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Financing Strategies: A missing link to translate NDCs into action

A discussion of building blocks, in-country experiences and lessons learned

Financing the implementation of a national climate policy is a costly endeavour. Globally, the implementation of the submitted (Intended) Nationally Determined Contributions (NDCs) is estimated to cost as much as USD 4.4 trillion.[1] Against this background it is obvious that countries seeking to embark on a low-emission, climate-resilient development path will require funding from a variety of sources.

While many countries already have climate change-related policy documents in place, which are often and most recently expressed in NDCs, implementation is a challenge not only due to weak pipelines of bankable projects generally but also due to a lack of capacities and funding. A strategy to mobilise and access climate finance is thus crucial and may be one of the missing links in moving from planning climate action to implementation.

The Climate Finance Readiness Programme[2] has gained valuable experience in advising countries on climate finance and financing strategies since its inception in 2013. Implemented by the Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ) the Programme is financed by the German Federal Ministry for Economic Cooperation and Development with co-funding from the United States Agency for International Development, the Czech Ministry of the Environment and the Green Climate Fund. A number of its partner countries have requested support for financing strategies, and the objective of this document is to identify the key building blocks of such an approach, present the Programme‘s practical in-country experiences and outline some pragmatic lessons learned for the future.

What is a “financing strategy”?

There is no single definition for the term ‘financing strategy’. In the context of climate finance, the Programme defines it as a national coordinated approach for the identification of financing options for climate change adaptation, mitigation and cross-cutting projects and programmes that together serve to achieve the national climate policy goals.[3] This approach relates to funding from national and international, public and private sources dedicated to climate change activities, which can be summarised under the term ‘climate finance’. The strategy does not necessarily need to be a specific stand-alone document, but can be part of existing strategies or plans. In many developing countries, especially in least developed countries (LDCs) with little fiscal space, the main purpose of the strategy will be the mobilisation of additional international resources. Given that the NDCs are typically informed by different national policies, the strategy will relate directly to the financing of the national contributions and may even provide the direct link from policy to NDC implementation.

The design of such a financing approach depends chiefly on the country-specific objectives. These include, for example, that the strategy can serve as a basis for governmental decision-making to prioritise the use of national and international funding and can thus contribute to the coordination of donor funding. On the other hand, a strategy could also promote access to finance and the implementation of specific projects/programmes.

The actors involved in the process of developing a financing strategy will also vary depending on the national context and will thus determine the focus of the strategy. Typically the responsibility will lie with the coordinating body of the national climate policy, oftentimes the environment ministry, as well as sector ministries that implement projects/programmes and the ministries of finance and planning, depending on their role in climate finance. The coordination of the leading institution with other relevant stakeholders, especially the finance and planning ministries, is key to ensure broad governmental commitment for the process. In addition, sub-national governance structures play a crucial role due to their responsibility in formulating and implementing projects and programmes.

1 According to the 2015 Germanwatch Briefing Paper ‘Investing in Ambition: Analysis of the financial aspects in (Intended) Nationally Determined Contributions’, as much as USD 4.4 trillion will be required to implement the climate change mitigation and adaptation activities put forward. This number is only indicative and associated with high uncertainty. Available at: https://germanwatch.org/de/download/15226.pdf

2 More information about the Programme is available at: https://www.giz.de/expertise/html/19694.html.

3 The term ‘project’ refers to stand-alone climate change-related activities, whereas ‘programme’ refers to more wide-ranging and systemic activities. The Green Climate Fund has expressed its ambition to fund especially the latter.

Building blocks of a financing strategy

While the scope of a financing strategy may differ depending on the context and the objective, the following building blocks will typically represent key elements of an approach for a strategy:

1 The financing gap

A key starting point for a financing strategy for climate change-relevant activities is specifying the amount of funding required for implementing national climate policy goals. National and sectoral policies and strategy documents such as national adaptation plans, low-emission development strategies or climate change strategies can serve as the basis for determining financial demand. If these are not in place, a key step is to identify priority areas and sectors (typically including vulnerable sectors such as water and agriculture and sectors with high emission reduction potential such as energy and transport), which requires a national process with stakeholder consultation. Significant effort has been put into formulating the NDCs so that they can serve as a basis for such a process. Once priority areas have been defined, the costs for implementing the national and/or sectoral goals can be estimated. The methodology to perform such costings can vary depending on the level of information available on investment projects that reflect sectoral priority investments.

With future costs estimated, governments must identify existing climate financing from different sources. For this step, officials can analyse state budget and off-budget expenditure, including bilateral and multilateral donor funding, that is related to climate-relevant issues. Since many countries have not (yet) institutionalised reporting on climate change expenditure in the budgeting process, budget-tracking methodologies like the Climate Public Expenditure and Institutional Review (CPEIR)[4] could provide a one-off overview.

Being aware of both the upcoming costs as well as the current spending on climate change activities enables stakeholders to develop scenarios for financing needs, which will reveal the ‘financing gap’ for climate-related activities. In some cases, the national financing gap is estimated in the NDCs.

2 Financing options

It is widely recognised that no single financing source will be able to cover the national costs for climate change adaptation and mitigation. Against this background, countries should consider the broad array of financing options available to cover the costs of climate change mitigation and adaptation priorities over the short-, medium- and long-term. This is again country-specific and may range from national fiscal policy measures, such as environmental fiscal reform (e.g. environmental tax and the removal of fuel subsidies) or additional allocation from the state budget, to bi- and multilateral development funding through direct donor support or climate change funds, such as the Green Climate Fund (GCF), the Global Environment Facility or the Adaptation Fund. A key component is the mobilisation of additional funding for climate-related activities, especially in LDCs.

Questions to be considered during the analysis of funding options include:

- In general, does the country prioritise mitigation or adaptation activities?
- Are processes in place to mainstream climate change in sectoral planning and budgeting to generate integrated sectoral solutions to climate change and enable their financing through national public funds?
- Does a focus exist to mobilize grants or loans?
- Does the country have access to specific international funds, e.g. for LDCs? Has it reached the funding limit of specific funds?
- Does the country provide a suitable environment for private sector investment in priority mitigation and adaptation measures?

A financing strategy should identify different options (such as private- or public-sector financing) and instruments (such as equity, loans or grants) for its financing needs. This allows stakeholders to employ the most suitable financing mechanisms. Furthermore, such diversification spreads and thus limits the overall risk of failure to receive funding from any one particular source.

4 More information available at: https://www.climatefinance-developmenteffectiveness.org

3 Implementation plan

To ensure that climate change policies are implemented, a successful financing strategy plots a direct route to action with a context-specific and realistic implementation plan.

This plan should be developed under the consideration of the following:

- The actors that play a key role in implementing the financing strategy need to be identified. Ministries of finance and environment typically play equally important roles in implementation as private sector actors working on project implementation or the private and public banking sectors.
- The responsibilities and tasks of the actors need to be specified, including a clear delineation of responsibilities and effective coordination and cooperation between institutions.
- A realistic timeline needs to be in place with achievable milestones in order to be able to monitor progress (or lack thereof). Part of this timeline should include planning for the short-, medium-, and long-term, whereby the medium- to long-term milestones may address more fundamental financing issues, such as changes in public financial management and banking systems as well as the enabling environment required for those changes. At the same time, the medium- to long-term perspective should also reflect the increasing ambition of countries to act on climate change, as envisioned in the NDCs.

4 Way forward

A key hurdle in translating a financing strategy into action is the lack of capacities among stakeholders. The effort required from project/programme proponents to develop a project/programme concept or proposal, for example, is significant. The relevant processes need to be managed and the required funding secured, either domestically or with external support. Capacity-building measures can help develop the needed skills in order to manage all these different processes.

These measures alone, however, do not reach far enough in addressing challenges such as limited staff resources in governmental institutions, competing policy priorities or the lack of coordination among actors. An integrated approach to strengthening national institutions throughout, including on broader issues, is thus crucial for the successful planning of climate finance.

Depending on the specific needs, the capacity-building measures can also target, for example, the private and banking sectors in order to raise awareness and provide training on innovative financing models and business opportunities for climate change-related activities. Furthermore, the capacities of public sector stakeholders to engage the private sector can be strengthened, for example, through public-private partnership models.

Country examples

Uganda

The Government of Uganda has already developed strategies and plans to address climate change, including a National Climate Change Policy and Implementation Strategy (2012), an NDC (2015) and, most recently, a GCF Country Programme (2016). These documents, which are at various stages of implementation, highlight the different adaptation and mitigation priorities of the country, and, in some cases, include programme/project ideas with indicative costing. Similarly, provisions have been made to plan for and monitor climate finance: the 2nd National Development Plan (2015/2016–2019/2020), for example, includes climate change.

Experience varies among sector ministries involved in mitigation and adaptation projects with different financing mechanisms. While experience has been gained in securing and implementing grant funding, the institutions lack capacities, for example, to develop project concepts and proposals for submission to climate funds. Furthermore, experience has and is also being made at ministerial level with various other financial mechanisms and alternative approaches ranging from feed-in tariffs to guarantees, labelling, standards and public-private partnerships (PPPs), with a key role being played by the private sector and their respective associations. These experiences should be built upon.

Although indicative knowledge of the financing gap and current climate finance flows exists, there is no coherent strategy to finance the different priorities of the climate policy and the NDCs. Such a strategy could include (1) an integrated approach to plan access to climate finance from various sources, including the private sector; and (2) technical capacities to manage the required processes. Against this background, the Climate Finance Readiness Programme is providing support to the Ministry of Finance, Planning and Economic Development for the development of a financing strategy that focuses on these areas.

Cambodia

In 2013, the Royal Government of Cambodia adopted the Cambodia Climate Change Strategic Plan 2014–2023 as an overarching policy framework responding to climate change issues in the country. It was integrated into the National Strategic Development Plan 2014–2018. At sectoral level, relevant ministries have started preparing Climate Change Action Plans that define sectoral priorities as well as priority actions. As agreed upon with the partner institution of the Climate Finance Readiness Programme, the National Council for Sustainable Development, these priority actions were taken as a basis for defining the financial demand and the financing gap as a first step towards developing a financing strategy, which will have a specific focus on climate change adaptation and will complement the National Adaptation Plan. In a next step, the ministries assessed the robustness of the costing as well as the potential for funding from the national budget and identified funding options for the most promising priority actions. These steps provided the Cambodian Government with a basis for making decisions on which project proposals to develop further.

Tajikistan

Climate change considerations have been integrated into the National Development Strategy 2030 and the Mid-term Development Strategy 2020. The Tajik Government is in the process of developing a national adaptation strategy with 30 investment project ideas, which is to reflect the most urgent priorities for the relevant sectors. Since national funding is limited, a major focus lies on assessing the funding opportunities through international climate funds. With over 60% of the population living in rural areas and engaged mainly in agriculture, vulnerability to climate change is high in the country. Therefore, Tajikistan has received funding through the World Bank's Climate Investment Funds Pilot Programme for Climate Resilience. At the current stage the country is focusing on accessing the GCF. In this context, the strategic prioritisation of projects/programmes in key sectors is essential. In response, GIZ provided support to the Ministry of Agriculture to develop a sectoral financing framework and to move ahead with a prioritised project proposal on seed production.

Lessons learned & recommendations

Over the years, much experience has been made with financing climate-related activities through different public and private sector mechanisms. More experience is needed to enhance climate action and thus contribute to the implementation of the NDCs. Some initial lessons learned and recommendations are outlined below:

Seeking: a new approach!

In order to achieve ambitious climate change objectives, innovative, cost-effective national solutions are necessary. The implementation of climate change policies can not only rely on additional international climate funds but has to be an inherent part of all governmental policy implementation. One important step towards that is mainstreaming climate change in sectoral planning and budgeting, leading to more systematic and integrated consideration of adaptation and mitigation aspects in governmental policy implementation. Strong alliances with the private sector can contribute to leveraging additional funds (see below). International funds can then target those projects/programmes for which no national public or private funds are available. Where a strategy focuses on climate funds, a financial exit strategy should be in place to ensure that the operation and maintenance of the project/programme, which are integrated into the national budget in the long-term, can be maintained throughout its lifetime.

➲ **Recommendation:** All planning options to enhance resilience and reduce emissions should be explored. A key component of a strategy should be the sustainability of investments.

How long is a piece of string?

Or: how much money is really needed? Specifying the costs of climate change and the respective funding needs is challenging and depends on the national context and available information. In some countries national and/ or sectoral planning documents with readily identified projects/programmes and cost estimates are already in place. Although these can be a good basis to establish the overall financing needs, the estimates are often based on assumptions of geographic scope, expected budget ceilings, etc. Changing those assumptions may lead to different estimations. Consequently, in-depth costings become most relevant when there are concrete options for financing.

➲ **Recommendation:** Indicative costs, including the related implementation costs surrounding preparation and trainings for implementation, are typically sufficient for a strategy and do not require too much time and effort to provide an overview of the financial demand. However, demand for funding can typically be adjusted depending on available supply.

Sequencing counts

Some countries may lack the capacity to plan for, mobilise or absorb large-scale climate finance immediately. In those cases it might make sense to prioritise a limited number of project/programme ideas to be developed into proper proposals for submission to international climate funds. By doing so, the most urgent demand could be addressed in the short-term. For the medium- to long-term, the country benefits from a more strategic and comprehensive approach with a variety of funding options to respond to climate change.

➲ **Recommendation:** A sequenced approach can be beneficial where capacities to absorb funding efficiently and effectively are limited.

Leading the way

Leadership on climate change issues by senior stakeholders and their institutions is crucial to advance a financing strategy. Moreover, in order to hold stakeholders accountable for their responsibilities in facilitating the financing of climate change actions, the strategy and its implementation plan need to follow official government procedures and be communicated to the public. Integrating the strategy into national decision-making processes also allows for the monitoring and evaluation of its implementation.

➲ **Recommendation:** Senior stakeholders need to be on board with the financing strategy, which should ideally also be available to the broader public inside and outside the government for scrutiny and monitoring.

Behind closed doors: political economy

Factors such as the political economy, including interests of stakeholders, their (dis)incentives and power structures, or political trends for donor funding often determine which project/programme proposals may be further developed. Considering the political economy as part of a financing strategy is thus crucial for its implementability.

➲ **Recommendation:** The political momentum and economy behind different funding options should be identified and considered in a strategy to ensure that projects/programmes with sufficient support can be implemented and that activities, that do not have a strong backing are not ignored and can be supported as needed.

Training for success

Many public and private organisations remain unfamiliar with climate finance mechanisms and their requirements. For example, sector ministries often have a high interest in international funding and express their need for additional training in order to manage the required processes.

➲ **Recommendation:** For a financing strategy to be implemented, it should be accompanied by adequate capacity development measures.

"Not another strategy!"

Strategies can be at risk of being shelved after some time without being implemented. Reasons for this can include unrealistic expectations and a lack of commitment to implement them. A successful financing strategy addresses these challenges and is embedded in activities to facilitate an enabling environment for the short- to long-term.

➲ **Recommendation:** Where it is suitable and the environment allows it it may make sense to specifically target a select number of strategic projects/programmes for financing in addition to developing a strategy.

Let the private sector take care of it

The private sector and the financial sector are key to leveraging climate-relevant finance. The public sector must do its part to ensure there is adequate and productive coordination and awareness raising measures.

➲ **Recommendation:** The private sector should be engaged in all stages of the strategy and policy-makers should highlight opportunities for engagement, ensure adequate communication with the public sector, and provide capacity-building support as required. Raising more awareness of the economic profitability of projects/programmes in the financial sector, especially for mitigation, is equally important to leverage additional private climate finance.

The Climate Finance Readiness Programme (CF Ready)

On behalf of BMZ and with co-finance from USAID, the Czech Ministry of the Environment and the Green Climate Fund, GIZ implements the CF Ready Programme, which is currently supporting 14 partner countries and one region to access and effectively use climate finance. The Programme is implemented jointly with KfW. It supports national climate finance institutions and NDAs to coordinate in the area of climate finance and assists potential national implementing entities and/or intermediaries during accreditation. Furthermore, the Programme provides support in developing strategic frameworks, national climate strategies and policy packages for ambitious, climate-resilient low-carbon development paths. The work in each country is based on an initial assessment of the challenges and barriers. In close dialogue with the partner countries, the services are customised to best respond to each countries' needs, to optimally supplement existing programmes in this field and to build expertise in each country. In addition to this Programme, GIZ also supports climate finance readiness as part of large climate change support programmes, and currently works on climate finance in more than 40 countries.

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Registered offices
Bonn and Eschborn, Germany

Godesberger Allee 119
53111 Bonn
T +49 228 24934 – 111
F +49 228 24934 – 215
c f-ready@g i z .de
E cf-ready@giz.de
I www.giz.de

Climate Finance Readiness Programme (CF Ready)
G320 Section Climate Change and Climate Policy
Climate Change, Environment and Infrastructure Division
GloBe Sectoral and Global Programmes Department

Responsible
Marius Kaiser, Bonn / Regina Bernhard, Eschborn

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On behalf of
German Federal Ministry for Economic Cooperation and Development (BMZ)
Special Unit 'Climate'

BMZ Bonn
Dahlmannstraße 4
53113 Bonn
Germany
T +49 228 99 535 - 0
F +49 228 99 535 - 3500

BMZ Berlin
Stresemannstraße 94
10963 Berlin
Germany
T +49 30 18 535 - 0
F +49 30 18 535 - 2501

poststelle@bmz.bund.de
www.bmz.de

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