



Ninth African Development Forum

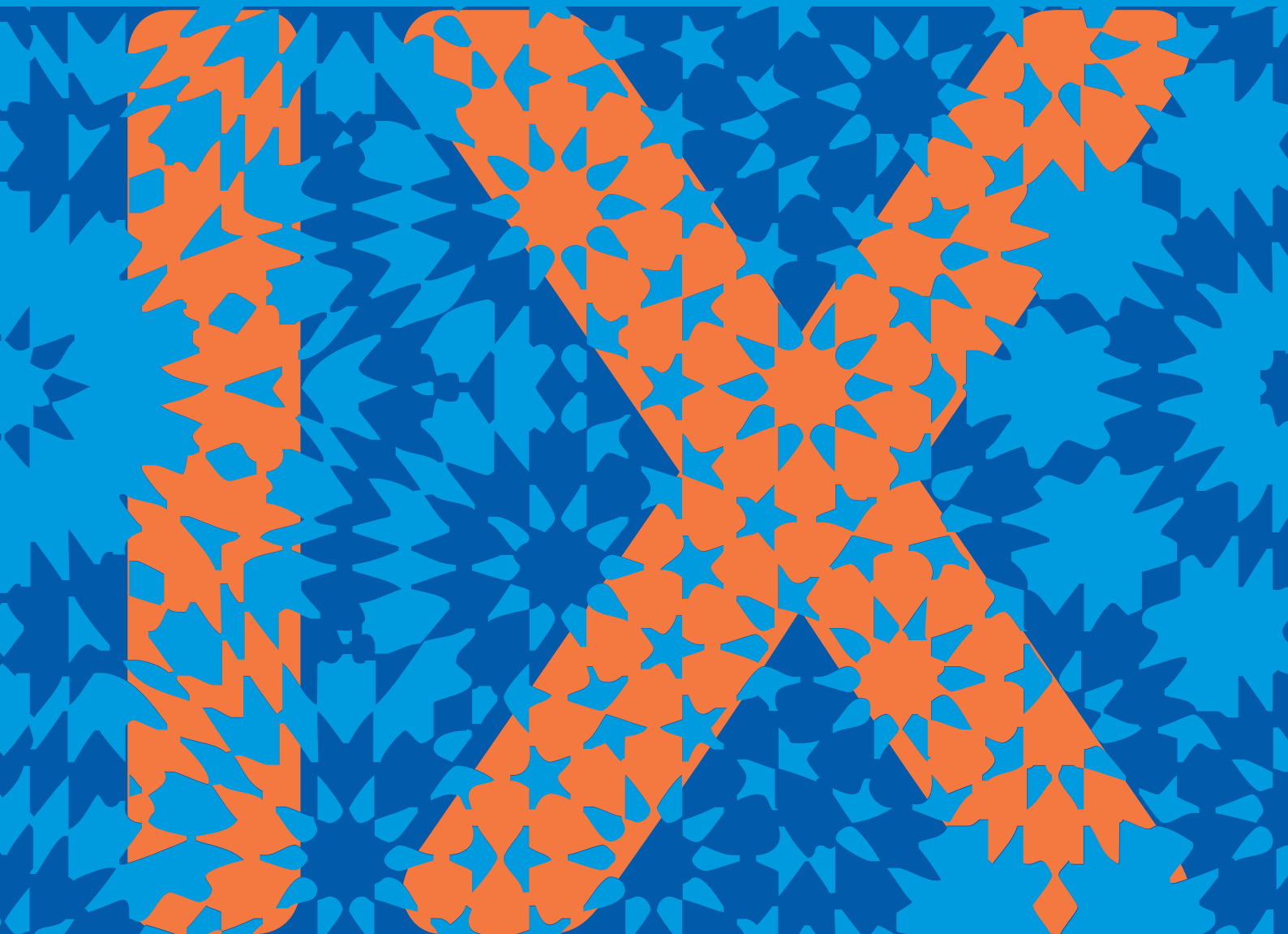
Innovative Financing
for Africa's
Transformation

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Marrakech, Morocco
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Climate financing: Implications for Africa's transformation

Issues paper





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I. Background

1. To date, all global assessments have concurred that Africa is the Earth's most vulnerable region to climate change. The Third Assessment Report of the Intergovernmental Panel on Climate Change (IPCC), which was published in 2001, was the first to introduce a so-called regional lens to the IPCC assessments. This triggered discussions during the global negotiations under the United Nations Framework Convention on Climate Change on how to contextualize the impacts and challenges posed by climate change. As a result, there was a unanimous agreement to provide support to those least developed countries considered to be highly vulnerable to climate change but lacking the capacity and resources to respond.

2. The severity of Africa's vulnerability to climate change was confirmed by the IPCC Fifth Assessment Report. Moreover, the International Research Institute for Climate and Society is warning of an El Niño that could result in above-average rainfall in the Horn of Africa.

3. In spite of all these challenges, Africa's determination to rise has never been stronger. Over the past decade, the continent has made remarkable economic and social development progress; indeed, seven out of the ten fastest-growing countries in the world are in Africa [1]. Unfortunately, the risk posed by climate change threatens to overturn the gains made so far and impede Africa's transformation.

II. Sources of climate finance

4. There are different types of climate finance flows, from both domestic and international sources (see figure 1). This paper will focus on international climate finance flows and their role in safeguarding Africa's transformation.

A. International and multilateral sources of finance

5. Dedicated global funds for climate intervention under the United Nations Framework Convention on Climate Change, such funds target both mitigation and adaptation. Examples include:

1. **Global Environment Facility, Least Developed Countries Fund and Special Climate Change Fund**

6. The Least Developed Countries Fund (LDCF) and the Special Climate Change Fund (SCCF), which are operated by the Global Environment Facility, were established by the seventh session of the Conference of the Parties, in 2001, with a view to providing financial support to least developed countries to help them to tackle the effects of climate change. Out of the 49 least developed countries in the world, 35 (about 70 per cent) are in Africa.

2. **Adaptation Fund**

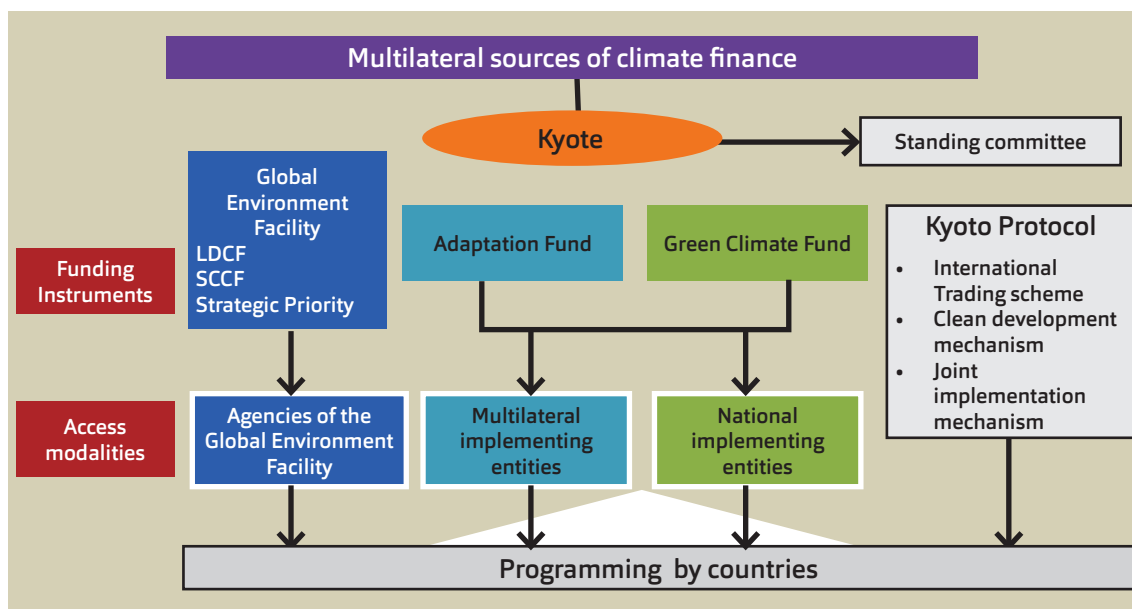
7. The Adaptation Fund was established in 2007 under the Kyoto Protocol by the parties to the United Nations Framework Convention on Climate Change. It is largely financed through a 2 per cent levy on revenue from the sale of certified emission reduction (CER) credits, and op-

erates on a project-based approach, with project proposals being submitted by implementing entities to a central board.

3. Green Climate Fund

8. The Green Climate Fund was established in 2010, at the sixteenth session of the Conference of the Parties. It is expected to provide a significant proportion of the medium-term financing goal of \$100 billion a year by 2020, a target set by developed countries in 2009. The Fund promotes the principles of national ownership; however, there is still considerable ongoing debate about what modalities will apply. Recipient countries (that is developing and middle-income countries) argue for strong national ownership, with fund management and project selection being delegated to government bodies, and with the Fund providing only coordination and supervision of fiduciary propriety. Funding countries (mainly developed countries) want a more cautious approach, at least initially, with a greater reliance on mechanisms similar to those used by the Adaptation Fund.

Figure 1: Multilateral sources of climate finance



9. There are also other international multilateral climate finance instruments that are not directly under the United Nations Framework Convention on Climate Change process. Those linked to adaptation include the Pilot Program for Climate Resilience, the Global Facility for Disaster Reduction and Recovery, and the Millennium Development Goal acceleration fund; those linked to mitigation include the Clean Technology Fund, the Forest Investment Program, the Carbon Fund, the Carbon Partnership Facility, the Forest Carbon Partnership Facility and the REDD+ mechanism for reducing emissions from deforestation and forest degradation in developing countries.

B. Regional and bilateral sources of climate finance

10. There are also regional and bilateral climate finance instruments. Some of the regional funds include:

- Global Climate Change Alliance (European Union)
- African and Latin American Resilience to Climate Change (United States Agency for International Development)
- Congo Basin Forest Fund (United Kingdom of Great Britain and Northern Ireland)
- Collaborative Adaptation Research Initiative in Africa and Asia (Department for International Development (DFID) and the International Development Research Centre)
- BioCarbon Fund (United States of America, United Kingdom and Norway)

11. Some developed countries have also set up bilateral funds to support developing countries with their climate change responses. Some of that bilateral support could be channelled through development assistance to developing countries.

C. Private sector investment

12. The role of the private sector is becoming increasingly important, both in terms of how it tackles the consequences of climate change for business value chains and with regard to corporate social responsibility. As businesses see the need to climate-proof their investments, climate financing is perceived as cost effective and as increasing profit margins.

III. Access modalities

13. The various multilateral climate finance instruments all have different modalities for accessing the funds (see figure 1). While direct access by countries is encouraged, intermediaries known as implementing entities also provide assistance, in particular in cases where the least developed countries in question lack the necessary capacity to comply with the complex application procedures. Implementing entities can be national, multinational or regional bodies. The website of the Adaptation Fund lists 28 accredited implementing entities, of which 15 are national, 10 are multinational (including major development banks and four United Nations agencies) and 3 are regional. The national institutions include ministries (Jordan and Rwanda), agencies or authorities (Chile, Kenya, Morocco and Uruguay), institutes (Argentina, Mexico, Senegal and South Africa), funds (Benin, Costa Rica), one bank (India) and one trust (Belize).

14. Although a number of the accredited national implementing entities are African, only two – Rwanda and Senegal – have successfully applied for programme funding from the Adaptation Fund. This emphasizes the fact that institutional and human capacity needs to be developed so that countries can achieve self-programming status.

15. The promotion of national implementing entities should be applauded as it helps to establish national ownership of the process. However, the Adaptation Fund's decision to cap the proportion of funding distributed by multilateral implementing entities at 50 per cent could pose major programming constraints for countries that are not yet ready for accreditation as national implementing entities, but which still need access to the Fund.

16. Other multilateral, regional and bilateral funding instruments have different access modalities, which are usually aligned to their internal regulations and tailored to their programme interests. There are also funding windows through competitive calls for proposals, which allows other potential stakeholders to get involved and creates a space for nurturing innovative ideas.

17. There is a great deal of uncertainty surrounding bilateral funding as result of the changing development assistance landscape. Following the economic downturn, many developed countries cut their foreign aid budgets, casting uncertainty over the future of bilateral aid.

18. Meanwhile, private sector funding is emerging as an important pool of climate finance. However, the lack of appropriate engagement approaches and public-private partnerships limit Africa's abilities to capitalize on the rapidly growing opportunities for private-sector funding for climate change.

IV. Financing Africa's climate response

19. Although many climate finance instruments have been set up, Africa's access to those funds remains limited. Moreover, it also faces the challenge of how to absorb effectively the funding it does receive.

20. There are various estimates of how much annual investment will be needed to reduce the risk profile of developing countries. Estimates of current climate finance flows to developing countries vary considerably, at anywhere between \$40 and \$120 billion per year [2]. The African Development Bank has concluded that adaptation costs in Africa will be in the region of \$20-\$30 billion over the next 10 to 20 years [3]. While such estimates provide indicative costs, the changing risk profiles as revealed by recent assessments could significantly increase the amount of financial resources required for adaptation responses. Indeed, the United Nations Environment Programme's 2013 report *Africa's Adaptation Gap* highlighted the gulf between the current climate risk profile of Africa and the level of funding expected [4].

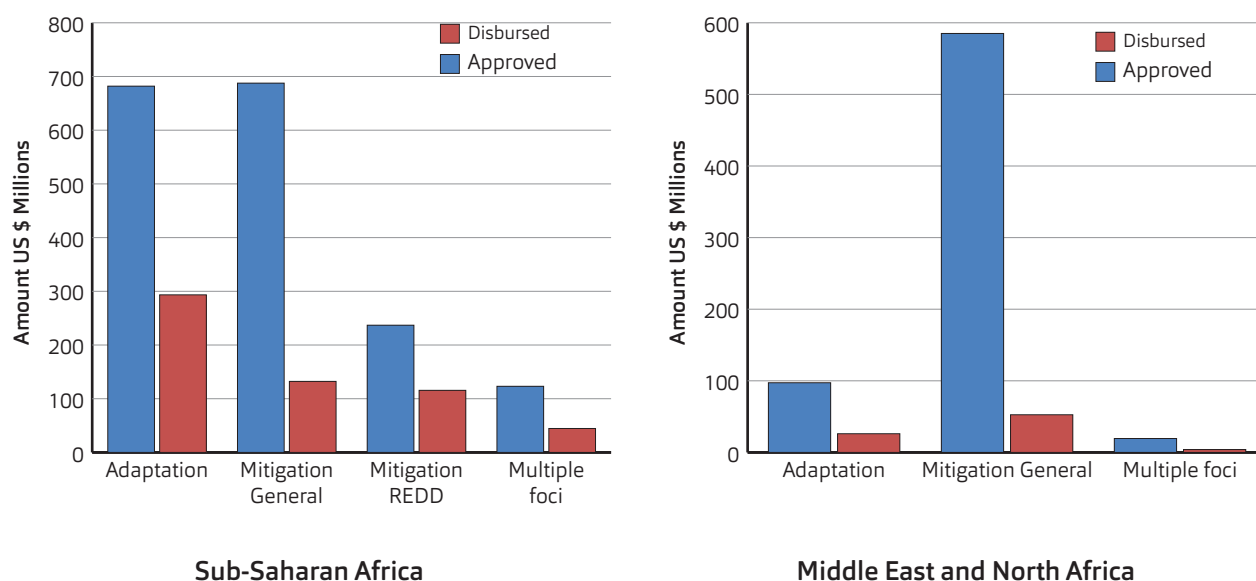
21. In terms of actual investment, of all the funding disbursed so far from all sources (including the Least Developed Countries Fund, the Pilot Program for Climate Resilience, the Global Climate Change Alliance and the Special Climate Change Fund), which amounts to \$395 million, 44 per cent has gone to sub-Saharan Africa. More specifically, of the funds allocated for the implementation of national adaptation programmes of action, 56 per cent of approved funding from the Least Developed Countries Fund (\$222 million) and 26 per cent of funding from the Special Climate Change Fund (\$50 million) have also gone to sub-Saharan Africa [5].

V. Financing adaptation and mitigation in Africa

22. Africa's climate change challenges are enormous. This requires both domestic and international sources of financing. One key concern in Africa is the allocation of funds between adaptation and mitigation actions. While in developed countries, the majority of climate finance is spent on mitigation, in most developing countries adaptation is much more important than mitigation. However, this is likely to change as some developing countries become middle-income countries and mitigation becomes an increasingly important priority for them. This is even more likely with growing private sector interest and an increasing share of mitigation funding, as nations develop their institutions and the enabling environment with regulations and incentives that encourage private sector investments.

23. In the case of Africa, the role of the private sector in climate finance is still very minimal and uncertain, especially as no good lessons or practical experiences have been drawn from the clean development mechanism, as a result of the very low participation rates. Furthermore, the

Figure 2: Approved and disbursed funding for sub-Saharan Africa, the Middle East and North Africa, as of 2013



Source: Climate Funds Update, November 2013 [6], [7].

price of carbon credits has been very volatile and currently stands at just \$1-\$2 per ton of carbon dioxide for clean development mechanism projects (down from about \$20 in 1997 and \$5-\$8 in 2011) and \$4-\$8 per ton for REDD projects.

24. With regard to REDD+, an enhanced version of the original mechanism, there has been more interest from African countries in participating. Readiness programmes are already underway in some countries, benefiting from various climate funds and targeting key forest areas such as the Congo rainforest and basin.

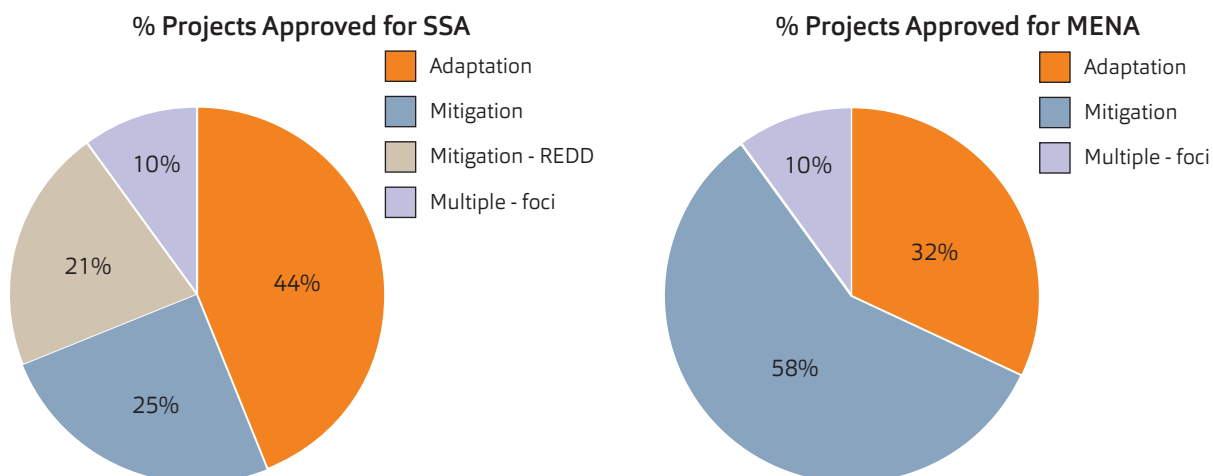
25. According to 2013 findings of the World Bank, less than one third of adaptation and mitigation funding approved for spending in Africa has been disbursed (see figure 2). Climate Funds Update, an independent website that provides information on international climate finance initiatives, states that a significant percentage of climate finance in sub-Saharan Africa is directed towards mitigation activities, despite the fact that adaptation should be given funding priority because of the high vulnerability of many sub-Saharan countries (see figure 3). There is a pressing need, therefore, to mobilize resources with a view to addressing the continent's limited ability to deal with climate events and future impacts related to climate change.

Table 1: Number of projects approved for sub-Saharan Africa, the Middle East and North Africa, as of 2013

Theme	No. of projects approved for sub-Saharan Africa	No. of projects approved for the Middle East and North Africa
Adaptation	165	19
Mitigation	96	35
Mitigation (REDD+)	81	N/A
Multiple focuses	39	6

Source: Climate Funds Update, November 2013 [6], [7].

Figure 3: Percentage of projects approved for sub-Saharan Africa, the Middle East and North Africa, as of 2013



Source: Climate Funds Update, November 2013 [6], [7].

26. With more than 45 per cent of Africa's population living in countries with the lowest adaptive capacity in the world, investment in health and education systems and in institutional capacity-building is essential. It cannot be stressed enough that funding for climate change adaptation and mitigation efforts has a multiplier effect and can simultaneously help to reduce poverty and boost sustainable development.

27. More targeted adaptation investments are needed in Africa, and decision-makers need to factor climate change into all long-term strategic planning. In particular, Africa has a large infrastructure deficit, but the design and location of future infrastructure investments need to take into consideration changes in the climate system. According to the World Bank, achieving this will be particularly costly in relation to water and sanitation measures, and new zoning rules and building codes will have to be introduced to complement such structural adaptation and mitigation measures. In the long run, however, the benefits will outweigh the additional costs.

28. The development of an African climate change fund, managed by an African institution, has also been touted as a way to meet Africa's specific needs. Climate finance can be a catalyst to leverage private and public resources, open up new economic opportunities, promote technology deployment and transform development pathways. With the purpose of pooling resources allocated to Africa from various sources and mobilizing new sources of funding, such a fund could support the financing of projects and programmes that contribute to climate resilience and low carbon development.

VI. Transparency of climate funds

29. Under the Copenhagen Accord, world leaders agreed that "scaled up, new and additional, predictable and adequate funding as well as improved access shall be provided to developing countries" [8]. However, because of the ambiguity of the words "new and additional", there is a need for a common benchmark so that countries can determine which funds are old and which are new. "Additional" funding and financial resources raised for climate change should not be substituted or diverted for other uses, such as economic or social development. The lack of an internationally agreed baseline has left each contributing country to use its own definition of

“new and additional”, and in some cases they do not accept the baselines put forward by developing countries.

30. Transparency of information is also needed in order to determine what is meant by “additional”, as at present some countries are re-packaging existing official development assistance or delivering on past pledges. For example, the majority of Japan’s pledge of \$11 billion under the Hatoyama initiative was announced in 2008, well before the talks in Copenhagen [9]. Similarly, the United Kingdom’s pledge of \$2.5 billion as part of the European Union’s package of \$10 billion for short-term climate finance will be drawn entirely from its already announced development aid budget. Indeed, Tim Jones, a policy officer at the World Development Movement, said that “over half of the money announced by the United Kingdom in Copenhagen had already been announced, allocated or spent. At least one third of it will be in the form of loans” [10]. Moreover, according to the Organisation for Economic Co-operation and Development (OECD), as of 2013, only 5 out of 23 donor Governments had met the target of spending 0.7 per cent of gross national income (GNI) on official development assistance.

31. Table 2 sets out some of the proposed methods for defining a baseline for “new and additional” funding. The first option is preferred by European countries such as Denmark and Norway since they have already hit the target of 0.7 per cent, making it easier for them to set a baseline of anything over 0.7 per cent. The second option would only utilize new United Nations channels such as the Green Climate Fund to disburse the funds, but would leave less flexibility for contributing countries and existing channels, which might be better suited to handling certain tasks.

Table 2: Baseline suggestions for defining “new and additional” funding

	Option	Advantage	Disadvantage
A	Aid over and above the threshold of 0.7% of GNI	<ul style="list-style-type: none"> • Easy to track as simply need to measure increase on past official development assistance (ODA) pledges • ODA tracking system already put in place by OECD 	<ul style="list-style-type: none"> • Raises questions about what gets counted as climate finance • Many countries have had difficulty reaching the initial target of 0.7% (such as the United States, with 0.2%) • No pressure on countries that have already met the target (Denmark, Luxembourg, the Netherlands, Norway and Sweden)
B	New United Nations channels only	<ul style="list-style-type: none"> • Clear, “clean slate” start • Easy to track and implement guidelines 	<ul style="list-style-type: none"> • Diversion of ODA funds still possible • Contributors may provide only token contributions • Less flexibility for contributors
C	New sources of funding only	<ul style="list-style-type: none"> • Easy to track new funds • Additionality likely 	<ul style="list-style-type: none"> • Contributors may reduce funding • Potential long wait for receiving countries • Existing channels may be better suited to certain tasks
D	Separation between ODA and climate finance	<ul style="list-style-type: none"> • No double counting, re-labelling or diversion of ODA funds as climate finance • Emphasis on separation of funds at source • Enhanced transparency 	<ul style="list-style-type: none"> • Most contributors are not likely to agree • Politically challenging to agree on what a new financial mechanism would look like • Old ODA funding sources may still be used • May create concerns regarding diversion of ODA funds away from development goals
E	Raising ODA, with increased priority for climate finance	<ul style="list-style-type: none"> • Predictability of funds • May clarify whether projects are climate related 	<ul style="list-style-type: none"> • Difficult to know what percentage is the right level • Diversion of ODA funds still possible • Definition of baseline will be contested by both sides

	Option	Advantage	Disadvantage
F	No action/no baseline	<ul style="list-style-type: none"> Acceptable by most contributors since they can define their own baseline 	<ul style="list-style-type: none"> Each contributor defines own baseline, resulting in loss of meaning for recipient countries No comparability of commitments and disbursements Big contributors may not get proper recognition Unacceptable by almost all developing countries

Sources: [11], [12] and [13].

32. This lack of transparency and the prevailing uncertainties regarding climate finance flows have created insecurity in responding to climate change in Africa. The ClimDev-Africa Special Fund was established to provide a solid foundation for the African response to climate change. It was launched by the three foremost development institutions on the continent – the African Union Commission, the Economic Commission for Africa and the African Development Bank – under the auspices of the ClimDev-Africa programme. It is managed by the Bank and provides financial resources and incentives for national agencies, regional bodies and other stakeholders to design and implement climate information services and policy projects. As of October 2013, the Fund had received 26 project proposals requesting some \$76 million.

VII. Innovative financing mechanisms to scale up climate change actions in Africa

33. Following the current impasse regarding the fulfillment of the climate finance pledges made by developed countries, it is important for Africa to develop more creative and innovative ways of generating funds from both domestic and external sources, at a scale and pace sufficient to match the impacts of climate change. There are innovative lessons of financing mechanisms that could be used to ramp up climate change activities and investment in Africa, although this requires strategic planning and enhanced climate finance readiness. Climate change is of national interest to all African countries, and as result, domestic sources of financing should also be in the mix of mechanisms driving climate finance.

A. National budgetary processes

34. Following the elaboration of Climate Public Expenditure and Institutional Reviews by some African countries, it is possible to view national spending on climate-related activities. Building on this, it is important for countries to fully integrate climate change into their national budgetary processes, whereby a portion of the budget is directly allocated to climate change actions. Having budgetary provisions for climate change is crucial for scaling up actions and ensuring their sustainability, and results in better returns on investment. This approach also ensures that climate investment is aligned with national development priorities and strategic goals.

B. Budgetary support

35. Development assistance (regional and bilateral) received by many African countries includes top-ups and budgetary support for both investment and recurrent expenditures. Such financial assistance constitutes a large percentage of national budgets for some countries.

Integrating climate change considerations into discussions with development partners to climate-proof the development assistance support they provide will constitute a compelling case in seeking climate funding support for aid investments to build resilience. This is particularly crucial with investments in infrastructure, agriculture and water systems. Addressing climate change in such sectors, where development assistance is growing rapidly, could be beneficial to countries. By using these approaches, it will be possible to increase climate-dedicated funds for key sectors as well as top-up funds for climate actions.

C. International sources

36. Some of the decisions emanating from sessions of the Conference of the Parties have the potential to encourage the development of innovative sources of financing for addressing climate change, and Africa should review and capitalize on some of these, such as nationally appropriate mitigation actions and non-market-based mechanisms. Africa must also seek ways of increasing its share of clean development mechanism activities and entering the carbon-trading marketplace.

D. Private sector

37. The private sector is already an important source of climate finance through capital markets. At present the focus is on mitigation but there are also emerging opportunities with regard to adaptation, such as debt and equity through direct project lending, and credit lines to local finance institutions. Microfinance and microinsurance products aimed at poor communities are already being piloted in various African countries.

E. Grants and concessionary loans

38. Many multilateral banks are beginning to provide concessionary loans as part of grant packages for climate-resilient investments, such as climate investment funds. While it could be argued that African developing countries should not be addressing climate change using loans, this is nevertheless an important funding stream that needs to be reviewed and explored.

F. Adopting synergistic approaches in targeting multilateral funds

39. The disproportionate allocation of climate finance in favour of mitigation efforts, as opposed to adaptation measures, is unlikely to change since they have different drivers. Africa therefore needs to institutionalize a synergistic approach in mobilizing climate finance for joint implementation of adaptation and mitigation initiatives, especially for REDD+. For example, safeguard mechanisms currently under discussion as an integral part of REDD+ should include adaptation measures.

G. Adaptation levy and bond systems

40. The extractive industries, which drive economic growth in Africa, offer opportunities for innovative climate financing through corporate social responsibility schemes. Like the Caribbean region, Africa should consider establishing a similar bond system to shield its economic growth

from climate change disasters. It should also consider instituting adaptation levies on the huge volume of extractive resources that leave the continent for markets overseas – not in the form of royalties, but as part of a collective responsibility to address climate change in the continent.

41. The European Union's airline carbon tax – might not be appealing to developing countries, but it is considered vital for addressing climate change in Europe. The United States has also put in place a pollution tax, and many other regions are also going in that direction. If Africa were to push for an adaptation levy on its natural resources (for example for every tree felled for timber in the Congo basin or for every barrel of crude oil exported), it would easily gain international support in the light of the global recognition of the continent's extreme vulnerability and its need for adequate resources to respond to the challenge.

H. Capitalizing on the African diaspora and philanthropists

42. Awareness of climate change should be raised among African philanthropists and the diaspora. This is critical for bridging external funding and building sustainability. The current lack of capacity and appropriately trained human resources in certain African countries could be easily overcome by establishing viable and functional connections with the African diaspora, the importance of which has already been demonstrated by the volume of remittances, which constitute a significant share of foreign exchange earnings for African countries.

VIII. Conclusion

43. There is a great deal of uncertainty about the level of international funding that is dedicated to climate change. It is unlikely that the targets established internationally will be met, including those of the Green Climate Fund.

44. Climate finance is an essential part of securing a low-carbon development future for Africa and Small Island Developing States and helping them to acquire the technologies and capacity needed to implement adaptation and mitigation actions. The climate financing needs of developing countries substantially exceed current financial flows from multilateral and bilateral sources. Increasing the amount of funding, especially through innovative financing mechanisms, is therefore imperative. Long-term climate finance needs to be accountable and transparent. African policymakers will need to examine carefully the proposals that emerge from negotiation processes and take into account the implications of each approach and how Africa stands to benefit.

45. Developed countries must also fully implement their commitments relating to financial resources and the transfer of technology. This will provide African countries with the necessary tools to address climate change.

46. In addition, greater efforts must be made to ensure the readiness of climate finance in order to enhance regional alertness and capabilities for programming these resources. More African countries should strive to become national implementing entities as a key step towards national ownership of their climate change responses.

47. Lastly, in the light of the growing role of the private sector in addressing climate change, there are considerable opportunities for attracting additional private-sector support, and it is essential that Africa strives to build creative, mutually beneficial partnerships with the private sector.

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