Submission German Board Member

Consultation by Secretariat on zero order draft – July/August 2022

- We would like to thank the Secretariat for this opportunity to submit our input for the zero order draft of the updated Strategic Plan, which is a key document for GCF-2. We believe that the GCF-Strategic Plan 2020-2023 has served its function for GCF-1 and contains key elements, which point to the right direction for GCF-2. We also welcome that the draft of the USP will incorporate inputs by multiple stakeholders received through the consultation process, and will take into account the findings of the policy review as well as summary findings of the second performance review, as outlined in decision B32/04.
- We are aware of some aspects of strategic policy planning already are relevant for GCF-1, and might be picked up already during the remainder of GCF-1.

<u>Changed environment since 2020</u>

- Since we approved the USP 2020-2023 in 2020, new scientific findings have provided further evidence of the increasing urgency of action to address the climate crisis. In addition, the global political and economic landscape has changed, and the international climate finance architecture has matured. These developments need to be reflected in the USP for GCF-2:

  1. **New scientific findings:**
  - The ***recent IPCC Working Group II and Woking Group III report*** **s**shows like never before how climate change is affecting us not at some point in the future but already today. The assessment provides strong support for urgent *mitigation to close gaps in this decade to keep the 1.5 limit within reach*, as well as for increased action and support *for more transformational adaptation and also addressing loss and damage.* More action is required to support developing countries' ambition in implementing the goals of Art. 2 of the Paris Agreement (PA), identifying those areas of action where highest impact in mitigation can be achieved (going down to sectoral level) in order to allow meeting the Paris agreement goals of limiting temperature increase to 1.5°C.
  - With regard to ***adaptation***, the IPCC highlights that many natural systems are already ***reaching the hard limits of their natural adaptation capacity***, with additional systems hitting their limits with increasing global warming. According to the IPCC, above 1.5°C warming, some ecosystem-based adaptation measures will lose their effectiveness in providing benefits to people as these ecosystems will reach hard adaptation limits.
  - In line with these findings, the IPCC Sixth Assessment Report emphasizes that ***adaptation finance needs are higher than presented in earlier IPCC reports***. Indeed, existing adaptation gaps are partially driven by widening disparities between the estimated costs of adaptation and financial resources allocated to adaptation. On top, adverse climate impacts can reduce the availability of financial resources by incurring ***losses and damages*** and by impeding national economic growth, thereby further increasing financial constraints for adaptation, particularly for developing and least developed countries.
  - With regard to ***mitigation***, the IPCC WG III report highlights the urgency for transformational action on mitigation within this decade in order to close the emissions gap for a 1.5°C pathway. For this, it is critical to increase financial

flows into mitigation: Tracked ***financial flows for mitigation fall short substantially*** across all sectors and regions, with the challenge of closing mitigation financing gaps largest in developing countries.

- While public and private finance flows for fossil fuels continue to be greater than climate adaptation and mitigation finance, which highlights the urgent need for action to redirect financial flows to align them with the Paris Agreement goals, IPCC findings also provide ***encouraging messages*** on which the GCF can build. Importantly, the IPCC concludes that given the size of the international financial system there is sufficient global capital to close global investment gaps. Moreover, governments can scale up mitigation/adaptation financial flows by ***sending clear policy signals*** in support of a Paris-aligned international financial system, with a particular focus on deconstructing barriers to redirect capital into climate.

2. Changing global political landscape:

- The global political-economic landscape has changed since 2019, most dramatically since the war of aggression Russia launched against Ukraine on February 24, 2022. At the same time, and as a partial consequence, many developing countries are facing a ***triple crisis of high-inflation, hunger and over-indebtedness***, potentially putting the climate agenda at risk. The persisting impacts from the ongoing COVID-19 pandemic add to the multiple crises.
- The GCF needs to be able to adapt and respond to these new challenges, ***ensuring that much needed climate action continues to be high on the policy agenda*** of developing countries, amongst others, by incorporating mitigation/adaptation activities into wider development agendas. This is not only crucial for ensuring climate objectives, but also for increasing developing countries' fiscal resilience against potential financial shocks derived from climate impacts and climate (in-)action elsewhere.

3. Evolving global climate finance architecture:

- Since 2019 the global climate finance architecture has developed. On the one hand, the ***GCF has matured*** into the biggest climate fund with a significant network of partners and instruments at its disposal. On the other hand, other institutions like the Adaptation Fund have scaled their activities and grown into experienced climate finance actors. In addition, a ***transformation in global finance has started***, with an increasing number of financial institutions striving to align their investments with the goals of the PA.
- GCF-2 should make use of these developments by: a) further developing and ***expanding the instruments*** at its disposal (importantly via foreign currency lending and guarantees). b) Utilising ***complementarities*** with other climate finance institutions, adding value to relevant existing partnerships and initiatives, such as the NDC-Partnership and the InsuResilience Global Partnership. c) ***Partnering*** with other financial institutions to shift the trillions by transforming the structures of global finance in line with Paris goals.

- Based on the new strategic environment outlined above, we consider the following key points particularly important for USP-2:

1. <u>Farther-reaching and more concrete vision of the GCF for Art. 2.1c</u>

- In line with the PA and the latest findings from the Working Group III of the IPCC AR6 Report, we would like the USP to provide a *bigger and broader vision of what* ***alignment of financial flows as per Art. 2.1c of PA actually means*** (including e.g. removing fossil fuel subsidies, green taxonomies, financial sector incentives, portfolio alignment of GCF partners, support to national policies and strategies) *and how the*

GCF can contribute to supporting the ***implementation of 2.1c*** *more effectively*. While in the current USP, Art. 2.1c is mainly addressed in terms of mobilising private sector (4.3 in USP), we consider it essential to go beyond the private sector and mainstream 2.1c throughout USP-2 (incl. in: II Strategic Vision and 2.1(a); III Strategic Objectives; IV Strategic Priorities, 4.2/4.3/4.4/5.2). Key initiatives may include:

- ***Support developing countries in enabling necessary institutional architectures*** to re-channel all their financial flows (real economy, financial markets, private and public sector) in line with PA (IV Strategic Priorities, 4.1). Re-channelling of financial flows should ideally account for both: a) focus on projects with climate action as the core objective; b) mainstreaming climate-related physical and transition risks across the entire economy (failure to do the latter may hamper developing countries' ability to build climate resilience, strengthen preparedness to climate-related shocks and fund other development projects).
- ***Explore suitable incentives and programmes*** through which the GCF can pilot and scale-up the implementation of Art. 2.1c in developing countries. Potential instruments may include the "Request for Proposals (RfP)" as well as the Readiness Programme (e.g., capacity-building and support on national policies, such as green finance regulations and climate disclosure standards, green taxonomies, establishment of green development banks, etc.).

- The GCF also needs to reflect on the objective of aligning financial flows with Paris goals ***in its own operations and in the portfolios of its partners***. In this vein, we deem the following to be critical:
  - The GCF commits to turn into a ***net-zero organisation***, ensuring that both its portfolio (scope 3 emissions) as well as its operations (scope 1 and 2 emissions) are net-zero.
  - The GCF commits to work with partners which are fully aligned with the 1.5°C limit and the Paris Agreement goals. In case Paris-alignment has not been achieved yet, partners should be required to provide comprehensive, explicit and credible strategies on how to achieve Paris-alignment.
  - ***With regard to its partners***, the GCF needs to further enhance the goal for GCF accredited entities to commit to and ***perform a portfolio shift*** – something which AEs should commit explicitly at accreditation, going beyond a mere consideration of a portfolio shift to align with the Paris Agreement goals (IV Strategic Priorities, 4.4, a / V Operational Priorities). Similarly, criteria need to be defined and operationalised for Paris-alignment for re-accreditation.
  - In order to incentivise AEs to accelerate their portfolio shift, the GCF could elaborate a ***"climate-performance-based" approach towards AEs***. This may entail the GCF setting stronger positive incentives for AEs to perform a portfolio shift. Such an approach would need to be identified and reviewed in line with the revision of the Accreditation Strategy and to be further detailed in the Updated Accreditation Framework.

2. Addressing Loss & Damage more prominently

- Given the increasing impact of extreme and slow on-set events related to climate change, we consider it critical to ***increase the GCF's activities on Loss & Damage***. Therefore, the GCF needs to reflect how its current modalities may address issues related to L&D more prominently, ***exploring further options for addressing L&D*** without compromising funding for adaptation/mitigation.

  Some elements could even already be implemented in GCF-1 and further developed for GCF2.

- For example, the GCF could develop ***specific guidelines*** and targeted pilot programmes on L&D (through RfP). Such guidelines/programmes should identify and prioritise relevant measures to address L&D. During the process of setting up guidelines/programmes, the GCF should ensure transparency and inclusiveness by consulting AEs, the Warsaw International Mechanism for L&D and specialised technical groups (III Strategic Objectives / IV Strategic Priorities, 4.2).
- Moreover, the GCF should consider ***integrating L&D in readiness activities***. Potential measures through the GCF's Readiness Programme may include: a) readiness funding for comprehensive risk assessments related to L&D, b) capacity building in areas relevant to L&D, c) knowledge-sharing among AEs and NDAs on L&D, d) project preparation for L&D-relevant activities

3. <u>Enhancing the Paris-alignment/the paradigm-shift in GCF operations</u>

- We continue our strong ***support for more paradigm-shifting results of the GCF in mitigation and adaptation.*** In this vein, we consider it key to maintain the balance between adaptation and mitigation in grant equivalence. (III Strategic Objectives)
- In order to further accelerate the paradigm-shift in GCF operations, we consider it critical to ***enhance GCF's definition of Paris-alignment within its operations***. We therefore call for concrete definitions of how the GCF's operations contribute to the paradigm shift. In this vein, the ***GCF should further develop including through its strategic objectives, programming targets and sectoral guidelines***, clearly outlining how **each sector** should contribute to the paradigm-shift and formulating concrete benchmarks/requirements which GCF operations need to fulfil in order to be considered "paradigm-shifting".
- ***Paradigm-shift in Forest Finance***: Given the importance of forests for both, mitigation and adaptation, further accelerating the paradigm-shift in GCF's forest-related activities is particularly relevant. The GCF should explore the potential for ***a programmatic focus on forest finance*** (IV Strategic Priorities). In this vein, GCF should ***further develop and diversify GCF forest funding instruments***, with funding instruments tailored to the capacities of recipient countries. This should include but go beyond results-based finance instruments (e.g. REDD+). ***Additional measures may include***: support for readiness/capacity conditions; investments into low-carbon land use; supporting actors that do not have access to forest-related carbon market access, yet; explore programmatic (non-market) approaches to tackle drivers of unsustainable practices (e.g. by supporting governance, land use planning, alternative income approaches).

4. <u>Improving access and country ownership</u>

- ***Further strengthening direct access***: While funding channelled through DAEs has increased from 12% to 23%, the share of DAEs in GE terms in overall portfolio is still only at 17%. GCF should therefore further strengthen direct access, building on lessons learned from enhanced direct access pilot as well as consultations with stakeholders. As already requested in the USP, USP-2 should ensure IAEs' support to DAEs, including with regard to reporting requirements of IAEs to the Board, which should comprise qualitative reporting – instead of quantitative reporting only. (IV Strategic Priorities, 4.1 and 4.4).
- ***Enhance external and internal capacity-building***: DAEs, NDA and other stakeholders from developing countries need to be better supported in 'getting ready' for GCF. Readiness Programme and Project Preparation Facility are good programmes, but they are still complicated to access and remain disintegrated. We would like USP-2 to contain a commitment on linking those programs better and embedding them into a GCF policy-framework (V Operational and institutional priorities). Similarly, the GCF needs to continue reviewing and improving ***its own capacities***, in particular of the Secretariat, in areas such as private sector engagement,

financial intermediation and operations with a diverse number of financial instruments (V Operational and institutional priorities, 5.2)

- ***Continue engagement on regional presence***: We believe that a stronger regional presence of the GCF would facilitate the communication/interaction between DAEs and NDA on the one hand and GCF on the other. USP-2 should therefore commit to moving GCF's regional presence forward, with a view to operationalize GCF's regional presence in due course. (V Operational and institutional priorities).
- ***Simplified Approval Process***: The GCF should strive continuously to further facilitate processes and identify areas where access can be improved. Full-scale implementation of the new Simplified Approval Process (adopted at B.32) should be a key priority for the GCF. This should include a regular, critical review of SAP, elaborating to what extent SAP is meeting its objectives and to what extent further adaptations to the SAP are necessary.
- ***More (flexible) forms of partnerships within the GCF***: The GCF should explore more ways to build partnership models providing targeted support, e.g. from IAEs or others instruments to support national or regional entities in the accreditation process but also to increase the implementing capacity of DAEs.
- ***Improving country ownership***: GCF should build capacities among DAEs towards country programming and portfolio management earlier on in the accreditation process. In this vein, further Board-discussions should be held on how to align the need for scaled-up ambition at global level with country-driven programming. (IV Strategic Priorities)
- ***AE network***: GCF should strengthen networking among AEs, thereby facilitating knowledge-sharing.

  We note that the accreditation strategy is still under discussion for GCF-1 and further input would be developed depending on how this discussion evolves and decisions taken during GCF-1.

5. **<u>Further developing GCF's governance and policy framework</u>**

- ***Clarify and enhance the operationalization of USP-2***: Drawing from past experiences, there is a need to clarify how GCF's strategic vision can be translated into action more effectively. USP-2 should therefore identify timelines and milestones for the implementation of the various priorities. It should also clarify responsibilities for implementation between different institutional actors (Board, Secretariat, Committees). These points are critical for a stronger operationalization of USP-2, ***increasing the binding nature of the GCF's strategic vision***.
- ***GCF policy framework*****:** GCF should commit to establishing a coherent and formalised fund-wise policy framework in USP-2, building on the recommendations by the Secretariat as outlined in GCF/B.33/Inf.08 which we support. As the fund matures, it is essential that we reduce complexity and arbitrary nature of processes, including the format and implementation of policies and their interrelations within a policy-hierarchy (V Operational and institutional Priorities).
- ***Improve GCF board governance:*** In order to improve Board governance, simplify GCF's processes and strengthen the maturation of the fund, we consider the following points to be critical for USP-2, ideally in a separate section of the strategic document(V Operational and institutional Priorities):
  - Elements to allow the board to work as ***"one board"*** need to be identified, with a view to facilitate work across constituencies – a crucial factor for GCF's future success. This may include moving beyond existing informal structures which contribute to bloc-building (developing countries – developed countries) in the Board.
  - ***Intensify efforts for ensuring the guidance of the Governing Instrument on gender balance of the Board***, thereby improving governance issues. A proposal for future application for Board nominations should be presented well on time before the next round of nominations.

- *Increase attractiveness of the GCF for staff*, including through a critical analysis on disadvantages and advantages of the GCF as an employer.

6. <u>Private sector mobilisation:</u>

- Further ***develop, expand and diversify the financial instruments*** available to GCF (esp. expand to guarantees and foreign currency lending), with a view to improve mobilization of private capital (III Strategic Objectives / IV Strategic Priorities).
- ***"Balanced risk appetite"*:** we would like to see an ambitious, new, more transparent and dynamic project-based risk rating matrix, which enlightens project-level risks and their interdependencies (IV Strategic Priorities).
- ***Private Sector Strategy***: in USP-2, the GCF should ensure to review the implementation of the private sector strategy, including a critical assessment of its strengths and weaknesses. Importantly, this should encompass: a) analysis of the needs of accredited private entities, b) potential tools to overcome existing barriers to private entities' accreditation, c) proposals to support AEs in mobilizing the private sector (capacity building).