Briefing

Policy and planning

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Policy pointers

Transitions to climate- resilient green economies (CRGEs) need very large investments, and planning must respond to the specific financing needs of these.

Policymakers should identify intermediaries that are best placed to mobilise and disburse finances into CRGE investments. Some countries are establishing national-level climate change funds as intermediaries to ensure maximum synergy between funding streams.

Policymakers can deploy a range of economic instruments (including policy and regulatory frameworks) and financial instruments (such as guarantees and insurance, grants and loans) to provide incentives for investments in CRGE initiatives.

Financial planning systems also play a key role. Policymakers should establish relevant policy frameworks, develop strong institutional arrangements, and embed CRGE activities into planning and budgeting systems.

Financing a transition to climate-resilient green economies

Many countries see the advantages of a climate-resilient green economy, and several developing nations are already taking important steps to ease the transition. This briefing shares how Bangladesh, Ethiopia, Kenya, Nepal, Rwanda, the Gambia and Zanzibar are designing intermediaries, economic and financial instruments and financial planning systems that fit within the global climate finance 'landscape' and will help ensure governments are ready to leverage, manage and disburse climate finance from both public and private sources. Such actions will help meet the very specific financing needs of climate-resilient green economy investments.

Adopting a climate-resilient green economy (CRGE) pathway to development is a growing trend. In 2012, an estimated US$359 billion was invested globally in projects targeting low-carbon and climate-resilient development.[1] In particular, there are major changes in sub-Saharan Africa, where national plans and strategies are being formed as the basis for future legislation and in Latin America where climate change plans are already enacted in legislation, providing an enabling environment for investment. At the end of 2013 the Globe Study of 62 countries reported 487 climate change laws or policies.[2]

But there are gaps in the financing for this transition to a CRGE pathway. For instance, Ethiopia anticipates it will need to invest more than US$150 billion in its CRGE over the next 20 years. That amounts to an average of US$7.5 billion per year. In 2012, the country received US$43.31 million from OECD countries for investments in adaptation and mitigation. Shortfalls like this mean that countries will need to make existing investments more efficient and focus on leveraging additional sources of finance to address CRGE investment needs.

It's also the case that private sector investments dominate climate finance, accounting for 62 per cent of the total. Since most private finance originates and stays in developed countries, developing countries must consider innovative ways to leverage additional public and private sources to fill the funding gaps.

And most investment has so far been targeted at mitigation (94 per cent in 2011). This too has significant implications for developing nations, many of which do not have high carbon emissions to mitigate. Rather, developing countries prioritise adaptation and will support green economy initiatives only if they contribute to development objectives.

Climate-resilient and green economy investments also have specific financing needs. On the one hand, green economy initiatives have the potential to bring returns on capital investments and can attract private finance. On the other, climate resilience is seen as a public good and would usually need public finance in the form of grants. Both climate resilient and green economy investments require long-term financing as the

Developing nations are taking steps to ensure they are ready to receive, manage and disburse climate finance

financial return is only expected to be seen after many years.

This briefing takes the climate finance landscape framework developed by the Climate Policy Initiative (see Table 1)[1] and outlines how public policymakers in several countries are using it to support CRGE investments. We draw on evidence and analysis emerging from case studies conducted in Ethiopia and Rwanda in 2013 and on the outcomes of a national dialogue in Ethiopia and a cross-country dialogue between Bangladesh, Ethiopia, Rwanda, Kenya, Nepal, the Gambia and Zanzibar. Policymakers shared their experiences of the financial framework and identified ways to move forward through establishing intermediaries, using economic and financial instruments and deploying appropriate financial planning systems.

Identify intermediaries

Intermediaries play an important role in mobilising and disbursing climate finance for CRGE investments. They include multilateral banks and agencies, bilateral agencies, national agencies such as central and sector ministries, national financial institutions such as development and commercial banks and micro finance institutions, and climate change funds established to mobilise and disburse climate finance.

Different intermediaries are best placed to draw down specific sources of climate finance and to channel funds towards specific investment areas and investors. For instance, national development banks are good at accessing and pooling international and national sources of public and private climate finance. They can also effectively disburse finances for CRGE investments to a range of public and private sector investors.

Policymakers are successfully using a range of these intermediaries. Ethiopia, Rwanda and Bangladesh provide examples of intermediaries that have helped governments shift away from a project-based approach towards a programmatic approach. This allows fund managers to pool different sources of funding and allocate them in a way that makes the investment outcome greater than its actual value.

Ethiopia. The Government of Ethiopia has established a national climate change fund, known as the CRGE Facility, as the primary intermediary for mobilising and disbursing climate finance for CRGE investments. The facility has been designed to draw down and pool multiple sources of international and national finance, thereby mobilising resources efficiently. So far it has successfully accessed bilateral sources of climate finance and has applied for accreditation to the Adaptation Fund under the United Nations Framework Convention on Climate Change in order to access multilateral sources directly. The facility enables Ethiopia to manage climate funds within a single coherent system that lets investors engage and determine how best to invest to support the country's CRGE objectives. This 'programmatic approach' aims to minimise transaction costs, fragmentation and duplication associated with funding unconnected projects.

Rwanda. The Government of Rwanda has established a national climate change and environment fund, known as FONERWA. The fund has been designed to evolve as different sources of finance and new investment areas become viable. In the short to medium term, the Ministry of Environment and Natural Resources manages the fund to mobilise and disburse public sources of finance, while the Development Bank of Rwanda manages a credit facility to incentivise private sector investment. If investments into low-carbon climate-resilient development become commercially viable, FONERWA has the scope to evolve and be managed as a venture capital fund in the long term.

Bangladesh. The Government of Bangladesh has established a range of intermediaries to draw down various sources of climate finance. The Bangladesh Climate Change Trust Fund has mobilised US$347 million from national revenue sources to date. The Bangladesh Climate Resilience Fund (BCCRF) has mobilised US$188.2 from bilateral and multilateral sources of climate finance and the Pilot Programme for Climate Resilience (PPCR) under the Climate Investment Funds has mobilised US$110 million from multilateral sources of climate finance. The Green Banking initiative within the Central Bank of Bangladesh is set to play a strong role in leveraging national sources of private finance into CRGE investments.[3]

Beyond these national intermediaries, multilateral and bilateral intermediaries continue to play a role in mobilising and disbursing climate finances. For instance, in Nepal, the Gambia and Zanzibar a significant proportion of climate finance is mobilised and disbursed via the World Bank, UN and bilateral agencies. These intermediaries are successful in drawing down finance, but some policymakers support moving towards the national approaches adopted by Ethiopia and Rwanda in order to look for synergies between projects when disbursing finance, and to ensure better long-term financial sustainability.

Sources	Intermediaries	Economic and financial instruments	Financial planning systems	Uses and users
Public international and national finance Private international and national finance Carbon finance Philanthropic climate finance	Multilateral banks and agencies Bilateral agencies National agencies National financial institutions Climate Funds	**Economic instruments:** Policy frameworks Regulatory frameworks **Financial instruments:** Risk management instruments (guarantee; insurance) Grants Concessional loans Capital (equity, debt financing)	Policy frameworks (climate finance legislation and operational manuals) Institutional arrangements Budget and planning systems	**Uses:** Adaptation, mitigation, green economy, climate resilience **Users:** Public, private and civil society organisations.

Economic and financial instruments

Economic and financial 'instruments' provide incentives for investment in CRGE. Economic instruments (which include policy and regulatory frameworks) affect producers' and consumers' behaviour by causing changes in prices. For instance, the Government of Ethiopia is using power purchase agreements and feed-in tariffs to encourage investment in diverse sources of renewable energy. Similarly, the Government of Kenya is providing subsidies, tax exemptions and is developing policies like the Renewable Energy Feed in Tariff Policy to incentivise investments in renewable energy.[4]

A financial instrument is any contract that gives one entity a financial asset and another a financial liability. Financial instruments that incentivise CRGE investments include risk management instruments like guarantees and insurance, grants, concessional loans, and capital instruments of equity and debt finance. Different instruments will suit different investment needs. For instance, risk management instruments enable investors to invest in high risk investment portfolios. Grants are effective in supporting investments in climate resilience. Capital instruments are effective once CRGE investments are commercially viable.

The Government of Ethiopia is also planning to deploy a range of financial instruments through the CRGE Facility to support investments in CRGE initiatives. These include grants, concessional loans and results-based payments.

Similarly, the Government of Rwanda plans to deploy financial instruments in a phased approach to support the evolving financial needs of CRGE investments. Short-term financial instruments (operating for up to a year) include in-kind support like technical assistance, grants to support investments by public sector investors and performance-based grants to support investments by private sector investors. Financial instruments planned for the medium term (two to five years) include guarantees and low interest/concessional loans. Instruments for the long term (over five years) include equity investments that are subject to FONERWA's performance and to private sector demand.

Financial planning systems

Financial planning systems play a key role in managing finances. Governments are using them to support better synergy between different sources of finance and different investment portfolios, thereby leveraging investment outcomes that are greater than the sum of their parts. Governments also use financial planning systems to support longer term financing for CRGE investments.

Countries are relying on three specific aspects of financial planning systems to manage climate finance effectively:

Establishing relevant policies. First, countries rely on policy frameworks to establish financial planning systems. For example, in Bangladesh and Rwanda, climate change funds have been established in law. In Nepal, the government has developed a climate change policy to finance local-level adaptation, among other objectives. Ethiopia and Rwanda have developed operational manuals to guide how their climate change funds are managed.

Institutional arrangements. Second, countries rely on institutional arrangements to support better synergy between different sources of finance and different investment portfolios.

In Rwanda institutional arrangements to manage the FONERWA fund include a management committee, which is the highest organ in the Government of Rwanda for FONERWA management and oversight. The committee approves budgets and work plans and makes the ultimate funding decisions, and is responsible for monitoring and directing the fund's activities. Both the management and technical committee

are staffed by members from central and sector ministries. The technical committee is supported by a team from the Ministry of Finance, which ensures that there is no duplication between FONERWA-funded activities and activities already in annual plans. It also means that FONERWA-supported activities are aligned with national priorities outlined in the National Development Plan.

In Ethiopia, institutional arrangements to manage the CRGE Facility include a management team housed in the Ministry of Finance and Economic Development that is responsible for financial management; a technical team housed in the Ministry of Environment and Forest that is responsible for coordinating the CRGE planning process; implementing entities (sector ministries) that are responsible for identifying CRGE investment priorities; and executing entities (public, private and civil society organisations) that are responsible for managing the spending of CRGE investments.

Bangladesh, the Gambia and Zanzibar also propose to establish institutional arrangements. Arrangements for financial management will be led best by institutions such as ministries of finance that have the capacity to manage and disburse climate finance. Arrangements for coordinating climate change actions, especially decisions on fund allocations, should be led by institutions like national planning commissions as their 'bird's eye view' of investment priorities across sectors is advantageous: climate change is a cross-cutting issue and investments will achieve the best outcomes when they build on an existing portfolio of investments.[5,6]

Planning and budgeting. Third, countries rely on planning and budgeting systems to leverage synergy in climate finance and to support longer term financing.

Nepal has developed a climate change budget code to support financial management for CRGE investments.[7] The budget code helps in three distinct ways:

1. Tracking climate-sensitive expenditure within the national budget lets policymakers assess the costs of addressing climate change and can also be used to assess the effectiveness targeted investments.
2. A climate change budget code helps integrate CRGE interventions into a broader portfolio of investment, thereby unlocking other sources of capital.
3. Integrating CRGE into the budget system also helps shift to longer term financial planning. Budget codes reflect a country's strategic priorities, helping ensure that government bodies plan to address these priorities through annual and mid-term planning and budgeting.

Rwanda has also used budget and planning systems to leverage greater synergy between investments. Funds disbursed by FONERWA are incorporated into the annual budget allocation of government ministries and public sector agencies to encourage integrated investment and avoid duplication and fragmentation. The fund uses the reporting systems of the Rwanda Development Bank to account for FONERWA funds disbursed to the private sector.

These evolving trends in the design of intermediaries, economic and financial instruments and financial planning systems show how many developing nations are taking important steps to ensure they are ready to receive, manage and disburse climate finance from both public and private sources. They are becoming better-placed to respond to the specific needs of the large-scale investments required to transition to climate resilient green economies.

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Notes

[1] Buchner, B et al. 2013. The global landscape of climate finance. Climate Policy Initiative http://climatepolicyinitiative.org/wp-content/uploads/2013/10/The-Global-Landscape-of-Climate-Finance-2013.pdf / [2] GLOBE. 2014. The Globe Climate Legislation Study, fourth edition. www.globeinternational.org/pdfviewer / [3] Pervin, M and Moin, S M I. 2014. Climate finance governance in Bangladesh: synergies in financial landscape. IIED. / [4] Nzau, V M. 2014. Climate change financing in Kenya. IIED / [5] Vuai, S H. 2014. Zanzibar planning and financing systems for climate change initiatives. IIED / [6] Camara, I F. 2014. Climate change financing in the Gambia. IIED / [7] Sharma, H P. 2014. Climate change financing in Nepal. IIED