Annex II: Annual Report 2014/15

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Foreword from the Co-Chairs of the Board

We are pleased to present this first issue of the Green Climate Fund (GCF) Annual Report. This report provides the Fund's stakeholders with an overview of GCF activities and achievements in the last year as well as the key tasks and challenges ahead. The past twelve months were a pivotal period for the Fund in terms of working towards making it fully operational.

Among the most significant achievements over this period are the nomination of more than 130 national designated authorities (NDAs) or focal points (FPs) to the GCF; the accreditation of 20 entities through which the resources of the GCF will be channelled; and an Initial Resource Mobilization of approximately USD 10.2 billion equivalent in pledges from 35 developed and developing countries, of which 60 per cent has been confirmed in formal agreements.

The GCF is an innovative institution committed to enhance country ownership and engage in working with a wide variety of partners including public and private, as well as international, regional and national entities. One of the key features of the Fund is its readiness programme, which aims to enable countries to engage with and directly access the Fund. Another priority is to mobilize larger resources and leverage additional investment from the private sector. This report also sets out the progress made by the Private Sector Facility, which constitutes another unique feature of the GCF.

Substantial progress has been made in these key areas. Readiness support has been committed for 17 countries to strengthen their NDAs or focal points and to develop their strategic frameworks. The GCF has also launched a pilot programme at USD 200 million for enhancing direct access to increase country ownership of the projects proposed to the Fund, and pilot programmes of up to USD 200 million to support micro-, small- and medium-sized enterprises (MSMEs), as well as to mobilize resources at scale (up to USD 500 million)

The Board has also taken a number of major policy decisions over the past year, for instance setting up the investment framework of the Fund and making substantial progress in setting the Fund's initial risk management framework. Moreover, the Board took very important decisions regarding the governance and internal structures of the Fund such as taking important steps towards the operationalization of the three accountability units of GCF and in establishing an independent Technical Advisory Panel to assess funding proposals. All these achievements and milestones have enabled the GCF to start operating this year.

The Board decided to start taking decisions on the approval of projects and programmes during its third meeting of 2015, and the first GCF-supported programmes and projects will unfold over the coming years, supporting developing countries in driving a paradigm shift to low-emission and climate-resilient development, and working to overcome the challenges of financing mitigation and adaptation activities. As the GCF works towards approving a larger number of projects and programmes to support developing countries, the demands to the Fund will outstrip the resources currently at its disposal. The Initial Resource Mobilization period lasts until 2018, and the Fund is open for new contributors to come forward and pledge funds.

The Fund also has many important tasks on the road ahead in order to consolidate its operational and institutional policies. The progress made over 2014–2015 is a very good start that needs to be enhanced and cemented over the years to come. We are confident that together with our implementing partners, civil society and the private sector, and political and financial support, the Green Climate Fund will play a major role in supporting low-emission and climate-resilient pathways in developing countries and be at the centre of international efforts on climate finance.

[Signed by Henrik Harboe and Gabriel Quijandria]

2014/15: A year in review

2014/15 in brief

2014/15 was a remarkable period for the Green Climate Fund (GCF), as it transitioned from a newly established institution to a financial institution with initial funding, a clear strategy, principles and policies in place, and a growing global network of implementing partners and developing countries. This period also marked the third anniversary of the beginning of the work of the Board of the GCF, which met for the first time in August 2012. Three years later, as a result of the decisions taken by the Board, the following achievements over the period can be reported:

- The Board has put in place a results management framework, an initial proposal approval process and an investment framework;
- The first country readiness grants are being prepared;
- The first 20 implementing entities have been accredited;
- Over 130 national designated authorities (NDAs) have been nominated by developing countries;
- The Fund has carried out its Initial Resource Mobilization, with approximately USD 10 billion equivalent from developed and developing countries; and
- The Private Sector Facility (PSF) has built a strategy to drive private investment.

1. Institutional and operational policies

A priority for the Board in early 2014 was to establish the policies and procedures needed to ensure the full operation of the GCF in an efficient and accountable manner.

To that end, the Board identified **eight essential requirements** to be established towards its Initial Resource Mobilization.

Eight essential requirements – the policies and procedures put in place by the Board in 2014:

(i) Fund structure and fiduciary, environmental and social standards;
(ii) Financial risk management and investment frameworks;
(iii) Results areas and indicators;
(iv) Accreditation framework;
(v) Resource allocation policies;
(vi) Proposal approval process;
(vii) Operating modalities of the Fund; and the
(viii) Terms for three accountability units.

To meet the target of mobilizing resources for the Fund by the end of 2014, the ambitious challenge was to develop, revise and agree on policies in all of the above-mentioned areas by the seventh meeting of the Board in May 2014.

These areas relating to governance and policy needed to be agreed upon before the GCF could start to disburse resources. Reaching agreement on these areas was also widely regarded as a trust-building exercise for the Fund, to give future contributors confidence in advance of resource mobilization. All of the elements would need to be agreed by consensus among the 24 Board members, who equally represent developing and developed countries.

The Fund worked intensively on these issues during its first two meetings in 2014, successfully reaching agreement on the last of the eight elements at the seventh meeting of the Board in May 2014.

An **accreditation process** was developed to allow organizations to partner with the Fund in executing its activities, with an Accreditation Committee and Accreditation Panel, and an Online Accreditation System to process applications. A **results management framework** was agreed upon, specifying the results that need to be achieved within each of the thematic results areas of the GCF. A **project and programme activity cycle** was adopted, encompassing a **proposal approval process** that covers the steps up until eventual Board funding decisions.

The GCF **financial risk management framework** includes policies to manage and mitigate risk within the GCF portfolio, while encouraging the Fund to maintain a risk profile that promotes the funding of innovative projects. It includes a system and structure for monitoring and reporting such risk. The Board also agreed on the **operational structure** of the Fund and how the **thematic funding windows for adaptation and mitigation** will operate, together with the **PSF**.

2. The investment framework

One of the most significant of the eight essential requirements was establishing the strategy and guidelines for future investments: the GCF investment framework. With large-scale climate funding expected to flow through the Fund over the coming years, ensuring that investments are targeted for maximum impact and fairness is essential, guided by the objective to promote a paradigm shift towards low-carbon and climate-resilient economies, while using the minimum concessional funding to make projects viable. The adoption of the GCF **allocation framework** by the Board in 2014 was the first step, establishing the general principles to govern future funding decisions.

The Allocation Framework principles:

(i) Aim for a 50:50 balance between adaptation and mitigation over time;

(ii) Floor of 50 per cent of the adaptation allocation to go to the least developed countries (LDCs), small island developing States (SIDS) and African States;

(iii) Geographical balance in funding across a wide range of countries; and

(iv) Significant allocation to the PSF to maximize engagement with the private sector.

Building upon these general principles, the Board approved a full **investment framework** at its seventh meeting in May 2014. The framework identifies a series of criteria and sub-criteria that will structure the investment decisions of the GCF in relation to both adaptation and mitigation funding.

Table 1. Investment guidelines

Criteria	Definitions
Impact/results potential	Potential to contribute to the objectives and results areas of the GCF
Paradigm shift potential	Systemic change to low-carbon and climate-resilient pathways Post-investment sustainability of the project
Needs of beneficiary country	Financing needs, lack of alternative funding sources
Country ownership	Beneficiary country ownership and capacity to implement the project
Efficiency and effectiveness	Cost–benefit analysis
Sustainable development impact	Gender, jobs and other benefits

3. The Initial Resource Mobilization

The successful completion of the eight essential requirements by the Board cleared the way for the Fund to begin mobilizing resources. The **Initial Resource Mobilization** was one of the most important developments of the year for the Fund, and an essential element in trust-building for the international climate agreement negotiations.

Potential contributors and observers were invited to preparatory meetings in Norway and Germany in September 2014. The first pledging conference took place in Berlin in November 2014, where the pledged total reached USD 9.3 billion equivalent from 21 countries, including four developing countries. This was the largest amount the international community had ever mobilized for a dedicated climate finance mechanism in such a short time frame.

The GCF continued to receive additional pledges, and by the twentieth session of the Conference of the Parties (COP) to the United Nations Framework Convention on Climate Change (UNFCCC) held in Lima, Peru, in December 2014, pledges had been made amounting to **USD 10.2 billion equivalent from 34 countries.**

The Fund moved to converting pledges to contributions. By mid-2015, **24 countries had already converted parts or all of their pledges** into signed agreements, amounting to a total of approximately USD 5.76 billion equivalent (as at 31 July 2015). This amount took the GCF above the effectiveness threshold of 50 per cent.

The attainment of effectiveness means that the GCF is in a position to start taking financing decisions on climate change mitigation and adaptation projects and programmes no later than its third meeting in 2015, as agreed by the Board.

Efforts to collaborate with the remaining contributors to convert pledges into contribution arrangements/agreements are ongoing. The Board, in decision B.10/02, welcomed the progress made by those countries that had converted their pledges into fully executed contribution agreements/arrangements and urged those countries that had not confirmed their pledges to do so.

With USD 10 billion equivalent mobilized, the Fund has made a good start; however, it is only the beginning of the resource mobilization efforts of the GCF. As scale is essential for the GCF to effectively deliver its mandate, there is a need to unlock climate finance at levels well beyond those raised so far. The figure of USD 100 billion a year of climate finance to be mobilized by developed countries by 2020, agreed at the sixteenth session of the COP held in Cancun, Mexico, in November 2010, has recently been reiterated by G7 leaders.

The Fund needs to continue growing annually at levels significantly beyond its initial resources if it is to catalyse a global paradigm shift. With significant and predictable funding in place, the GCF can play a key role in driving the transition to climate-resilient and low-emission societies, and in unlocking private climate investments in the developing world.

The GCF Initial Resource Mobilization is ongoing during the period 2015–2018, and further contributions are welcomed from national, regional and local governments, cities, foundations and the private sector.

4. Building a network of accredited partners

Starting to build a **network of trusted partners** to implement projects and programmes has been one of the key achievements of the Fund in 2014/15. Following the adoption by the Board of the accreditation framework, the Fund opened an Online Accreditation System. Deploying financing via accredited and well-established institutions is a significant feature of the operations of the GCF; by mid-2015, the Fund had **accredited 20 organizations**. With over 100 organizations working towards accreditation, this number will continue to grow.

Such entities may be subnational, national, regional or international, public, private or non-governmental. **Countries may access the Fund through any entity of their choice for a given investment proposal**. The GCF accreditation process ensures that these institutions are aligned with the objectives of the GCF and meet its fiduciary standards, environmental and social safeguards, and gender policy through a process of accreditation. The network of accredited entities operates in more than 100 developing countries, covering various geographical regions and sectors including public, private and non-governmental, and varying scales of operation in terms of financial activities, size of projects and programmes, and levels of environmental and social risk.

The Fund is also developing its monitoring and accountability framework for accredited entities, as well as a pilot programme for enhancing direct access to the resources of the GCF. Applications for accreditation are continuing on an ongoing basis through the GCF Online Accreditation System.

5. Providing readiness support to strengthen the capacity of developing countries

The **readiness programme** is a special feature of the Fund. It seeks to prepare developing countries to work with the Fund, providing support and using the resources to support their country strategies, and helping to ensure effective programming of such resources. To build capacity and accelerate access for developing countries, a total of USD 16 million had been allocated for readiness and preparatory support in October 2014.

Chosen by governments to act as the core interface between a developing country and the GCF, **NDAs** and focal points (FPs) provide broad strategic oversight of the activities of the GCF in a country and serve as the point of communication with the Fund. The GCF has been working to ensure that countries rapidly establish NDAs or FPs. More than **130 developing countries** have already done so, demonstrating the demand to work with the GCF.

NDAs and FPs also provide leadership on the deployment of readiness and preparatory funding support in their country. This stream of funding is designed and implemented based on the choices made by the NDA or FP. The **first GCF grant agreement** for readiness was signed with Mali in April 2015. By mid-2015, the Fund had reached the grant agreement stage with five countries, totalling USD 1.3 million, with over 70 proposals under consideration. At least 50 per cent of the readiness funding will be delivered to particularly vulnerable countries, including SIDS, LDCs and African States.

6. Catalysing private climate investment: the Private Sector Facility

According to estimates, developing **countries need USD 450 billion per year** between 2010 and 2029 to make their long-term investments low-emission and climate-resilient. This objective cannot be achieved without fully engaging the private sector, which represents two-thirds of the global gross domestic product (GDP). The Fund's unique Private Sector Facility (PSF) was created with this in mind. Its primary mission is to mobilize enterprises, financial intermediaries and the capital markets into making climate-sensitive investments in developing countries.

The PSF works with accredited entities to provide equity, debt, grants and guarantees for several sectors, including, but not limited to, renewable energy generation, energy efficiency (public transportation, waste management, efficient buildings and industry), and forestry and agriculture.

During 2014/15, the Fund made major efforts to develop the role of the PSF and ensure that it is best positioned to catalyse private investment for maximum impact. The **Private Sector Advisory Group** (PSAG) was established to provide expertise to the PSF and the Board. Its members include representatives from the private sector as well as civil society and Board members.

The PSAG provided input on the development of the investment framework and risk management framework in relation to the PSF. The connection between leveraging private finance and investment risk is particularly significant, with the aim that the PSF will **lower the risk of investments** aimed at transformational change. This may include aggregating small-scale projects and supporting a large-scale small- and medium-sized enterprise (SME) finance programme. The PSAG also made recommendations to the Board on **mobilizing funds at scale**, focusing on how to leverage Fund resources to engage private investors with the GCF pipeline.

The **accreditation of the first three private sector entities** in 2015 (in addition to several other entities with significant private sector track records in developing countries) provided tangible evidence of the commitment of the GCF to an innovative approach to the private sector. The PSF also consulted with accredited entities, NDAs and local stakeholders, with the aim of launching requests for proposals in 2016.

Outlook from the Executive Director, Héla Cheikhrouhou

This first Annual Report sets out the important strides we have taken together so far, but it also captures the enormous challenges and opportunities ahead.

We are now poised to support action on the ground in developing countries through grants and concessional loans to governments, as well as private sector instruments.

Yet, USD 10 billion falls a long way short of the identified needs for mitigation and adaptation. It is also dwarfed by the USD 200 trillion in financial assets the world needs to shift towards low-emission and climate-resilient development.

At COP 16 in Cancun in 2010, world leaders committed to reaching a target of USD 100 billion a year towards climate finance by 2020. This was recently reiterated by G7 leaders. Given the scale and urgency of financial needs for climate change action, we need to generate more resources from countries, State-owned entities and local governments that have not yet partnered with us.

To be paradigm-shifting, climate finance must be able to bring large amounts of concessional financing to the table.

The Fund will leverage the existing climate finance landscape by sending strong market signals and stimulating private and public sector funds to flow into climate-sensitive investments. It will do this through a demand- and country-driven approach that is balanced and addresses the overall climate challenge, and the economic and developmental needs of countries.

However, the Fund needs sufficient finance and sufficient political support to make this happen. It is only by building a more effective global climate finance architecture that we will achieve the paradigm shift required to keep global temperature increases to below 2 degrees Celsius. That is the challenge for the world and the challenge for the Green Climate Fund.

About the GCF

The Green Climate Fund is an operating entity of the Financial Mechanism of the United Nations Framework Convention on Climate Change (UNFCCC). It was given the mandate to make "an ambitious contribution to the global efforts towards attaining the goals set by the international community to combat climate change".[1] The Conference of the Parties (COP) to the UNFCCC established the GCF to promote a paradigm shift towards low-emission and climate-resilient development pathways in developing countries in the context of sustainable development.

The GCF is the largest climate-dedicated fund whose sole mandate is to serve the Convention and that aims to deliver balanced funding for mitigation and adaptation. The key features of the GCF include:

1. A **balanced governance structure** that ensures consensus-based decisions between 12 developing and 12 developed countries;
2. The **ability to engage directly with both the public and the private sectors** in transformational climate-sensitive investments;
3. **At least 50 per cent of its adaptation funding** is targeted to the most vulnerable countries, including SIDS, LDCs and African States;
4. The **capacity to bear significant climate-related risk**, allowing it to leverage and crowd-in additional financing;
5. A **wide range of financial products**, enabling it to match project needs; and
6. A **singular mandate** to contribute towards the implementation of the goals set by the international community to address climate change.

[1] Governing Instrument for the GCF, UNFCCC decision 3/CP.17, annex.