

GCF PSF STRATEGY ROADMAP

Project overview and conclusions



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PRIVATE FINANCE IS ESSENTIAL TO PARADIGM SHIFT



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CLIMATE
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At the country level, the mobilization of private finance support can promote:

- **Transformation** — of economic sectors primarily in private hands
- **Sustainable development** — including discouraging GHG lock-in and maladaptation
- **Policy effectiveness** — multiplier of domestic public spending, financing mechanisms for implementation programs
- **Domestic financial sector and capital market development** — specifically for climate-smart investments
- **Fiscal sustainability** — no sovereign guarantee required; generates new tax revenue

Globally, and at the GCF portfolio level, it can promote:

- **Redirection of existing flows**, including inward flows to low carbon, resilient activities
- **Unlocking of new sources** of capital for climate-compatible development

GOVERNING INSTRUMENT ENVISAGES PSF AS CORE TO GCF THAT COMPLEMENTS REST OF ARCHITECTURE



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Para. 41-44 describe the PSF, including country-driven approach, focus on local actors and financial intermediaries, and MSMEs; and need to engage PS in SIDS and LDCs

- “The Fund will have a private sector facility that enables it to directly and indirectly finance private sector mitigation and adaptation activities at the national, regional and international levels.
- The operation of the facility will be consistent with a country-driven approach.
- The facility will promote the participation of private sector actors in developing countries, in particular local actors, including small- and medium-sized enterprises and local financial intermediaries. The facility will also support activities to enable private sector involvement in SIDS and LDCs.
- The Board will develop the necessary arrangements, including access modalities, to operationalize the facility.”

Para. 34 highlights the importance of complementarity and in-country coherence of GCF as a whole

- “The Board will develop methods to enhance complementarity between the activities of the Fund and the activities of other relevant bilateral, regional and global funding mechanisms and institutions, to better mobilize the full range of financial and technical capacities. The Fund will promote coherence in programming at the national level through appropriate mechanisms.”

PROJECT OBJECTIVES



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Develop Roadmap

- Develop a strategic road map for engagement with private sector
- Map demand and supply

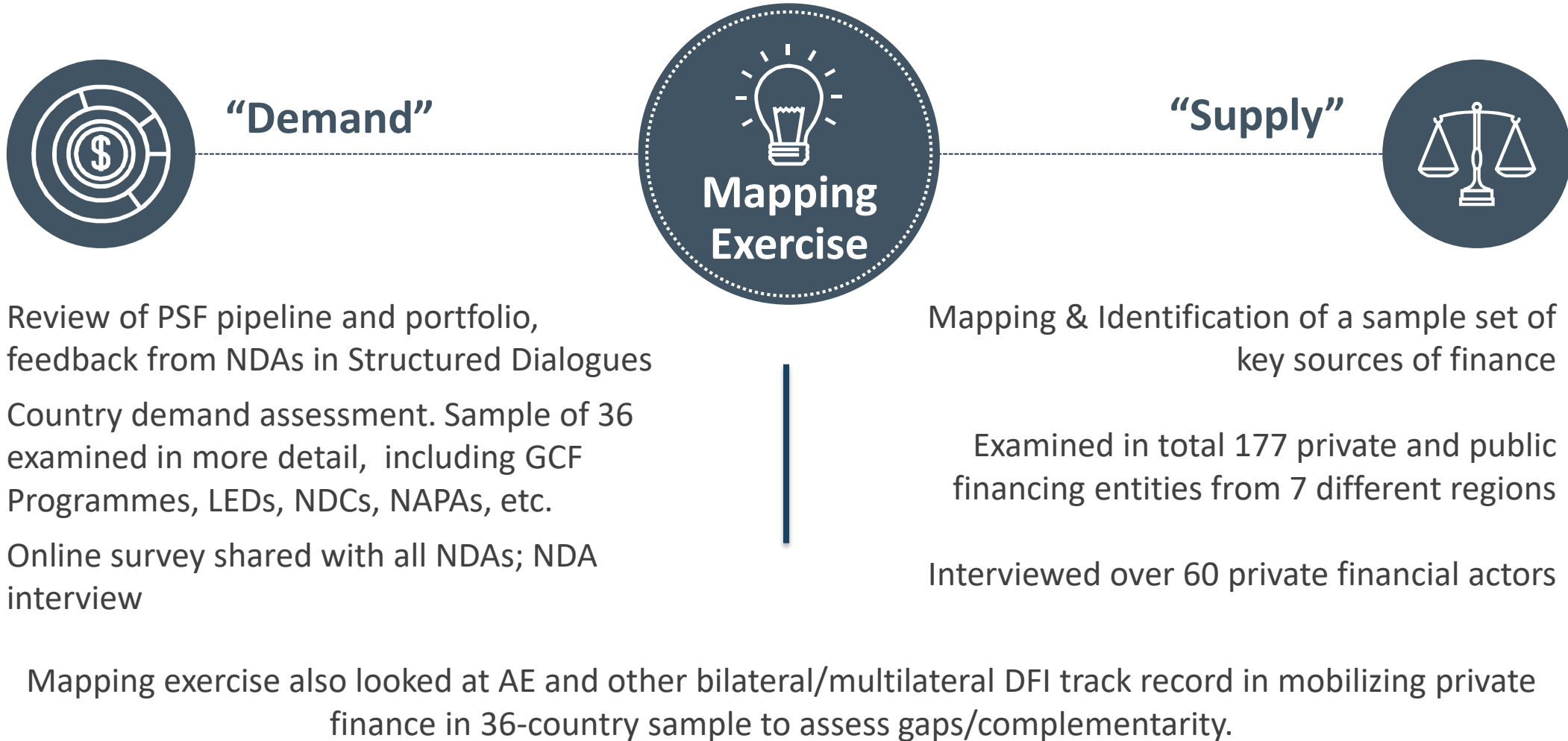
Identify Niche

- Determine areas of uniqueness, complementarity and collaboration in the climate finance space

Develop Recommendations

- Flesh out scenarios for PSF
- Recommend actions for GCF PSF business plan

MAPPING FRAMEWORK



DEMAND ANALYSIS METHODOLOGY (1)

Sample Selection

Identified countries as a focus group of GCF recipients

Based on PSF's pipeline, literature review, and Secretariat advice, identified 36 countries, with particular attention to LDCs and SIDS

Desk Research

Reviewed country policies to ID demand patterns

Reviewed climate policies and documents (incl. adaptation plans, low emissions development strategies, CIF plans, etc.)

Survey and interviews

To better understand NDA perspectives

- Designed 22-question survey for NDAs. Sent to 146 countries through CPD.
- Conducted phone interviews with (available) NDAs in sample
- Focus on PS engagement at the dom. level, hurdles, & role of the GCF/PSF

Analysis

- Collated and analyzed views heard, desk research, etc.
- Looked at DFI track record in providing PS-related support in sample countries

DEMAND ANALYSIS METHODOLOGY (2)



Survey

- 22 questions on: NDA's role, NDC context and role of the private sector in implementing it, barriers for private sector engagement, GCF support required, and south-south cooperation
- 44 responses, 30.1% of total NDAs, 66.6 % of sample countries

Interviews

- Phone interviews
- 16 countries, 44.4 % of sample



CHALLENGE: UNDERSTANDING PSF AND ITS ROLE

Guidance to private sector

- Some NDAs struggle to guide the private sector on tapping strategically into GCF resources, particularly for paradigm shift/ innovative investments

Concerns about crowding out

- When aware of the Fund, domestic private actors tend to see it as only a source of “cheaper-than-market” finance, often competing with DFIs, not as a financier of riskier investments

GCF comparative advantage

- There is a need to make GCF’s comparative advantage more compelling in the climate finance landscape/DFI marketplace: as a source of capital that takes more risk to achieve more impact

CHALLENGE: ENGAGING PRIVATE SECTOR

The structure of the GCF makes reaching MSMEs, inc. businesses run by the poorest, difficult. Community organizations and MSMEs lack the knowledge, time, and capacity to deal with complex proposal and approval processes

- *“Legal frameworks and incentives exist, but it’s difficult for small companies to enjoy them”*
- *“Working with MSMEs is the best bet at the domestic level. But the GCF needs to make sure it can deliver”*
- *"Economic growth opportunities in most countries depend to a large extent on MSMEs. PSF needs to differentiate what it can do with large, international private actors, from how it can support small-size organizations that are essential to the economy"*
- *"MSMEs may know what the incentives are at the domestic level, but knowledge about developing climate projects is seriously lacking"*

NEARLY ALL NDAS FLAGGED READINESS AS A KEY ISSUE

Most NDAs interviewed emphasized the need for better- targeted readiness funding for PS project development, particularly idea development prior to accessing the PPF or submitting a concept note

- *“Support during early stages is essential to build capacity of local financial systems and the real sector”*
- *“Need GCF readiness to build capacity of NDAs to look at the right financial instruments, to focus on scalability of projects”*
- *“Need funding to build capacity at the local level to develop private sector proposals, help translate what NDC commitments mean in terms of business opportunities”*
- *“Would welcome advice from the PSF on how to best target readiness resources to work with the private sector”*
- *“Readiness can help with project development. Challenges to access the PPF are high. Need readiness for idea development, prior to developing a concept note”*

KEY COUNTRY MESSAGES

Instruments and technical assistance

- PS needs enhanced access to credit (tenor, rates, currency, speed)
- Want GCF to help intermediate between int. private sources & domestic capital markets; don't have clear view on how
- Need support in ID'ing opportunities, inc. in converting NDCs into financeable plans and on priv. fin. for adaptation
- Want help to build stronger local financial institutions
- Want better targeting of readiness to support proj. development & origination, more rapid deployment of readiness overall
- Interested in flexible country driven approaches to encourage replication

Structure and operations

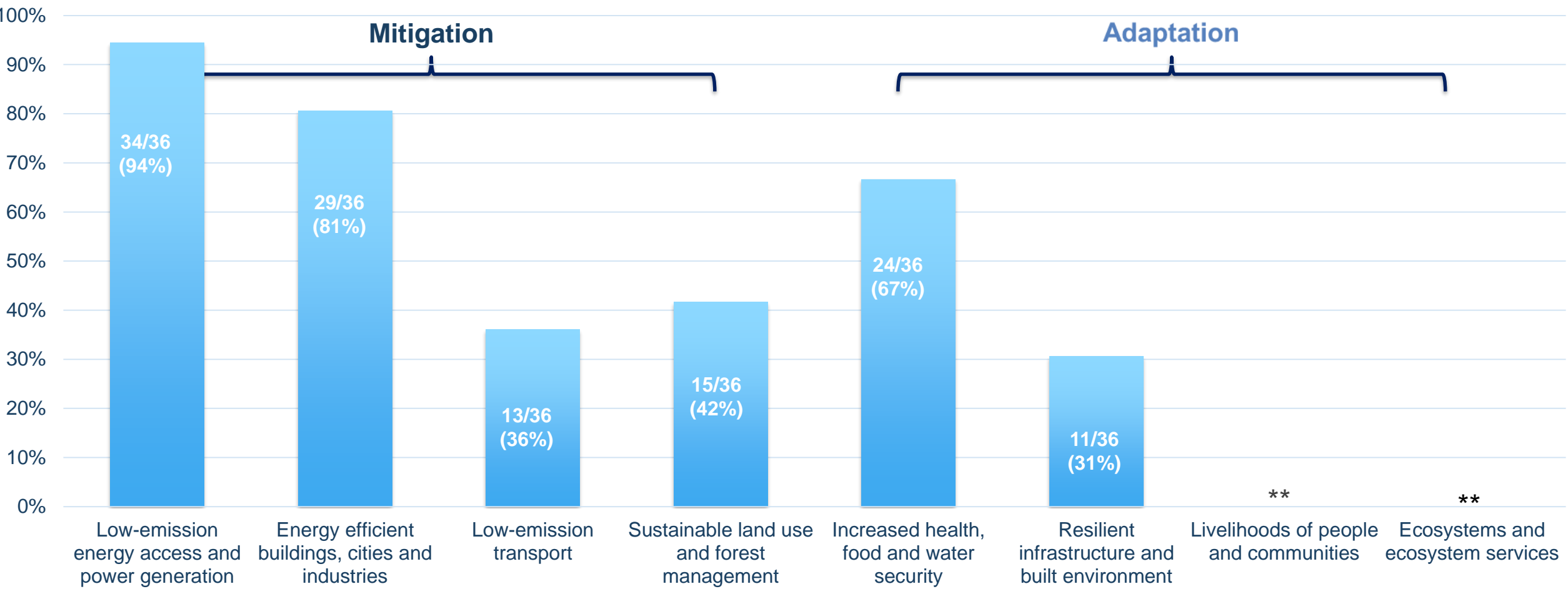
- Better communication channels between PSF/NDA: lack of local presence
- Improve PSF staff awareness of nat. circumstances/policies, consideration of these in proj. origination, selection
- DMA/PSF to work closely together to deploy country-driven programmatic approaches across public and private toolkit
- Better articulation between PSF and local PS & FIs is wanted, including for MSMEs
- Would welcome South South knowledge sharing platforms

GCF Policies and selection criteria

- Want more risk taking from GCF and AEs: focus on higher impact projects
- Simplify processes and decision-making to better suit MSMEs and BOP activities
- Transparency on criteria for financial terms could help PS proponents determine whether GCF viable source

DEMAND FOR PRIVATE INVESTMENT BY SECTOR

Data source: Desk research for the 36 sample countries. Chart shows the percentage of sample countries and absolute number of sample countries indicating demand for private investment by GCF result area.



** Note that the last two categories in the chart, livelihoods of people and communities and ecosystems and ecosystem services, were occasionally noted as additional or secondary benefits of desired private sector investments, or part of the rationale for a sectoral investment.

SUPPLY ANALYSIS METHODOLOGY

Financial Sector Mapping 441 Entities

Financial Sector Mapping – Macro Analysis

Researched 441 private and public financing entities, including private sector financial entities in LDCs and SIDS

Refined Sample Pool 177 Entities

Financial Sector Mapping – Refined Sample Pool

Obtained detailed information on 177 entities with regard to their balance sheet size, investment products/tools and return target/appetite(s).

Financial Entity Interview Over 60 Entities

Financial Entity Interview

Selected a balanced sample of over 60 financial entities to interview, covering all sub regions and types of entities.

Analysis

Analysis

Gathered critical market intelligence across all sub regions and types of private finance
Collected insights from interviewees on barriers, gaps, opportunities for climate investment
Assessed opportunities for the GCF to engage with range of private financial actors

MAPPING/INTERVIEW SUMMARY

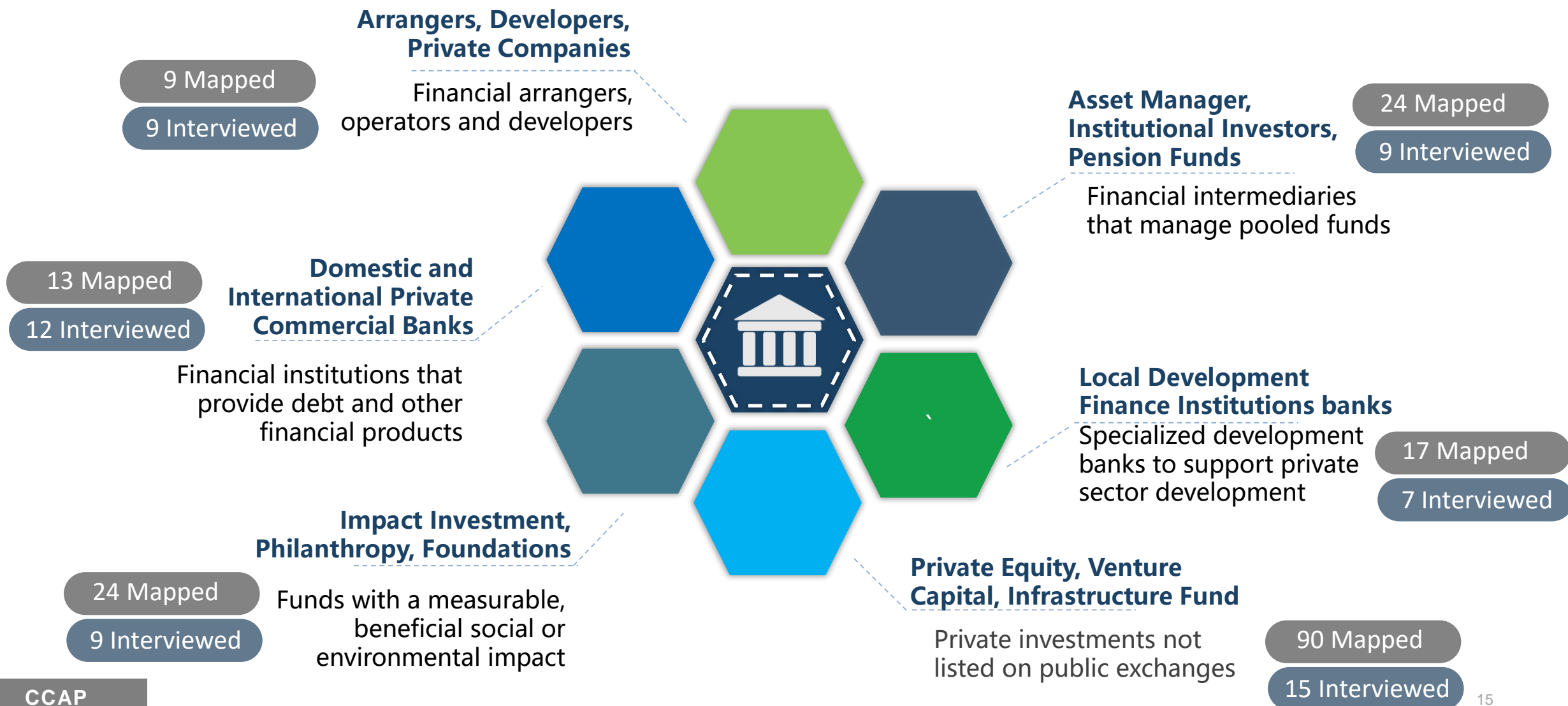


Mapping Interview

- Conducted both phone and in-person interviews with over 60 entities out of a 177 entity sample
- Interviews focused on understanding current trends/challenges in climate finance
- Evaluated market intelligence and insights on areas where GCF can best engage and add-value



ENTITIES INTERVIEWED: SOURCES OF PRIVATE FINANCE



CONCLUSION: WHAT PS WANTS FROM PSF

Instruments and technical assistance

- FX risk support and hedging
- Guarantees, price off-taker support and other credit enhancements
- In some regions, DFIs crowding out private sector, in others, only game in town
- Support financial intermediaries that channel financing to SMEs and smaller projects
- Investment platforms suitable for institutional investors
- Support vehicles aimed at mobilizing local capital markets
- Longer tenor debt in local currency at reasonable rates
- Early stage equity to build out investable project pipelines
- Capacity building for governments to build private sector solutions

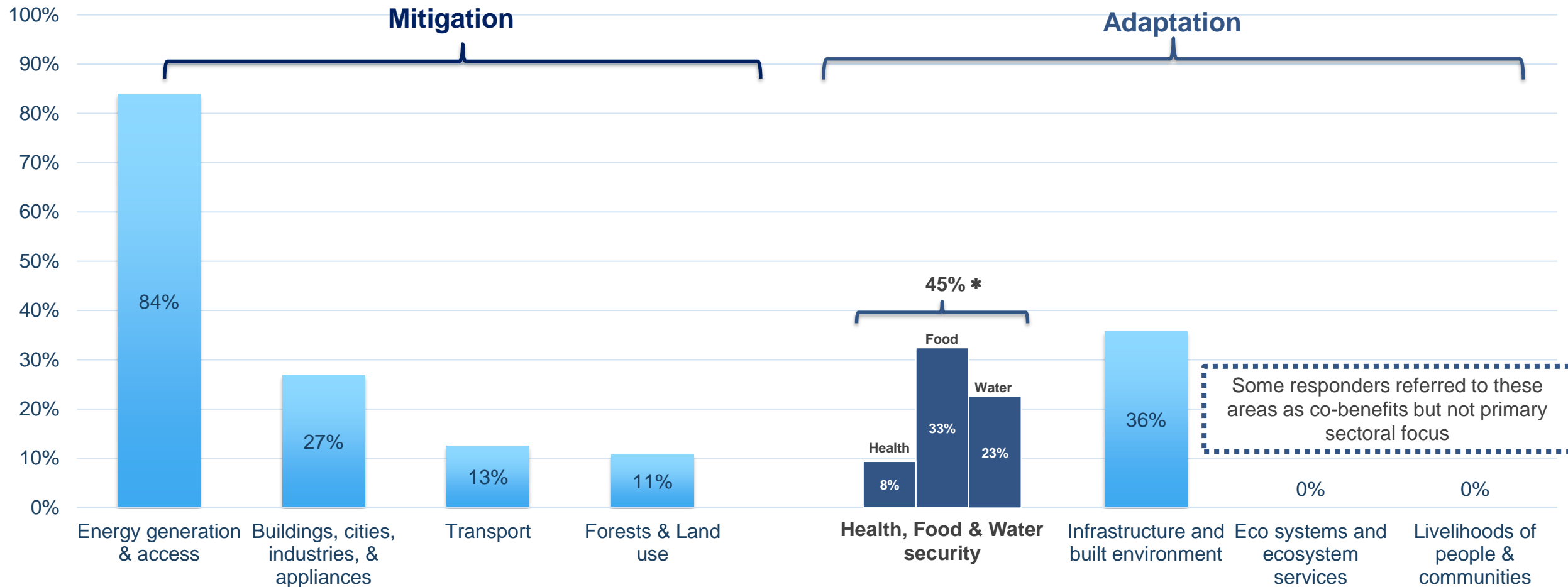
Structure and operations

- Speed, efficiency and accountability with processing and reviewing deals
- Expert partners who understand the private sector
- Clear pathway to capital with commitment from GCF (e.g. product specific RFPs)
- Proactive market-making to address gaps in climate finance
- AEs need to improve channeling function

GCF Policies and selection criteria

- Flexibility to adapt accreditation criteria to diverse governance structures
- Allow the private sector to co-invest or partner with the GCF without becoming Accredited Entities
- Improve transparency of GCF access and decision-making process

SECTOR PRIORITIES FOR PFAS INTERVIEWED



Data source: Interviews with 61 private entities. Chart shows percentage of interviewed entities investing in different sectors corresponding with GCF result areas.

* 45% of respondents said they were active in this result area. Smaller bars show individual answers given – total is less than 45% as responders that flagged more than one sub-sector were counted only once for the result area total.

IDENTIFY NICHE

Key gaps and opportunities

CONSOLIDATED PRIVATE FINANCE OBSERVATIONS



Key Gaps in the Financial Ecosystem

- Financing for smaller scale projects (between \$500k - \$10M)
- Financing for projects targeting BOP
- Support for early-stage project preparation and technical assistance
- Affordable low-cost debt in local currency
- Guarantees and off-taker risk support



Gaps in Focus and Topics

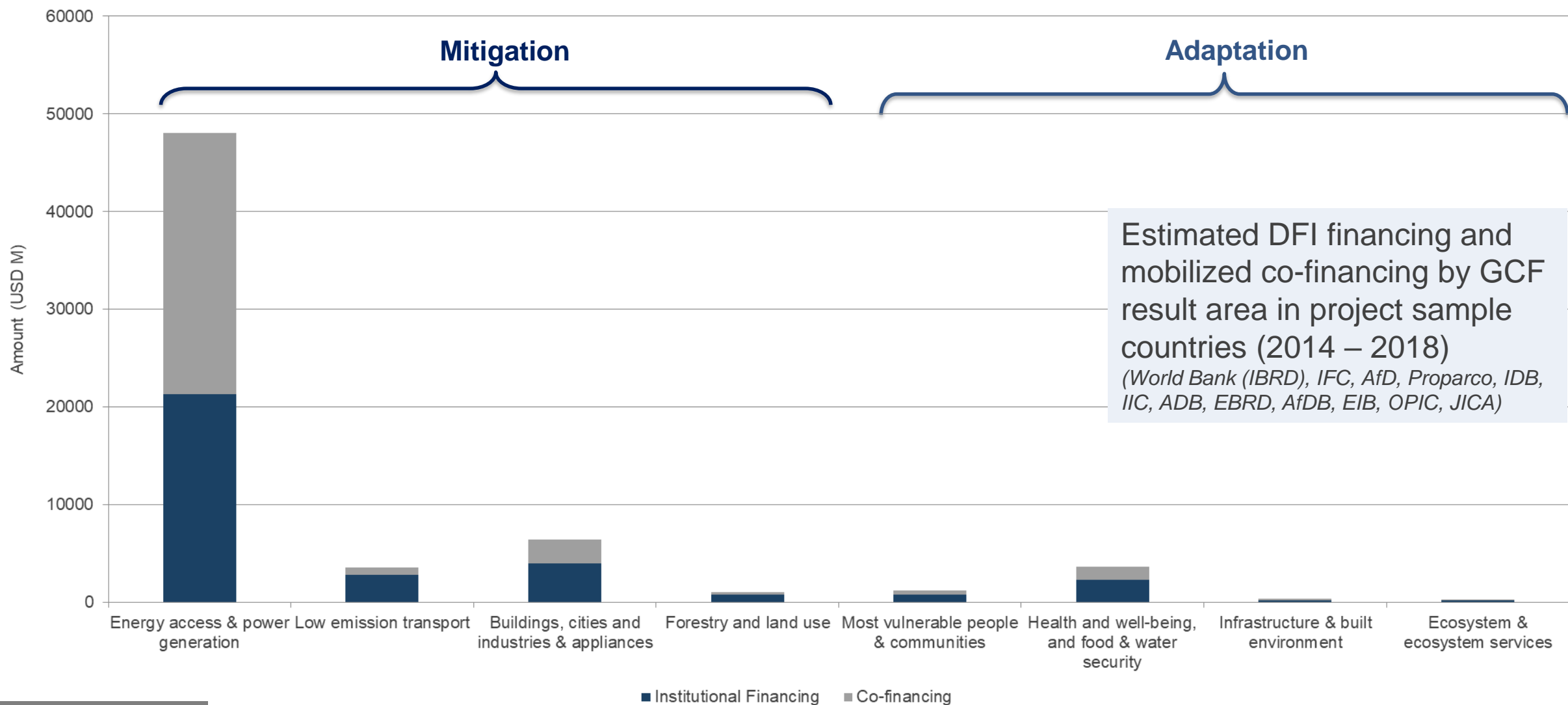
- Investment in adaptation and resilience
- Investment in small-scale, off-grid renewable energies
- Investment in grassroots organizations providing last mile delivery or support for BOP, including credit lines
- Investment in LDCs/SIDS
- Investment in forestry, land use and low-carbon transportation
- Incubation of new climate finance vehicles, inc. project preparation support



Private Sector Needs

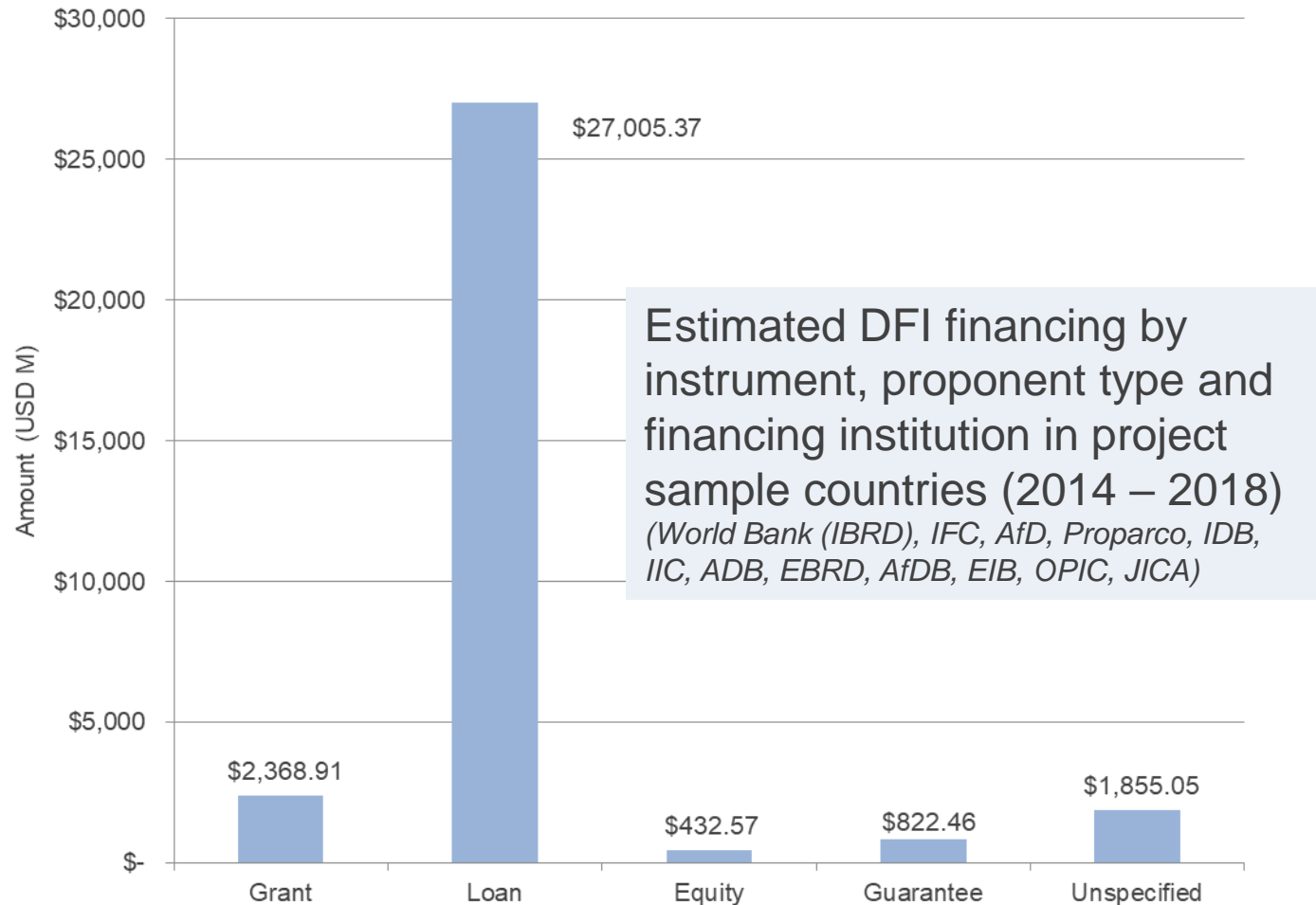
- Private sector requires speed (weeks not years) and clarity in all transactions.
- Simpler and more efficient way to access and engage with the GCF
- In addition to capital, private sector investors expect co-investors or partners to offer additionality e.g. ESG know-how and access to government stakeholders

PRIVATE SECTOR ORIENTED CLIMATE FINANCE BY LARGE DFIS VERY SKEWED TO ENERGY

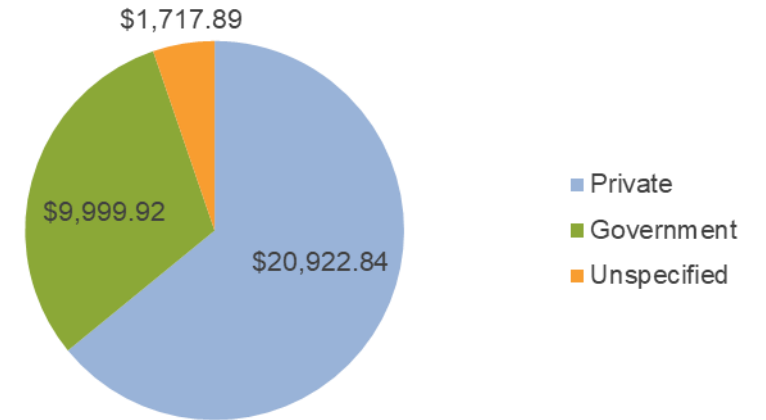


WE ALSO ESTIMATE IT TO BE HEAVILY FOCUSED ON HARD CURRENCY DEBT

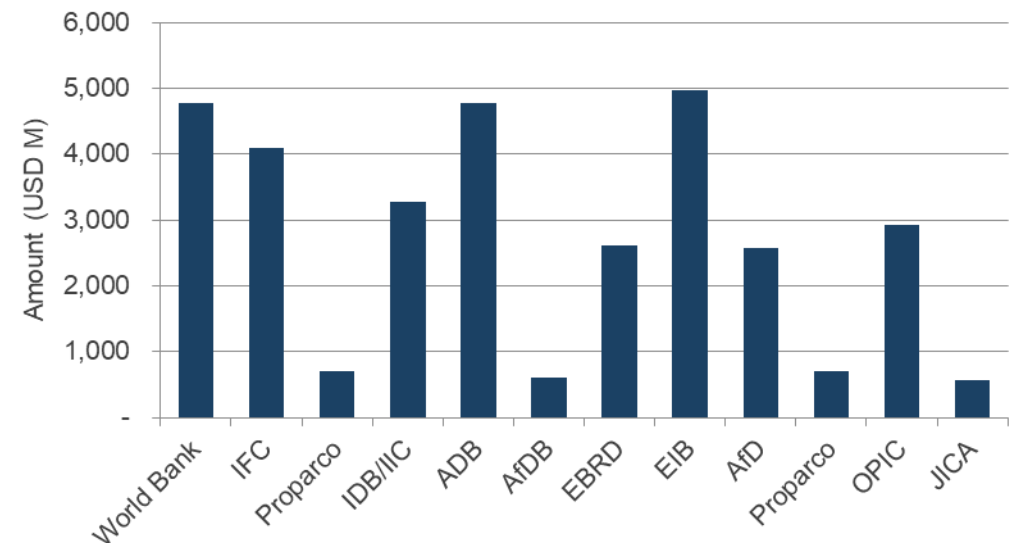
Finance by Instrument



Amount by Type of Proponent (USD M)



Amount by Institution



PSF NICHE: A STRATEGY TO BALANCE NDA AND PFA VIEWS

A strategy built around NDA perspectives would focus on country ownership and impacts

- PSF support through strengthened national institutions, but preference in practice for public-only solutions
- NDA approval is key eligibility factor
- Readiness to build NDA capacity and programs to implement national policies
- GCF should proactively program to implement country commitments
- Equity: all countries benefit from PSF
- Key word: impacts

A strategy built around PFA perspectives would focus on efficiency and returns

- A ring-fenced PSF supports private intermediaries directly
- Projects selected based on commercial potential and scalability
- Readiness to improve enabling environments and develop pipeline
- PSF should proactively program as a market maker and solutions builder
- Efficiency: market drives PSF allocations
- Key word: risk/reward

Potential elements of a balanced PSF strategy

The project team heard from stakeholders that the GCF, and its PSF, should focus on achieving paradigm shift by acting proactively as a risk-inclined and impact-oriented keystone institution in the climate finance space

Take more risk
to achieve
more impact

Enhance local
FIs and capital
markets

Build and
catalyze
pipeline

Country and
market
expertise

Improve
MSME/BOP
Modalities

Be a “market
maker” for
implementation

Flexibility/
clarity for PS
proponents

OVERVIEW OF SCENARIOS

Scenario 1: Take more project risk to achieve more impact

- Strengthen risk taking at project and portfolio level to achieve more impact, moving away from plain vanilla projects that risk crowding out.
- Focus on local currency financing, early stage equity, beefing up risk mitigation, to achieve transformation rather than simply quick wins.

Scenario 2: Build local financial markets and institutions

- Engage at national level to improve systemic conditions, institutions and facilities for climate financing, spurring sustainable, climate-compatible growth, and channeling financing to SMEs PSF can't reach directly.
- Focus on enabling policies, financial institutions and capital markets, to create the ecosystem for climate investment.

Scenario 3: Act as a “market maker” for sectoral implementation

- Build programmatic approaches, using “whole of GCF” and AE capacities, to address high impact sectoral opportunities for mitigation and adaptation.
- All national, regional, and international programs to focus on three key co-catalysts for policy-led transformation, namely enabling policy, financial mechanisms for private transformation, and project pipeline development.

Notes on scenarios

- **Logic model** presented to show how indicative activities flow to ultimate impacts through GCF outputs and the outcomes they achieve. The logic models are not meant to be comprehensive.
- **Scenario portfolio** illustrates how applying the scenario would affect key parameters of the **PSF baseline portfolio**, namely approved projects plus projects targeted for B21 and B22
- **Impacts** are broadly described with respect to fund level results as well as implications for specific results like CO2 reductions

EXAMPLE: SCENARIO 1: TAKE MORE PROJECT RISK

IMPACT

Innovative projects demonstrate climate compatible investment at scale and “crowd in” additional sources of finance

OUTCOMES

Private finance is not crowded out

New business models are demonstrated

Local currency financing is available

Key financing gaps are filled with diversified instruments that mitigate project risk efficiently

OUTPUTS

PSF invest in projects with low crowding out risk

Highly risk-inclined capital and technical support are deployed by PSF to innovative projects

Large share of PSF financing is delivered in local currency

PSF instruments cover range of options: grant, equity quasi-equity, debt, and guarantees

PS proponents know what PSF can offer and PSF delivers, or refuses, transparently

INDICATIVE ACTIVITIES

Crowding out test to screen projects during origination phase

Projects that risk crowding out are rejected

Early stage support for concept design and development

Early stage equity, including investment in incubators

GCF/PSF takes unhedged currency risk

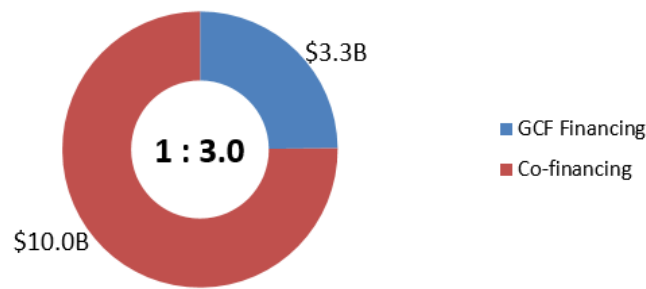
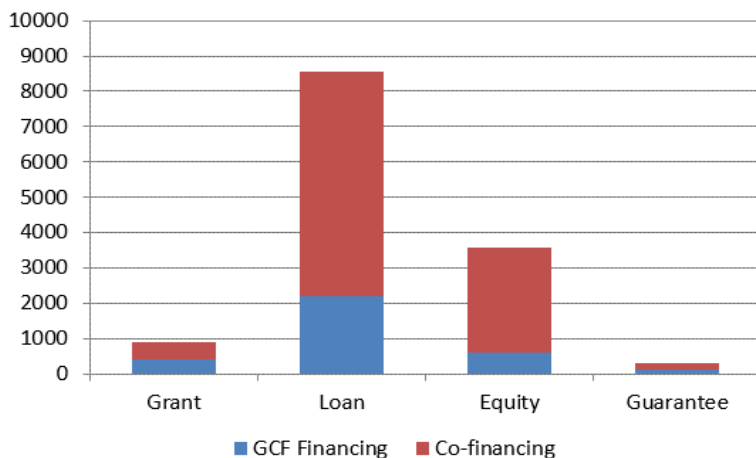
Financial management of PSF allows for efficient provisioning, especially guarantees

Guarantees more fully utilized where appropriate

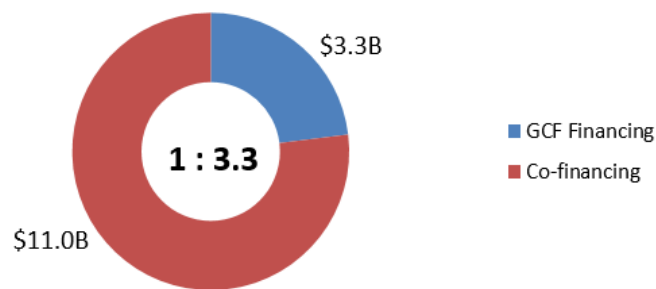
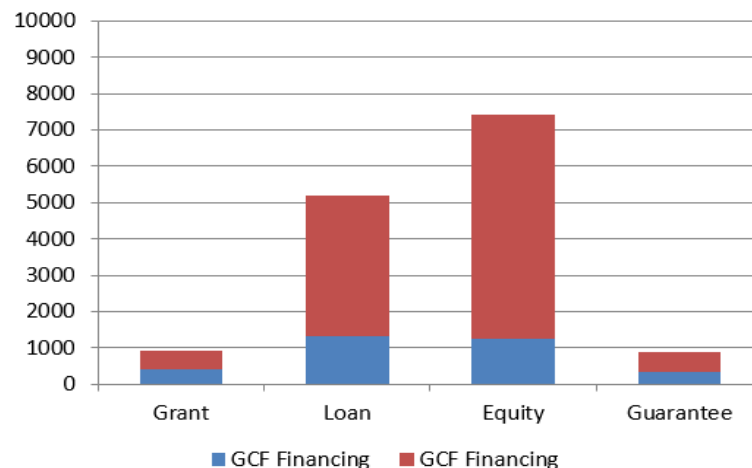
PSF publicizes concessionality considerations for its instruments.

EXAMPLE: SCENARIO 1: TAKE MORE PROJECT RISK

PSF ESTIMATED PORTFOLIO
Approved & Targeted for B.21 and B.22



PORTFOLIO SCENARIO 1



Key illustrative parameters

- Loans: 66% ☐ 40%
- Equity: 18% ☐ 37.5%
- Guarantees: 3% ☐ 10%
- Grants assumed to remain the same
- Leverage ratios are assumed constant: have not modeled potential changes in guarantee leverage.
- “Unspecified” co-financing included in internal PSF forecast is re-distributed by instrument according to weight

Impacts

- With local currency component, turning down projects that risk crowding out, and higher share of equity, the portfolio will help PSF fulfil its mandate but may be complex to risk-manage.
- Greater reliance on equity increases leverage ratio of portfolio: \$1B more co-financing in this example
- May potentially achieve higher impact by aligning better with PFA and NDA demand.
- More active role of PSF staff in equity transactions may require higher staffing levels, different skills, and enhanced portfolio management, with budgetary implications.

RECOMMENDATIONS

I. Take **more risk** to crowd in finance for paradigm shift

e.g. (i) local currency financing and (ii) more equity / less debt

II. Support the development of **climate-compatible national financial systems**

e.g. (i) readiness, financing for national climate banks and (ii) support to build capital markets for “green” securities

III. Act as a “market maker” for **sector transformation**

e.g. (i) strengthened GCF Country Programs and (ii) targeted programs and RFPs to implement national sector priorities

IV. Consider **reforms** that can improve impact and engagement with PS

e.g. (i) PSF direct financing; (ii) Project cycle (“notification”) and accreditation reforms and (iii) capitalise PSF

THANK YOU

ANNEX: SELECTED NDA SURVEY ANSWERS

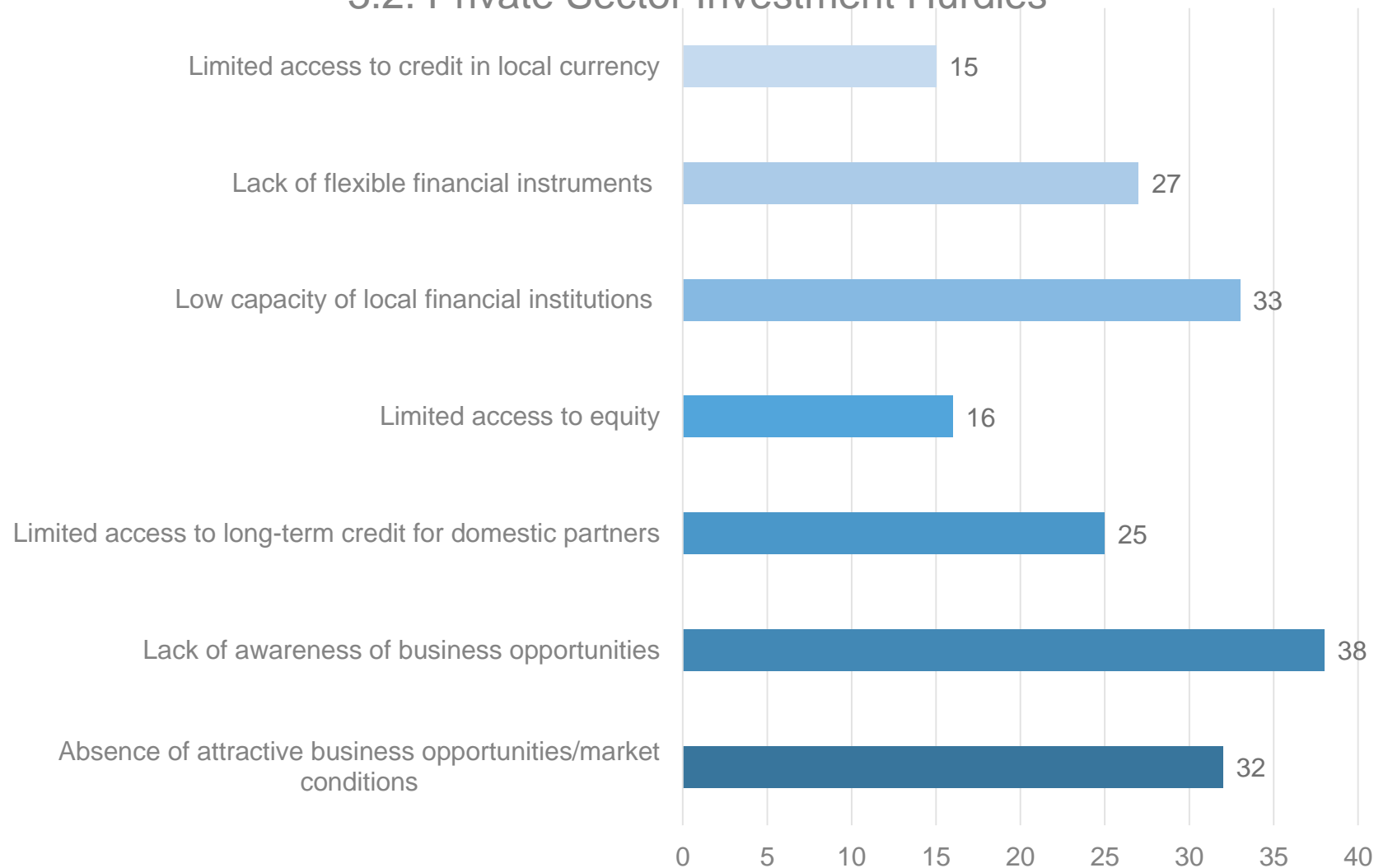
NDAS HAVE AWARENESS OF ISSUES HAMPERING PRIVATE INVESTMENT...

Most NDAs reported a lack of awareness of business opportunities, as well as absence of attractive business opportunities, as hurdles. Low capacity of local financial institutions was also ranked high.

“[Our country] has a GCF Country Programme with high-level priorities, but our challenge now is developing a PS pipeline, find project ideas. The role of direct access AE’s in local PS engagement is essential”

CCAP

3.2. Private Sector Investment Hurdles



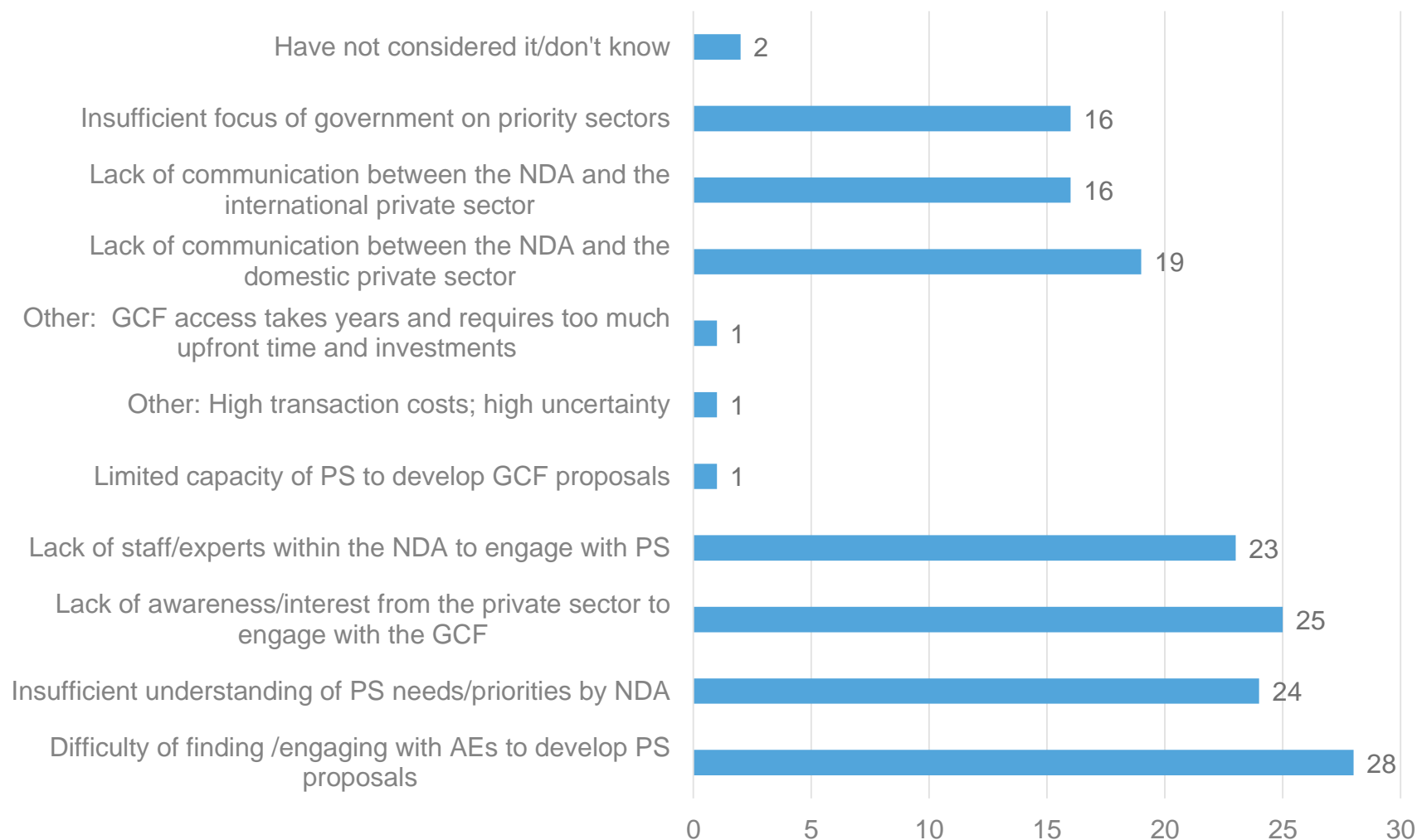
Source: Survey and interviews

...AND THE DEVELOPMENT OF PSF PROPOSALS

NDAAs we spoke to identified a range of issues in encouraging PS proposals. NDAs in particular were concerned that AEs are not focused on high impact. Challenges of engaging PS and AEs were also commonly raised.

“We need AEs less focused on the Fund’s approval tendencies, and more supportive of innovative approaches”

3.3. Proposal Development Hurdles



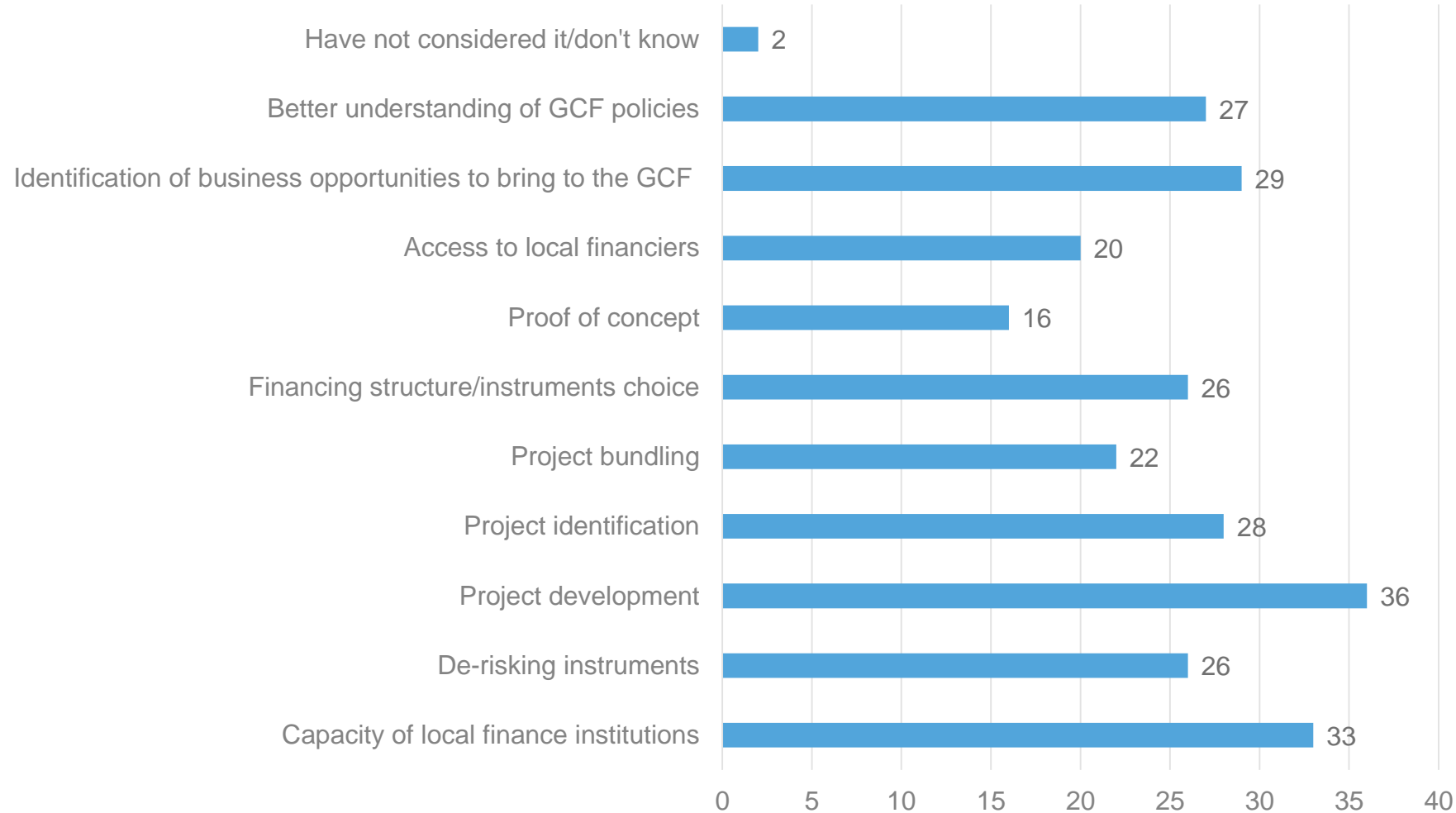
Source: Survey and interviews

THE DEVELOPMENT OF LOCAL INSTITUTIONS IS TOP OF MIND FOR NDAS WHEN ASKED ABOUT SUPPORT NEEDS

NDAs we spoke to identified challenges for project development and origination as key areas for support, as well as the limited capacity of local financial institutions.

“Training of local private commercial banks on risk assessment and climate change financial structures is essential”

4.1 Where NDAs need GCF support



... AS IS PROMOTING LOCAL FINANCIAL INSTITUTIONS' ACCESS TO GCF RESOURCES.

Half of the NDAs reported engaging with local financial institutions with a view to nominate them as direct access entities. Many see them as a promising opportunity to channel GCF resources for the local private sector.

“Private actors in [our country] have limited capacity to develop PSF proposals, except for our direct access AE [local commercial bank], which is also the primary provider of finance for MSMEs.”

2.10 PS Engagement for nomination as direct access AEs

