V-LED | STIMULATING URBAN CLIMATE ACTION

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CLIMATE FINANCE

OPPORTUNITIES FOR ENHANCED LOCAL ACTION

V-LED AFRICA WORKSHOP: LOCALISING CLIMATE FINANCE AND ACTION

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ILEG Institute For Law & Environmental Governance

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”CC expenditure will absorb ~ 70% of domestic budgets” – City officials, NEPAD

- Mainstreaming climate action
- Enhancing basic service delivery
- Stimulating local socio-economic development

Small Scale Embedded Generation – City Power, Johannesburg
Water solutions, City of Cape Town

South Africa’s Triple Challenges - Equality – Poverty – Employment

Why Local Climate Finance?

Cities in South Africa

- Urbanisation relatively high (at 62%) and progressing rapidly, in line with, although slower than Sub Saharan African trends
- Local climate change response “largely fragmented and lacking in scale” (TAU & Western Cape Government 2013)
- Local Government will be responsible for delivering SA’s NDC

Example: eThekwini Municipality

- Important urban, economic and political center of South Africa
- Approx. 3.5 million people
- High poverty rate, HIV/AIDS, teenage pregnancy, etc.
- Service backlog: almost 400,000 houses; electricity and basic sanitation for 25% of population
- Emerging from the country-wide drought

Institutional framework for Local Climate Finance

Regulatory environment

- Municipal Systems Act
  - Determines the power and functions of municipalities, including integrated development planning, credit + debt management
- Municipal Finance Management Act (MFMA)
  - Rules and requirements for financial planning and management, borrowing, handling financial problems, etc.
- Division of Revenue Act
  - Determines division of revenue between levels of government for the financial year; describes the "duties of receiving officers"

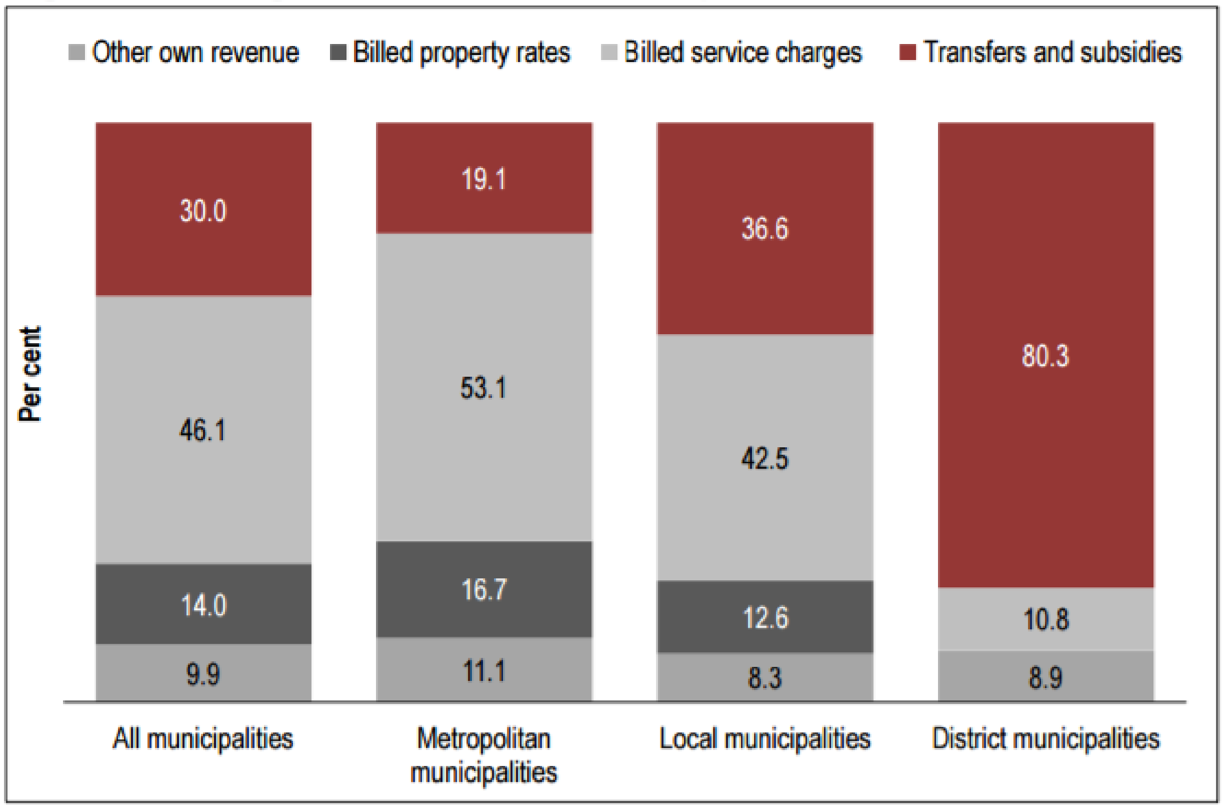
Institutional framework for Local Climate Finance

Mechanisms of municipal planning and finance

- Integrated Development Plan
  - 5-year policy framework for the development of a municipality
  - Basis for annual budget and annual implementation plan
  - In the main, are developed on paper but not implemented plans across SA
- Spatial Development Frameworks
  - Critical for climate change planning
  - Not well aligned with sector plans or IDPs
- Sector plans
  - Mandatory for housing, water, electricity, waste management, transport, local economic development, environmental management and disaster management
  - Specify how service delivery can be improved

Institutional framework for Local Climate Finance

Municipal revenues



eThekwini (2015):

- 48,2% services charges *(Electricity sales: 38% of total revenue)*
- 19,9% property tax
- 13,6% other
- 18% transfers/subsidies

Landscape of Domestic Climate Finance

Tracking climate finance

- No formal, publicly transparent system exists for tracking climate expenditure
- Various sources of international funding is used to supplement municipal resources, on an ad-hoc basis – predictability of climate finance is not yet secured, making planning difficult
- In eThekwini, project site selection is based on the City’s people-first approach, with projects prioritised in locations where unemployment and poverty prevail

Landscape of Domestic Climate Finance

Sources and mechanisms of funding

- Conditional grants – closing service delivery deficit and promote socio-economic development e.g. infrastructure and rehabilitation relief
- Unconditional grants – linked to broad goals, e.g. fulfilling constitutional service delivery mandate
- Transfers – e.g. general fuel levy sharing; assets transfers
- External sources (international, national, provincial) (95% Energy office budget, eThekwini)
- Intergovernmental grants, e.g. DOE Energy Efficiency funding (international sources - Danish Energy Agency) is provided through the EE Demand Side Management Grant, the Integrated Cities Development Grant and the Cities Support Programme
- Other sources include the Municipal Infrastructure Grant, Municipal Water Infrastructure Grant, the Municipal Disaster (Recovery) Grant

However, "Given the weak economic outlook and constrained resources, provinces and municipalities will be required to improve efficiency and increase revenue streams in order to support growth." National Treasury 2016

Examples of Local Climate Finance

- **Bergriver Municipality**: Climate Knowledge Network - successful joint funding application to Treasury for a currency project, FLOW focusing on youth to address social, economic and environmental issues
- **eThekwini Metropolitan Municipality** – Durban CC Strategy and Climate Change Compact - People First approach – increased access to disaster and donor funding
- **City of Johannesburg**: Green Bonds at 1,5 bn ZAR with market related financial returns; 150 new dual fuel buses and converting 30 buses to biogas; raised a 2 cents per kWh levy of electricity consumed above 500kWh/month, approved by NERSA: financed the roll out of 78 000 solar water heaters (SWHs) in low income areas.
- **City of Cape Town:** Progressive RE and EE strategies help the City leverage finance, e.g. from AFD; also raising a Green Bond with 10,1% financial return over 10 yrs – strengthen water infrastructure and purchase electric buses
- **Ekurhuleni:** adopted an Energy and Climate Change Strategy – leverage domestic funds

Challenges for Domestic Climate Finance

Political will for climate action

- **Climate change "competes" with other priorities**: eThekwini still struggles with many basic economic, social and environmental issues that seem to be more urgent
- **Effects of climate action across value chains are uncertain**: Loss of jobs, access to long term and decent jobs, protection of enterprises and equality issues are among the main concerns
- **The municipal revenue model creates a conflict of interests**: the bulk of municipal revenues come from electricity sales, creating a disincentive for emission reductions

Challenges for Domestic Climate Finance

Local knowledge and skills

- **Capacity issues prevail**, through a combination of inadequate human resources (many jobs vacant) and under-skilled staff
- **Knowledge of how to access international climate funds and to use these to leverage domestic sources** and what they fund, is low in most municipalities

Lack and inadequate use of resources

- **Service revenues are under invested in maintenance**, reducing water and energy efficiencies and increasing climate exposure (e.g. current drought)
- **Increasing electricity prices** have negatively affected municipal revenue from electricity sales, as has decreasing demand
- **Domestic budget allocations** are still relatively low (2015: 18%) and might become more restricted in the future:

Challenges for Domestic Climate Finance

Detrimental national legal and regulatory framework

- **The regulatory environment is limiting**, e.g. the MFMA does not lend itself to municipalities accessing climate finance, imposing limitations on what local government can do
  - Rolling three-year budget period prevents long-term planning
  - Municipalities may not independently seek international loans, with approval required at all times from the Minister of Finance
  - There is no system of national government guarantees in place
- **Interpretation of regulation** by national key players is often conservative, finding adequate compromises can significantly delay the implementation of climate projects; there is no incentive to establish solutions that are legal but outside a strict interpretation of the regulations

Challenges for Domestic Climate Finance

Credit worthiness

- South Africa is on the precipice of a downgrade to junk status, which also affects Metros, even though they have their own credit rating status; e.g. eThekwini has a solid credit rating

Lack or inadequacy of funds and financial mechanisms

- **The links between national structures for CF are tenuous** and urban centres are under accessing the global funds
- The secondary market for finance is under developed in SA, affecting liquidity and bonds for example are not cheaper than loans with relatively low impact but high transaction costs

Opportunities for Domestic Climate Finance

Improving climate planning and financial management

- A more strategic approach to CF access will help local government leverage further funds from donor and development banks which are increasingly available to municipalities that demonstrate success
- **Robust and consistent monitoring & evaluation (M&E) is a significant opportunity** for increasing climate finance access
- **Tracking climate finance** through M&E, Monitoring, Reporting & Verification and public expenditure frameworks will increase ability to access climate finance
- **Understanding and awareness of socio-economic impacts** of climate responses - SA's triple challenges - needs to be better understood and widely communicated

Opportunities for Domestic Climate Finance

Using international financial instruments

- The GCF provides a platform for accessing CF for scale, transformation and replication – and for contributing to the emerging performance metrics for the Fund

De-risking and credit enhancement

- Metros are well positioned to proactively distancing itself from the precariousness of national credit ratings, through careful M&E, following the principles of results based finance and effective reporting and verification

Opportunities for Domestic Climate Finance

National and international policy improvements

- SA's M&E Framework for CC is evolving – possibly strengthened through pilots
- SA's international climate contributions are under further development; local government has an opportunity to make a valuable and visible contribution to the realisation of both its adaptation and mitigation targets – toward sustainable development
- Enhanced disaster risk reduction (preparedness) as a policy direction, is a critical opportunity for many municipalities given increasing intensities and frequencies of climate disasters and is an important adaptation strategy

Recommendations for increasing domestic climate finance

- **Revise Intergovernmental Grants for climate resilience and low carbon development** (low hanging fruit) through transformative approaches that result in improvements to national poverty, employment and equality
- **Strengthen climate finance tracking and monitor progress of CC** – across all spheres of governance
- **Consider alternatives to municipal revenue models**, e.g. for embedded generation to demonstrate possibilities and gradually transform the electricity sales mind set
- **Improve structures** for climate planning and budgeting
- **Review interpretations of regulatory framework,** e.g. MFMA - in light of triple challenges and climate resilience

Benefits for different levels of governance

- Improved capacities for decentralised water and energy services, with socio-economic co-benefits – greater trickle down effect throughout the economy

- Risk mitigation for national fiscus - e.g. energy delivery no 100% dependent on one institution

- Achieved global climate targets = enhanced sustainable development across all spheres of governance

- Improved accountability – bottom to top

- Regulatory environment that is more modern and user friendly

An equitable transition to low carbon and climate resilient economy is feasible ito the National Development Plan

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