investments are in place during counterparties' transition toward alignment.
- the methodology contains mechanisms for monitoring and stopping support if the counterparty does not implement its plan for Paris alignment within the agreed period.

We also examined two criteria regarding counterparty-intermediated transactions where the use of proceeds is known and where most MDBs apply the so-called transaction-based approach. These are whether the methodology:

- applies the same 1.5°C compatibility test required for non-intermediated financing.
- seeks to ensure the financed activities' responsiveness to climate vulnerabilities.

3.5.1 Counterparty-based versus transaction-based approach

The joint MDB methodological principles offer two different approaches for intermediary finance depending on whether the use of proceeds is known (e.g. finance for specific, defined activities or asset types) or unknown (e.g. general corporate purpose finance). The joint methodological principles for both intermediated and general corporate purpose finance require an assessment of the counterparties' Paris alignment. For intermediated finance, the methodology includes a transaction-based approach based on an analysis of the use of proceeds and a counterparty-based approach based on an analysis of the counterparty's Paris alignment pathway.⁵⁶ Either approach can be used when investments finance specific and predefined activities or assets; otherwise, only the counterparty approach is applied. The joint methodological principles let each MDB decide whether to combine the two options, but states that, over time, the counterparty-based option may supersede the transaction-based one as counterparty capabilities improve. For general corporate purpose finance, only the counterparty approach is applicable.⁵⁷ This means that FIs may not always be required to align their entire portfolio and policies, but can, in some cases, limit their alignment to ensuring that MDB-financed projects and assets are aligned.⁵⁸ In this case, MDB funds might indirectly support non-aligned FI investments by bolstering the FIs' balance sheets. At the same time, MDB investments' Paris alignment cannot be verified when the use of proceeds is unknown. Therefore, the counterparty-based approach is an indirect means of ensuring Paris alignment, which, in many cases, only becomes effective over time. Note also that differences in the regulatory environment across countries in which MDBs operate can make it easier or harder to implement a counterparty-based approach. The level of support the counterparties need will also vary greatly.

The joint methodological principles require corporate clients to develop a Paris alignment pathway that includes a decarbonisation plan and addresses carbon lock-in and stranded asset risks, as well as the risk of expansion into high biodiversity areas. Regarding adaptation, it partially requires corporates to implement climate risk management processes (see textbox on p. 59 for further details). For FIs, the joint methodological principles require a pathway containing a climate strategy that includes internal risk management systems. However, the joint methodological principles do not require these Paris alignment pathways to be clearly time-bound and rather link them to the MDB finance's tenor.

Notably, the joint methodological principles' counterparty-based approach for FIs and corporates also

⁵⁶ Notably, the counterparty-based approach used for corporate finance differs slightly from that used for FIs, though they consider similar elements and require the development of Paris-aligned pathways if risks of non-alignment exist.

⁵⁷ This includes, among other aspects, working capital, trade finance through a corporate, supply chain finance, general purpose corporate loans and bonds, equity investments for corporates, and general guarantees.

⁵⁸ The counterparty-based approach also requires no assessment of risks for short-term finance or a response and development of climate risk management processes for long-term finance for which risks were identified as low or immaterial. The definition and parameters to consider for a risk to be 'low' and 'immaterial' are unclear.

applies the Universally Aligned and Universally Non-aligned Lists to counterparties' portfolios, further limiting the assessment scope. Other exceptions further limit the approach's scope in its ability to support counterparties' alignment. For example, the approach already considers short-term transactions to be aligned only if they are consistent with national targets, which are expressed in NDCs, LTSs, and other such plans. Additionally, only operations with material risk of non-alignment require the development of a Paris-aligned pathway for the counterparty. All these factors combined limit the scope of the counterparty-based approach, potentially leading to non-alignment, and they make proactive seeking of opportunities to promote climate action extremely difficult.

BB2 alignment in the joint methodological principles for general corporate purpose financing

The largest gaps and missed opportunities regarding alignment with the adaptation and resilience goals are in the joint methodological principles for general corporate purpose finance – private real sector investment operations without targeted use of proceeds. No assessment for risks from climate hazards is required for short-term general corporate purpose finance. There is only a request for counterparties' ex-post reporting of the occurrence of any climate impact or material climate risk 'throughout the tenor of the MDB financing.' This means a counterparty should report if its supply chain or own production was, for example, affected by a severe drought throughout the tenor. The counterparty must establish or 'commit to establish' climate risk management processes only in the case of short-term finance renewal. The same approach is in place for long-term general corporate purpose financing for which MDBs have assessed low or immaterial risks. On a positive note, even if no material climate risks were identified and, thus, no climate risk management process deemed necessary at the time of approval, the joint principles foresee the MDBs requesting the counterparty to periodically review its exposure to physical climate risks during the tenor of the loan and, if material risks were identified, ask the counterparty to establish a climate risk management process. If the MDB cannot determine the climate risks because of the analysis' complexity (e.g. for counterparties with multiple assets in multiple locations), the counterparties are requested to develop and implement an adequate process for managing material risks from climate hazards.

However, aspects of this approach for general corporate purpose finance in the joint methodological principles are problematic:

- 1.** The main exposure to climate risks will predominantly occur in the future. Therefore, it is insufficient to only look at exposure to risks from climate hazards 'throughout the tenor of the loan,' as this raises questions regarding MDB investments' overall sustainability and long-term effectiveness.
- 2.** Having no requirement for ex ante climate risk assessments for short-term finance misses a critical opportunity to raise awareness among counterparties for the general need for such an assessment, and for corresponding processes and measures to reduce such risks from climate hazards. Having no clear definitions and thresholds for 'short-term' and 'long-term' MDB finance might open further room for interpretation and potentially lead to a significant amount of activities to fall under the weaker criteria for short-term MDB finance.
- 3.** If counterparties are requested to 'commit to establish' climate risk management processes, it is unclear whether the MDBs will follow-up on this commitment and monitor implementation. The procedures also are unclear on what happens if a counterparty fails to establish the required processes.
- 4.** Corporate counterparties are not required to assess the potential for their operations and activities to increase existing vulnerabilities to climate hazards.

3.5.2 Counterparty-based approach

The MDBs' approach is to continually engage with non-aligned counterparties to support their progressive alignment, rather than excluding them from cooperation. Thus, their methodologies contain a counterparty-based approach to ensure Paris alignment of their FIs. Individual MDB methodologies largely follow the joint methodological principles for the counterparty-based approach, though for the EBRD, this only applies in the short term. Over the medium term,⁵⁹ the bank will apply a full assessment to its FIs, requiring them to develop transition plans. Additionally, the EBRD's methodology requires all FIs with which it enters into new financing agreements to commit to Paris alignment. This commitment can take different forms, including an affirmative covenant in transaction-related or other formal documentation between the EBRD and the FI, or the FI expressing such commitment in other forms, such as annual reports, business strategies, and other corporate communications.

Lack of time-bound Paris alignment commitments from counterparties

Generally, when the MDBs apply the counterparty approach to FIs, and determine an operation's potential non-alignment, they require the partner FIs to make commitments to Paris alignment and develop transition pathways. However, these commitments are mostly not required to be clearly time-bound and could establish timelines beyond 2030. This is problematic given that financing for oil and gas exploration and extraction should be stopped immediately, with full alignment no later than 2030, in line with the science.⁶⁰ This situation, thus, intensifies the need to add direct and indirect financing for oil and gas exploration and extraction to the Universally Non-aligned List applied by the MDBs. Only the AIIB's methodology requires a set of time-bound targets for establishing Paris alignment requirements. This requirement is in the form of establishing or improving climate risk management and disclosure, and accompanied by verifiable commitments and targets, including reducing portfolio emissions in line with jurisdictional commitments. The AIIB requires a timescale and resource plan for achieving the identified actions and targets, over the short (2025) and medium (2025–2030) terms. The EBRD requires, in the short term, a transition plan with time-bound milestones from FIs when the use of transaction proceeds is not defined or when they could be exposed to material carbon transition risks or physical climate risks in their lending activities, and when they lack an adequate framework for managing those risks. Yet, the EBRD methodology does not specify the required timeline for these milestones. In the case of certain financial instruments, included separately in the EBRD's methodology in section 4,⁶¹ for counterparties involved in Paris-non-aligned activities, the methodology states a transition plan consistent with the Paris goals should be in place, only specifying that the timeline should be based on low-carbon pathways.

MDB support for counterparty alignment

The EBRD, World Bank, and IDB methodologies foresee some type of support for FIs to develop their Paris alignment plans and management systems. The EBRD's support is not clearly specified and will be provided where needed, including for non-financial corporates, and potentially in coordination with other MDBs and development finance institutions. The IDB mentions it will continue offering support through its counterparty-based approach, but also lacks further specificity. The World Bank indicates it will offer technical assistance, training, and institutional development support to help FIs operationalise their Paris alignment methods. Most counterparty expectations and targeted support focus on managing risks and ensuring a do-no-harm approach. There are no attempts to support FIs in proactively seeking opportunities to promote climate action through their portfolios.

⁵⁹ The EBRD established this will be the case within four years, beginning in 2023.

⁶⁰ For example, the International Energy Agency's net zero pathway include no new oil and gas fields approved for development after 2021, in: EIA, 2021, *Net Zero by 2050: A Roadmap for the Global Energy Sector* (accessed 26 March 2024)

⁶¹ These instruments are a minority of the EBRD finance and include: directly financed investments unrelated to specific capital expenditures or clearly identified and ring-fenced economic activities; where the use of proceeds or activities to be financed cannot be readily identified at the time an investment project is being approved; where the financial flow is linked to multiple investment activities and where individual assessment would be impractical; where the EBRD takes an equity stake in a corporate counterparty; debt or equity funds where the EBRD has direct exposure to underlying sub-transactions; and donor financing the EBRD manages or facilitates to support its investments.

Need to combine the counterparty and transaction-based approach in the medium term

While counterparties are developing their Paris alignment pathways and plans, no safeguards are foreseen to ensure that finance does not flow to non-aligned activities in the meantime. The transaction-based approach is the only available means and it will not always apply to relevant counterparties and, in particular, will not apply to MDB-provided general corporate purpose finance, such as equity and trade finance.⁶² Hence, when the transaction-based approach can be applied, MDBs should use this approach to avert non-alignment.

Monitoring the progress of FI's alignment commitments and halting support in case of non-fulfilment

Additionally, almost no MDBs have established a clear way of monitoring the counterparties' Paris alignment implementation and halting support if commitments are not kept. The joint methodological principles do include a reporting requirement for counterparties on their progress toward aligning their operations, though it specifies no actions to be taken if a counterparty's commitment is not met. Only the EBRD, which will monitor progress in developing and implementing expected transition plans annually, will use this monitoring to ensure a plan is being implemented as planned, determining whether a revised transition plan is required or determining non-alignment. A non-alignment determination requires undertaking remedial measures to address the non-alignment. If the FI fails to implement these measures, the EBRD will take actions including exercising rights and remedies, as contained in the financing agreements signed with the FIs, up to stopping further engagement with the intermediary. The World Bank will monitor process and policy improvements as part of project implementation, after including agreements as parts of legal covenants with FIs. However, it is unclear what happens if these agreements are not kept. The AIIB also requires periodic reporting, though what happens if agreed milestones are not reached is also unclear.

3.5.3 Transaction-based approach

As mentioned, when proceed use is known, the MDBs can also apply a transaction-based approach looking at the financed activities to assess their Paris alignment. Ideally, this assessment of sub-transactions should follow the same steps proposed in our framework for assessing Paris alignment, both in terms of 1.5°C compatibility⁶³ and responsiveness to climate vulnerabilities. In some cases, such as when the sub-transactions' location is not known in advance and, therefore, potential physical risks cannot be analysed, a comprehensive assessment and management of risks might not be possible and other alternatives should be explored and implemented. One way to do this is requiring counterparties to have robust risk management systems in place (as included in the counterparty-based approach). Depending on the sub-transaction size and type, allowing for some flexibility in assessment tool use could make sense; for example, for small-scale, short-term operations unlikely to result in lock-in risks, a lock-in risk analysis might not be necessary. However, in such cases, transparency in the decision-making process is important for ensuring this flexibility is justified.

For both mitigation and adaptation, the joint methodological principles propose the use of a simplified version of the steps used for MDBs' own operations. The AIIB follows the joint methodological principles' approach, which for mitigation only includes assessing the potential for lock-in and impact on the country's transition pathway. For adaptation, it relies on a list of investments universally aligned, which includes trade finance, supply chain finance, diversified SME financing, and geographically dispersed or mobile assets, without clarifying why these activities would have no implications on a country's climate vulnerability. For the remaining activities, it analyses physical risks and relies on the counterparty's risk management processes to manage them. The EBRD and IDB use a different approach. The EBRD focuses mostly on using

⁶² Specifically for the World Bank, there is no particular methodology for corporates, and, as mentioned, its methodologies do not seem to include IFC and MIGA operations. For trade finance, a publicly disclosed Paris alignment methodology is important, given that, to date, the IFC has had no provisions for restricting trade finance from supporting climate-problematic activities. See, for example: urgewald, n.d., *Is the World Bank giving billions of trade finance to fossil fuels?* (accessed 3 June 2024).

⁶³ Including the use of low-emissions pathways, analysis of lock-in risks, analysis of alternatives, and indirect impacts.

the bank's safeguards, as expressed in their Environmental and Social Policy's Performance Requirement 9, related to FIs, and the nature of the sub-transaction, to determine alignment.⁶⁴ The IDB only mentions the need to develop its transaction-based approach as part of additional guidance needed for implementing the methodology. Only the World Bank mentions using the same steps used in its Investment Project Finance approach for mitigation. For adaptation, its approach is similar to that of the AIIB in that the method analyses physical risks, but these risks are managed by assessing the counterparty's ability to manage them. MDB support is needed, given that many counterparties will not have sufficient capacity to comprehensively assess transactions. This situation also highlights the importance of applying the counterparty alignment approach to all counterparties.

Overall, there is substantial room for improvement in MDBs' approaches regarding the alignment of finance directed to both FIs and corporate counterparties.

	
SCOPE OF IMPROVEMENT	BEST PRACTICE
<p>The counterparty-based approach is currently only an indirect means of ensuring Paris alignment, which may only become effective over time. If only the counterparty-based approach is applied, MDBs may not be able to verify their investments' Paris alignment during the transition period of FIs. Hence, during the transition period of FIs, an immediate stoppage of the most climate-damaging investment types (e.g. exploration and extraction of coal, oil, and gas) should be a required precondition for receiving MDB finance.</p>	<p>Only the World Bank mentions that for its transaction-based approach, it will be using the same steps used in its Investment Project Finance approach for mitigation.</p>
<p>MDBs that have not yet clearly defined a transaction-based approach should do so, including a full 1.5°C compatibility test and responsiveness to climate vulnerabilities as outlined in this paper, even if flexibility is required under certain circumstances.</p> <p>If MDBs only apply the transaction-based approach, FIs only need to ensure that MDB-financed projects and assets are Paris aligned. This may lead to MDB funds indirectly supporting non-aligned FI investments by bolstering the FIs' balance sheets. Thus, in addition to restricting the proceed use to Paris-aligned activities, the counterparty approach should be applied to all FIs to prevent fungible MDB finance from indirectly supporting counterparties' climate-problematic activities.</p>	<p>The EBRD's methodology requires all FIs with which it enters into new financing agreements to commit to Paris alignment.</p>

Scope for improvement and best practices identified for the assessment category 'Financial intermediaries and corporate counterparties'

⁶⁴ For example, the size and whether the transaction is targeted toward SMEs or contributes to climate goals.

MDBs should demand clear requirements for FIs' transition plans, including clear time-bound milestones ensuring full alignment by no later than 2030, with earlier deadlines for exiting fossil energy financing.

The AIIB's methodology requires a set of time-bound targets for establishing Paris alignment requirements. It requires a timescale and resource plan for achieving the identified actions and targets, over the short (2025) and medium (2025–2030) terms.

The joint methodological principles do not require the MDBs to provide support for counterparties to implement their Paris alignment commitments. MDBs should provide support for counterparties' transitions by default, including seizing opportunities for supporting the Paris goals in respective business areas.

The EBRD, World Bank, and IDB methodologies foresee some type of support for FIs to develop their Paris alignment plans and management systems. The World Bank specifies the type of support such as technical assistance, training, and institutional development support to help FIs operationalise their Paris alignment methods.

The joint methodological principles and most individual MDB Paris alignment methodologies do not establish a clear way of monitoring the counterparties' Paris alignment implementation and halting support if FIs do not keep their commitments. MDBs need to ensure that respective monitoring is undertaken; resulting in clear negative consequences when there is non-compliance.

Only the EBRD will annually monitor progress in the FI's development and implementation of expected transition plans – including exercising rights and remedies up to stopping further engagement with the FI in case that FI fails to fulfil its Paris alignment commitment.

3.6 Transparency and participation

3.6.1 Transparency

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Transparency and Participation	Transparency	Does the methodology include a commitment that individual operations' Paris alignment assessments will be publicly available, including detailed results of the individual tools and methods applied?	–	–	–	–	–
		Does the methodology foresee inclusion of Paris alignment considerations in intermediate evaluation of individual MDB operations?	–	–	–	–	–
		Does the methodology foresee an ex-post evaluation of lessons learned and effectiveness of Paris alignment for individual MDB operations, which can inform the design of future operations?	–	–	–	–	–

 Yes
  Partially
  No

Table 13: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Transparency'

Regarding transparency, two main aspects were assessed herein:

- Whether the methodology includes a commitment for Paris alignment assessment of individual operations to be publicly available and communicated to interested and affected stakeholders. This should include detailed results of the individual tools and methods applied, as part of the operations' documentation.
- Whether the methodology foresees including Paris alignment considerations in the monitoring and reporting for certain MDB operations, such as in progress reports or intermediate and ex-post evaluations of operations. Requiring information on lessons learned and effectiveness of Paris alignment in operations' progress reports or evaluations would enhance transparency and could also inform the design of future operations.

Neither the MDB joint methodological principles nor the MDB Paris alignment methodologies assessed

include a commitment to making the full Paris alignment assessment of their individual operations public, including the details on applying specific assessment tools. However, in practice, MDBs such as the AIIB provide either a reference to Paris alignment in their project summary documents or a short summary of the Paris alignment investment results, though the detail and structure of what is provided vary substantially. The IDB discloses a full climate change annex for most of its operations, including detailed application of the Paris alignment assessment. Other MDBs should follow the IDB's lead and disclose comprehensive Paris alignment assessment results. All MDBs, including the IDB, should also specifically commit to doing so (including for corporate and private sector operations) in their Paris alignment methods. Mere summaries lack sufficient detail to be meaningful.

Neither the joint principles nor the individual Paris alignment methodologies establish the inclusion of Paris alignment considerations in their operations' intermediate and final reports and evaluations. This absence is a missed opportunity to draw important lessons on how Paris alignment fares during implementation. All MDBs should commit to including aspects of Paris alignment implementation in the monitoring and evaluation processes of individual operations, and report on this at an aggregate level.

Finally, no methodologies allow for a period for interested stakeholders to provide feedback on individual Paris alignment assessments of operations. This is unsurprising considering MDBs have not even committed to publishing these assessments.

Such lacking transparency will make any independent assessment of the implementation, as well as board oversight and accountability of the MDBs' Paris alignment methodologies, impossible. Considering the methodologies leave ample scope and flexibility for individual teams within the banks to apply them differently and with different tools, relevant independent assessments of the consistency in their application across operations will also be impossible. This is a missed opportunity for MDBs to enter into dialogue with other stakeholders to improve methodologies and extract important lessons from their implementation. Transparency is crucial for any form of good governance and accountability. Without transparency, there is no way to prove MDB operations' Paris alignment.

Scope for improvement and best practices
identified for the assessment category
'Transparency'



SCOPE OF IMPROVEMENT

In their methodologies, MDBs should include a commitment to making the full assessment of individual operations public.

In their alignment methodologies, MDBs should also commit to including Paris alignment aspects in monitoring and reporting processes for individual operations.



BEST PRACTICE

Though the IDB does not specifically commit to full public availability in its Paris alignment methodology, in practice, the full Paris alignment assessment for most IDB operations (except IDB Invest) is publicly available.

3.6.2 Participatory process

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Transparency and Participation	Participatory processes	Does the methodology anticipate a feedback period for public stakeholders to submit views on an operation's Paris alignment assessment results once the assessment is published?	–	–	–	–	–
		Does the methodology foresee for the possibility of recourse on the grounds of a project's non-alignment with the Paris Agreement (through, for example, redress or complaint mechanisms, at the planning and implementation stage of certain operations)?	–	–	–	–	–
		Does the methodology foresee a participatory process when conducting the Paris alignment assessment? Is MDB personnel required to contact relevant national stakeholders or consult with relevant stakeholders to obtain pertinent information for an operation's Paris alignment assessment?	–	–	–	–	–

 Yes
  Partially
  No

Table 14: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Participatory processes'

Regarding participatory process, the focus is on processes that allow for stakeholders' input on Paris alignment at an operation's planning stage, and on the possibility of recourse concerning an operation's approval, on the grounds of the operation's non-alignment, such as through existing redress or complaint mechanisms.

No MDB methodologies assessed explicitly allow for either of these two forms of participation, making it difficult for interested and relevant stakeholders to shape the Paris alignment aspects of individual opera-

tions or to prevent potentially non-aligned operations from progressing.⁶⁵ This latter point is compounded by the lack of transparency in the individual assessments, which are not expected to be made public in full by all banks. MDBs should commit to including Paris alignment as part of their consultations during the operations' design, and to making these consultations as inclusive as possible.

Stakeholder participation should be encouraged in MDBs' methodologies to ensure additional checks on operations' Paris alignment. All MDBs have committed to regularly reviewing and updating their methodologies.



⁶⁵ For some banks, existing redress mechanisms might extend to appeals on the grounds of Paris alignment, but it is unclear for which banks this is the case, depending on the institutional status of their Paris alignment methodology.

3.6.3 Review of the methodology

Category	Indicator	Sub-Indicator	Joint MDB	EBRD	IDB	World Bank	AIIB
Transparency and Participation	Review of the methodology	Will the methodology be regularly reviewed and updated to integrate lessons learned, new international developments, and the latest science?	✓	✓	✓	✓	✓
		Does the methodology specify a process for the review that includes participation and consultation with different stakeholders?	✗	✎	✗	✗	✎

 Yes
  Partially
  No

Table 15: Assessment results for the joint MDB methodological principles and for individual MDB Paris alignment methodologies for the category 'Review of the methodology'

Finally, this assessment looked at the MDBs' processes for reviewing and updating their Paris alignment methodologies, including whether a process allows for participation by and consultation with relevant stakeholders. All MDBs have committed to reviewing and updating their methodologies, which is important given that insights arising from practical application should be fed back into the methodology, and that changes in scientific evidence and pathways necessitate adjustments to ensure quality. Some banks, such as the IDB and EBRD, have established timelines for this review. The EBRD uses an annual review, with updates as required, while the IDB will review its methodology one year after approval.

The EBRD has clearly defined its review and updating process and any major updates to its methodology will be subject to public consultation. However, how major updates and specific processes are defined is less clear. The AIIB will update its Paris alignment methodology periodically and already expects and welcomes feedback from a range of stakeholders during the application of its Paris Agreement methodology, though this feedback collection process also is not further defined.

Though it is not specifically mentioned in their Paris alignment methodologies, in practice, certain MDBs may still have policies or processes in place that promote and/or require exchange and consultation with civil society. The World Bank, for example, mentions on its website⁶⁶ that as it began implementing Paris alignment, it has been committed to receiving feedback and learning. The website notably mentions that the bank welcomes stakeholder views as it continues to refine and review its experience with clients, other MDBs, and civil society. However, its Paris alignment methodologies should also specifically mention a clear commitment to including feedback from stakeholders, such as civil society.

⁶⁶ World Bank, n.d., *About the Paris Alignment Assessments* (accessed 2 June 2024).

Scope for improvement and best practices
identified for the assessment category
'Review of the methodology'



SCOPE OF IMPROVEMENT

All MDBs, as part of their commitment to review and update their Paris alignment methodologies, should further specify the process in terms of regular timelines for review and feedback collection from a range of stakeholders, including civil society.



BEST PRACTICE

All MDBs have committed to reviewing and updating their methodologies. The EBRD commits to an annual review, with updates as required.

In their methodologies, the EBRD and AIIB specifically refer to public consultations and the inclusion of feedback from a range of stakeholders.

4 Conclusion

By publishing five Paris alignment methodologies in 2023, the MDBs have made substantial progress on their 2017 Paris alignment commitments. Ambitious Paris alignment methodologies can be effective tools for supporting the climate transformation and important in addressing the current crisis cascade. However, there is clear scope for making the methodologies more transformative.

- MDBs should transition from a risk-based, do-no-harm approach to a more proactive approach. MDBs' methodologies should be revised to ensure that *all* MDB financing seeks to support the transition *wherever possible*, and that Paris goals are considered from the country engagement process' inception through to the investments' impact assessment. These actions require implementing systematic mainstreaming processes within the MDBs, which the methodologies should speak to.
- The joint MDBs' List of Activities Considered Universally Aligned with the Paris Agreement's Mitigation Goals or Not Aligned with the Mitigation Goals should be updated. The update could focus on revising the Universally Aligned List's 'preface' on fossil fuels to determine that operations on the list should undergo a shorter specific assessment, focused on assessing and managing lock-in and transition risks, in certain cases. Alternatively, infrastructure that can benefit and expand fossil fuels – such as ports and electricity transmission and distribution – should be removed from the automatically aligned list. Direct and indirect finance of activities related to expansion of upstream and midstream fossil gas, oil, and coal should be added to the non-aligned list.
- MDBs should use their counterparty engagement, and particularly their counterparty-based approach, to support their counterparties' alignment, further driving action beyond the direct scope of their finance. The counterparty-based approach should be strengthened to increase its reach, include safeguards against non-alignment during transition periods, and move away from a risk focus and toward a more proactive, do-good approach.

MDBs, in line with recent commitments for stronger cooperation,⁶⁷ should continue collaborating on Paris alignment to learn from each other, share analytical capacity and insights, and improve and harmonise their approaches. The upcoming and regular reviews of the Paris alignment approaches, as announced by several banks, are a favourable opportunity to do so. Moreover, the MDBs' recently communicated support for country-led platforms to enhance in-country coordination⁶⁸ could be a vehicle for systematically mainstreaming Paris alignment in country diagnostics, partner country dialogue, and country strategies, and in donor coordination. These efforts should come with a view to seizing opportunities for transformative climate action and a just transition, based on forward-looking climate transition and development pathways developed jointly with client countries. Scaling up support for countries in improving their national climate strategies and policies, such as through policy-based financing⁶⁹ and existing NDC and LTS support programmes, is a key aspect of aligning climate and development goals and will facilitate MDB operations' future Paris alignment.

This paper provides MDBs with specific suggestions for revising their Paris alignment methodologies, as well as the joint MDB methodology. MDBs' upcoming updates of their individual methodologies should take these recommendations into account. Jointly with their learnings from the first year of practical implementation, all insights and review should be fed into a process for also revising the joint MDB principles, which form the basis of MDB methodologies, including those still being developed by, for example, the AfDB and IsDB. While a joint principles update may require greater political effort to implement, ensuring consistency of standards across the MDBs – a demand by partner countries and a declared objective by the MDBs themselves – is all the more important.⁷⁰

Similarly, the MDBs (such as the ADB) or MDB arms (such as the IFC) that have not yet developed their own methodologies will benefit from publishing such a document. Along with ensuring personnel's consistent application through providing further guidance on how the joint principles are to be operationalised and adapted to the bank's own institutional processes, this is important for enabling transparency and accountability. Monitoring how the IFC and MIGA ensure Paris alignment of instruments such as trade finance is particularly important.

Given the MDBs' forerunner role, many subregional and national development banks will seek to learn from them in establishing, refining, and evaluating their own climate-related processes. Thus, the MDBs' methodologies have an exemplary function and can set important standards for Paris alignment in the international development finance system. This function makes an ambitious and clear design, and regular quality updates, even more essential.

Finally, it will be helpful for Paris alignment methodologies to be given sufficient weight in the governance structures of individual MDBs, improving their official character. When the methodologies are merely internal procedural documents, providing operation design guidance for teams, they lack the same status and weight as strategic documents and policies within the MDBs. This disparity makes it more difficult to mainstream alignment considerations and initiate broader internal changes in MDBs' tools, frameworks, and policies. It may also pose challenges regarding the legal status of decisions made based on the methodologies and regarding the application of complaint mechanisms. Therefore, alignment principles should be adopted at a more strategic and policy level, following each MDB's specific decision-making processes.

67 Development Committee, 2023, [Ending Poverty on a Livable Planet: Report to Governors on World Bank Evolution](#) (accessed 23 January 2024); European Bank for Reconstruction and Development, 2023, [COP28 Multilateral Development Banks \(MDB\) Joint Statement](#) (accessed 16 January 2024).

68 European Bank for Reconstruction and Development, 2023, [COP28 Multilateral Development Banks \(MDB\) Joint Statement](#) (accessed 16 January 2024).

69 Recommendations for designing Paris-aligned policy-based operations are provided in Germanwatch, NewClimate Institute, and World Resources Institute, 2021, [Aligning Policy-Based Finance with the Paris Agreement](#) (accessed 24 January 2024).

70 International Finance Corporation, 2023, [COP28 Multilateral Development Banks \(MDB\) Joint Statement](#) (accessed 23 January 2024).

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