T20 Policy Brief

Task Force 06

STRENGTHENING MULTILATERALISM AND GLOBAL GOVERNANCE

Improving Access to Climate Finance Funds for National and Subnational Development Banks

Lavinia Barros de Castro, Visiting Professor, CBAE, Brazil

Rogerio Studart, Senior Fellow, CEBRI (Brazilian Center for International Relations), Brazil

TF06

TF06

Abstract[1]

There is a global consensus on the urgent need to increase green investments in developing countries. However, the main international funding channels—such as the Green Climate Fund (GCF), Climate Investment Funds (CIFs), and Adaptation Fund (AF)—face challenges due to their complex, slow processes and limited scalability, which impede quick climate action. This article proposes that improving the collaboration and coordination between green vertical funds and national and subnational Public Development Banks (PDBs) can address these issues, potentially mobilizing greater resources for developing nations. To achieve this, developing countries, governments, international funds and PDBs should make a joint effort to improve green investment business climate, streamline and coordinate their requirements, and to expedite their procedures, and develop new instruments.

Keywords: Climate Finance; DFIs; GCF; PDBs Sustainable Development.

[1] The authors thank Vivian Machado, Cristina Blaso e Gabriel Gomes for their comments. The content of this paper is solely the responsibility of the authors.

TF06

Problem Diagnosis

In 2009, at the 15th Conference of Parties (Cop15), countries agreed to mobilize USD 100 billion per year by 2020 for climate action. In 2022, developed countries provided and mobilized a total of USD 115.9 billion in climate finance for developing countries, exceeding the annual USD 100 billion goal for the first time. Achieving US$ 100 billion goal is good news. However, 100 billion U.S. dollars represents only a fraction of the total climate finance required to face the climate emergency - which has been estimated at 1.3 trillion U.S. dollars annually (Songe et al, 2022). It is imperative to mobilize resources beyond the existing ones, and the focus should be on the nations that have the least capacity to do so: developing countries. This will require thinking outside the boxes, such as enhancing national and subnational Public Development Banks' (PDBs thereafter) capacity to deliver climate finance with the support of funds such as the GFC. Below we discuss why and how.

Why an Improved Relationship Between PDBs and GCF Matters

Using PDBs to canalize green finance and help mobilize additional resources requires some innovative solutions to both overcome their potential constraints. It is not so much the case of creating new PDBs institutions, as there are already plenty of robust ones (see **Appendix 1**), but to use the existing ones, enhancing and enlarging existing policy instruments, and improving process, practices, and capabilities. That change can perhaps come from working in a different way with vertical international green funds, such as the Green Climate Fund (GCF).

Although 64% of approvals come from projects with the Public Sector, the number of projects having National Development Banks as accredited entities seems low.[2] The GCF itself recognizes that access to its resources has been challenging for national and regional institutions (direct access accredited entities – DAEs), "leaving countries with a heavy dependence on international access entities that do not necessarily share compatible country programming agendas and have to respond to their own mandate" (GCF, 2024b)

The challenges in accessing Green Climate Fund (GCF) financing are not solely the responsibility of the GCF itself. National implementing agencies also encounter significant obstacles. An internal assessment from the International Development Finance Club (IDFC) on Direct Access Entities (DAE) members of the GCF highlighted these challenges: "[p]reliminary internal IDFC climate finance assessment on DAE-GCF members have shown that constraints such as limited internal technical capacity (tools and methodologies for reliable climate impact assessment) and/or the lack of harmonization of Environmental and Social Safeguards (ESS) and/or gender policies have negatively impacted on DAE overall institutional capacity to structure and develop high-quality concept notes and funding proposals to the GCF, resulting in a negative lag with regards to their access to GCF's financing." (GCF, 2024b).

There has been a notable increase in project approvals by GCF in recent years, depicted in Figure 1 of **Appendix 2**. Efforts to streamline the approval process, as shown in Figure 2 of the same Appendix 2, are also evident. The median time from project approval to first disbursement reduced by 16%, comparing 2015-2016 period with 2021-2022. The

---

[2] For example, Brazil has only four national projects approved by GCF - none of them has a Brazilian Development Financial Institution (DFI) as an accredited entity. GCF only accredited three Brazilian financial institutions.

improvements made might be explained: a) by the efforts to reduce the Readiness and Preparatory Support Programme approval time, b) by the initiatives created under the Project Preparation Facility (PPF)[3], and 3) by the introduction of the Simplified Approval Process (SAP), which is, however, restricted for projects where GCF contribution is up to US$ 10 million – **Appendix 3**.

Given the urgency of the climate crisis and the limited resources available to GCF's developing nation clients, accelerating disbursements while ensuring meaningful impact is paramount.

How to Make Climate Finance Speedier: The Case of the GCF

The approval process for funding with the Green Climate Fund (GCF) is notably slow and complex.[4] Initially, to be considered an eligible institution, one must undergo an approval process to be listed as an Accredited Institution and fill out an application form clarifying the requested modalities and instruments. Completing this form usually

---

[3] The GCF's Project Preparation Facility (PPF) provides financial support to Accredited Entities (AE) in preparing funding proposals for submission to the Green Climate Fund (GCF).

[4] From the beginning of the process until approval there are 7 stages to be undertaken: STAGE 1. Country and entity work programs, STAGE 2. Targeted project generation, STAGE 3. Concept note submission, STAGE 4. Funding proposal development, STAGE 5. Funding proposal review, STAGE 6. Board approval, STAGE 7. Legal arrangements. Described in GCF (2024c).

requires the involvement of a consultant due to its complexity. The GCF provides consultants at no cost for this role.

Among the initial requirements is the submission of the Concept Note, presenting a Theory of Change (TOC) for a particular project/programa. The TOC framework should be according to the GCF's specific demanding models and concepts. This is particularly challenging to complete and involves considering various elements: problem statement, barriers/risks, project activities, outputs, outcomes, goal statement, long-term impacts, and assumptions. These concepts are not perfectly defined nor homogenous among donors and funds. They can require significant discussion with project proponents, who often are not familiar with the nuances of these concepts. Additionally, the GCF requires that all elements of the TOC demonstrate their multiple interactions with each other.

The creation of the Concept Note for project submission to the GCF involves some elements that are traditional requirements for the approval of any climate project, but not necessarily easy to address: description of the context and baseline (including estimations on market demand and description of the institutional environment), GHG estimates and targets (often requiring the applicant to have or develop estimation models with consultants), Project/Program description, Expected Project Results "aligned with the GCF investment criteria," and indicative financing/cost information. It is also necessary to indicate the dashboard with the co-financiers (as the GCF usually does not finance projects alone).

Beyond these demands, GCF has specific requirements such as: a) describing the Engagement among the NDA, AE, and/or other relevant stakeholders in the country, b) Justification of GCF funding request, c) Sustainability, and replicability of the project (exit strategy). As the process evolves (if the Concept Note is accepted), the institution will have to fulfill the GCF Funding Proposal, which is even more challenging. In that

stage the institution has to fill out about 20 Annexes, including some that are challenging to execute. These include: E&S document (which includes in turn Environmental and Social Impact Assessment, Environmental and Social Management Plan, Environmental and Social Management Systems); Gender Assessment and Project/program-level action plan; Legal due diligence (regulation, taxation, and insurance); Co-financing commitment letter; Appraisal, due diligence, or evaluation report for proposals based on up-scaling or replicating a pilot project; Procedures for controlling procurement by third parties or executing entities undertaking project finance by the entity, among others.

Funding proposal review is a process that alone takes about 190 days, according to GCF. Practice shows, however, that term happens only if the financing proposal is complete and meets the standard the GCF expects. In other words, the process is expected to be much longer. The well-known intensive policy due diligence during PDBs accreditation process by GCF seems to have little effect in reducing hurdles during the financial application process.

After all these steps, the final approval process also requires consideration by the Board of the Green Climate Fund, which generally holds three meetings per year. These meetings are typically attended by more than 300 participants, including observers from civil society and private sector organizations, National Designated Authorities (NDAs), which are the national conduits to the Fund, and Accredited Entities and other partners who assist in delivering climate finance to developing countries.

The analysis presented above reveals substantial opportunities for enhancing the governance and processes that govern the relationship between the GFC and national PDBs. Such improvements could lead to a more agile and impactful approach. In the following section, we offer several recommendations aimed at achieving these improvements.

Recommendations

I. **Developing nations governments should Improve national Taxation Regimes, Regulations and accountability practices to facilitate green finance flowing in the country.** For instance:

- **Create Special Taxation Regimes in Developing Countries for Climate Financing:** There should be special taxation regimes in developing countries for climate financing and for grants.
- **Special Regulatory Regimes:** Often, PDBs operate through accredited financial agents (second tier). In a new fund, the banks receiving the resources from the PDBs will have to allocate capital for the loans or guarantees received. It is important that there is a consensus among regulators so that resources received in climate guarantees from wellestablished international sources do not carry an excessive capital cost.
- **Develop Accounting Alternatives to Minimize Costs and Improve Accountability:** PDBs should discuss with their controlling bodies and other responsible entities the best accounting alternative for receiving climate resources from international multilateral sources. It is vital to develop financing schemes that make the financial product viable. For example, allowing the receipt of climate resources into separate funds off the balance sheet to be managed by PDBs, receiving modest remuneration to cover administrative costs. It is desirable that these issues are resolved and regulated before applying for resources from the funds and that standard forms are created to expedite the process of receiving resources. It should also be avoided, for example, that the financial return from resources donated by a climate fund be incorporated into the capital of the PDBs, but instead be reinvested in new projects.

II. Both GCF and PDBs should continue efforts to simplify processes

- The goal here is to reduce ***ex ante* demands from multilateral climate funds** or DFIs that do not match the reality of firms in developing countries. This is particularly crucial for projects aimed at MPE or for less developed regions of emerging countries. The demands (e.g., safeguards) before project approval should be replaced with accessory technical assistance or, gradually increasing requirements over time, allowing institutions to provide training and give firms time to adapt to. This could significantly reduce the number of projects that begin applications with multilateral financing mechanisms and fail to get approved.
- **PDBs should also improve their processes**, by creating simplified practical manuals for climate finance, promoting training on climate risk assessment across all operational units (not limited to the risk management division), and also by developing ready-made climate financial products.

III. GFC and PDBs should work together to:

- **Harmonize Requirements Among Climate Finance Mechanisms:** There is a need to simplify the access to funds by harmonizing safeguard policies across multilateral climate finance mechanisms, such as the GCF, Climate Investment Funds (CIFs), Adaptation Fund (AF), and others, to discover synergies and enhance the compatibility of funding streams.
- **Increase Systemic Coherence**: It's essential to develop integrated approaches that align the entire development finance system with climate and sustainability objectives, which would encourage financial innovation and the adoption of sustainable practices. Implementing these recommendations can transform DFIs into effective catalysts for climate financing, helping to overcome existing barriers. This transformation has the

potential to significantly increase the resources available for climate action and to promote fairness in the distribution of funds, ensuring that the countries and regions most in need have equitable access to the necessary financing to tackle the climate crisis (See GCF, 2020).

- **Urgently develop risk management instruments:** A well-known and significant barrier to green business is the limited ability of firms to provide guarantees in the forms and amounts demanded by the private market. Although guarantee products/funds are a common tool offered by climate funds, often there are difficulties for the recipients of the resources to manage the currency risk involved in the financial instrument. This is because the resources for guarantees are offered in foreign currency by the climate funds without the final borrowing firms having sources of revenue in foreign currency. Also PDBs in developing countries should receive international advice to create long-term exchange rate hedge mechanisms to manage exchange rate risk, especially (but not exclusively) for loan instruments. Alternatively, multilateral climate funds could provide the longterm hedge.

- **Improve joint Monitoring and Evaluation:** One of the major obstacles to accessing international green resources is the PDBs' low capacity for accountability in the manner required by international green funds. Multilateral climate finance mechanisms should offer international training on monitoring and evaluation practices and routines for PDBs, utilizing international experience (and not only request the service that will probably depend on an external consultant).

- **Create Auditing Capabilities in Developing Countries:** Developing countries have few auditors for the assessment of climate projects. Multilateral climate finance mechanisms should assist in creating auditing capabilities in these countries, potentially through the establishment of certified training courses promoted by climate funds.

IV. GCF could improve its Governance:

- **GCF's governance is very participative, but also very complex**. The open and participatory Board could be more engaged in appreciating strategy and policies instead of approving project by project.

- **Create joint committee to Evaluate Countries "Strategic Projects":** An Executive Board could approve more significant and strategic projects, following the Board's guidelines. For projects recommended as strategic by countries, whether due to their potential impact on emission reduction, or because of their capacity to serve as a "model project," their financial requirements could be reduced, case by case. This includes, for example, a reduction on the collaterals, acceptance of the exchange rate risk by the donor (using grant resources for that goal), or reducing other financial requests that the borrowers have financial difficulties to attend. Rules for flexibility and a Committee to judge exceptions should be created to ensure good governance and accountability, as well as an incentive to strategic projects

Scenarios of Outcomes

We believe that implementing the proposed recommendations could help transform the landscape of climate finance, particularly in developing countries. Below we present some examples.

By minimizing the capital cost associated with climate guarantees and offering attractive tax incentives, we can encourage more investments in green projects. Additionally, harmonized regulatory frameworks could ease the operational challenges for PDBs and their financial agents, enhancing their ability to extend climate finance to remote and underserved areas.

By simplifying the processes for accessing climate finance, and reducing ***ex ante*** demands and increasing requirements gradually, PDBs and the GCF could lower the barriers for these enterprises to undertake sustainable projects. Harmonizing requirements among different climate finance mechanisms can streamline the application process, reducing bureaucratic hurdles and making it easier for projects. This could lead to a more efficient allocation of resources, ensuring that funds reach projects with the highest potential for impact.

Developing risk management instruments to address currency and other financial risks is crucial for the viability of green investments. Providing long-term hedge mechanisms and international advice on managing exchange rate risks can make climate financing more accessible and sustainable. This would encourage more green investors to embark on projects that they might have previously deemed too risky, leading to a diversification of the green economy.

Creating a joint committee to evaluate "strategic projects" and offering financial flexibility can fast-track projects with significant potential for emission reduction or

model projects that could set precedents for future initiatives. This flexibility, including the reduction of collateral requirements and accepting exchange rate risks, can make critical projects feasible.

By allowing PDBs to manage climate resources in separate funds off the balance sheet, the administrative burden is reduced, and funds can be more readily reinvested in new projects. This could lead to a sustainable cycle of financing and refinancing that propels continuous investment in climate action.

Finally, improving joint monitoring, evaluation, and auditing capabilities is essential for accountability and effective use of climate funds. Along with establishing auditing capabilities in developing countries, implementing this recommendation can enhance transparency and trust between funders and recipients, increasing willingness among international donors.

The ultimate consequence could be a significant step forward in the global fight against climate change, promoting sustainable development and resilience in the world's most vulnerable regions.

References

Green Climate Fund. n.d. “About.” Accessed March 31, 2024.

Lee, Nancy, Clemence Landers, and Samuel Matthews. 2023. "Concessional Climate Finance: Is the MDB Architecture Working?" CGD Policy Paper 287. Washington, DC. Center for Global Development. Accessed March 30, 2024.

Chandrasekhar, C.P. Year. "Public Development Banks and the SDGs: A Global Architecture for Global Good." Accessed March 20, 2024.

DFI DATABASE. 2024. Accessed March 20, 2024.

Finance in Common. 2020. “Joint Declaration of all Public Development Banks in the World.” Accessed March 20, 2024. Accessed March 30, 2024.

GCF. 2021. “Update of the simplified approval process”. Accessed May 30, 2024.

GCF. 2024a. Accessed March 30, 2024. Search at https://www.greenclimate.fund/projects, visited on March 31, 2024.

GCF. 2024b. Accessed March 30, 2024. Search at https://www.greenclimate.fund/sites/default/files/document/synergies-climatefinance.pdf.

GCF.2024c. Accessed March 30, 2024. Available in https://www.greenclimate.fund/project-cycle

Songwe, Vera, Nicholas Stern, Amar Bhattacharya, United Nations Economic Commission for Africa, and United Nations Economic Commission for Africa. 2022. Finance for Climate Action: Scaling Up Investment for Climate and Development. Addis Ababa: UN. ECA.

Let's
rethink
the world