CLIMATE FINANCE SERIES

POLICY BRIEF 42

ENHANCING READINESS FOR CLIMATE FINANCE

EXPERIENCES FROM EASTERN AND SOUTHERN AFRICA

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POLICY BRIEF

CLIMATE FINANCE READINESS
IN EASTERN AND SOUTHERN AFRICA

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KEY POLICY RECOMMENDATIONS

- **Politically endorse** inter-ministerial and cross-sectoral institutional arrangements
- **Align** climate investment planning with national development **priorities**
- Implement incentives for **leveraging** banking and private sector resources
- **Integrate** climate change into public finance systems

Introduction

The UNDP-OneWorld climate finance readiness (CFR) (CFR) in Eastern (Ethiopia, Kenya and Tanzania) and Southern Africa (Lesotho, Mozambique and Zambia) to assess the CFR status and aspirations of these countries. The outcomes informed these policy recommendations – with the aim to accelerate the climate finance readiness status of each country, and thus of the African continent.

The outcomes of this study strongly indicate that CFR progress (against all the indicators of readiness) will flow if ***four conditions*** are in place: if coordination is cross-cutting and politically mandated, if climate and development priorities are aligned with investor requirements, if the engagement of all key resources and stakeholders is incentivized and understood, and if climate finance expenditure is transparent within a fiscal system that stimulates domestic investment.

CFR is firmly on the development agenda

Climate finance readiness has become an increasingly prominent feature of development discussions throughout the developing world, as countries grapple with ways to finance their responses to climate change. This UNDP-OneWorld CFR project complements a body of work conducted by a range of institutions which continue to produce important work on climate finance. Institutions such as the World Bank, donor agencies and UNDP regional and country offices typically provide capacity-building support, for example in establishing modalities for direct access and integrating climate finance into public fiscal systems. The support provided by regional and global institutions is further supported by research and consulting organizations with climate finance capacity.

Climate finance readiness is crucial for Africa

The high impact of climate change in Africa provides more than sufficient motivation for structured, large-scale financial responses – and a rationale for climate finance. A country's CFR status is a combined function of its financial, economic, political and social systems. Being climate finance ready means that a country is able to plan for, access and mobilize financial resources from both public and private sources and to track and verify the correct use of these resources.

Developing countries are characterized by stretched fiscal resources and debilitating socio-economic challenges. This forces an almost exclusive dependence on external funding for climate mitigation and adaptation. Developed countries acknowledge this situation primarily through funding pledges via multilateral funds. However, pledges do not always materialize and the challenges to developing countries accessing funds that do flow are not insubstantial. Climate finance is thus unpredictable and frequently elusive.

Africa, a continent that is particularly vulnerable to climate change, needs to be constantly on the alert. Eight of the world's 20 most vulnerable countries are in Africa, with many already experiencing the reality of climate change (Wheeler, 2011). In Mozambique, recent severe climate events have cost the government an estimated US$4 billion per event; in Kenya during 1998-2000, a protracted drought cost the country 16 per cent of its GDP; in Zambia, flooding in 2006-2007 left hundreds dead and 1.25 million homeless.

This supports the contention that damage from climate change, relative to GDP and population, is likely to be higher in Africa than in any other region. Studies suggest that the cost of climate damage in Africa, as a percentage of GDP, could be 10 per cent higher than in India (which is the next most exposed region), and more than twice as high as in the US, Russia, Eurasia or Latin America (AfDB, 2011).

The most crucial step for countries receiving climate finance is to make climate change an explicit component of their national development objectives and financing structures. The UNDP CFR framework thus defines readiness for climate finance as:

> *"The capacities of countries to plan for, access, deliver, and monitor and report on climate finance, both international and domestic, in ways that are catalytic and fully integrated with national development priorities and achievement of the MDGs"*
>
> VANDEWEERD, GLEMAREC AND BILLETT, 2012

All eyes are currently on the Green Climate Fund (GCF), which is emerging as a central fund in the global climate finance architecture. African countries have an opportunity now to get ready to access the GCF when it opens for business in 2015. Focusing on the four conditions (as outlined) will ensure that countries meet the GCF requirements for different governance and delivery systems. Furthermore, establishing these conditions will greatly assist countries in demonstrating a paradigm shift, or transformational change, towards practices that are compatible with the challenges of climate change (low emissions and climate resilient development pathways). Transformational change was a key principle of the GCF, included in the GCF agreement at COP 17 in Durban (2011).

Countries that can demonstrate a clear plan and progress towards transformation will be termed as ready to access the GCF. Aligned closely with the CFR Indicators considered in this study, this transformative approach is embedded in the key principles of ownership and country-led approaches, enhanced accountability, engaged stakeholders and systems for measuring transformation.

Indicators for readiness emerged from the participatory analysis

If the countries in this study are representative of a continental situation, then CFR as a topic is high on Africa's agenda. The level of observed political will and engagement is instructive, facilitating ease of sharing of domestic and global climate finance successes and barriers between project countries. Interviews complemented the desktop review, allowing the OneWorld team to examine the institutional framework for implementation, the level of national planning and coordination, and the presence of social, environmental and fiduciary systems and standards. Designated members of lead and sector ministries on climate change, mandated national authorities, development partners, financial institutions, NGOs and civil society, and national experts all helped to clarify the criteria for country readiness to access multiple sources of funds. Critically, a shared learning platform among all six countries facilitated a deeper discussion on understanding exactly what constitutes readiness, proving to be a useful tool in itself.

However, being climate finance ready is a moving target, and countries will do well to evaluate their readiness status regularly. A set of CFR Indicators (Table 1) built on the four UNDP pillars of planning, accessing, delivering and monitoring climate finance, emerged from the discussions and expert analysis arising from the UNDP-OneWorld project. These indicators define the ideal state of readiness, creating a benchmark for charting Africa's progress.

Table 1. CFR Indicators

FINANCIAL PLANNING
1. Cohesive Policy Framework 2. Resource Mobilization Plan 3. Politically-endorsed Institutional Arrangements 4. Mechanisms for Local Delivery
ACCESSING FINANCE
5. Accredited National Modalities for Direct Access 6. Established Mechanism for Blending Resources 7. Optimized Access to Global Funds
DELIVERING FINANCE
8. Leveraging Development Bank Partnerships 9. Incentivized Private Sector Participation
MONITOR, REPORT & VERIFY (MRV)
10. Harmonized M&E framework 11. Cohesive tracking framework, including CPEIRs

CFR challenges are common but differentiated

Although many of the challenges facing African countries are common to them all, the ways in which they manifest themselves in the six countries vary significantly. The impediments to the adoption of CFR measures, which affect all countries in the region, can be summarized as follows:

- Climate finance has, for a long time, been loaded in favour of mitigation, whereas African countries are more needful of adaptation finance.
- The overlap of development and climate change needs in most of Africa tends to widen the adaptation finance gap.
- Bilateral funding, to which African countries tend to have easier access, is too often driven by donor agendas, leaving recipient countries vulnerable to the vagaries of donor funding cycles and agendas.

Global challenges derive, in the main, from the complex institutional architecture of the global funds. Capacity constraints on the other hand typify internal access issues, negatively affecting a country's absorptive capacity. A country's inability to absorb climate funds can further affect predictability, as pledges consequently do not convert to financial flows.

The combination of these factors results in unpredictable climate finance flows, often leading to small, project-based responses, rather than the scalable programmatic responses that are really needed. This significantly slows progress in building overall resilience to climate change and contributes to the variable status of CFR in the six countries studied. It also explains why some countries have stronger policy frameworks than others, and why some are stuck in critical processes such as the establishment of direct access modalities.

Given the rapid evolution of the climate finance landscape over the last decade, it is not surprising that most of the countries studied have struggled to domesticate new requirements while at the same time striving to access funds and implement projects. As mentioned, the tendency towards project-based responses driven by bilateral agreements, rather than programmatic national resource mobilization plans, is a progress inhibitor. Whereas most of the countries have made some progress towards developing policy frameworks and institutional arrangements, none has made significant progress with implementing the UNFCCC negotiated system of Monitoring, Reporting and Verification (MRV).

Successes in accessing finance, optimizing access to global funds, partnering with and incentivizing the private sector, or coordinating with implementing NGOs are among the aspects of CFR that manifest themselves differently between countries. These differences are the result of different systems, politics, cultural factors and development priorities.

The 2009 Copenhagen Accord required a commitment of substantial "new and additional" resources by the developed world, without defining precisely what this term should mean. This concept of "additionality" compounds the uncertainties faced by developing countries. Clarity on this issue is necessary. However, the recommendations in this policy brief are premised on the key analytical finding that climate and development activities should be integrated as far as possible.

There are domestic challenges that are within a country's reach. Issues of institutional coordination across sectors and the ability to mobilize domestic sources of finance, including private sector resources, dominate. Governments in Africa have an opportunity to accelerate readiness through political mandates and institutional reform, taking more control of their own agendas.

The Plan for Action guides transformation

Taking action to accelerate readiness requires enhanced capacity ***across all key stakeholder groups.*** This will ensure that Africa is alert, ready and able to access climate change funds, especially when the GCF opens for business in 2015.

Enabling actors for CFR

Climate finance flows are neither purely public nor purely private. There are capacity requirements at each level of government, across many sectors, as well as within support and partner institutions, including the private sector. ***The main stakeholders for CFR can be broadly categorized as government, the private sector and civil society***. These stakeholders are incentivized by very different forces and therefore have significantly different skills and capabilities. Clarifying roles and responsibilities and the related capacities required at the policy, institutional and individual levels, across government, the private sector and civil society, is essential to effect the Plan for Action.

Government is the custodian of climate-smart development and is responsible for stimulating private sector action and for leveraging critical strategic partnerships. Its fundamental function is in strategic planning and ensuring alignment of climate change with national priorities, accessing and leveraging climate finance and creating an enabling environment for delivery and implementation. It has ultimate responsibility for ensuring that monitoring, reporting and verification are coherent and coordinated.

The private sector includes multinational corporations, commercial banks, small and medium enterprises, micro-finance institutions and households. Many of these actors have something to contribute to building climate resilience, through financial and human resources, skills and technologies. National development banks, although not purely private sector institutions, also play a crucial role in supporting access to and delivery of climate finance, for which their financial and technical capacities are required.

Civil society, or the array of non-governmental and not-for-profit organizations (NGOs/NPOs) that include community groups, labour unions, indigenous groups, charitable organizations, faith-based organizations, professional associations, and foundations, often has skills and capacity that can be used to plug government gaps. In this way, civil society can link high-level policy to grassroots-level implementation of climate finance. Organizations that play an accountability role are critical overseers and monitors of government spending on climate finance. Civil society therefore promotes transparency and accountability on the part of the government in making effective use of accessed funds. Moreover, NGOs, as implementing agents, often provide the skills and capacity lacking in government. Through both roles of accountability and implementation, civil society is well positioned to influence and enact climate policy, integral to planning for and delivering climate finance.

Enhanced institutional capacity is needed to enable most actions and to establish the critical conditions for readiness.

Establishing the conditions for accelerating readiness

In establishing the four identified critical enabling conditions, African Governments will be able to accelerate readiness, further supported by country ownership of their climate agendas. Ownership is demonstrated through clear prioritization of climate-smart development action, and reinforced by regular evaluation. Achieving these conditions will enable progress towards successful fulfilment of all 11 CFR Indicators. Taking targeted actions toward achieving the CFR Indicators will enhance absorptive capacity even in the face of a changing global climate finance landscape and shifts in developmental demands on governments.

Critical conditions for CFR

For the many African countries that face multiple demands for change, working towards each of the CFR Indicators under all four UNDP Framework pillars may be overwhelming. The reality of limited resources andcapacities heightens the need to identify the most important steps that African countries can take now to build an enabling environment for fast-tracking climate finance readiness. **The critical conditions for accelerated readiness are:**

- Politically-endorsed inter-ministerial and cross-sectoral institutional arrangements;
- Coherent, aligned investment planning;
- Established policy incentives for leveraging partnerships and resources; and,
- Climate-integrated public finance systems.

Although this study covered only six countries from two of Africa's five sub-regions, the outcomes can inform Africa-wide action for readiness. ***All African countries can benefit*** from sharpening their focus on these four most important conditions.

Politically-endorsed inter-ministerial and cross-sectoral institutional arrangements

Although a significant challenge, all case study countries have made progress – some substantially so. The study demonstrated that once coordination was mandated at the highest political level and suitable inter-ministerial arrangements were created, previously slow progress towards overall CFR accelerated rapidly. In the main though, these arrangements fall short of embracing other sectors and partners such as development banks, the private sector, civil society and research institutions. Consequently, the private sector and banks are unaware of their own climate risks, needs and roles. CSOs are not fulfilling their key functions of accountability and back-stopping capacity within government. Moreover, research institutions are often underutilized.

Coherent, aligned investment planning

The climate finance architecture is frequently said to be complex and difficult to navigate. Typical complaints include stringent criteria, lack of capacity to develop funder-acceptable projects and under-investment – for example by the development finance institutions (DFIs) in priority projects – particularly those that programmatically meet Africa's essential adaptation needs. Nonetheless, the countries analysed are accessing multi- and bilateral funds. A review of their record in accessing the funds allocated in the various rounds of the Global Environmental Fund (GEF) shows incremental improvement in most countries. Yet, many of Africa's adaptation priorities remain under-resourced and it would be simplistic to attribute this to issues of stringency and complexity only. Rather, national governments and investors do not talk to each other and when they do, timing and information are usually out of kilter.

National climate change and investment strategies and plans that are well aligned with development objectives are a critical success factor. However, investors need to comprehend and identify with them. It is the role of government to drive this process. It cannot expect the private sector to produce expertise, finance and technology without an understanding of the reasons for application or implementation. The same applies to CSOs and research institutions. Similarly, DFIs need insight into national requirements, while governments need to understand the reasons for their investment criteria. Bringing the two closer together will, for example, increase DFI investments into Africa's biggest climate-smart development projects. Water, already scarce but crucial to development and significantly threatened by climate change, is an important example of a sector that suffers from under-investment.

Incentivized and leveraged partnerships

Government may well play the leading role in financing climate-smart development, but it cannot chart and navigate this route alone. Partnerships must be leveraged across all the other stakeholder groups of the private sector and civil society. Experience demonstrates that leverage needs to be enabled and stimulated. Private sector engagement will be optimal only if incentivized. A partnership approach (between the public and private sector) to designing and implementing policy incentives is urgently required. These incentives need to be oriented toward Africa's adaptation agenda, drawing on prior and existing mitigation successes.

Ideally, civil society should be perceived and established as a critical partner to government. This necessitates effort by both stakeholder groups. Governments in Africa frequently perceive CSOs in a negative light, seeing them as either ineffectual or threatening. CSOs would do well to position themselves as partners rather than opponents to government. Conversely, the nature of civil society participation is dependent on government leadership in bringing itself and citizen groupings together in the climate finance discourse. Government needs to establish enabling policy for building inclusive climate-smart development responses and harnessing valuable CSO capacity and skills. Critically, the voice of CSOs needs to be enabled and heard.

Climate-integrated public finance systems

Africa wants the developed world to account for and reduce greenhouse gas emissions and recognize Africa's adaptation gap. It also needs predictable and adequate sources of finance for climate change. The developed world wants developing countries to quantify the adaptation gap (while taking some responsibility for reducing emissions), account for their climate finance expenditure in a transparent manner, and allocate domestic resources to climate finance. If predictable and substantial global sources of finance are to continue to flow into Africa, then African countries must ensure they are in a position to not only receive, but to adequately manage and track funding. Simply put, this means that recipient countries will access greater and continued resources if they can effectively monitor, report on and verify (MRV) their climate finance expenditure. This includes reporting on domestic and international resources.

The only way this can work is if climate finance is integrated into national public finance systems. Mainstreaming climate change strategies into national development agendas is the first step. This enables allocation of domestic resources. It also provides the basis for transparent accounting for climate change, gives ongoing insight into where the returns on climate investments are made, and builds the evidence for arguing the case for "additionality". Although several of the countries studied seem to shy away from the transparent allocation of domestic resources, most spend on adaptation and resilience building. However public finance systems are not codified to track climate spend. Consequently, in-country investments are under-recognized, compromising Africa's voice in the global negotiations when it comes to a balanced deal on adaptation and for finance to support this.

In summary, the study outcomes indicate that progress against all 11 CFR Indicators will flow if all four conditions are in place: if coordination is cross-cutting and politically mandated, if climate and development priorities are aligned with investor requirements, if the engagement of all key resources and stakeholders is incentivized and understood, and if climate finance expenditure is transparent within a fiscal system that stimulates domestic investment.

UNDP partners with people at all levels of society to help build nations that can withstand crisis, and drive and sustain the kind of growth that improves the quality of life for everyone. On the ground in 177 countries and territories, we offer global perspective and local insight to help empower lives and build resilient nations.

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OneWorld Sustainable Investments (OneWorld) is a climate and development consultancy and partner based in South Africa and operating across the African continent. OneWorld produces applied research, strategy development, policy analysis, thought leadership and interventions towards resilient development together with its partners and programme beneficiaries. For more information, see www.oneworldgroup.co.za.

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