



Delivering real change

Getting international
climate finance to the
local level

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Clare Shakya and James Macgregor

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With the rapid ratification of the Paris Agreement, international climate funds will be important in scaling-up developing countries climate action. Evidence shows climate finance reaching the local level – as part of a coherent approach to climate action – delivers effective, efficient and sustainable results that enhance the impact of each dollar disbursed. This working paper explores the flows of climate finance within the main international climate funds, to understand how effective they are in getting finance to the local level and what design features enable or prevent local financing. It distils lessons from development funds that are experienced in local financing. It concludes by highlighting the ways in which local climate financing can be enhanced – to further improve the effectiveness of aid.

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Summary

With its rapid ratification, we are moving more quickly than expected into delivering the Paris Agreement. This will require a scale-up in climate finance – for which international funds will play an important role. To deliver the ambition of Paris, it is crucial that every penny of the finance available is used effectively and efficiently, addressing the vulnerabilities of those most in need and helping them escape poverty through climate-resilient sustainable development. Delivering climate and development finance to the local level – through community engagement and with devolved decision-making can bring such results.

This paper recognises that climate action is needed at the international, regional and national levels. However, given the value of enabling communities to engage in setting priorities and the limited flows of flexible finance to the local level, the question we ask is **how can the delivery of international finance be improved so it is more effective in reaching the local level?**

The flow of finance to the local level is unknown

There is no definitive understanding of the amount of climate or development finance that reaches local actors. A preliminary estimate of the finance channelled to local climate activities puts the flow below ten per cent (US\$1.5 billion) from international, regional and national climate funds between 2003 and 2016.

Getting to the true figure would require donors disclosing much more information about how the finance they disburse is delivered, to whom, for what purpose and whether communities are engaged in deciding how it is spent. At present, climate and development funds do not provide this level of transparency. Nevertheless, this initial estimate indicates an imbalance in how climate finance is distributed.

Why is climate finance struggling to reach the local level?

The metrics of success: the investment strategies of many funds prioritise large-scale results. For example, the Clean Technology Fund (CTF) and the Green Climate Fund (GCF) primarily judge projects on the tonnes of carbon reduced and the mobilisation of private co-finance, all of which incentivise large energy investments. This deprioritises services to the local level. If the numbers of people with access to energy were given greater weight, decentralised energy programmes could gain greater investment and provide poor communities with access to energy faster.

Business-as-usual intermediaries: traditional financing intermediaries, such as the multilateral development banks, are less able to finance small-scale projects directly, given the higher transaction costs. Where funds like the GCF can provide direct access for developing countries, they still mostly go through the UN and multilateral banks, with no specific priority to reach local actors.

Risk-averse funding: although a range of innovative financial instruments are available which could help unlock domestic private and public finance, few of these instruments have been used – suggesting a low tolerance to risk. The GCF has used a range of guarantees and equity funding within its early investments, indicating that it is willing to take greater risks.

Limited support to build local capacity: local management capacity is often a barrier to financing, with concerns over financial mismanagement. However, few funds provide capacity support for building local capacity, and those that do seldom allow sufficient time to build the skills needed.

Inappropriate co-financing targets: many international climate funds require co-financing, which has led to unsustainable projects and delays when co-financing has not come through as expected. There is also a preference for working with national governments who can co-finance, again reducing the potential for ownership by, and accountability to, local communities.

Poor oversight of policies for local finance: although innovative local financing policies have been designed, as outlined below, inadequate monitoring of these policies has led to non-compliance. Most funds suggest at least some level of community engagement in funding decisions, appraisal and evaluation. However, despite the Addis Ababa Action Agenda and the Paris Agreement recognising the importance of local engagement, no international goal on local financing exists. The US Agency for International Development (USAID), through its *Local Solutions* programme, has set a target of 30 per cent of its total financing portfolio to reach the local level. Although this ambitious target has not been met, it has increased the flow and led to improved policies.

What lessons can be drawn to improve the delivery of local financing?

Evidence from international development, bilateral and climate funds that focus on reaching local communities has shown that local programmes can deliver a ‘triple win’, producing more sustainable results at lower cost, developing local capacity and generating climate-positive local economic development benefits, such as improved livelihoods, reduced pollution, and access to clean energy. Examples of such funds include:

- The Global Environment Facility’s (GEF) Small Grants Programme.
- The Forest Investment Programme’s (FIP) Dedicated Grants Mechanism.
- DFID financed Decentralised Climate Funds in Kenya – County Climate Change Funds.
- The Local Disaster Risk Reduction Fund in Bangladesh.
- The Global Fund for Aids, Malaria and Tuberculosis (Global Fund).
- The UN Capital Development Fund (UNCDF).
- The Caribbean Development Bank’s Basic Needs Trust Fund (BNTF), and
- The World Bank’s Community-Driven Development (CDD) initiatives.

What funding policies and architecture promote local finance within these funds?

Priorities for locally relevant results: where there is a greater emphasis on community-relevant interventions, more local projects have been supported. This includes climate change adaptation, where the results frameworks of the Adaptation Fund and Least Developed Countries Fund (LDCF) include more locally specific indicators to deliver improved resilience or to reduce vulnerability to climate change, measured at the household and community levels.

Many small results can deliver big impact: climate funds focused on local results have allocated individual grants at scales below US\$500,000 – which are more appropriate for local activities. Small initiatives have been scaled up within development funds, especially the World Bank’s CDD, by undertaking a programmatic approach that brings a range of implementers together to deliver low carbon climate-resilient development to communities at significant scale.

Grants and innovative financing: these funds have all used grants to finance community-based projects that are appropriate, the Kenyan County Climate Change Funds have even used these grants to mobilise significant local public sector finance. There is little evidence, however, that the funds are experimenting with innovative financial instruments at any scale to unlock local private sector finance, such as municipal bonds, guarantees, and equity investments that have been undertaken through the UNCDF.

Simplified access and approval: as local actors have a limited track record in managing climate finance, some funds such as the FIP, have designed simplified funding frameworks that make it easier to apply for funding. USAID are using third party monitors and spot checks of grant recipients who are weaker on financial management to help manage fiduciary risk.

Participatory funding structures: the best performing funds – the GEF Small Grants Programme and the BNTF – have participatory funding structures whereby local communities are able to engage directly in the design, appraisal and evaluation of climate and development projects. As well as the FIP Dedicated Grants Programme, the Global Fund and UNCDF programmes, these funds are governed by multi-stakeholder committees at the national level that include local community representatives.

What needs to be done to improve local climate and development finance?

To be effective, climate and sustainable development interventions must take place at every level. Evidence suggests that this is not happening and that too little finance is reaching local communities. Action needs to be taken to address this imbalance. By both reforming how the finance is tracked and the funding architectures, climate and development finance could deliver improved results to those who need it most. We recommend that donors and the international funds:

1. Identify the baseline of finance that reaches the local level and involves community participatory processes.
2. Use the baseline to set an international goal for local finance.
3. Earmark flexible, grant-based, programmatic finance for local financing through international funds.
4. Revise the international funds policies to increase their willingness to undertake risks, for: supporting innovative financial instruments, to be more flexible on co-financing, and to use more appropriate measurement frameworks that promote local level results.
5. Provide tailored capacity-building support to build local institutions' capabilities in managing climate finance.
6. Create national and local level mechanisms for donors, governments, NGO and representatives from communities that are most vulnerable to the effects of climate change, to oversee the design and distribution of climate finance, ensuring it meets their priorities and achieves sustainable development that is appropriate to a changing climate.
7. Ensure national climate and development focal points have adequate capacity, and assistance, to oversee devolved financing and decision making which follow the principles of subsidiarity.

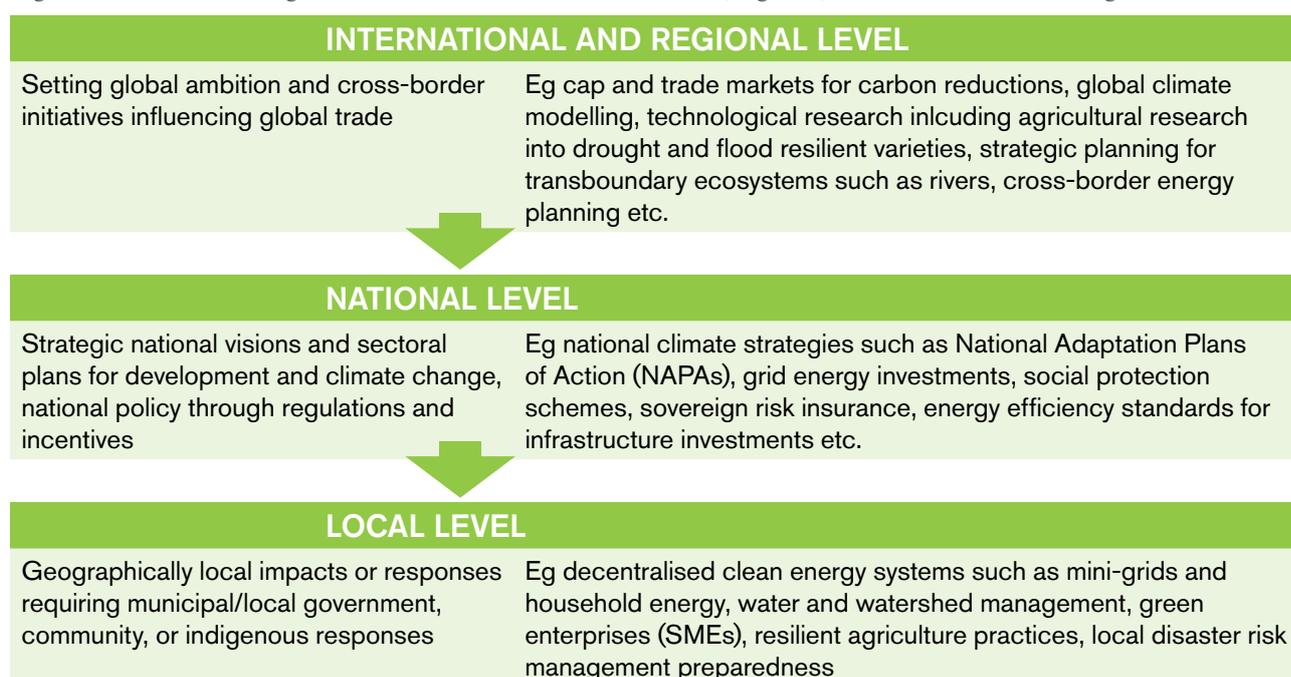
1

Introduction

In 2015, we witnessed significant changes to the international development and climate agenda, with the establishment of the Sustainable Development Goals (SDGs) and the Paris Agreement. The Paris Agreement has now entered into force, much sooner than expected. This puts the goal of US\$100 billion in annual climate finance reaching all developing countries by 2020 at the forefront of discussions. However, research into the financial requirements of the Least Development Countries' (LDC's) Nationally Determined Contributions (NDCs) estimates US\$93.7 billion will be required annually for them alone, indicating that even US\$100 billion is far less than what is needed across all developing countries.

To meet these financing needs, we will need to use what finance is available as effectively and efficiently as possible. This means ensuring climate change adaptation and mitigation action takes place at the appropriate levels. Mitigation produces global public goods – often leading to action at the national and international level, from large-scale renewable energy systems to cross-border cap and trade mechanisms. Conversely, adaptation more commonly produces local public goods, that vary according to geographic variation in climate change impacts, meaning the balance of responses is more often focused at the local level. In reality, climate action is required at every level, depending on the specific geographical and socio-economic context (see Figure 1).

Figure 1: Climate-relevant goods and services across the international, regional, national and local levels of governance



Many climate responses will be best delivered at national, regional and international levels. At whatever level they are delivered, they should fall under strategic national oversight. However, there is compelling evidence that in many cases more effective, efficient, and sustainable results can be achieved at the local level. This is because:

- It is easier to integrate the development and climate agendas at the local level. This is achieved where local stakeholders are engaged in participatory decision making – empowering local communities and small- and medium-sized enterprises (SMEs) to decide what investments are most needed to achieve low-carbon, climate-resilient development. Inclusive and agile local institutions can be effective agents of development as local people know their context best and are able to respond rapidly to changing local circumstances.
- Women, the disabled, youth and the socially excluded can have a greater voice by setting priorities locally rather than at higher levels. Local institutions, by virtue of being closer to the ground, are more transparent and accountable to communities and build trust between government, donors and local communities through effective investment, enhancing the state-citizen contract.
- Local institutions can pay greater attention to the trade-offs between groups due to being better connected to local realities. Whilst some interventions are more cost-effective when planned centrally, significant efficiency can be achieved by planning local public goods with engagement of local stakeholders.

Despite the evidence of the benefits of channelling climate and development finance directly to the local level, it is not the norm. Most development finance flows only from international to national government actors, who have limited capacity to understand and reach the needs of poor and vulnerable communities – those most in need of climate-resilient development interventions. Moreover, accountability for the effective spend of finance tends to flow up to the donor rather than down to the local communities. Without local input, many climate change projects may prove to produce maladaptive solutions, that equally miss development co-benefits, such as improved energy access, reduced

local pollution and livelihood gains. It is therefore crucial that international financing architectures contain mechanisms to safeguard and promote the needs of poor and vulnerable local communities. However, no consensus exists on the amount of development and climate finance that should reach the local level, despite the Addis Ababa Action Agenda and the Paris Agreement recognising the importance of local communities.

1.1 Study aims

Taking into account the evidence of the benefits of local level financing, compared to the limited international leadership to provide it, this report seeks to stimulate discussion on the design of international development and climate finance so that it better reflects the needs of local communities.

Our unit of enquiry is international development and climate funds, which offer relatively stronger transparency and accountability principles. Although international funds are designed for a range of different sectors and beneficiaries and therefore are designed to work at different levels (see Figure 1), we focus on identifying the lessons and innovation that can help climate finance flow more to the local level. The Green Climate Fund (GCF) is a particular focus of the lessons and innovation identified in this report, as it is set to become the largest international climate fund ever established. Its design is still being consolidated, so this presents an opportunity to ensure that its architecture responds to the needs of poor and vulnerable communities.

Thus, the central question we ask is **how can the international financing landscape be improved so it enables better reach to the local level?** We address this through three sub-questions:

- How does climate and development finance flow to the local level from international funds?
- What are the barriers and enablers within international funds affecting this flow of finance to the local level?
- How can we improve financing policies and modalities to promote local level climate financing?

1.2 Research methods

The report analyses the policies and architecture of a purposeful sample of international climate and development funds, seeking to guide future funding innovations from their past successes and failures. The sample includes 12 climate funds and four development funds:

- The Global Environment Facility (GEF) and its Small Grants Programme.
 - The Least Developed Countries Fund (LDCF) and the Special Climate Change Fund (SCCF).
 - The Adaptation Fund.
 - The Green Climate Fund (GCF).
 - The four Climate Investment Funds (CIFs).
- The UK's International Climate Fund (UK ICF) and Germany's International Climate Initiative (IKI).
 - The Global Fund for Aids, Tuberculosis and Malaria (Global Fund).
 - The UN Capital Development Fund (UNCDF).
 - The Caribbean Development Banks Basic Needs Trust Fund (BNTF).
 - The World Bank's Community-Driven Development (CDD) initiatives.

First, we introduce contextual evidence to why climate and development finance should be decentralised, illustrated through in-country examples from Kenya and Bangladesh.

2

Why decentralise climate and development finance? Results from practice

The success of participatory and community-driven processes in climate and development action is highly context-specific, and depends on the national and local processes in play. Successes in Kenya and Bangladesh display practical examples of the efficiency and effectiveness gains delivered when national institutions are supported in developing devolved financing mechanisms that support local priorities.

2.1 Kenya's County Climate Change Funds

The County Climate Change Funds (CCCF) were developed to channel climate finance to the local level for investing in the priorities of local people in Kenya's arid and semi-arid lands. These lands occupy 80 per cent of Kenya's land mass, are home to over 10 million people, and are particularly vulnerable to climate change. Structural inequalities have exacerbated these vulnerabilities; a disconnect between local communities and national development planners inhibits local people from adapting effectively in areas where local and flexible resource management is crucial.

Kenya's devolution in governance has, however, created a new opportunity to mainstream the climate concerns of the arid and semi-arid lands into national and subnational development. The CCCF acts as the vehicle to implement local climate change adaptation. This mechanism was initially developed in Isiolo County of northern Kenya (through support from DFID), and now covers 30 per cent of the country. The CCCF is premised around:

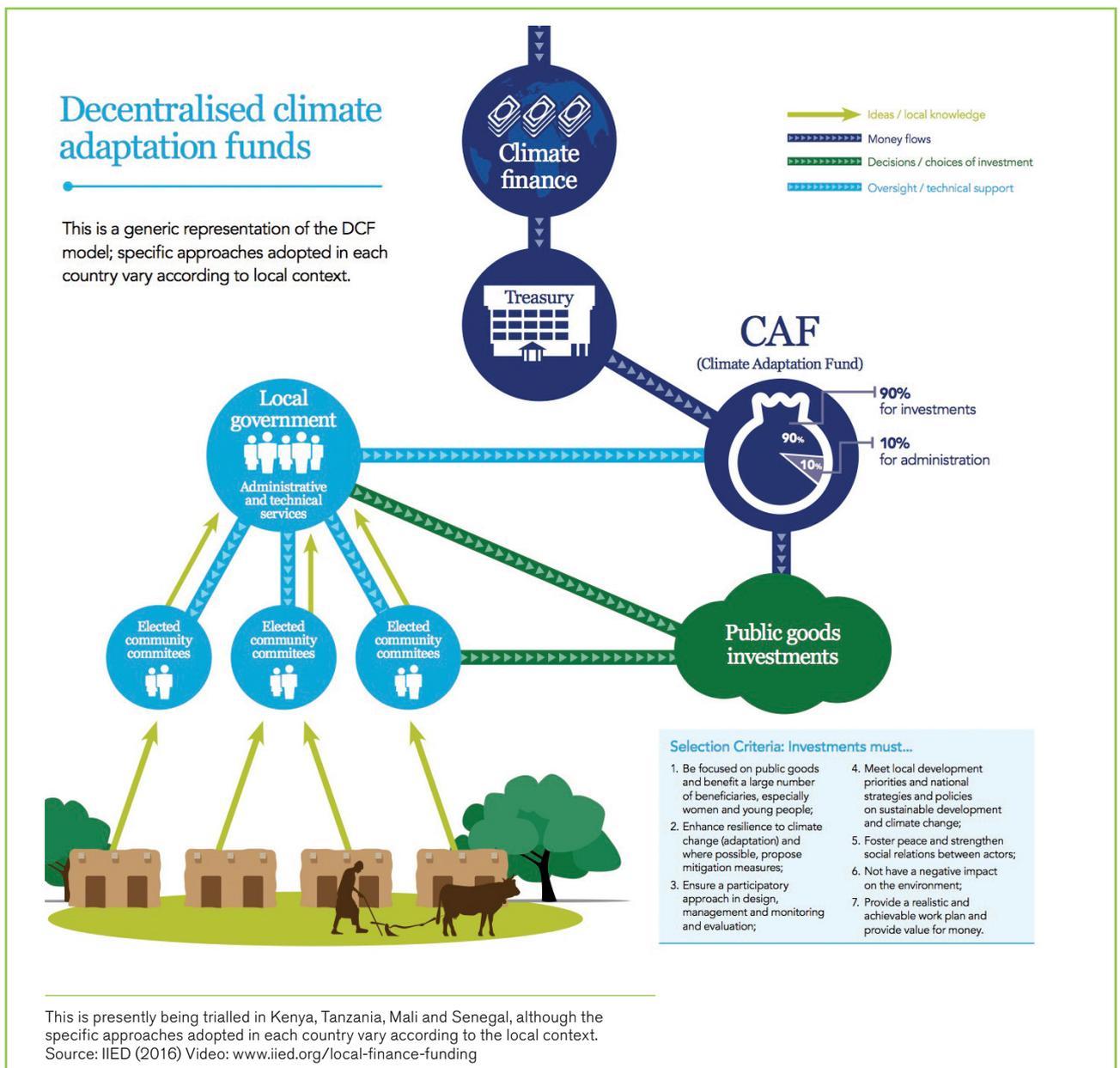
- Flexible approaches to planning to encourage participation of, and communication between, a diverse set of local stakeholders that improve governance structures, enabling action on climate resilience.
- Devolved adaptation finance managed by county governments who can support locally prioritised adaptation investments that utilise local knowledge and technical expertise.
- Promotion of cross-boundary and cross-border planning which is critical for supporting climate-resilient development in the arid and semi-arid drylands. This is due to their high climate variability that in turn has created fluid and responsive pastoralist economies that cross administrative and national boundaries.

The CCCF enables local communities to add their knowledge on local climate resilience through the process of **shared learning dialogues** led by ward and county committees. The ward committees submit their proposals to country adaptation planning committees for approval and are composed of representatives from ward committees, local government and other local stakeholders. This process builds capacity in local institutions and enables investments to increase climate resilience across the ward, county and country level. Even at the county level, the local level is given greatest weight with 70 per cent of CCCF funding allocated for wards to prioritise local public-good investments. The County Adaptation Planning Committee oversees each investment to ensure strategic oversight and alignment

with national climate change strategies. By facilitating equitable dialogue between local actors up to national governments, participation of vulnerable communities in local adaptive decision making has been improved, leading to the mobilisation of county public finance behind the resilience objectives of the communities and to fairer resource allocation outcomes. Conflict has also been reduced locally, due to the rules agreed within communities and reciprocal arrangements made with neighbouring communities to manage common grazing areas.

The theoretical approach to Kenya's CCCF – Decentralising Climate Funds or Climate Adaptation Fund's – is outlined in Figure 2, below.

Figure 2: The generic representation of the Decentralising Climate Funds model



2.2 Bangladesh's Local Disaster Risk Reduction Fund

The Bangladesh Local Disaster Risk Reduction Fund (LDRRF) is one of six components under the government of Bangladesh's Comprehensive Disaster Management Programme, supported by funding from a range of multilateral and bilateral donors, as well as budget support from the government of Bangladesh. The fund provides small grants directly to local and county governments, and is used to finance community-designed and implemented projects in climate change adaptation and disaster risk management.

The Ministry of Disaster Risk Management and Relief lead the LDRRF, providing strategic oversight and cross-sectoral coordination. Projects themselves are developed through inclusive and participatory processes. Community risk assessments are undertaken to identify community requirements, feeding into local risk reduction action plans from which project concepts are formed. A disaster risk management committee, formed at the local or county government level, approves these concepts.

Local ownership with support from line ministries and the national government has led to significant improvements in local resilience and delivered a series of development co-benefits:

- More than 820,000 people have benefited from 249 disaster risk reduction schemes, ranging from secure and safe drinking water to the construction of cyclone shelters.
- 80,000 people have gained financially from short-term employment, with over 245,000 families receiving livelihood support.
- The capacity of local and national government ministries to understand and act on climate adaptation and disaster risk management has significantly improved, and these lessons can be disseminated to other ministries and local governments.
- The added local development and climate benefits achieved have helped mobilise additional local and international finance, with the former enhancing local ownership and accountability.

With these identified benefits, do we know how much finance flows from the international down to the local level?

3

Do we know how much international climate and development finance flows to the local level?

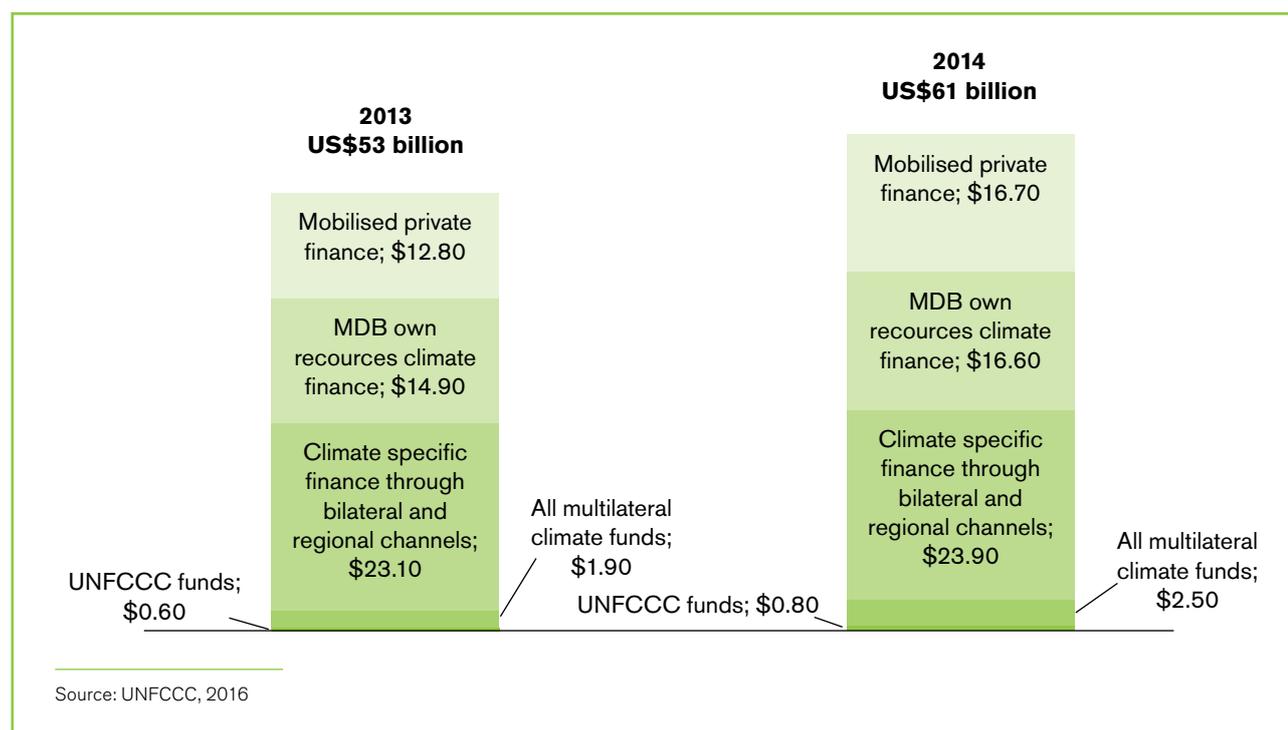
It is hard to estimate the flows of climate finance.

The United Nations Framework for the Convention on Climate Change's (UNFCCC) second Biennial Assessment report estimates the flow of public and leveraged private climate finance to developing countries at US\$53 billion in 2013, which rose to US\$61 billion in 2014 (Figure 3) (UNFCCC, 2016). Here, we look at the portion flowing from dedicated multilateral, bilateral and regional climate funds, estimated at US\$1.9 billion in 2013 and US\$2.5 billion in 2014. We do so as most dedicated climate funds residing within and outside the UNFCCC process are recorded within the Climate Funds Update (CFU) database, which to our knowledge is the most transparent source of information, therefore making international climate funds easier for developing countries to track and influence, compared to core multilateral development bank (MDB) and bilateral finance.

Finance flowing is significantly lower than that committed.

Total 'pledged' international public finance for dedicated climate funds as recorded within the CFU database reached US\$39.6 billion between 2003 and September 2016. Of this, 44 per cent has been approved for spending (US\$17.4 billion), which is classified as the 'flows' of climate finance reported in the UNFCCC's second Biennial Assessment. However, only 27 per cent (US\$4.8 billion) of this approved finance has actually been disbursed. According to the CFU database, mitigation projects receive 52 per cent of approved climate finance from these specialised funds, with adaptation projects receiving a quarter of total approved funding, and the remainder flowing to Reducing Emissions from Deforestation and Forest Degradation (REDD) activities and those with cross-cutting purposes.

Figure 3: Distribution of climate finance flows from developed to developing countries in 2013 (left) and 2014 (right) as reported within the UNFCCC's second Biennial Assessment report, in US\$ billions.



3.1 How much finance is flowing to the local level?

Initial estimates suggest under 10 per cent of climate finance is prioritised for the local level.

There is no definitive number on the quantity of climate or development finance reaching or utilising local actors. Based on our interrogation of the CFU database using key 'local' search words (see Annex I), we estimate that out of the US\$17.4 billion total, less than ten per cent (US\$1.5 billion) was approved for locally focused climate change projects between 2003 and 2016. Of this, over half appears to have been approved for locally based adaptation, versus less than a quarter for general mitigation. This is in contrast to the trends in overall climate finance.

But, it remains unclear how far local actors can set priorities. Accurately defining local level finance even across the major climate funds would require a review of project documents and analysis of implementation – beyond the scope of this study.

Even if projects are locally orientated, there are no assurances that local actors are involved in the design, execution or are even direct beneficiaries from approved finance. Performing such an analysis for development finance is even more challenging given its appreciably greater scale. Thus, a true picture of local level climate and development finance remains a major gap in our knowledge.

We need to understand what incentivises funding flows to the local level. This initial figure of less than ten per cent of climate finance from specialised funds gives an indication of the imbalance that characterises the present funding landscape. With this in mind, we look to identify how the funding policies and modalities of international climate and development funds are incentivising or inhibiting the flow of finance to the local level. Although these international funds are designed to work at different levels, their comparison helps to inform the next wave of climate and development finance so that it achieves greater efficiency, effectiveness and sustainability.

4

Inner workings of climate and development funds

The policies and procedures of international climate and development funds govern how accessible finance is for actors capable of working at the local level, as well as for local projects themselves. Here, we look at these funding policies (see Box 1) to identify how funds incentivise or dis-incentivise local level activities. First, we characterise the 12 international climate funds, followed by a review of four development-focused funds.

4.1 Climate funds

Multilateral climate funds under the UNFCCC

The Global Environmental Facility (GEF) is the oldest financial mechanism under the UNFCCC, and serves as the secretariat for all UNFCCC funds other than the GCF. The GEF Trust Fund is the main funding arm, delivering a total of US\$5.2 billion since it was established in 1992. The GEF Trust Fund also operates as the financial facility for four other multilateral environmental agreements to finance 'Global Environment Benefits' across six areas.¹ Although the Trust Fund's dedicated climate investments focus on

mitigation, the Fund's other environmental objectives also cover adaptation. The GEF Trust Fund previously funded adaptation through the Strategic Priority for Adaptation (SPA), but has since concluded its US\$50 million funding cycle (GEF, 2014a). Since 1992, the Trust Fund has completed five full operating periods, and is now in its sixth, covering 143 developing countries with US\$941 million available for climate change mitigation (GEF, 2014b). The GEF Small Grants Programme finances community-based projects behind four strategic initiatives, two of which are climate change relevant – climate smart innovative agro-ecology, and low-carbon energy access co-benefits (GEF, 2014b).

The GEF also governs two adaptation-dedicated funds under the UNFCCC – the Least Developed Countries Fund (LDCF) and the Strategic Climate Change Fund (SCCF), both operational since 2002. The LDCF specifically funds the preparation and implementation of National Adaptation Programmes of Action (NAPAs) and National Adaptation Plans (NAPs) (GEF, 2011a), approving US\$1 billion in total. The SCCF funds adaptation and technology transfer activities within all developing countries (GEF, 2011b), totalling US\$289.9 million.

¹ GEF focal areas are biodiversity, climate change, chemicals and waste, land degradation, international waters, and sustainable management of forests (REDD+).

BOX 1. DESIGN FEATURES OF FUNDS

Investment framework: the criteria used to assess and decide upon investment decisions. It governs the kind of projects and programmes which are supported. This can include the level of urgency, the ability to scale up, and potential to leverage other public and private resources. To incentivise support for local projects it is important that these criteria reflect local capabilities.

Administration: decisions on funding policies, investment decisions and the day-to-day management of the fund can all influence the appropriateness and accessibility of finance for local projects. Therefore, it is important that local intermediaries' and beneficiaries' voices are heard, and that all decisions are transparent and inclusive.

Resource allocation: includes the countries and the entities eligible or prioritised for funding, and the amounts over a given period of time. To incentivise local financing, it is important to reserve funding specifically for local projects of the appropriate scale, and/or to intermediaries best able to work at the local level.

Access modalities: there are generally three mechanisms for actors to access finance from international funds: direct access, which normally requires accreditation by proving the entity meets specified requirements; international access, whereby finance is channelled through accredited international entities, such as the multilateral development banks or the UN; or whereby all eligible organisations can submit funding requests directly to the fund. Where accreditation is required, it is important to provide simplified access reflecting local actor's capacities, and promote the accreditation of intermediaries capable of working at the local level.

Proposal development: for local actors to access funding they must be able to develop appropriate projects. Where funding is small in scale, ideally the project appraisal processes should be streamlined and simplified. Where local financing occurs indirectly, local beneficiaries should still be involved from project design all the way through to evaluation.

Funding scale: although local projects can be large-scale at the city and municipal levels, community-

based projects are small, requiring just tens to a few hundred thousand US dollars. Therefore, international funds should provide smaller pots of funding.

Funding instruments: the appropriate financial instruments will vary significantly depending on the local financial market and maturity of proposed technologies. To enhance local private sector engagement – such as domestic commercial banks and SMEs – innovative financial solutions will be required, with appropriate financial terms including longer maturity and grace periods for loans, and often grants in the early stages.

Capacity and readiness support: local actors, including local governments, CBOs and local NGOs, will often possess inadequate technical and fiduciary capacities to design, implement and monitor sustainable projects. International funds should provide grant-based resources and dedicated readiness programmes to strengthen local capacity.

Risk management: to be innovative, funds must possess the necessary risk appetite, generally needing to be higher for local projects, compared to standard development and climate investments.

Co-finance requirement: in locally managed funds co-financing from beneficiaries has proven highly effective at enhancing local ownership and accountability; however, given the scale at which many international funds operate, it is most important that co-financing (or leveraging) requirements are achievable by local actors.

Results frameworks, monitoring and evaluation: govern, measure and report upon the success of financing. For local projects to be incentivised, funds must provide locally achievable and relevant success criteria, as well as promote local beneficiary participation in monitoring and evaluation to enhance accountability. Ideally this should also include direct feedback to the donor and implementing entities.

The Adaptation Fund was launched in 2001 through the Marrakesh Accord, and became operational in 2009. It operates as the financial mechanism to the Kyoto Protocol, and aims to increase climate change resilience through 'concrete' adaptation projects within all signatory developing countries. Resources are allocated based on a country's vulnerability and urgency for action, capped at US\$10 million. The Adaptation Fund aims to pay special attention to the most vulnerable communities (AF, n.d.).

The Green Climate Fund (GCF) is the world's largest climate fund, with US\$10.3 billion in pledged resources. It aims to finance country-driven projects that create a 'paradigm shift' in both adaptation and mitigation projects, and to achieve a balance between the two (GCF, 2011). Half of adaptation resources are reserved for LDCs and small island developing states (SIDS), and there is to be a specific focus on private sector financing. The GCF became operational in late 2015, and as of December 2016 has approved US\$1.5 billion. Given its aim to play a leading role in the US\$100 billion annual target of climate finance by 2020 and the implementation of the Paris Agreement (Bodnar *et al.*, 2015), the recommendations from this paper are particularly important to the GCF.

Multilateral funds outside the UNFCCC

The Climate Investment Funds (CIFs), administered by the World Bank, are the main multilateral funds residing outside the UNFCCC, and have collectively approved the largest volume of climate finance. They were formed in 2008 in response to large donors seeking to pilot financing for climate change at greater scale than ever before – and were set up under the multilateral development banks (MDBs) (Nakhoda and Norman, 2014a). The CIFs are composed of four funds which aim to deliver programmatic funding that offer scale, efficiency and can mobilise co-financing, through nationally-led approaches (CIFs, 2014; 2010a; 2010b). The four funds are the Clean Technology Fund (CTF) with US\$5.1 billion deposited, the Scaling-up Renewable Energy Programme (SREP) with US\$528 million deposited; the Pilot Programme for Climate Resilience (PPCR) with US\$1.1 billion; and the Forest Investment Programme (FIP) with US\$528 million. The CIFs contain a 'sunset' clause, whereby they will close once the GCF becomes 'operational'. Although the GCF is now operational it has not yet reached the scale required, thus the CIFs remain active and an agreement needs to be reached on what parameters of GCF financing will trigger the sunset clause.

The CTF is the largest Climate Investment Fund and provides concessional finance at significant scale for long-term carbon emissions reductions within 15 middle income developing countries – selected for their high greenhouse gas abatement potential (CIFs,

2014). **The SREP**, like the CTF, finances mitigation projects but focuses on enhancing clean energy access and developing local capacity and advisory services, within 25 low income countries (CIFs, 2010a). SREP initiatives are to be integrated into national energy plans, and prioritise the delivery of local economic benefits (CIFs, 2010a). **The PPCR** is an adaptation fund that aims to scale up finance for – and integrate climate resilience into – national planning. Projects place particular emphasis on NAPAs in 19 developing countries (CIFs, 2015a; CIFs, 2009a). The PPCR has mobilised the largest source of adaptation finance to date. Finally, **the FIP** aims to deliver mitigation at scale by directly financing and leveraging additional resources for REDD projects. It places a particular focus on poverty reduction and rural livelihood enhancement within indigenous peoples and local forest communities in 24 developing countries (CIFs, 2015b). The FIP also contains a US\$80 million Dedicated Grants Mechanism, established by indigenous peoples and local community representatives from FIP pilot and non-pilot countries, where funding is channelled directly to local communities for REDD projects (CIFs, 2010b). It consists of two funding streams: grants for capacity building and REDD projects in pilot countries and a global knowledge management system disseminating lessons learned on community forestry projects to non-pilot countries (FIP, 2013).

Bilateral climate funds

We also look at two bilateral climate funds: Germany's International Climate Initiative (IKI), and the UK's International Climate Fund (UK ICF). **The IKI** operates through Germany's Federal Ministry for Environment, Nature Conservation, Building and Nuclear Safety (BMUB), implementing projects and programmes across four funding areas: climate change mitigation; climate adaptation; conservation of natural carbon sinks; and protection of biodiversity. IKI also supports NAPAs and Nationally Appropriate Mitigation Actions (NAMAs). Unlike the multilateral funds, each application for funding from its US\$1.1 billion resources are considered on a case-by-case basis (BMUB, 2015a; 2015b).

The UK ICF operates through three UK government ministries: the Department for Energy and Climate Change (DECC),² the Department for International Development (DFID), and the Department for Environment, Food and Rural Affairs (DEFRA). Its US\$1.3 billion resources make it the world's largest bilateral climate fund. The UK ICF aims to maximise value for money and impact through delivery at scale, producing replicable projects, promoting innovation, and mobilising additional resources within its three priority areas. These include: adaptation to climate change; low carbon development, and energy access; and forest protection (DECC, 2011). Adaptation receives 50 per cent of resources, with low carbon development

and forestry receiving 30 and 20 per cent respectively (DECC, 2011).

4.2 Funding policies and procedures of climate funds

Investment criteria and resource allocations dictate the types of projects and countries supported by climate funds. Their specific financing policies (as outlined in Box 1) will determine how accessible funding is to local actors. Here, we outline the characteristics and compare their access procedures, proposal development processes, financial instruments, co-financing requirements, capacity support, and results frameworks.

Access procedures

Most climate funds are only accessible through international intermediaries. All of the CIFs work through the MDBs (CIFs, 2014), as do all funds under the GEF. The GEF has also eight accredited entities, including several international NGOs and four southern regional development banks (GEF, 2015). The bilateral German IKI allows any entity, including CBOs, to directly access funding as long as it can develop and submit a sufficient proposal to BMUB (see **Proposal development**) (BMUB, 2015a).

Direct access is available under the LDCF for NAPA formation (GEF, 2015; 2011a) and National Communications and Biennial Update Reports to the UNFCCC under the GEF Trust Fund (GEF, 2010). However, the Adaptation Fund and GCF are the only climate funds providing direct access as a primary financing window. The Adaptation Fund has allocated a minimum of 50 per cent of its resources to direct access entities (Tango Int. and ODI, 2015).³ So far, 14 out of the 48 accredited entities under the GCF (as of December 2016) are national direct access entities – most of which are national government agencies (GCF, 2016a). The GCF provides four different scales of funding and different procedures required for the different levels of funding with the smallest allowing grants up to US\$10 million.⁴ The procedures focus around three different levels of financial, environmental and social risk competence, to simplify access for smaller and less risky projects (GCF, 2015a). The GCF has also recently launched a pilot scheme for Enhancing Direct Access (EDA), which aims to create devolved and participatory financing mechanisms as developed under the GEF Small Grants Programme and FIP Dedicated Grants Mechanisms (see below). At present, this EDA pilot has US\$200 million available for ten programmes which may offer opportunities to scale up community- and SME-based climate financing approaches (see Box 2).

BOX 2. ENHANCED DIRECT ACCESS IN THE GCF

In efforts to enhance country ownership of climate finance, the GCF has launched the Enhanced Direct Access (EDA) modality. EDA offers the opportunity for nominated national entities to undertake a programmatic approach to climate finance with greater decision making at the national level, whilst also enhancing the voices of local actors. EDA expands on the direct access modality to further enhance country ownership through the following measures (GCF, 2016d):

- **Devolved decision making:** rather than projects being approved by the GCF Board, the screening, assessment and selection of climate change projects are devolved to the regional, national, or subnational level – wherever the national implementing entity (NIE) resides;

- **Focused on local intermediaries:** the EDA programmes are expected to support a significant number of small-scale projects that use local intermediaries, such as local government and local banks, to reach communities and SMEs who are able to execute climate change projects grounded in local realities; and
- **National multi-stakeholder engagement:** to ensure all projects contribute towards national climate change strategies and to enable local actors to engage in the EDA process, EDA programmes are to be overseen and strategically guided by a multi-stakeholder oversight and steering function at the national level.

EDA is not simply devolving funding decisions to the national level, but a system by which international financial support invests in scaling up local action on climate change.

² Now the Department of Business, Energy and Industrial Strategy (BEIS).

³ Direct access entities under the Adaptation Fund are classed only as national (or below) entities, whereas regional entities are also classed as direct access under the GCF.

⁴ Termed 'micro-scale', with 'small' between US\$10-50 million, 'medium' between US\$50-250 million, and 'large' between US\$250 million (GCF, 2015a).

Proposal development

Most climate funds follow country-driven processes for project development. The CIFs undertake 'joint missions' within eligible countries to develop investment plans (Strategic Programmes for Climate Resilience under the PPCR) (CIFs, 2009a). These are led by MDBs and national focal points⁵ (CIFs, 2014). Guidance from the CIFs instructs each fund's investment plan to be developed through a participatory process involving local communities, to gain inputs into specific adaptation solutions under the PPCR (CIFs, 2009a), develop local markets and manufacturing skills under the SREP (CIFs, 2010a), and gain indigenous and community input as potential executing entities under the FIP (CIFs, 2010b). The FIP takes this further, with national-level multi-stakeholder steering committees identifying and approving projects as well as providing monitoring and evaluation inputs. These committees are expected to include representatives from indigenous and local authority forest communities (CIFs, 2010b; 2009b). Moreover, to ease access for weaker national organisations, applicants only need to provide a brief project proposal for grants under US\$50,000. Another legal entity can apply on the local organisation's behalf, or the Dedicated Grant Mechanism's secretariat can perform country visits to review organisational capacities where a local organisation lacks the financial track record needed (FIP, 2013).

Country work programmes are promoted under the GCF to develop project pipelines through stakeholder engagement, including sub-national and community-based institutions – although this is not a requirement as it is under the CIFs (GCF, 2016b). Any legal entity can develop projects as long as they are themselves accredited or they act through an accredited entity. Project applications are simplified if of smaller size and risk, and an optional concept note can be submitted to gain provisional feedback and recommendations (GCF, 2014a). The Adaption Fund also provides a 'small' funding window for those below US\$1 million (AF, 2013; Tango Int. and ODI, 2015).

Simplified project application and appraisal procedures for small grants are available under the GEF Trust Fund as well as the LDCF and SCCF funds that GEF administers. This allows those seeking under US\$2 million – termed 'medium-sized-projects' – to apply without a full concept note, whilst 'full-sized-projects' (above US\$2 million) require a concept note (GEF, 2015). Project proposals and concepts are submitted through one of the GEF's project agencies, from any entity as long as the project aligns with country priorities (GEF, 2015). Similar to the FIP Dedicated Grants Mechanism, the GEF Small Grants Programme performs project selection and review through national-level multi-stakeholder steering committees, which include local community and NGO representatives. These projects are selected from 'country programme strategies', that themselves are developed through participatory processes (GEF and UNDP, n.d.).

Any entity can apply for funding under Germany's IKI (FEA, 2013; PIK and BMUB, n.d.), although all funding applications are subject to exactly the same appraisal procedures, independent of the size of funding or risk involved. There is no single window for applying for the UK ICF funding and little publicly available information on project development requirements and appraisal. A large proportion of UK ICF finance is channelled through multilateral and bilateral funds (ICF International, 2014).

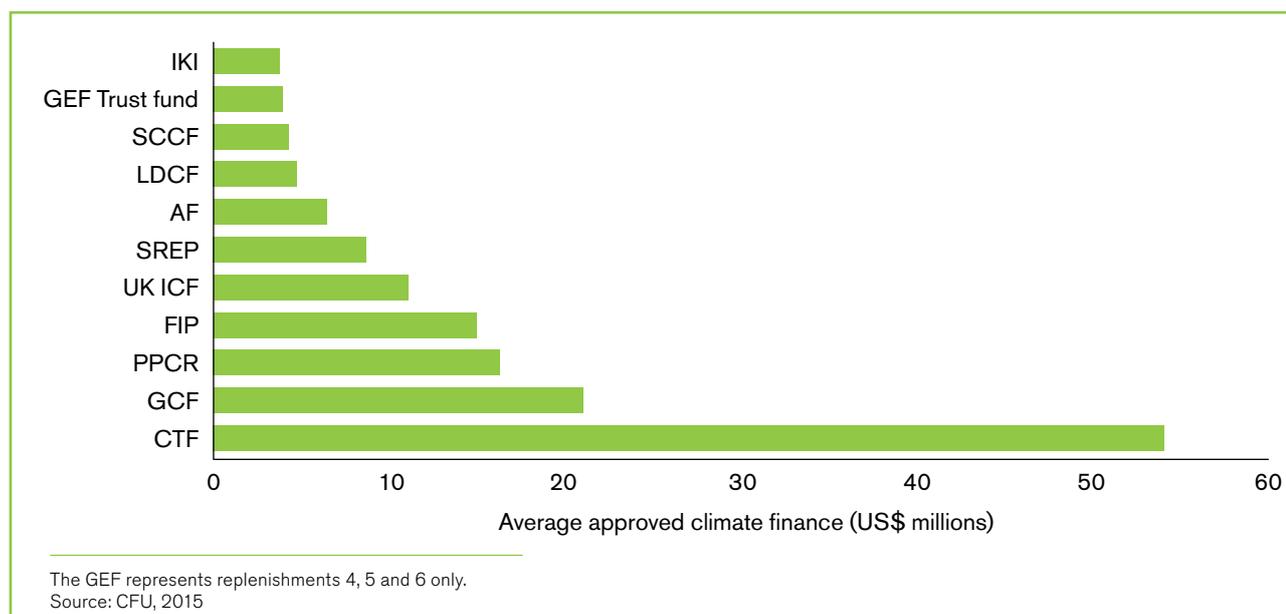
Funding scale and instruments

Germany's IKI has provided the smallest average funding size of all the major climate funds at just US\$3.8 million, of which all is in grant form (Figure 4) (BMUB, 2015a). The Adaptation Fund also only provides grants (AF, 2013b), as does the majority of GEF funding. However, these are an order of magnitude larger than the FIP Dedicated Grant Mechanism,⁶ which provides maximum project financing of US\$500,000 (CIFs, 2009b). The GEF Small Grants Programme is even smaller, at up to just US\$50,000 per project (GEF, 2014c).

⁵ National focal points (or agencies) perform the key communication and national decision making function between the international fund and those implementing funded projects. They are known by different names depending on the fund, eg national designated authorities under the GCF.

⁶ The FIP Dedicated Grants Mechanism is not separated from the main FIP in the CFU database, and the climate change projects of the GEF Small Grants Programme are not recorded.

Figure 4: Average funding per project and/or programme within the 11 climate funds analysed between 2003 and November 2015, for total not local climate finance.



The other climate funds, including GEF, provide a larger range of financial instruments, including: grants; concessional loans; guarantees; and equity investments (CIFs, 2015c; 2010c; GEF, 2014d; ICAI, 2014). The CIFs provide perhaps the most diverse set of financial instruments, including: equity; subordinated debt, mezzanine financing; performance-based payments; and local currency lending (CIFs, 2015c). Despite the availability of these innovative financial instruments, the CFU reports that only three guarantees and one equity investment across the GEF Trust Fund and CIFs have been approved, in Honduras, India and Columbia respectively (CFU, 2015). The GCF has approved one guarantee and equity investment since it commenced in November 2015 (GCF, 2015b).

The CTF provides the largest average project financing, surpassing US\$50 million. Although the other funds in the CIF also operate at scale, they provide smaller funding allocations, and have a greater tendency to use grants (CIFs, 2010d).

Co-finance requirements

Most climate funds require co-financing to be raised, or will act as co-financiers themselves. Although the LDCF, SCCF, Adaptation Fund, and GCF can finance full project costs in theory, the LDCF and SCCF usually require executing entities to raise co-financing, with indicative amounts included within project concepts (GEF, 2011a; 2011b). Similarly, the GEF Trust Fund and GEF Small Grants Programme

only provide finance for the additional costs of achieving Global Environmental Benefits beyond the development benefits (GEF, 2015, 2007). Achieving co-financing under Germany’s IKI is also the full responsibility of the project developer (PIK and BMUB, n.d.). The UK ICF programming documents provide little detail on co-financing requirements, but public and private co-finance mobilised are key performance indicators.

The CIFs place a particularly high priority on co-financing, with all funding blended with additional resources – the vast majority coming from the MDBs themselves (CIFs, 2015c; 2010c; 2010d; 2010e). Only around 14 per cent comes from national recipient country governments, and the amount mobilised from the domestic private sector is unclear (Nakhouda and Norman, 2014b).

Capacity and readiness support

Most climate funds provide capacity support through grant financing. The GEF funds provide project preparation grants of up to US\$50,000 for medium-sized projects, and higher for full-sized projects (GEF, 2015). The GEF Small Grants Programme provides much smaller allocations of between US\$2,000 and US\$5,000 to community-based organisations, to access local capacity support (GEF and UNDP, n.d.).

The CIFs provide over US\$1 million in project preparation grants and investment plan support (CIFs, 2015d; 2010c; 2010d), with smaller allocations

of up to US\$250,000 available under the FIP. These enable recipient executed capacity building and consultation workshops within CIF pilot countries (CIFs, 2015d; 2010c; 2010d; 2010e). The SREP and the FIP Dedicated Grants Mechanism place greatest emphasis on capacity building, forming a core part of their investment strategies (CIFs, 2010a; 2010d; FIP, 2013).

Germany's IKI also states provision of capacity support within its investment strategy, although specific allocations are not provided (BMUB, 2015a; 2015b), whereas the UK ICF is again not transparent on if and how it provides specific capacity support in addition to its standard project and programme based financing.

The Adaptation Fund now provides specific readiness support programmes of between US\$20,000 and US\$50,000 (AF, n.d.). Following these programmes, accreditation approvals have risen consistently (Tango Int. and ODI, 2015). Project formulation grants are also available for direct access projects (AF, 2013). The GCF has built upon the Adaptation Fund's readiness programmes, with readiness support institutionalised within its governing instrument (GCF, 2011). It possesses the most comprehensive readiness programmes, providing standardised readiness packages. Project preparation grants are also available, with up to US\$1.5 million for 'micro-' and 'small-'scale direct access entities (GCF, 2016b).

Results frameworks, monitoring and evaluation

Results frameworks and monitoring and evaluation (M&E) are what climate funds use to set, monitor, and report upon the results of their finance. The characteristics of mitigation- and adaptation-based objectives, outcomes, and indicators are of course different.

To recap, the funds with a mitigation focus include the GEF Trust Fund, the GCF, the CTF, the SREP (CIFs, 2012), the FIP and the bilateral German IKI and UK ICF. Their objectives generally cover reductions in greenhouse gas emissions through activity areas such as:

- Increased renewable energy supply
- Improvements in built environment and industrial energy efficiency
- Low carbon transport, and
- REDD.

The core measurement for achieving these results extends from the national to subnational level (city and province scale) and includes:

- Tonnes of CO₂ equivalent (tCO₂e) reduced or avoided compared to business-as-usual, and
- The amount of co-finance raised per tCO₂e reduced.

Other secondary objectives include the number of people taking up low carbon transport methods, the capacity increase in renewable energy, the reduced energy capacity requirements because of energy efficiency improvements, and the number of people with increased access to energy. The SREP is the only fund that places increased access to renewable energy as its core indicator.

Secondary and tertiary indicators commonly include sustainable development co-benefits, from reducing local pollution to increasing local employment and health. These are optional in the CTF, but local livelihood improvements are core in the FIP. Further locally specific indicators are set out under the GEF Small Grants Programme, and energy access is a secondary indicator of the GCF.

Climate change adaptation objectives are included within the LDCF, the SCCF, the Adaptation Fund, the GCF, the PPCR, and the UK ICF. These commonly cover:

- Reductions in vulnerability and increasing resilience to the impacts of climate change.
- Improving early warning systems and the use of climate data, and
- Implementing these strategies into national and subnational levels of governance and development.

The core results areas are measured from the national down to the community and local level, including:

- The numbers of beneficiaries of these actions, through greater capacity to cope with climate impacts and extremes, and
- The numbers of people, businesses, and communities more aware of the impacts of climate change.

The responsibility and requirements for M&E differ in each fund given the range of intermediaries involved. M&E under the GCF is the responsibility of the implementing entity or financial intermediary. However, the GCF also promotes input and participation from all 'relevant' stakeholders, including CSOs, vulnerable groups, women, and indigenous peoples. Similar requirements are stated within the Adaptation Fund (AF, 2015) and three of the CIF's results framework guidance (CIFs, 2009a), requiring local stakeholder engagement throughout project life cycle. However, under the CTF,

implementing MDBs are only required to engage with government, development, and private sector partners. The GEF funds have perhaps the most comprehensive guidance on M&E, with their own Public Involvement Policy (GEF, 2012), instructing project agencies to conduct consultations throughout the project cycle, with community stakeholders engaged by the national focal point. The GEF also provides differentiation in M&E requirements, with only full-sized projects required to undertake mid-term reviews.

M&E requirements under the bilateral UK ICF and German IKI are far less clear. In fact, the only information provided is found within their external evaluation reports, which suggests improvements are required in both transparency and stakeholder consultations (FEA, 2013; ICF International, 2014).

Annex II provides the full results frameworks for each of these climate funds.

4.3 Development funds

Financing for development has evolved extensively through learning from past successes and failures. Although climate finance is distinct from development finance, there are many lessons that can be learned to improve local level financing (Bird and Glennie, 2011). Moreover, development finance itself continues to evolve – with a recent focus on the need for more flexible and adaptive programming approaches, learning faster from delivery experience. With the scale-up in financing required for successful implementation of the SDGs, many leading donors are looking to ensure their finance is ‘fit-for-purpose’ for the post-2015 development agenda. Thus, the results of this paper are equally important for development as for climate finance. Given the scale of active development funds, we focus on four international development funds that have historically placed emphasis on local financing.

Global multilateral funds

Global vertical funds for development have focused predominantly on health, agriculture, and education (Isenman *et al.*, 2010). Some of the main funds include:

- The GAVI Alliance, a global health partnership focused on increasing access to vaccines and immunisations within the world’s poorest countries.
- The Education for All Fast-Track Initiative (EFA-FTI), helping low-income countries to develop national education plans and increase national education spending, and
- The Global Fund for AIDS, Tuberculosis and Malaria (Global Fund), the world’s largest international health fund, which aims to tackle and prevent AIDS, tuberculosis, and malaria.

Here, we focus on the **Global Fund**, which, since its first funding disbursement in 2002, has financed on average US\$3 billion per year and over US\$30 billion in total, representing two thirds of international funding for tuberculosis and malaria, and one fifth of AIDS funding (The GF, 2014a). We decided to look at the Global Fund as it sees communities as integral to the sustainable provision of healthcare services, and it provides a number of innovative policies to mobilise their effective participation in projects funded.

UN funds

The UN itself operates a number of funds, including:

- The International Fund for Agricultural Development (IFAD), a specialised UN agency that aims to eradicate rural poverty within developing countries.
- The UN Children’s Fund, providing long term funding for humanitarian and development assistance to children and mothers.
- The UN Population Fund, the lead UN agency for delivering safe childbirth and ensuring a young person’s potential is fulfilled.
- The UN Peacebuilding Fund, an impact investor of first resort to sustain peace within fragile and conflict-affected states, and
- UN Capital Development Fund (UNCDF), promoting economic development within developing countries, with a particular emphasis on poor and marginalised populations.

Here, we look at the **UNCDF**. The fund promotes financial inclusion of the poor and local economic development, through country and regional programmes totalling US\$88.3 million as of 2014 (UNCDF, 2015). Each programme differs in approach. However, a common theme is supplementing existing sources of bilateral and multilateral development assistance, termed ‘smart ODA’, to unlock local capital and deliver fiscal decentralisation. Thus, UNCDF places particular emphasis on promoting the role of local governments in receiving, channelling, and implementing development assistance (UNCDF, 2014a).

Given the diversity in global programmes, we focus on two specific UNCDF examples. The first is the **Local Finance Initiative** (LFI), a global programme which unlocks domestic capital from local organisations for small-medium scale infrastructure projects, providing proof of concept that can stimulate private investment. This programme is active within Tanzania and Uganda, and programmes in Bangladesh, Senegal, Cambodia, and Rwanda are planned. The programme totals US\$33.3 million, with a US\$5.2 million contribution from the UNCDF (UNCDF, 2016a; 2016b).

The second UNCDF programme is the **Local Climate Adaptive Living Facility (LoCAL)**, a global programme which uses performance-based grants to invest in local level climate resilience projects in 12 LDCs. Total LoCAL funding required is estimated at US\$40 million, with US\$700,000 from the UNCDF, and the remainder supplemented from donor and domestic finance (UNCDF, 2016c; 2015).

Multilateral Development Banks concessional funds

The MDBs play a crucial role as financial intermediaries, co-financiers, and as funding agents in both climate and development finance. Two new MDBs have also emerged for the first time in 20 years – BRICS New Development Bank and the Asian Infrastructure Investment Bank (Faure *et al.*, 2015) – continuing to increase the diversity of this funding landscape. MDBs provide significant concessional resources in addition to their ordinary capital windows, including:

- The Asian Development Fund of the Asian Development Bank
- The African Development Fund of the African Development Bank
- The Fund for Special Operations of the Inter-American Development Bank, and
- The International Development Association (IDA) financing window of the World Bank.

Here, we look at the largest single source of concessional resources – the IDA window of the World Bank, which supports 77 of the world's poorest countries through concessional loans and grants. Established in 1960 to accompany the World Bank's traditional non-concessional lending arm, IDA has financed an array of sustainable development programmes, including education, health services, water and sanitation, agriculture, climate change, business development, infrastructure, and institutional reforms. Now in its 17th replenishment worth US\$52.1 billion (2014–2017), it is focused on climate change, fragile and conflict affected countries, gender equality, and inclusive economic growth (WBG, 2016a).

We are specifically interested in the World Bank's **Community-Driven Development (CDD)** approach under IDA. CDD is not unique to the World Bank, but is the largest fund using CDD, providing on average US\$1.3 billion per year between 2000 and 2009 (WBG, 2009). The CDD approach has demonstrated increasing efficiency and empowerment of local communities and decision makers by giving them direct control of their financial resources (WBG, 2009). It has also financed numerous climate change adaptation projects, totalling US\$12 billion between 2001 and 2011 (Arnold *et al.*, 2014).

Regional development funds

The final category we look at is regional development funds. These funds pool resources from geographically or politically likeminded countries. Some key examples include:

- The Nordic Development Fund, established in 1989 by five Nordic donors: Denmark, Finland, Iceland, Norway, and Sweden, financing climate change and poverty reduction across 20 MICs and LDCs (NDF, 2016).
- The OPEC Fund for International Development, established by the OPEC member countries in 1976 to support sustainable development and poverty alleviation within the LDCs (OFID, 2016)
- The Caribbean Development Banks Basic Needs Trust Fund (BNTF), the community-focused sub-fund of the Bank's Special Development Fund.

Here we focus on the Caribbean Development Bank's **Basic Needs Trust Fund (BNTF)**, which began financing poverty alleviation within the neediest communities across ten Caribbean countries in 1979. It finances projects across three thematic areas, including water and sanitation, community access and drainage, and education and human resource development – in line with the Caribbean Millennium Development Goals. In doing so, the BNTF aims to empower poor communities through participation and direct implementation of funded 'sub-projects' (CDB, 2013), and to date has funded US\$300 million towards community-based development projects (CDB, 2016).

4.4 Funding policies and architecture in development funds

As development funds are designed for various different purposes unlike climate funds, not all the funding policies and modalities are applicable. Nevertheless, we identify innovation in programming that promotes local development financing, covering proposal development, funding scale and instruments, co-financing, and capacity support.

Project and programme development

Any entity, including CBOs, can access health funding from the Global Fund directly. A multi-stakeholder committee, known as the Country Coordinating Mechanism, includes representatives from affected communities and makes the funding decisions. The Country Coordinating Mechanism is responsible for developing concepts for national disease response and prevention, in line with national priorities, taking a

programmatic funding approach. Grant proposals are taken from these disease response and prevention concepts and submitted to the Global Fund from nominated 'principal recipients'. These principal recipients can include government line ministries, CSOs, private sector entities, or multilaterals, who either implement Global Fund grants or sub-contract projects to 'sub-recipients'. Multilaterals can only be funded if there are no alternative domestic institutions available, and are required to develop the capacity of suitable domestic entities in the process (The GF, 2016; 2014a). The Global Fund encourages affected communities to take a central role in the design, implementation, and monitoring of all funded projects, beyond simply being participants.

A 'community systems strengthening' component is required in each Global Fund concept and grant proposal as it is recognised that affected communities often lack the capacity to participate in, or deliver, health services effectively (The GF, 2014b). In this, community systems are understood to be the structures, mechanisms, and processes through which communities are able to effectively respond to health and development challenges. Further Global Fund policies promoting community systems strengthening are outlined in detail in the **Capacity support** section below.

Projects funded by the BNTF must have a direct impact on poverty reduction within communities.

They are demand-led, requiring sponsorship from target communities, including CBOs, NGOs, and faith-based organisations. Various in-country structures are formed to promote multi-stakeholder and community engagement in these projects:

- An 'oversight entity' coordinates each country's BNTF programme, composed of multiple stakeholders, including relevant government line ministries, NGOs, and private sector representatives.
- 'Community liaison officers' lead the identification and selection of projects through a range of participatory approaches, who sit within the country 'implementing agency'.
- The implementing agency is responsible for the overall monitoring and evaluation of BNTF-funded projects, acting as an in-country secretariat.

Community liaison officers lead on project development and delivery, focused around the following steps:

- First, a 'poverty reduction action plan' is developed from wider national policies on poverty alleviation. This contains a community focus, whereby capacity gaps and obstacles within communities to benefit from poverty reduction strategies are identified.

- An initial list of projects are identified, informed by the poverty reduction action plan, and set out in a 'country project portfolio'.
- Sector portfolios retain community ownership through 'community needs asset assessments', led by the community liaison officers. These are the key community participatory mechanisms in the BNTF, identifying the positive capacities and assets within communities towards projects.
- As community engagement by community liaison officers is so essential throughout the project cycle, the country implementing agency develops a 'project monitoring committee' for each project. This committee is composed of voluntary local members acting as focal points for community engagement, and providing input into data gathering and project M&E.
- Finally, local consultants and contractors are prioritised in project procurement, to bring additional local economic benefits to the communities (CDB, 2013).

Both the poverty reduction action plan and country project portfolio are validated by the operating entity and by the Bank itself, ensuring they are in line with national poverty alleviation strategies and BNTF priority areas. They must outline how communities were consulted, the amount of time spent with them, and the number of people who were engaged, amongst others.

Project development within both the UNCDF and CDD approaches are more flexible. A range of entities can identify and develop UNCDF LFI projects and programmes, including national and local governments, private sector entities, CBOs, and even other development partners. An LFI technical team reviews each submission, followed by validation by the local governments to ensure programmes contribute to local economic development. An LFI steering committee formed of multiple stakeholders, including national and local government ministries, business and investment councils, and development partners, amongst others, provides oversight in the design, implementation and evaluation of LFI programmes in line with the LFI results framework (UNCDF, 2014b).

UNCDF LoCAL projects are identified from an 'investment menu' for local climate resilience priority action areas. These investment menus consider the local climate change impacts, the potential local challenges, and the local government capacity, mandate, and financial absorption capacity. As LoCAL also aims to connect with existing development and climate initiatives within partner countries, the way in which projects are developed varies from country to country. In Bhutan, LoCAL provides a capacity-building component for improved aid effectiveness, connected to

the Swiss- and EU-funded Local Government Support Programme. In Cambodia, LoCAL finance is channelled through the National Committee on Decentralisation and Development, piggybacking on the Global Climate Change Alliance programme for the Cambodia Climate Change Adaptation Trust Fund (UNCDF, 2014c).

World Bank IDA interventions are identified through 'country partnership frameworks', developed every four to six years by the World Bank for each country it supports. These outline the key objectives for World Bank interventions within the country, and are informed by a 'systematic country diagnostic', prepared in close consultation with governments, the private sector, and civil society (WBG, 2014). Conversely, **CDD interventions are not predetermined, and offer flexible approaches to project identification and development.** Often, CDD programmes involve communities undertaking a village level participatory planning exercise, with assistance from local government officials and technical line ministries – ensuring there is no duplication of other programmes, and that they are in line with local economic development plans. Communities are therefore able to directly identify their priority areas for action and tailor interventions to the local context. Inter-village, district, or provincial level forums decide upon programme proposals, depending on what level of decentralised decision-making platform is most appropriate. Some CDD decision-making bodies will be composed entirely of communities, whereas others will be composed of higher level government bodies (Arnold *et al.*, 2014; Wong, 2012).

Funding scale and instruments

Both the Global Fund and BNTF are entirely grant-based funds. The Global Fund has no specific funding thresholds, with grants varying from an average of US\$4.9 million in 2006, up to US\$27.5 million in 2016 (OECD, 2016). The BNTF provides much smaller funding allocations per project, with small grants classified at below US\$100,000, or US\$200,000 in Jamaica, and large projects below US\$600,000 (CDB, 2013).

IDA CDD approaches are mostly block grants to villages and municipalities, averaging US\$27.5 million per programme between 2011 and 2013 (WBG, 2016b). These individual grants are determined from the level of poverty, remoteness, and local population of the village or municipality. The programmatic approach to CDD funding has evolved significantly. First generation CDD projects were often smaller in scale, working outside of government systems. Second and third generation CDD approaches have expanded to regional and national levels (Wong, 2012), allowing the World Bank to engage with communities on a much larger

scale. For instance, in Indonesia, CDD approaches have invested in more than 60,000 villages, whilst in the Philippines, they have invested US\$118 million across 5,326 community sub-projects (Arnold *et al.*, 2014).

The UNCDF provides a larger range innovative financial instruments, including grants, loans, credit enhancements, and guarantees (UNCDF, 2014d). The nature of the financial instrument used and their size is flexible, dependant on the country and programme. In the LFI programme, collateral guarantees are utilised to unlock domestic private finance, reducing investor risk. Municipal debt finance is blended with local finance, such as taxes and remittances. LFI can also aid the issuance of municipal bonds, acting as a buyer of last resort if necessary. Project financing size will vary from anywhere between US\$100,000 to US\$20 million (UNCDF, 2014b). LoCAL programmes are financed entirely through performance-based grants – around US\$200,000 in size – designed to be large enough to create impact, but small enough to avoid crowding out local private investment. These grants are generally channelled as standard local government budget support through national governments, tagged specifically for local climate resilience investment, and are fungible with local resources. The size and requirements for these grants are identified as the incremental cost required to build climate resilience into local economic development projects, taking into consideration the local government financial absorption capacity (UNCDF, 2014c; 2013a).

Co-financing

The Global Fund requires government co-financing within all funded programmes, known as 'counterpart financing', to ensure a sustainable national disease response. An innovative approach to co-financing is provided through a 'willingness to pay' component, where an additional 15 per cent of grant funding, on top of that originally agreed, is available if government co-financing is increased (The GF, 2014a). **The BNTF's co-financing requirements also focus at the government level,** with requirements for an additional 5 per cent to all funded sub-projects (CDB, 2013).

UNCDF requires co-financing from all partner countries, local governments, and private sector entities to be effective (UNCDF, 2014d). LFI specifically requires a minimum of 25 per cent co-financing from in-country project partners, and they must also contribute towards the costs of technical project requirements, such as feasibility studies (UNCDF, 2014b). As LoCAL requires full local government ownership, it must provide co-financing from its own budget, and the performance-based grant often tops up existing development and climate finance regardless (UNCDF, 2014c).

World Bank CDD initiatives go one level further, with co-financing from communities themselves to ensure community buy-in and ownership. Although community co-financing has been met in the majority of IDA CDD programmes, it is flexible. Some programmes will mandatorily require co-financing, whilst it is optional in others, dependant on the local circumstances. It will often be made as 'in-kind' contributions, such as community labour, materials, or land. Flexibility is continuous throughout the programme life cycle, whereby co-financing requirements can be adjusted to more achievable levels (Wong, 2012).

Capacity support

The Global Fund has developed policies for community systems strengthening, recognising the importance of communities to deliver effective health services. The Community Strengthening Framework requires that all concepts and grant proposals include a community systems strengthening component. The fund has developed the 'Technical Assistance Programme on Community, Rights and Gender' to ensure this takes place. This provides a range of support to communities, funded as part of US\$100 million pot for special initiatives, including:

- Situational analysis and needs assessments to provide the necessary evidence to communities to be able to validate concepts and grant proposals.
- Translation of funding policy documents into local languages, and
- Legal and project development training, amongst others.

Community capacity-building programmes are provided by local practitioners, selected transparently by the Global Fund secretariat. The aim is to ensure that communities are able to act as effective health service providers, perform programme M&E, and establish improved communications between the local and national level (The GF, 2014b).

The BNTF also provides capacity support directly to communities, to improve the institutional capacity of community organisations ensuring the long-term sustainability of projects (CDB, 2013). The remaining BNTFs US\$3 million capacity support budget (Universalia, 2012) focuses upon improving stakeholder and project beneficiary engagement to enhance the community-driven process.

Capacity support is considered essential to the success of all UNCDF programmes. LFI provides capacity support to both governments and private sector entities to promote the scale-up of local development. This support is mostly technical assistance (UNCDF, 2014b). Under LoCAL, capacity support is provided based on the results from the performance-based grants (UNCDF, 2014c). Whenever possible this support is provided through local consultants, known as 'technical service providers', capacitated by the UNCDF to provide locally tailored support, particularly to local governments (UNCDF, 2014b).

Under the World Bank's CDD approaches, local capacity is gained from the community-driven nature of programmes (Arnold *et al.*, 2014). Additional capacity support is provided in most programmes to national and local government actors to help them undertake participatory approaches and improve the quality of M&E (Wong, 2012).

5

Enablers to local climate financing

Through reviewing the climate funds which appear to have most successfully channelled finance to the local level, and the characteristics of the four locally focused development funds, we have identified five enablers to be prioritised in reforming the architecture of funds to promote local level climate finance. These are: local priorities reflected within funding results and investment frameworks, the use of small grants, simplified access and project approval procedures and, the use of participatory processes, from project selection through to the evaluation of results.

- **Priorities for locally relevant results:** there is a greater emphasis on local- and community-based adaptation versus climate change mitigation, found most within the LDCF and Adaptation Fund. Indeed, local adaptation projects commonly contain specific community-based adaptation approaches, from enhancing resilience in rural and coastal communities to smallholder farms. As adaptation to climate change requires action on locally specific variables, their results frameworks incentivise action at the local level through indicators for enhancing resilience specifically at the household and community level.
- **Many small results deliver big impact:** apart from the PPCR, all the adaptation funds and the mitigation-focused German IKI and GEF Trust Fund operate at funding allocations below US\$10 million per project (see Figure 4). This makes them more appropriate for financing individual local projects. Smaller still, the GEF Small Grants Programme has financed the largest number of community-based climate change

projects with funding no larger than US\$50,000 per project, successfully achieving local livelihood benefits and poverty reduction (GEF IEO and UNDP, 2015). However, to scale up, programmatic approaches to local level climate financing are required.

Of the four development funds, only the BNTF provides funding on a similar scale to the most locally appropriate climate funds, but this has often been insufficient to ensure sustainability of projects (Universalia, 2012). Conversely, the World Bank's CDD, Global Fund and UNCDF approaches have provided programmatic funding at much larger scales, doing so flexibly and taking into consideration local capacity and financial circumstances.

- **Grant-based and innovative financing:** the majority of international funds that provide local finance have used grants, and the two community-focused funds – the FIP and GEF – are also grant providers. Grants are often more appropriate for financing community-based adaptation, which are often non-revenue generating. However, to incentivise the local private sector and unlock domestic capital, innovative financial instruments that de-risk climate change investments can also be used. The early approval of guarantee and equity investments by the GCF offers optimism of the potential scale-up in these financial instruments in the future, compared to their limited use in the other large climate funds. The UNCDF programmes have specifically targeted innovative financial instruments, such as performance-based grants and municipal bonds, helping to

unlock local private sector and municipal finance. By engaging the local private sector in climate change investments, notable benefits are accrued by stimulating local green economies through income generating activities. Moreover, the majority of LDC economies are composed of SMEs in the informal sector, which need to be reached to stimulate low-carbon climate-resilient development.

- **Simplified access and approval:** the Adaptation Fund and GCF both enable direct access to funding which may enhance access to climate finance for local actors and intermediaries experienced at working at the local level, bypassing international organisations (Fenton *et al.*, 2015a). However, there is little evidence to suggest direct access is promoting local project delivery. Innovation by the FIP Dedicated Grants Mechanism can be learnt from, whereby project development and approval processes have been simplified, taking local capacity constraints into consideration to provide communities with improved access to project funding and capacity support (FIP, 2013). However, despite simplified approval processes being a common agenda item with the GCF's Board, this issue has still not been resolved. The Global Fund also offers an important precedent with multilaterals only funded if there are no alternative domestic institutions available, and they are required to develop the capacity of suitable domestic entities in the process.
- **Participatory funding structures:** the LDCF may enable greater participation through NAPA implementation. A high proportion of NAPA's have been delivered through local partnerships, for instance, in Bhutan and Mozambique, local beneficiaries have themselves been able to select tangible deliverables enhancing project effectiveness (GEF IEO, 2014). However, the GEF Small Grants Programme and FIP Dedicated Grants Mechanism provide best practice by using multi-stakeholder steering groups and committees. These structures provide local communities with greater say in the design of funding policies and modalities, and in the selection, appraisal, and monitoring and evaluation of projects.

All four development funds mandate the participation of local communities through multi-stakeholder decision-making processes, similar to the FIP and GEF Small Grants Programmes. From country coordinating mechanisms in the Global Fund, to village and local government forums in the World Bank's CDD, these structures provide improved oversight of community participation, rather than recommendations to project developers to engage with local actors. The BNTF shows best practice through the creation of a project monitoring committee in each funded sub-project, providing local communities with a focal point for direct engagement and requiring sponsorship by the community before approving the project. Community interviews confirm that the BNTF's projects are reaching the most vulnerable and poor communities.

To summarise, there are numerous examples of innovative funding approaches within international climate funds, predominantly within the smaller sub-funds of the FIP and GEF. In order to scale up local climate financing, the larger climate funds should take note of the success of the four international development funds which have provided innovative approaches to ensure communities are engaged, not simply as participants, but as owners and contributors to sustainable development. They have done so through policies and funding structures similarly represented within the community-focused FIP and GEF, but have also been scaled up to create greater impact through programmatic approaches retaining multi-stakeholder engagement.

6

Barriers to local climate financing

Six barriers have been identified which may hinder the flow of climate finance from the international to the local level. These are: priorities for large-scale results from mitigation-focused funds; the preference for business-as-usual financial intermediaries; risk-averse behaviour; inadequate local capacity support; inappropriate co-financing requirements; and ineffective oversight of participatory processes.

- **Priorities for large-scale results:** unlike adaptation, the investment strategies and results frameworks of the mitigation-focused CTF and GEF Trust Fund contain no locally specific indicators – prioritising carbon reductions and leveraging of co-finance, which incentivise large-scale projects. This is not to say that local activities have not been supported. With the CTF focusing on achieving results at scale, it has approved funding for district renewable energy schemes in Ukraine and Kazakhstan, and urban energy and transport schemes are under development for Bogota, Cairo, Mexico City, Hanoi, and Ho Chi Minh City (Nakhoda and Norman, 2014b). The GEF Trust Fund has also supported provincial and city-scale renewable energy projects, as well as rural and community-based decentralised energy projects in Chad, Malawi, and Cameroon.

Energy access programmes provide real opportunities for community interventions, however, only 3.4 per cent has been approved for decentralised energy projects as of 2015 (Rai *et al.*, 2016). Although many renewable energy investments are best delivered centrally to expand grid generation, there is a clear imbalance in investment given the huge energy access need within rural communities that would be fastest

met through mini-grid and off grid energy solutions. The results frameworks of some funds, including the GCF's mitigation window and the SREP, do include requirements to increase access to mini-grid and off-grid energy supply to households and communities (CIFs, 2012; GCF, 2014b). The GCF's results framework further states that energy access results will only qualify if from mini or off-grid energy and it has approved close to US\$500 million for energy access focused programmes, although greenhouse gas reductions and co-financing still remain the core mitigation criteria (GCF, 2014b). The GEF Trust Fund, during its third replenishment, also enabled results in off-grid electrification. However, fewer greenhouse gas emissions reductions resulted from these investments, forcing GEF to focus back towards on-grid energy solutions (Nakhoda, 2013).

The requirement for the GEF to achieve Global Environmental Benefits may also hinder local financing, given that local actions may not necessarily achieve global benefits (GEF IEO, 2015). However, the GEF Small Grants Programme support for community-based mitigation has far outweighed community-based adaptation (GEF and UNDP, 2016). This shows that local climate change mitigation does provide significant local opportunities to achieve globally notable environment benefits when financing strategies are designed appropriately. In addition, by scaling up local approaches to mitigation, appreciable results can be achieved. CDD has been praised for its flexible yet large-scale approach, allowing it to support a large number of community interventions (Wong, 2012).

- **Approach to local intermediaries:** the MDBs are less comfortable directly implementing small-scale funding (GEF IEO, 2015), which is associated with higher transaction costs (Nakhooda, 2013). However, the CDD's large-scale programmatic funding approach has shown how MDBs can work effectively whilst retaining significant scale, something they have been unable to do so far with their climate funds. In reality, most local actors are not able to directly access climate finance, although some, including city governments and local commercial banks, may possess the necessary financial track record.

Another way to reach local actors is to channel finance through intermediaries that are more comfortable managing smaller resources. This includes local financial institutions, such as commercial banks and microfinance lenders (Nakhooda and Amin, 2013), or CSOs (Glennie *et al.*, 2012). Despite requests for a minimum of 15 per cent of GEF funding to be reserved for CSO implementation under the GEF – to ensure the Global Environmental Benefits also provide local value – international agencies have been favoured (GEF IEO, 2015). Similarly, under the CIFs, the MDBs have tended to work through their regular development partners (ICF International, 2014). German federal organisations GIZ and KfW undertake the majority of projects under Germany's IKI, with other applicants commonly subject to hidden political selection. Short project planning periods, coupled with stringent appraisal conditions, have further favoured entities with significant experience and capacity (FEA, 2013).

Furthermore, there is currently little evidence that direct access promotes local project delivery. Initial experiences under the Adaptation Fund suggest that many national and subnational entities lack the capacity to meet the stringent accreditation standards, leading to a reliance on international entities (Tango Int. and ODI, 2015). At present in the GCF, over half of the 48 accredited entities are international organisations, including the multinational commercial banks HSBC, Credit Agricole, and Deutsche Bank. These may have been able to easily meet the fiduciary standards of the fund, but they are poorly suited for local investments. Moreover, out of the 14 accredited direct access entities, six are from upper-middle and high-income economies. In short, direct access was designed to enhance country ownership of climate finance, but traditional international financial intermediaries are still being favoured. These funds could undertake approaches such as under the Global Fund, where international agencies can only act as temporary intermediaries, required to build the capacity of national and subnational entities in the interim.

- **Risk-averse behaviour:** despite the range of innovative financial instruments available – from equity to guarantees – very few have been used. The prime reason is risk-averseness. The resource capitalisation of all the CIFs occurs through a mix of loans and grants with risk tolerances attached. Low risk tolerance from both donors and the MDBs has led to the dominant use of concessional loans, leading to a greater focus on larger and more centrally controlled mitigation projects under the CTF (Nakhooda and Amin, 2013), and large infrastructure adaptation projects under the PPCR (Trujillo *et al.*, 2014). The UK ICF financial instruments are also controlled by risk, with increasing expectations to use returnable capital. External pressure to spend resources quickly has lowered the UK ICF's risk appetite and reduced the resources available for capacity support, with a focus on large-scale projects with greater potential to generate revenue (ICAI, 2014). The GCF's low number of accredited entities suitable for working at the local level is also linked to the risk-averse behaviour of the fund. Innovative approaches can be learnt from the development funds reviewed above to mitigate the greater perceived fiduciary risk that domestic entities are expected to bring.
- **Poor local capacity support:** climate change adaptation and mitigation projects produce further challenges for local actors, such as needing basic knowledge of the impacts of adaptation to climate change (Terpstra *et al.*, 2016), to more technical needs, such as understanding the complex architecture of climate finance, meeting accreditation standards and developing the planning and budgeting systems required (Wilkinson *et al.*, 2014).

Despite improving readiness programmes, it remains difficult to assess how effective these funds have been at truly enhancing local capacity. Only the FIP Dedicated Grants Mechanism and GEF Small Grants Programme provide capacity support at the appropriate scale for local actors. This support is also implemented by local consultants, enabling localised learning (GEF and UNDP, n.d.). The four international development funds also provide capacity support specifically for local communities and to the stakeholders responsible for ensuring local engagement. These funds have shown the need for a long-term commitment to building capacity as, despite their more appropriate levels of support to partners, these funds have continued to struggle with low local capacity.

The GEF Small Grants Programme has faced challenges from the limited capacity within many local communities. It has experienced financial mismanagement, poor M&E, and, in some cases, exacerbated local environmental degradation (GEF, 2014c). The BNTF's participatory processes require a significant commitment and investment of time, especially when working with weaker communities. Finally, despite the community-strengthening framework of the Global Fund, most of its concept notes contain no community strengthening activities. Community participation and strengthening of their capabilities could be improved through changes in the Global Fund's requirements for co-financing – which shifts incentives away from investing in local partners' capabilities. Although most countries are meeting their co-financing requirements for health interventions, it is often at the expense of community groups engaging, rather than through promoting local ownership (The GF TRP, 2015).

▪ **Inappropriate co-financing requirements:**

co-financing is an important requirement for developing effective projects at scale. However, many international climate funds' requirements for co-financing have led to unsustainable projects when the domestic co-financing has not materialised as expected. Likewise, the expectation of understanding and securing co-financing from the start of the GEF project design has placed a significant burden on project developers, especially smaller entities with less experience, creating project delays (GEF IEO, 2015). Delays are especially damaging to local project developers where contingency plans are uncommon (Fenton *et al.*, 2015a). Lost momentum in project design reduces project effectiveness, leading to the need to restructure financing and increased likelihood of project cancellation (GEF IEO, 2015). Local actors have also struggled to contribute significantly to LDCF NAPA projects, with local governments providing just 1 per cent of co-financing, with the most provided by national governments and INGOs (GEF IEO, 2014). Many local governments are limited by small and delayed discretionary funding as part of their intergovernmental fiscal transfers. This limits local ownership and leads to upward rather than downward accountability. Even co-financing requirements under the GEF Small Grants Programme have been a significant hurdle for local entities (Both ENDS *et al.*, 2013).

The four development funds have taken approaches that are more appropriate to co-financing, creating an opportunity to improve community buy-in and ownership. Both the UNCDF and World Bank's CDD require co-financing from local participants, but on flexible terms more appropriate for local actors. This includes varying co-financing requests, depending on the local socio-economic circumstances and in-kind contributions for poorer communities. This promotes, rather than sidelines local engagement, making results accountable to communities.

- **Poor funding oversight:** many of the climate funds analysed provide progressive policies to enhance local participation and ownership of projects and programmes. However, poor oversight by these funds means there is limited compliance. Initial joint missions under the CIFs were successful at engaging local stakeholders, however, local engagement reduced significantly following approval of the projects. Even PPCR projects specifically designed to reach local communities often failed to continue engaging with local stakeholders following the approval of the investment plan itself (ICF International, 2014).

These projects have included inadequate structures for feedback from local stakeholders, with most decisions made by national governments rather than project beneficiaries (ICF International, 2014). Within both bilateral climate funds, the requirements for stakeholder engagement are also seen as inadequate (BMUB, 2015a; ICAI, 2014; ICF International, 2014) – the UK ICF has been heavily criticised for poor stakeholder engagement (ICAI, 2014), and the short planning periods and insufficient capacity of the IKI itself have inhibited effective stakeholder engagement (FEA, 2013).

Better practice is observed in the Adaptation Fund. Its NGO Network, composed of both INGOs and local CSOs (AF NGO Network, 2012), has been instrumental in strengthening the fund's focus on communities, such as mandating community engagement for all projects (Junghans *et al.*, 2015). However, whilst CSO representatives are present as observers on most multilateral climate funds, they are observers, and therefore do not possess decision-making powers (ICF International, 2014; Tango Int. and ODI, 2015). CSO representatives are also not given a budget to engage those who they are expected to represent – and whilst there are NGO networks in many countries and regions that could provide a sounding board for the representatives, this expectation is rarely explicit.

BOX 3. USAID’S LOCAL SOLUTIONS

Local Solutions is an agency wide reform of USAID’s funding policies and processes, aiming to increase the financing that directly reaches local CSOs and enterprises to 30 per cent of its total funding by 2015. This ‘radical’ shift in funding direction was initiated following the recognition that USAID had become far too reliant on large US-based organisations to provide its funding to developing countries. Momentum also came from two major administrative reviews within the US government on aid effectiveness in 2010: the Presidential Policy Directive on Global Development and the Quadrennial Diplomacy and Development Review, both defining the ultimate goal of US development finance as creating the necessary conditions in partner countries that enable US aid to be phased out. Moreover, USAID recognised that directly financing local actors would be less costly and more sustainable overall.

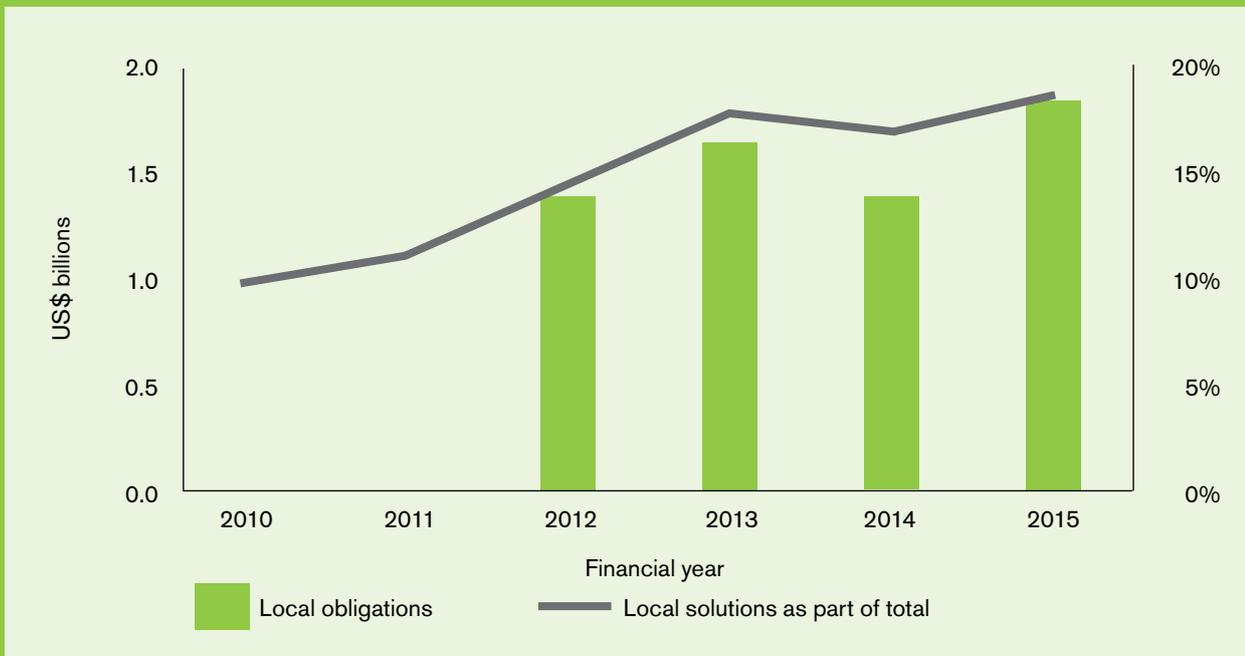
The implementation of *Local Solutions* varies from country to country, in recognition that there exist significant constraints to effective local financing within many partner countries, therefore aiming for an aggregate goal of 30 per cent local financing overall.

To mitigate the risks of financing local partners, which USAID saw as the biggest risk of *Local Solutions*, they have established mechanisms to support local procurement. USAID is mapping potential CSOs and

local businesses, often already engaged in funding through a US-based partner as sub-grantees. In 15 partner countries, USAID has established ‘local capacity development teams’ to help build the financial and fiduciary management capabilities required in the local organisations. Those who have been able to work with these teams have successfully submitted grant proposals to USAID, traversing the stringent fiduciary requirements.

USAID is also using specialised financial instruments to engage with these local organisations. Performance-based grants are based on project outputs rather than inputs. This allows capable local organisations that have limited experience to directly access and implement funding, whilst mitigating risks and ensuring accountability of results.

Whilst USAID failed to hit its 30 per cent local financing target for 2015, the goal has forced USAID to modify its policies and procedures to be more suitable for local financing. Local financing surpassed US\$1.5 billion in 2013 and 2015 (see figure below), rising from 9.7 per cent of its funding portfolio in 2010 to over 18 per cent in 2015. Local projects have also provided a ‘double dividend’, producing more sustainable results at a lower cost, whilst developing local capacity and providing local economic development (Dunning, 2016; 2013).



In short, despite positive intentions from a range of international funds to increase the flow of finance to the local level, they are seldom accompanied by the adequate oversight and in-country structures to ensure the intentions are realised. One way to improve this would be to set an international mandate for finance to be channelled to the local level, whilst strengthening the role of national entities for strategic oversight. However, despite the fact that local governments and communities are recognised as important actors in both the Addis Ababa Action Agenda and the Paris Agreement, no international goal exists. To our knowledge, the only major donor possessing a quantitative goal for finance that should reach the local level is USAID – the world's largest bilateral donor in absolute terms. Driven by a high level statement of ambition, USAID's *Local Solutions* reform has incorporated many of the enablers of local financing identified here. These include the use of locally appropriate, innovative financial instruments, and locally specific capacity building programmes helping to overcome the greater perceived fiduciary risk of local institutions (see Box 3). As a result, USAID's local financing portfolio rose by over 8 per cent between 2010 and 2015. This proves the value of a target in donor and fund policy frameworks to deliver a step change in climate and development financing to the local level.

However, despite these successes, USAID often bypasses country systems to channel finance to the local level, potentially limiting strategic national oversight and therefore longer-term sustainability. Country ownership is becoming ever more central to climate and development finance; national focal points are the apex institutions for coordinating multi-stakeholder engagement, providing oversight, identifying appropriate intermediaries and ensuring they are strengthened to deliver their remit. National focal points therefore play a critical role in channelling finance to the local level. However, national focal points also need to understand the value of finance reaching the local level. Without the political support for local financing, national focal points can also present a serious bottleneck to achieving appropriate flows to the local level (Christensen *et al.*, 2013; ICF International, 2014; Tango Int. and ODI, 2015), regardless of the policies and incentives in place at the fund level. Thus, it is also crucial that national focal points are given the support to learn the value of community engagement in setting climate and development priorities within their own countries. In addition, that they are supported in developing guidance on how to achieve the principles of subsidiarity. The ideal being is for climate financing to be both country owned and for it to strengthen communities engagement to define how to develop in ways that address and respond to climate change.

7

Conclusions

Given the benefits in efficiency, effectiveness, and sustainability of locally designed, locally implemented, and locally owned activities, this report has aimed to identify **whether international funds are creating the necessary frameworks to deliver local financing.**

Our unit of enquiry was official development assistance and international funds. Although these funds represent a small proportion of total international financing for development and climate action, they are important vehicles for the financing challenges set out by the SDGs and the Paris Agreement.

Analysis of the CFU database indicates an imbalance in the flows of climate finance with less than ten per cent (US\$1.5 billion) directed to local level activities between 2003 and 2016. However, it is presently not possible to identify an accurate figure of this international to local flow of climate finance. Obtaining the true figure would require improved reporting from the funds themselves. Given the scale and heterogeneity of development finance, a good estimate of local development financing was not possible.

Our analysis of the 12 climate and four development funds uncovered five enabling characteristics which promote local activities, either through intermediaries that can work effectively at the local level, or directly to the local actors themselves. Adaptation and small-grant-based climate funds contain common policies and procedures for enhancing local finance. These enabling funding characteristics are also observed within all four development funds, furthermore, they have been able to use them to achieve local financing at large monetary scale. However, we also uncovered six characteristics across these funds which promote business-as-

usual financing to large-scale and centrally controlled programmes. Although these top down financing approaches are necessary for many mitigation and adaptation activities, it is crucial that mechanisms are also available that facilitate local engagement and local delivery in recognition of the efficiency, effectiveness, and sustainability benefits that local communities and local enterprises can bring. With these barriers and enablers in mind, we propose seven reforms to improve the tracking of finance and a more effective international funding architecture, which will in turn enhance the flow of climate finance to the local level.

1. **Identify the baseline of financing that reaches the local level and involves community engagement.** Effectively tracking development and climate finance to the local level is presently not possible. The transparency and reporting of international and bilateral funds are simply too poor to track finance through delivery partners, to the local geographies and beneficiaries that are the ultimate purpose of the finance. We recommend that specific indicators are developed and integrated into financial reporting that capture the amount of finance that is delivered through local actors, that involve participatory decision making with communities, and that reach local level beneficiaries.
2. **Use this baseline to set an international goal for local financing.** Despite the Addis Ababa Action Agenda and the Paris Agreement recognising the importance of communities, there is no international goal for local financing. By establishing a robust baseline for local level development and climate financing, we can better set an international goal for the finance that should reach and engage

local actors. As demonstrated by USAID's *Local Solutions*, a high-level goal helps to incentivise progressive reform of funding policies and procedures to better fit local contexts and ultimately deliver more effective development results.

As well as earmarking the scale of finance that should reach the local level, there are policies that can incentivise local level climate financing.

3. **Allocate flexible, grant-based, programmatic finance for local financing.** All the climate funds that we found were successfully channelling finance to the local level, including the FIP Dedicated Grants Mechanism and the GEF Small Grants Programme, have primarily utilised small grant-based financing, more appropriate for individual projects at the local level. However, development funds have developed programmatic approaches that can deliver many small projects and retain community participation. These can deliver the large-scale results that many donors and the MDBs are looking for, best displayed by the World Bank's CDD. By providing flexibility in how funding is designed for each community's context, the finance can be delivered in ways that prevent crowding out of local engagement, including unlocking local municipal and private sector finance.
4. **Revise the policies of international funds to increase their risk appetite for supporting innovative financial instruments, to be more flexible on co-financing, and to use locally appropriate results frameworks.** To unlock local municipal and private sector finance, innovative financial instruments need to be used. Many climate funds have failed to use these instruments and this is commonly attributed to their risk aversion. The UNCDF has mainstreamed climate resilience into local development by prioritising such instruments, and the GCF has begun to use equity and guarantees in its early projects.

Beyond the types of instruments, development funds have incentivised enhanced local ownership and downward accountability by ensuring community co-financing is flexible and appropriate to the local context, such as in-kind contributions. However, climate funds have often created unsustainable projects by setting co-financing requirements that are often not achievable in practice.

Finally, those funds most successfully channelling finance to the local level have included locally appropriate indicators, including results at the household and community levels. Adaptation funds have better reflected these, whereas mitigation funds supporting carbon emissions reductions and co-financing have tended to support large-scale

and centrally controlled programmes, unless energy access is a core indicator.

5. **Provide tailored capacity building support to local institutions to manage climate finance.** Despite progress in tailored capacity support, most funds target national institutions, which will not build the capacity of local actors to receive climate finance. The FIP, the GEF Small Grants Programme, and the four development funds all provide capacity support tailored for local actors, both in scale and by working through local service providers. However, despite these enabling characteristics, all these funds have struggled in many cases to build local capacity sufficiently, often because of insufficient oversight and accountability, and because of the long term nature of the investment required.
6. **Build national and local level platforms for governments, NGOs, representatives of the climate vulnerable, and the donors, to oversee climate finance flows, ensuring they respond to the priorities of the poor to achieve climate-positive development.** Underpinning all these recommendations is the need to ensure enabling policies are implemented effectively across scales of governance. Establishing in-country systems that promote participation of multiple stakeholders from the national down to the local level, can ensure activities deliver the priorities of the vulnerable whilst reflecting national strategies. The FIP, the GEF Small Grants Programme and the four development funds all mandate multi-stakeholder participatory processes that deliver enhanced decision-making powers to local communities but retain connection to national and even international policy processes.
7. **Ensure national focal points have adequate capacity and assistance to oversee the principles of subsidiarity.** National focal points are crucial entities in all climate and development funds, responsible for oversight, stakeholder engagement, identifying appropriate financial intermediaries, and facilitating capacity support, amongst other responsibilities. Within the new EDA modality of the GCF, national focal points will lead the oversight of devolved financing mechanisms that specifically aim to enhance local public and private sector climate finance through participatory processes. International funds must ensure their capacity is sufficient to execute these responsibilities in a way that ensures country ownership and maximises the principles of subsidiarity, by using existing country systems that enable citizens to have real influence in how climate finance is spent.

7.1 Looking forward

Funding policy documents and external evaluations were used to identify the barriers and enablers to local financing outlined in this report. However, there remains limited evidence from implementation of these policies, especially evidence drawn from local communities themselves. In order to enhance the findings of this paper, it is important to:

- Engage directly with beneficiaries and members of multi-stakeholder committees at the national and local levels to identify the effectiveness of these funding policies in practice. To enquire about what has worked and what has not.
- Compare and contrast the funding modalities for engaging local private sector entities – specifically SMEs – in climate-compatible development.
- Evaluate the effectiveness of capacity and readiness support programmes in strengthening national climate finance focal points and local communities, to oversee and implement climate finance.

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Annex I. Finance tracking methodology

The **Climate Funds Update (CFU)** database was used to generate an initial estimate of the volume and share of climate finance reaching the local level. The CFU database covers public finance from all major international climate, and some regional and national climate funds. We defined local actors as any entity below the district administration level, including: local governments, community-based organisations (CBOs), local non-governmental organisations (NGOs), households, and the local private sector – such as local commercial banks, microfinance institutions, and SMEs.

To identify projects and programmes which may be executed and/or benefit local actors we used key search words, including: civic, community, cooperative, decentralised, home, household, indigenous, local, municipal, province, rural, slums, smallholders, SMEs, subnational, town, and village.

Study limitations

- By focusing on international funds, we cover just a small proportion of international development and climate financing. However, it is not feasible to analyse all development and climate finance flows.
- The search words used to identify local climate change projects and programmes are likely to provide only indicative financing trends. The CFU database is only designed to track finance to the national, not the local level. Accurately defining local level access and beneficiaries even just across the major international funds would require an in-depth review of all project documents, which is not possible given the limited scale of this research project. Even if projects are locally orientated there are no assurances that local actors executed, or are beneficiaries of, approved finance. Furthermore, even with high correlations between the project overview and executing entities or beneficiaries, other costs, such as for proposal preparation, agency and administration fees, would need to be removed to identify the true funding reaching local actors (Fenton *et al.*, 2015b). Thus, a true picture of local level climate and development finance remains a major gap in our knowledge.

Annex II. Climate funds results frameworks

Table 1. Priority outcomes and indicators of ten of the major multilateral and bilateral climate funds

MITIGATION FOCUSED FUNDS		
GEF Trust Fund	Green Climate Fund (GCF)	Clean Technology Fund (CTF)
<p>GEF 6 is composed of objectives, programmes, expected outcomes, and indicators.</p> <p>Overall indicator: tCO₂e avoided, both direct and indirect, over the investment or impact period of the projects.</p> <p>Corporate level outcome target: 750 million tCO₂e.</p> <p>Objective 1: promote innovation, technology transfer, and supportive policies and strategies.</p> <p>Objective 2: demonstrate systematic impacts of mitigation options.</p> <p>Objective 3: foster enabling conditions to mainstream mitigation concerns into sustainable development strategies.</p>	<p>Fund-level impacts</p> <ol style="list-style-type: none"> 1. Reduced emissions through increased low-emission energy access and power generation. 2. Reduced emissions through increased access to low-emission transport. 3. Reduced emissions from buildings, cities, industries and appliances. 4. Reduced emissions from land use, deforestation, and sustainable management of forests and conservation and enhancement of forest carbon stocks. 5. Strengthened institutional and regulatory systems for low-emission planning and development. 6. Increased number of small, medium and large low-emission power suppliers. 7. Low energy intensity buildings, cities, industries, and appliances. 8. Increased use of low carbon transport. 9. Improved management of land or forest areas contributing to emissions reductions. <p>Core indicator: tCO₂e reduced, cost per tCO₂e decreased, and volume of finance leveraged by funding.</p> <p>Other indicators: number of households, and individuals with improved access to low carbon energy sources.</p>	<p>Contains one transformation indicator and five programme outcomes. Core indicators:</p> <ol style="list-style-type: none"> 1. Tonnes of GHG emissions reduced or avoided. 2. Volume of finance leveraged, by public and private sources. 3. Installed capacity (MW). 4. Number of additional men and women passengers using low carbon transport. 5. Annual energy savings (GWh). <p>Transformative co-benefits:</p> <ol style="list-style-type: none"> 1. Reduced cost of low carbon technologies and practices. 2. Energy security. 3. Improved enabling policy and regulatory environment for low carbon technologies and practices. <p>Outcome level co-benefits:</p> <ol style="list-style-type: none"> 1. Access to energy. 2. Health. 3. Employment.

MITIGATION FOCUSED FUNDS

Scaling-up Renewable Energy Programme (SREP)

Transformative:

1. Support low carbon development pathways by reducing energy poverty and/or increasing energy security:
 - a) National measure of energy poverty based on multi-dimensional energy poverty index or other;
 - b) Annual electricity output from renewable energy in GWh;
 - c) Increased public and private investment in targeted subsectors per year (US\$).

Programme outcomes:

1. Increased supply of renewable energy:
 - a) Annual electricity output from renewable energy (GWh).
2. Increased access to modern energy services:
 - a) Number of women and men, businesses and community services benefiting from improved access to electricity and fuels.

Forest Investment Programme (FIP)

Common themes:

1. GHG emission reductions/ enhancement of carbon stocks – tCO₂/yr.
2. Livelihood co-benefits – number of people directly benefiting out of total number of targeted people.

Co-benefit themes:

1. Biodiversity and environmental services.
2. Governance.
3. Tenure, rights and access.
4. Capacity building.

Elements for narrative:

1. Theory of change and assumptions.
2. Contribution to national REDD+ plus other.
3. Support received from other partners.
4. Link of Dedicated Grant Mechanism investments from government point of view.

CROSS-CUTTING

United Kingdom's International Climate Fund (UK ICF)

Formed of one goal, four strategic objectives, seven intermediate outcome key performance indicators (KPIs), and nine direct output KPIs. Intermediate outcome KPIs:

- Level of integration of climate change into national planning.
- Number of people with improved resilience to climate change.
- Extent to which ICF interventions achieve growth and prosperity.
- Number of people with improved access to clean energy.
- Change in GHG emissions reduced or avoided.
- Value of ecosystem goods and services generated or protected.

ADAPTATION-FOCUSED FUNDS

Least Developed Countries Fund and Special Climate Change Fund (LDCF/SCCF)	Adaptation Fund (AF)	Green Climate Fund (GCF)
<p>Composed of one goal, 3 objectives, 10 outcome and 14 indicators.</p> <p>Objective 1: reduce the vulnerability of people, livelihoods, physical assets and natural systems to the adverse effects of climate change.</p> <p>Objective 2: strengthen institutional and technical capacities for effective climate change adaptation, including – access to improved climate information and early warning systems enhanced at regional, national, subnational and local levels.</p> <p>Objective 3: integrate climate change adaptation into relevant policies, plans and associated processes.</p> <p>Indicators: 7 refer specifically to individual beneficiaries and 2 to subnational plans and institutions.</p>	<p>Composed of 7 outcomes, 8 outputs and 26 indicators.</p> <p>Outcome 1: reduced exposure at national level to climate-related hazards and threats.</p> <p>Outcome 2: strengthened institutional capacity to reduce climate risks and losses.</p> <p>Outcome 3: strengthened awareness and ownership of adaptation and climate risk-reduction processes at local level.</p> <p>Outcome 4: increased adaptive capacity within relevant development and natural-resource sectors.</p> <p>Outcome 5: increased ecosystem resilience in response to climate change and variability-induced stress.</p> <p>Outcome 6: diversified and strengthened livelihoods and sources of income for vulnerable people in targeted areas.</p> <p>Outcome 7: improved policies and regulations that promote and enforce resilience.</p> <p>Indicators: include the number and type of risk reduction actions and strategies introduced at the local levels, local press and media involved, and number of beneficiary households and communities.</p>	<p>Includes the paradigm shift objective, fund and project level results, and indicators.</p> <p>Fund-level impacts</p> <ol style="list-style-type: none"> 1: increased resilience and enhanced livelihoods of the most vulnerable people, communities and regions. 2: increased resilience of health and well-being, and food and water security. 3: increased resilience of infrastructure and the built environment to climate change threats. 4: improved resilience of ecosystems and ecosystem services. <p>Project/programme outcomes</p> <ol style="list-style-type: none"> 5: strengthened institutional and regulatory systems for climate responsive planning and development 6: increased generation and use of climate information in decision making. 7: strengthened adaptive capacity and reduced exposure to climate risks. 8: strengthened awareness of climate threats and risk-reduction processes <p>Core indicator: total number of direct and indirect beneficiaries, or that relevant to total population.</p>

Pilot Programme for Climate Resilience (PPCR)

Composed of two transformational impact results and four indicators, and five programme outcomes and five indicators. Five indicators are core:

1. Number of people supported to cope with effects of climate change.
2. Degree of integration of climate change in national, including sectoral planning.
3. Extent to which vulnerable households, communities and businesses and public services use improved tools, instruments, strategies, activities to respond to climate variability and resilience.
4. Evidence of strengthened government capacity and coordination mechanism to mainstream climate resilience.
5. Quality of and extent to which climate responsive instruments/investment models are developed and tested.

Acronyms

AF	Adaptation Fund
BMUB	Germany's Federal Ministry for Environment, Nature Conservation, Building and Nuclear Safety
BNTF	Basic Needs Trust Fund
BRICS	Brazil, Russia, India, China, and South Africa
CAF	Kenya's Climate Adaptation Fund
CBO	Community-based organisation
CCCF	County Climate Change Funds
CDD	Community-Driven development
CFU	Climate Funds Update
CIF	Climate Investment Fund
CSO	Civil society organisation
CTF	Clean Technology Fund
DAC	Development Assistance Committee
DCF	Decentralising climate adaptation funds
DECC	UK Department for Energy and Climate Change
DEFRA	UK Department for Environment Food and Rural Affairs
DFID	UK Department for International Development
EDA	Enhancing Direct Access
FIP	Forest Investment Programme
GCF	Green Climate Fund
GEF	Global Environmental Facility
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GNI	Gross National Income
IDA	International Development Association
IKI	German International Climate Initiative
INGO	International non-government organisation
KfW	Kreditanstalt für Wiederaufbau (Germany government-owned development bank)
KPI	Key performance indicators
LDC	Least developed country
LDCF	Least Developed Countries Fund
LDRRF	Bangladesh's Local Disaster Risk Reduction Fund
LFI	UNCDF Local Finance Initiative
LoCAL	UNCDF Local Climate Adaptive Living Facility M&E Monitoring and evaluation
MDB	Multilateral Development Bank
MIC	Middle income country
NAMA	Nationally Appropriate Mitigation Actions
NAPA	National Adaptation Plan of Action
NDC	Nationally determined contribution
NGO	Non-government organisation
ODA	Official development assistance

ODI	Overseas Development Institute (UK)
OECD	Organisation for Economic Co-operation and Development
PPCR	Pilot Programme for Climate Resilience
REDD	Reducing Emissions for Deforestation and Forest Degradation
SCF	Strategic Climate Fund
SCCF	Special Climate Change Fund
SDGs	Sustainable Development Goals
SIDS	Small Island Developing States
SME	Small- and medium-sized enterprises
SPCR	Strategic Programmes for Climate Resilience
SREP	Scaling-up Renewable Energy Programme
UK ICF	United Kingdom International Climate Fund
UN	United Nations
UNCDF	United Nations Capital Development Fund
UNDP	United Nations Development Programme
UNFCCC	United Nations Framework for the Convention on Climate Change
USAID	United States Agency for International Development

With the rapid ratification of the Paris Agreement, international climate funds will be important in scaling-up developing countries climate action. Evidence shows climate finance reaching the local level – as part of a coherent approach to climate action – delivers effective, efficient and sustainable results that enhance the impact of each dollar disbursed. This working paper explores the flows of climate finance within the main international climate funds, to understand how effective they are in getting finance to the local level and what design features enable or prevent local financing. It distils lessons from development funds that are experienced in local financing. It concludes by highlighting the ways in which local climate financing can be enhanced – to further improve the effectiveness of aid.

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