Tackling Climate Change Through Policy-based Finance: Options for the Green Climate Fund

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Colophon

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Disclaimer
The views expressed are those of the authors based on independent research and do not necessarily reflect those of the German Federal Ministry of Economic Cooperation and Development (BMZ).

Any mistakes remaining are those of the authors.
## Abbreviations

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
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<tr>
<td>AE</td>
<td>Accredited Entity</td>
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<td>AFD</td>
<td>Agence Francaise de Developpement</td>
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<td>AFDB</td>
<td>African Development Bank</td>
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<tr>
<td>AP</td>
<td>Adaptation Planning</td>
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<tr>
<td>B.30</td>
<td>Thirtieth Board Meeting of the Green Climate Fund</td>
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<td>CCPL</td>
<td>Climate Change Programme Loan</td>
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<td>CIFs</td>
<td>Climate Investment Funds</td>
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<td>DBP</td>
<td>Development Bank of the Philippines</td>
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<td>DBZ</td>
<td>Development Bank of Zambia</td>
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<td>DPF</td>
<td>Development Policy Financing</td>
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<td>DPO</td>
<td>Development Policy Operations</td>
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<td>DRM</td>
<td>Disaster Risk Management</td>
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<td>FAO</td>
<td>Food and Agriculture Organization</td>
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<td>FP</td>
<td>Funding Proposal</td>
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<td>GCF</td>
<td>Green Climate Fund</td>
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<td>GEF</td>
<td>Global Environment Fund</td>
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<td>GGGI</td>
<td>Global Green Growth Institute</td>
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<td>GHG</td>
<td>Greenhouse Gas</td>
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<td>IDB</td>
<td>Inter-American Development Bank</td>
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<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
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<tr>
<td>IRMF</td>
<td>Integrated Results Management Framework</td>
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<tr>
<td>JICA</td>
<td>Japan International Cooperation Agency</td>
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<tr>
<td>KFW</td>
<td>Kreditanstalt für Wiederaufbau</td>
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<tr>
<td>LDCs</td>
<td>Least Developed Countries</td>
</tr>
<tr>
<td>MDB</td>
<td>Multilateral Development Bank</td>
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NAMAs - Nationally Appropriate Mitigation Actions
NAP - National Adaptation Plan
NAPA - National Adaptation Programmes of Action
NDA - National Designated Authority
NDC - Nationally Determined Contribution
PAR - Programme Appraisal Report
PBF - Policy-based Finance
PBL - Policy-based Loan
PBO - Program-based Operations
PSSA - Project-specific Assessment Approach
UNFCCC - United Nations Framework Convention on Climate Change
SAL - Structural Adjustment Loans
SAS - Structural Adjustment Strategies
WBG - World Bank Group
RPSP - Readiness and Preparatory Support Programme
SAP - Simplified Approval Process
REDD+ - Reduce Emissions from Deforestation and Forest Degradation “plus”¹
RMF - Initial Results Management Framework
PMF - Performance Measurement Framework
SIDS - Small Island Development States
SF - Strategic Framework
UNDP - United Nations Development Programme
UNEP - United Nations Environment Programme

¹ “plus” meaning the role of conservation, sustainable management of forests and enhancement of forest carbon stocks in developing countries
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1. Introduction

The financing required to achieve the transformational change towards a net zero, climate-resilient economy will need to come from domestic and international, public and private sources (IEA 2021). Hereby the role of the public sector is key in stimulating and leveraging private investments, for instance, by creating an effective and enabling environment. This requires a rethinking of traditional project and programme investments and shifting towards a more holistic approach to improve the contribution of investment to economic, social and environmental welfare (Gordon 2002). To leverage available sources for climate investments, there is an urgent need to optimize policy, legal and regulatory frameworks (Kissinger et al. 2019).

As of January 2022, more than 130 countries have adopted net zero mid-century targets, covering three-quarters of global carbon emissions. However, only a few countries have a policy framework in place that would lead to zero emissions. A comprehensive climate change policy framework is a crucial driver for the transformational change towards a net zero and climate-resilient economy; it sets the target and guides the formulation of more specific policies and the development of policy instruments to achieve the desired outcomes. Effective policies alter the behaviour of public and private sector agents to address risks and return simultaneously, and in turn, risk and return affect investor decisions (Polzin et al. 2019). The objective of a net zero, climate-resilient economy needs fair, rigorous and transparent plans (Rogelj et al. 2021), with aligned policies and regulatory frameworks across countries to foster a coherent transformational change.

The development of these policies in developing countries can be supported by policy-based finance (PBF), initially defined as “the provision of balance of payments support in the context of a World Bank and IMF supported adjustment programme” or in aid statistics terminology as “programme aid” (Sandersley 1992). The development and implementation of transformational policies can be done through PBF as a dedicated instrument, but also indirectly as part of development assistance within projects. PBF takes a holistic approach with the aim of supporting systemic change and can thus, contribute towards a net zero, resilient economy. The financing of policies outside of PBF entails projects which often include a component where policy reform is achieved to improve the project outcome or long-term impact, though the development of a policy (framework) is not the primary goal.

The importance of developing and financing national policy frameworks that are addressing climate change accordingly is increasing continuously. Especially since the adoption of the Paris Agreement in December 2015 (UNFCCC 2015), all Parties\(^2\) are responsible to take policies and measures in order to achieve to the overall objectives of the Paris Agreement (limiting the long-term global temperature rise; adaptation; redirecting financial flows) and ultimately the objective of the UNFCCC (prevent dangerous climate change) (UN 1992). The operational architecture of the Paris Agreement is fundamentally grounded in Nationally Determined Contributions (NDCs).

Mandated to support developing countries raise and realize their NDC ambitions towards low-emission, climate-resilient pathways, the Green Climate Fund (GCF) plays a vital element within the UNFCCC and the Paris Agreement. The GCF is the world’s largest dedicated multilateral climate fund. It was created under the financial mechanism of the UNFCCC in 2010 (and became operational in 2015) to channel a large share of the 100 billion USD of climate finance that developed countries pledged to mobilise annually by 2020 to support developing countries with adaptation and mitigation. The GCF pursues a country-driven approach to promote and strengthen engagement at the country level (Antimiani et al. 2017; \(^\text{2 Representing 197 member Parties of the UNFCCC. See } \text{https://unfccc.int/process/parties-non-party-stakeholders/parties-convention-and-observer-states (Assessed online 26 January 2022)}\))
Zamarioli, Pauw, and Grüning 2020). With its governance structure and its function as operating entity in accordance with Article 11 of the UNFCCC to support projects, programmes and policies and other activities in developing country Parties, the GCF is an important vehicle to foster a sound regulatory environment through climate change policies.

Although the GCF is not explicitly mandated to offer PBF as a dedicated policy support instrument, its current funding proposal structure and its readiness and preparatory support programme allow the GCF to support policy development. This report reviews the GCF’s practice in more detail and elaborates on opportunities to strengthen country support for financing the development and implementation of policy.

The remainder of this report is structured as follows. Section 2 elaborates on financing dedicated to developing policies in developing countries, in particular the difference between financing for policies and policy-based financing (PBF) as a specific instrument. Section 3 analyses GCF’s current support for policy development and implementation within its current funding structure. Section 4 focuses on whether and how PBF financing could be adopted and implemented within the GCF financing framework. The report concludes with an outlook on how the GCF might consider PBF in the mid- to long-term, and the implications for the broader financial system.

2. Financing the development of policies

In 2007, the influential Stern Report called climate change the “greatest market failure in history” (Stern 2007). This unique challenge especially requires the channelling of funding from developed to developing countries for them to achieve the goals set in the Paris Agreement and address climate change. The public sector has a key role in stimulating and leveraging private investments in low-carbon and climate resilient development by creating an effective enabling environment. The public sector should also make investments in development that is not carbon-intensive or reduces resilience. The challenge of creating an effective investment environment lies in its complexity as it touches on the one hand, a range of market imperfections and barriers, and, on the other hand, on different cross-sectoral policy areas, such as fiscal, public-sector management, energy, environment, labour, etc. This requires moving beyond traditional investment facilitation, towards a holistic approach to enhance the contribution of investment to economic, social and environmental welfare (Gordon 2002).

International donors support developing countries in developing policies and institutional actions that promote sustainable development. Such development is supported by policy-based finance (PBF) as a dedicated instrument, but also as parts of development assistance within projects. PBF has a more holistic approach with the aim to support systems change, keeping in mind the long-term interconnectedness of climate, social and economic challenges, necessary to overcome the fragmentation and silo planning processes of policies. On the other hand, development projects can also include a component in which policy reform is achieved to improve the project outcome or its long-term impact, though policy development is not the primary goal. As this chapter will explain, both financing options have been by used by multilateral development banks (MDBs) in the context of aiding developing countries, but often with slightly different nuances. International climate funds also typically offer financing of policies as part of development assistance.

The objective of this section is to provide an overview of the common features and differences in the use of the PBF instrument, the lessons learnt from its use, as well as the financing of policies as part of development assistance.
2.1 Support for policy development though Policy-based financing (PBF)

In the early years of the World Bank’s operations, the link between policy frameworks and country development was not as strong. Lending was not primarily considered as an instrument for implementing policy reform (Dubey 1985). This view changed with the deteriorating economic situation of the 1970s and early 1980s, when it was evident that aid for projects did not produce the expected benefits in poor policy environments (Dubey 1985). In addition, developing countries struggled to service their debts and forced international finance institutions to reconsider their approach. Thus, institutions such as the International Monetary Fund (IMF) and the World Bank broadened their perspectives from project-based finance to include policy-based finance, and implemented reforms in parallel to rescue packages to improve the policy environment in which projects were being developed (Omprasad 2016).

For instance, the World Bank assisted developing countries in their balancing of payments through Structural Adjustment Loans (SAL). This tool allowed for rapid disbursement of funds to aid in macroeconomic adjustment policies, though later it shifted onto other sectors and goals (Omprasad 2016). Preconditions within these programmes were related to liberalising market forces through freeing foreign trade and currency exchange, and cease heavy government intervention in the economy (Heidhues and Obare 2011). Critics of these programmes underscore the fact that reforms did not take into consideration context-specific characteristics, such as institutional weaknesses and political implications of the reforms, as well as the social aspects of development, thus making the Washington Consensus development an “overly economic approach, characterised by excessive conditionality as well as the absence of genuine ownership by the countries concerned” (Heidhues and Obare 2011). Thus, these reforms were not very effective in stimulating economic growth and reducing poverty. Debates on the effectiveness of these reforms are still ongoing.

Nevertheless, throughout the 1990s and afterwards, policy programmes have started to integrate the lessons learned from the previous decades by taking into consideration the social dimension of development and the role of the state (Heidhues and Obare 2011). Objectives have become more social in nature, targeting long-term structural, institutional, and sectoral issues, such as reducing poverty and building institutions (Koeberle 2003). More specifically, the World Bank’s adjustment lending has become “quick-disbursing policy-based financing” to 1) serve as a cushion against economic shocks; 2) provide external financing to trigger local funds in support of government development programmes, thus promoting country ownership; and 3) encourage policy reforms (Koeberle 2003).

**Common features and differences**

Today, PBF serves as an instrument to promote (sectoral) policy reforms, which can help to improve the general conditions for sustainable development in partner countries, also with the aim to create more favourable investment environments. It is primarily offered by multilateral and bilateral development banks (Heidebrecht and Kemper 2018).

The way PBF is defined and implemented can vary across institutions (see Table 1), however, the main common features are:

- **Conditionality:** generally present in loans where disbursement is conditional on policy actions (König, Club, and Apampa 2020). The aspect of conditionality is present throughout almost all institutions, both in the 1980s and in current programmes.

- **Programme structure along a policy matrix:** PBF programmes are traditionally structured through policy matrices with clear objectives and one or multiple phases, with financing tranches at the
end of each phase. The accomplishment of specific targets generally triggers the next disbursement (Heidebrecht and Kemper 2018).

- **Technical assistance**: programmes are typically accompanied by technical assistance to ensure government is able to implement policy reforms (Guérin 2013).

- **Short duration**: policy-based programmes are not long term – they are implemented in two to three years on average (Guérin 2013).

- **Disbursement and implementation**: funds are channelled such that they directly increase the budget of the recipient country and programmes are generally implemented by technical (line) ministries, while coordinated by ministries of finance or planning (Guérin 2013).

- **Country ownership – government institutions**: close and constant policy dialogue between the governments of recipient countries and financial institutions is essential for the success of PBF programmes (Omprasad 2016). Countries seeking to obtain support for policy and institutional development are required to approach institutions on their own initiative and show that such policy reforms align with national strategies and development plans (Heidebrecht and Kemper 2018). Moreover, countries generally need to demonstrate commitment to carry through the policy matrices developed from these discussions, independent of election cycles (Omprasad 2016).

- **Financing instrument**: PBF is based on different instruments to structure the financing, which can take the form of loans, credits and guarantees. In line with the selected financing instrument, the policy-based finance is then referred to policy-based loan, if the financing is structure by a loan.
<table>
<thead>
<tr>
<th><strong>Name</strong></th>
<th><strong>Type of financial instrument</strong></th>
<th><strong>Features</strong></th>
<th><strong>Project examples</strong></th>
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</thead>
<tbody>
<tr>
<td>WBG</td>
<td>Development Policy Financing (DPF)</td>
<td>Loans, Credits, Guarantees</td>
<td>Panama: Development Policy Financing (100m USD, conc. loan) (World Bank 2022) Support overall government objective of increasing fiscal space, strengthen fiscal management, enhance transparency, improve efficiency of public spending and strengthen social programs. The operation is envisaged in the Country Partnership Strategy.</td>
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<td>Development Policy Operations (DPOs)</td>
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<td>Structural Adjustment Lending (SAL)</td>
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<td>Sector Adjustment Strategies (SASs)</td>
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<td></td>
<td>Loans, Credits, Guarantees</td>
<td>Financing conditional on the country’s real commitment to sustain its macroeconomic policy framework, the adequate implementation of the reform programme, and the completion of the policy and institutional actions previously agreed upon with the Bank (World Bank Group 2021) Has a set of programmes and operations under the Development Policy Financing (DPF) instrument, which can take on the form of loans, credits and guarantees</td>
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<tr>
<td>KFW</td>
<td>Policy-based Finance (PBF)</td>
<td>Guarantees, Grants, Loans, Debt service subsidies, Often paired with technical assistance</td>
<td>Peru: Support to back reforms in the sustainable urban transport sector (100m EUR, conc. loan) (Heidebrecht and Kemper 2018) Efforts planned include measures to limit pollutant emissions from private vehicles, to better coordinate public transport, and to promote non-motorised transport. The PBL project is a supplement to KfW investment finance packages in the transport sector that are being implemented in parallel.</td>
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<td></td>
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<td>Aims to incentivise countries to improve their policy framework by linking payments to the implementation of policy reform (König, Club, and Apampa 2020) Financing instruments include loans, credit and guarantees, though generally the financing is channelled through loans, and is often paired with technical assistance</td>
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<td>IDB</td>
<td>Policy-based Loans (PBLs)</td>
<td>Multi-tranche policy-based loans, Programmatic policy-based loans lending</td>
<td>Barbados: Sustainable Development Policy Program (100m USD, programmatic PBL) (IDB 2022) The operation is the second of three consecutives to improve country’s governance for sustainability through strengthening and modernization of the regulatory framework. To improve: i) efficiency and sustainability of spatial planning, development control and water resource management; ii) natural asset management; and iii) disaster risk management and resilience</td>
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<td>Categorizes all policy operations under the umbrella term Policy-Based Loans (PBL), defined similarly to the World Bank</td>
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<td>The funding aims to provide support for policy and institutional changes and could be restricted to a particular sector or subsector (Inter-American Development Bank 2021) Borrowing country is required to have an adequate macroeconomic policy framework, determined as such by an independent assessment by the IDB Instruments take the form of multi-tranche lending or programmatic lending</td>
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<td>AfDB</td>
<td>Program-based Operations (PBOs)</td>
<td>Budget support (general / sector / crisis response budget support)</td>
<td>Seychelles: Inclusive Private Sector Development and Competitiveness PBO-II (7.1m UAC, budget support loan) (African Development Bank 2019) 2nd phase of reforms to address key constraints to private sector development (domestic SMEs), including measures to improve</td>
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<td>Fast-disbursing financing instruments provided to the national budget in the form of loans or grants, to address actual, planned or unexpected development financing requirements of its Regional Member Countries, together with associated policy dialogue and economic and sector</td>
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**Table 1: Different names for PBF and types of financial instruments used by international finance institutions (exemplary)**
<table>
<thead>
<tr>
<th>Name</th>
<th>Type of financial instrument</th>
<th>Features</th>
<th>Project examples</th>
</tr>
</thead>
</table>
| ADB    | Policy-based Loans                                                | • Balance of Payments support (import support)  
• Programme appraisal report (PAR) will define specific loan/grant conditions for the PBO programme, guided by prior analytical work (analyses of economy/sector-wide policies and institutions, poverty and social impacts of proposed policies, environment governance, accountability systems, etc.)  
• Project examples:  
  - Cook Islands: Disaster Resilience Program (Phase 2) (10m USD, loan) (ADB 2019)  
    Support for policy actions in disaster risk management (DRM) and provision of contingent financing for timely disaster response and early recovery activities  
    Second phase of programme to help manage fiscal risk from disasters triggered by natural hazards |                                                                                                                                                                                                                     |
|        | Policy-based Lending Operations                                  | • Policy-based Loans  
• Stand-alone policy-based lending  
• Policy-based guarantee  
• Special policy-based lending  
• Subnational policy-based lending  
• Sovereign budget support  
• Sovereign guarantee  
• (Sub-) national sector policy lending  
• Categorises sovereign budget support and sovereign guarantee to support policy reform as PBL.  
• Can include introduction or revision of laws, regulations, and policies, as well as capacity strengthening within institutions (Asian Development Bank 2021).  
• Categorises its PBL operations as either conventional (stand alone or programmatic approach), or crisis response (special PBL or through a Countercyclical Support Facility) (Asian Development Bank 2021). |                                                                                                                                                                                                                     |
| JICA   | Climate Change Programme Loans (CCPL)                            | • Provision of loans similar to PBL thorough their Climate Change Program Loans (CCPL), which aims to implement climate change policies through financial and technical assistance aligned with the recipient country’s national development strategies (JICA 2015)  
• Implementation of instruments through public policy matrices to be achieved in multi-year pillars. |                                                                                                                                                                                                                     |
| AFD    | Appui budgétaire climat (Climate budgetary support)              | • Loans  
• Employment of instruments through public policy matrices, to be achieved in multi-year pillars. | Indonesia: Climate Change Programme Loan (1.9 billion USD) (AFD 2014)  
Both agencies in collaboration provided budgetary assistance to the Government of Indonesia to support climate change policy implementation.  
Funds were channelled untargeted into annual state budget but released on a yearly basis pending on performance checks on the agreed-upon implementation of policies (policy matrix) |
Lessons learnt from financial institutions

The literature on PBF suggests the success of policy reform programmes mostly depends on political-economy variables, such as whether the country has a politically stable, democratic government with a low degrees of ethnic fractionalization (Dollar and Svensson 2000) and a high degree of ownership and commitment (Omprasad 2016). In fact, a small number of political economy variables can predict the outcome of an adjustment loan accurately around 75 per cent of the time (Dollar and Svensson 2000).

These findings are reflected in current practices by international finance institutions, such as the World Bank and KfW, before carrying out PBF programmes; they typically assess the policy and institutional framework of the country in order to determine whether a PBF programme is the best instrument of choice (Heidebrecht and Kemper 2018). This is done to ensure programme success. Weak capacities and low law enforcement of recipient countries inevitably affect the manner in which policy development is implemented, and could compromise programme implementation (World Bank Independent Evaluation Group 2016). For instance, in countries with high poverty rates, support for climate change policy reform is difficult to obtain, unless the policies implemented simultaneously alleviate the poor economic context (World Bank Independent Evaluation Group 2016).

This goes hand-in-hand with the need for a strong commitment on the part of the partner government to make reforms within an overarching national policy framework as the base of support for the PBF measures. The partner country must be in the lead for both the development and the implementation of the PBF, with donor institutions providing support in the form of short-term consultancy inputs – often based on experiences, policy dialogue and financing (Heidebrecht and Kemper 2018).

Challenges in implementation could arise due to poor preparation from both financial institutions and countries, and especially if the financing institution does not have in-depth, prior knowledge of the country context, strong institutional relationships, nor extensive knowledge of sector in which the programme will be implemented (World Bank Independent Evaluation Group 2016). If discussions between the parties are not thorough enough beforehand, there could be potential conflict when expectations from long-term results of the programme are misaligned, and potential tensions and trade-offs were not foreseen.

For these reasons, PBF is primarily offered by multilateral and bilateral development banks and concentrated in middle income countries with robust institutions and stable governments, and thus, higher capacity to implement reforms independent of the diverse political and socio-economic fabrics. Programmes can also be implemented in low income countries where governance and institutions have shown to be robust enough (König et al. 2020).

2.2 Supporting policy finance as part of development assistance

Not all financing of policies is categorised as PBF. There are interdependencies between policy goals, implementation instruments and the effectiveness of projects, projects also being a crucial factor for the successful implementation of policies (Kapsali 2011). Thus, development projects often include a component in which policy reform is achieved to improve the project outcome or long-term impact, though policy development is only a secondary goal. Such projects can be financed through grants (for instance, in the form of capacity building and technical assistance), as well as loans, guarantees, among others.

This can be seen in the aforementioned institutions, but is also often the case in the context of climate finance institutions, where PBF as an instrument is not generally used. It is common among international climate funds such as the Global Environment Fund (GEF) and the Climate Investment Funds (CIF), to finance policy support through grants and technical assistance. Among these institutions dedicated to
providing financing for climate, the policy reform component generally depends on the overall programme objective. For example, in 2017, the GEF implemented a technical assistance project aiming to strengthen policies, laws and criminal justice capacities to address poaching and illegal wildlife trade within five countries in Africa (GEF 2020). Targeting the biodiversity sector and implemented through the Ministries of Environment of the target countries, the project is currently enhancing policy and legal frameworks regarding conservation and crime, as well as strengthening national capacities on combatting wildlife crime.

The CIFs have used a similar approach with a focus on climate change. For example, the CIFs disburses financing through grants to provide technical assistance at a national level, for instance in the project “Technical Assistance for the Development of a Climate Resilience Policy and Strategy and Drought Insurance Products for the Arid and Semi-Arid Zones of Southern and Central Parts of Mozambique” (African Development Bank 2021). The project targets the water sector and aims to strengthen the resilience of communities in arid and semi-arid areas, as well as build capacity within government institutions to develop climate resilient programmes in the southern areas of Mozambique. This will be achieved through the development of Climate Resilience Policy and Strategy for the region, as well as through Climate Resilience Studies and Market Assessments that will contribute to the development of Drought Insurance Financing products (African Development Bank 2021).

Similarly, the GCF’s support for financing policies does not include the use of PBF instruments. Instead, its policy development is included in its funding proposals and readiness support, explained in more detail in the next section.

3. Supporting policy development within the GCF

In order to analyse if and how PBF as a dedicated policy support instrument could be adopted and implemented by the GCF, it is important to understand the GCF’s current support for policy development and implementation within its current funding structure. To date, the GCF approaches policy reform and development as optional elements in funding proposals (FPs and proposals submitted under the simplified approval process SAPs) and the GCF Readiness and Preparatory Support Programme (RPSP).

3.1 Strengthening and development of policies through GCF funding proposals

Support for policies through funding proposals generally comes from project components that aim to improve the target country’s institutional and policy framework, producing an enabling environment for successful projects. For instance, the GCF Board approved funding proposal FP010 in 2016 in Armenia for improving energy efficiency through building retrofits, including a component on policy de-risking. The GCF provided a grant of USD 890,000 to support public instruments for the promotion of investments in energy efficiency, ongoing legal reform in energy efficiency, and the creation of an enabling policy framework for energy efficiency retrofits in residential buildings (GCF 2016).

Accessing the GCF through funding proposals

To discuss if and how PBF could be adapted within financing activities through funding proposals, the subsequent paragraph shortly elaborates on how funding proposals are developed and financed, as well as it elaborates on the involved partners. The financial instruments deployed in the GCF portfolio include (non-) reimbursable grants, (senior and subordinated) loans, equity, result-based payments (REDD+), and guarantees, with a strong bias towards loan and grant funding. As of the 30th Board Meeting (B.30), the
GCF has approved in total 190 FPs/SAPs with a commitment of USD 10 billion. In total, 42% of the GCF financing is disbursed as grants and 44% as loans.

It is not possible so far to apply and implement projects/programmes through a project-specific assessment approach (PSSA), FPs/SAPs can only be submitted by Accredited Entities (AEs). AEs can be private (e.g. Deutsche Bank AG) or public (e.g. Ministry of Water and Environment, Uganda), non-governmental (e.g. World Wildlife Fund), sub-national, national (e.g. Fiji Development Bank), regional (e.g. Caribbean Development Bank) or international (e.g. European Investment Bank), and have to be accredited to develop, submit, manage and monitor projects and programmes. To date, 113 AEs are accredited, half of them being a direct national AE mainly from the financial sector. The GCF’s accreditation process assesses the AEs’ capacity to meet the GCF’s basic and applicable fiduciary standards for the intended project size, type, financing instrument and risk category, as well as the capacity to manage relevant environmental and social risks, and to ensure gender equality and empowerment throughout project design and implementation (Green Climate Fund 2014). Thus, accreditation determines the types of proposals that are submitted.

**GCF’s approach to measure policy support**

The GCF’s approach to assess how its investments deliver climate results and how the results contribute to the overall objectives of the GCF to promote a paradigm shift towards low-emission and climate-resilient development pathways in the context of sustainable development, is set out in the integrated results management framework (IRMF). The IRMF, approved at B.29 (Decision B.29/01), is based on the initial results management framework (RMF) and includes three levels of results measurement:

(a) **GCF impact level – paradigm shift potential.**

(b) **GCF outcome level** comprising (IRMF core indicators 1-4, quantitative indicators)

   (i) reduced emissions and increased resilience (impact potential) and

   (ii) **enabling environment** (e.g.) measure how GCF projects/programmes have contributed to creating enabling conditions and environments for paradigm shift in a country-driven manner and are derived from activity-specific sub-criteria of paradigm shift potential in the initial investment framework; and

(c) **project/programme level results** (IRMF core indicators 5-8). This includes core indicator 5, the **Degree to which GCF investments contribute to strengthening institutional and regulatory frameworks for low-emission climate-resilient development pathways in a country-driven manner** (IRMF, GCF/B.29/14). An illustrative guiding sheet of the planned details and technical guidance on the IRMF application has been presented at B.28 (Annex V GCF/B.28/09). Once implemented, the IRMF will enable to analyse in depth the GCF’s contribution.

For a review of the already approved FPs/SAPs, this analysis is based on the mitigation and adaptation performance measurement frameworks (PMFs) and RMF. PMF and RMF are the predecessors of the IRMF.

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3 Incl. 23 projects/programmes applied via the Simplified Approval Process (SAP), characterized by a smaller funding volume of up to USD 10 million (without Co-Finance).


5 Currently, the GCFs follows an institutional approach. After accreditation, accredited entities can submit funding proposals within their scope of accreditation. The project-specific assessment approach (PSSA) represents a complementary approach that would allow the GCF to target specific projects. A PSSA would require a review of the proposed project AND the entity’s capacity to deliver it.

6 Core Indicator 6: Degree to which GCF investments contribute to technology deployment, dissemination, development or transfer and innovation; Core Indicator 7: Degree to which GCF investments contribute to market development/transition at the sectoral, local, or national level; Core Indicator 8: Degree to which GCF investments contribute to effective knowledge generation and learning processes, and use of good practices, methodologies, and standards.
and were authoritative at the time of the project application. Within the PMF, indicators serve as the basis for measuring mitigation and adaptation paradigm-shift results (Integrated Results Management Framework 2021). Within the set of pre-defined project outcomes, indicator 5.1 corresponds to activities aiming to strengthen institutional and regulatory systems at the project level as shown in Table 2. This indicator is part of the FP/SAP proposal template.

Table 2: Outcomes at project level – GCF funding proposal template

<table>
<thead>
<tr>
<th>Expected result</th>
<th>Indicator * = Core</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.0 Strengthened institutional and regulatory systems for low-emission planning and development</td>
<td>☐ 5.1 Institutional and regulatory systems that improve incentives for low emission planning and development and their effective implementation</td>
</tr>
<tr>
<td></td>
<td>☐ 5.2 Number and level of effective coordination mechanisms</td>
</tr>
</tbody>
</table>

Note: In the IRMF the wording in the funding proposal template changed to: “Core Indicator 5: Degree to which GCF investments contribute to strengthening institutional and regulatory frameworks for low emission climate-resilient development pathways in a country-driven manner” (GCF Funding Template, last update 17 January 2022). Section renamed to E.4. GCF Outcome level: Enabling environment). The GCF requests AEs to select at least two out of the four enabling environment outcome indicators from the IRMF core indicators 5-8 as applicable. Source: Mitigation and adaptation performance measurement frameworks; IRMF, GCF/B.29/14.

Notably, funding proposals offer a wide range of activities - captured and elaborated differently under this indicator 5.1. For instance, some projects aim to introduce norms and standards through introducing operating procedures, such as FP012 (in Mali; led by the World Bank), which develops last-mile community warning systems, or the implementation of construction norms, such as FP133 (Antigua and Barbuda, Department of Environment, Ministry of Health and Environment), which updates building codes at the national level to ensure effective uptake across all future infrastructural developments. Other projects focus on the development of a sound legal systems for low-carbon energy projects, such as FP033 (Mauritius; UNDP) via building on legal texts and capabilities to effectively manage the evolution and growth of the renewable energy sector at centralised and decentralised scale. Furthermore, some projects focus on increased decision-making via regulatory frameworks for marginalized or underrepresented societal groups, such as FP058 (Ethiopia; MOFEC), which aims to increase the involvement of women in community-based and local government institutions by targeting a 50/50 representation.

Once the IRMF is implemented, a more granular analysis of the impact will be possible because a scorecard approach would be introduced (3-score scale: low; medium; high). This will help AEs gain an independent assessment of how GCF-funded projects/programmes are contributing to create an enabling environment. For the analysis below, the existence of activity 5.1 provides an indication on how actively AEs aim to deliver policy support.

Quantitative estimations of the policy support through funding proposals

To estimate the current support by the GCF for policy activities, all GCF proposals have been assessed by the dedicated sub-activity using a binary code. All FPs/SAPs stating a dedicated sub-activity for policy development with allocated budget and indicator linked to indicator 5.1 were coded with “yes”, while all others were coded as “No”. Unfortunately, analysing the share of the allocated budget for indicator 5.1 as a percentage of the total project budget is not possible due to inconsistencies in filling the application form. For this indicator, only a few projects provide a budget break-down by activity. Consequently, it is also not possible to analyse which of the GCF financing instruments is proposed by activity, but detailed in-depth assessments confirm that activities under indicator 5.1 are typically delivered via grant funding.

The subsequent analysis is based on the number of projects with indicator 5.1 as an explicit activity. Assessing all approved FPs/SAPs by the GCF Board as of B.30, the results show that overall, about 45% of the FPs/SAPs include indicator 5.1 (see Table 2) in their proposals. It can be stated that direct AEs (national
and regional) are slightly more prone to add indicator 5.1 in the GCF funding proposal form compared to International AEs (see Figure 1a). A core GCF principle is to follow a country-driven approach, which means that developing countries lead the country programming, consideration of executing entities, enhancing of capacities and ultimately coordinate in-country GCF involvement and monitoring of impacts (Zamarioli, Pauw, and Grüning 2020). Typically, national and regional AEs are more involved and cross-linked in national affairs. In line with a country-driven approach and a high degree of country ownership, direct AEs may be more in the position to develop, outline and implement policy reforms compared to (large) international AEs, as they have a different institutional structure, different portfolio distribution, and are less rooted in recipient countries.

With respect to the regional distribution, GCF priority regions (African countries, Least Developed Countries (LDCs) and Small Island Development States (SIDS)) use the policy indicator significantly more often compared to non-priority countries (see Figure 1b.). From a decision-maker’s perspective, the focus on policy reforms in priority countries is consistent with the positive relation that countries with better policy frameworks have higher investment efficiency (World Bank Group 2017). For instance, industrial policy frameworks for enhancing productive capacities (e.g., reduce market failures and strengthen economic linkages) is critical for sustainable growth, especially for priority regions (UNCTAD 2021). However, policy reform in this context is developed and implemented to address specific gaps only. Policy reform at a larger scale is typically implemented in middle income countries with more robust institutional infrastructures, among other characteristics, as discussed in the previous section. With respect to the project type, the share is higher among public sector projects (47%) compared to private sector projects (38%), which appear as more hesitant to address policy reforms as indicated in Figure 1c.

Finally, the analysis by result area theme shows that there is no significant difference in the share of project funding allocated to policy support between mitigation and adaptation projects.

Figure 1: Share of funding proposals with indicator 5.1 - Institutional and regulatory systems that improve incentives for low emission planning and development and their effective implementation - by Type of AE and region

<table>
<thead>
<tr>
<th></th>
<th>Accredited Entity</th>
<th>Priority Region</th>
<th>By Type</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Direct</td>
<td>International</td>
<td>Non-Priority</td>
</tr>
<tr>
<td>Yes</td>
<td>21</td>
<td>65</td>
<td>29</td>
</tr>
<tr>
<td>No</td>
<td>23</td>
<td>81</td>
<td>46</td>
</tr>
</tbody>
</table>

Note: FPs/SAPs (n=190; incl. B.30) have been assessed in this analysis. Orange (green) bars shows sum of projects excluding (including) indicator 5.1 in the GCF funding proposal by a.) Accredited Entity, b.) Priority Region, and c.) Type.
3.2 Strengthening and development of policies through readiness support

In addition to policy support within Funding Proposals, the GCF is mandated by the Governing Instrument via the Readiness and Preparatory Support Programme (RPSP) to help developing countries strengthen their institutional capacities, governance mechanisms, as well as their planning and programming frameworks (e.g. preparation of National Adaptation Plans - NAPs) in order to determine a climate action agenda (Green Climate Fund 2020a).

**Accessing the GCF through the readiness and support programme (RPSP)**

Funded activities under the RPSP benefit from grants (e.g. for technical assistance). Readiness proposals can only be submitted by National Designated Authorities (NDAs) and/or Focal Points (FPs). NDAs are government institutions that serve as an interface with the GCF to provide broad strategic oversight of the GCF’s activities in the country and communicate the country’s priorities for financing low-emission and climate-resilient development. NDAs can apply for up to USD 1 million per country per year for support related to institutional capacity building, coordination, policy and planning, and programming for investment, or for up to USD 3 million overall per country for the formulation of NAPs, Nationally Appropriate Mitigation Action (NAMAs), or National Adaptation Programmes of Action (NAPAs), and/or other related planning processes.9

The Readiness Programme Strategy 2019-2021 puts a focus on capacity for climate finance coordination, strategic frameworks for low-emission investment, strengthening adaptive planning, and paradigm-shifting pipeline development. In fact, Objective 2 of the Readiness Programme Strategy 2019-2021 titled ‘Strategic frameworks for low-emission investment’ aims to improve the enabling environment for climate finance, developing or enhancing frameworks to address policy gaps (Green Climate Fund 2020a).

RPSP is a tool for the GCF to support policy development, for instance, for adaptation planning processes. This reflects Article 7 of the Paris Agreement on adaptation, which is about “enhancing adaptive capacity, strengthening resilience and reducing vulnerability to climate change”. In 2020, the GCF approved such a programme for Guinea with the goal of mainstreaming climate change adaptation into developing policies. The programme addressed barriers such as the absence of links connecting research and policy in order to inform decision-making processes (Green Climate Fund 2020b). Another example of GCF policy support through RPSP was the introduction of a paradigm shift in the Bangladesh’s policy framework on green banking for Shariah Based Banks and Financial Institutions (approved in 2019). The outcome of this programme was the drafting of an evidence-based policy framework on shariah-based green financing and an updated environmental and social risk management framework for the central bank, commercial banks and financial institutions (Green Climate Fund 2019).

**Estimating the policy support through the Readiness Programme**

The above-mentioned examples illustrate that the GCF is already providing support for policy development. Nevertheless, it is noticeable that significantly less funding is spent for the RPSP compared to FPs (projects and programmes). To date, USD 348 million has been channelled for readiness activities

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7 The governing instruments defines the GCFs mandates and working methods. It was approved by the 17th COP in Durban, South Africa. at its seventeenth session on 11 December 2011 in Durban, South Africa.

8 As a result of decision B.22/11, the Board authorized the Secretariat to consider “multiple-year strategic Readiness implementation requests”. This allows NDAs to submit a single Readiness proposal for up to a total of USD 3 million over a maximum of 36 months, provided the annual implementation value remains under the USD 1 million per year cap referenced above. For more information on this modality, please see Annex IV.

9 See Readiness and Preparatory Support Programme Guidebook - A practical guide on how to prepare readiness proposals for the Green Climate Fund for further details.
through the RPSP, representing less than 4% of total GCF budget allocation, of which only USD 182 million has been disbursed as of January 2022.

Figure 2 provides an estimated overview of the RPSP by strategic area and funding volume. Most of the funding is allocated towards ‘Adaptation planning (AP)’, while the least funding is directed towards ‘Strategic frameworks (SF)’. Thus, policy support within RPSP focuses on adaptation planning, while all other policy areas relevant for sustainable transformation are yet not targeted by the NDAs. In addition, the delivery partners for the deployment of RPSP are majorly international organizations. The UNDP (around USD 80 million), UNEP (around USD 57 million), Food and Agriculture Organization (FAO, around USD 25 million), and the Global Green Growth Institute (GGGI, around USD 23 million) represent more than 50% of all RPSP financing. Therefore, the argument to maximize country ownership in projects and programmes and to follow a country-driven approach should also be considered within the GCF’s current RPSP activities.

It is important to note that providing policy support does not automatically translate into policy implementation. Therefore, although GCF provides financing for policy reform through the RPSP, ‘adaptation planning’ and ‘strategic frameworks,’ this may not directly lead to policymaking. Instead, their impact would need to be assessed on a case-by-case basis, depending on the type of project.

**Figure 2: GCF Readiness and Preparatory Support Programme (RPSP) by Activity and Region**

LATAM: Latin America and the Caribbean.

In summary, the GCF is already allocating funds to support policy development. Almost half of the FPs include a component in which policy reforms are envisaged to improve the project outcome. However, this supporting measure is not necessarily a systemic transformation with policy development as a primary goal. The same argument could be applied for the RPSP, where the GCF’s current support does not aim for a systemic transformation through policy development.
4. PBF as potential financing instrument for the GCF

As an instrument, PBF can make a significant and ambitious contribution to the global efforts towards attaining the goals set by the international community to combat climate change within the GCF. This support to national action could streamline the policy development process to foster positive environments for the development of climate projects and initiatives, beyond other project components within its funding proposals and its Readiness Programme (Zamarioli et al. 2021). In addition, the strengthening of policy frameworks could aid in the broader mainstreaming of climate considerations across the economy, effecting the shift of national finance flows towards low-emission and climate resilient activities. For example, by improving the economic and institutional context of the recipient country, as well as by increasing the transparency about public strategies and the accountability on its commitments. In this way, investments could be effectively de-risked, with direct effects for climate objectives and potential co-benefits for other development areas.

However, lessons learnt from implementing this instrument (Section 2) illustrate that PBF is best applied under certain common features. This serves as a basis for how PBF could be integrated in the current GCF structure and its programmes: i) introducing PBF as new financing instrument for FPs; and ii) RPSP (Section 3).

**Challenges in implementing PBF in funding proposals**

Introducing PBF as a new financing instrument for FPs has the advantage that the GCF could combine this new financing structure with the existing financing instruments (grant, loan, equity and guarantees), while adding common PBF features such as conditionality. The GCF also has experience with conditionality, e.g. through its REDD+ result-based financing instrument, which could also be extrapolated into a potential GCF PBF instrument. It should be noted that the GCF would need to make further adjustments, as the conditionalities required under the PBF instrument often touch on more politically sensible topics. Furthermore, FPs offer some degree of flexibility with respect to project volume, length/SAPs and disbursement schedules.

In the context FPs, a first challenge for implementation relates to country ownership, and the general notion that PBF programmes should be based on a strong commitment from the partner government and a clear national policy framework or strategy (Heidebrecht and Kemper 2018). As a foundation of support, PBF requires a strong government commitment to make reforms within an overarching national policy framework. Government institutions should therefore be heavily involved in developing and implementing FPs. This could be addressed through the GCF country programmes (e.g., RPSP), where countries are encouraged to drive their project and programme pipelines in collaboration with the Fund, aligned with the priorities identified in a country’s national climate plans or strategies.

Secondly, strong government commitment might pose a challenge for some countries. One of the core components of PBF programmes is the direct dialogue between the financing institution and the country government, and that financing flows from institutions directly into the national budget of the recipient country. In addition, the experience of implementing PBF underlines the importance of the partner country taking the lead. However, the GCF operates through an open partnership structure, where GCF financing flows through the AE, and then to implementing partners such as national governments, ministries, private sector actors or civil-society organisations. GCF’s unique approach as a partnership institution does not allow for direct dialogue with governments, and instead relies on Accredited Entities (AEs) and Nationally Designated Authorities (NDAs) to ensure country ownership. If a PBF instrument were to be developed, the submitting AE should preferentially be a public national AE to have the mandate and
knowledge on developing a relevant policy matrix. In addition, they should be able to assess and approve the funds accounted for in the recipient country's national budget.

Thirdly, there are to date only three public national AEs accredited for large projects, all from the financial sector. The analysis of the accreditation of public national AEs reveals that these AEs are often limited to smaller project sizes and basic fiduciary standards and/or grants. Indeed, out of the 114 AEs (up to B.30), there are only 22 national AEs, and 6 regional AEs endowed with the fiduciary standards to disburse grants and loans of the size larger 50 million USD. Out of this 22 AEs, only a couple are public sector actors such as the Development Bank of Philippines (DBP) or Zambia (DBZ). The national AEs from the private sector might not have the mandate or knowledge to offer the required country commitment and develop a policy matrix. Thus, even if the GCF would introduce PBF instruments in the short-term, only a small share of national AEs would be in the position to implement these instruments via projects or programmes that meet the common features elaborated in Section 2, such as strong country ownership, conditionality, programme structure along a policy matrix, financing volume, among others (see Table 3). The challenge could be addressed in the mid- or long-term, if countries strategically decide to accredit new AEs or re-accredit national AEs addressing these requirements. Since the selection of national AE candidates, the preparation of accreditation documents, and the completion of the actual accreditation process under the GCF takes between 2 and 5 years, a short-term or even mid-term solution to this problem would most likely not be possible.

**Challenges in implementing PBF within the Readiness and Preparatory Support Programme (RPSP)**

With regards to the RPSP, the consideration of country ownership for a PBF programme would be possible. Readiness programmes must be submitted by NDAs, which (often) have the mandate and knowledge on developing policy matrices and can steer the required country commitment. Content-wise, the objective of strengthening policy and planning within the RPSP also matches the aim of PBF to create more favourable investment environments and support sustainable development. However, under the current RPSP, the PBF programme would be limited to grant funding and to a maximum of USD 1 million per country per year for institutional capacity building, coordination, policy and planning, and programming for investment.

Secondly, as previously mentioned, only 182 million USD out of the 348 million committed RPSP has been disbursed until January 2022. In comparison, the average volume of PBF and the objective to holistically support a transitional change through policy reforms require certain funding volume (see also Table 1 above). Discussions on implementing PBF within RPSP would need to take place within the ambitions of the GCF to increase readiness activities but also address the maximum RPSP funding volumes per country.

**General challenges in implementing PBF (within the GCF)**

Additionally, overall challenges, irrespective of a whether PBF would be implemented through projects/programmes (FPs/SAPs) or readiness activities (RPSP), include:

- Firstly, there is a risk that the conditionality aspect of PBF can question national sovereignty. At recent GCF Board meetings, discussions indicated that the conditions imposed on the approval of some FPs touch upon the issues of country ownership and developing countries’ access to GCF financing. Per the Governing Instrument, the GCF is mandated to pursue a country-driven approach, as well as promote and strengthen engagement at the country level through meaningful engagement with relevant institutions and stakeholders (Governing Instrument of the GCF 2011). Policy discussions could quickly turn controversial, if countries feel too many conditions are preventing them from accessing finance. This is based especially on historical
precedent in which international development banks imposed structural adjustment programmes with sometimes damaging consequences (as mentioned in Section 2).

- Secondly, one of the main challenges of PBF implementation relates to weak capacity and enforcement of existing regulations, which is why financial institutions prefer to implement PBF with middle-income countries (see Section 2). However, the GCF is mandated, through one of its overall strategic objectives, to deliver balanced funding, as well as use minimum resource allocation floors for adaptation, taking into account the needs of developing countries particularly vulnerable to climate change, including least developed countries (LDCs), small island developing states (SIDS) and African countries (GCF 2020), only a minority of which are middle-income countries. Thus, programmes for policy development and implementation could be an additional instrument but would have a limited applicability in priority countries.

- Thirdly, PBF has historically been implemented for quick disbursements, triggered by specific policy objectives. To date, the GCF is still improving its efforts in accelerating its disbursement and implementation, especially within its Simplified Approval Process (SAP) and Readiness. Further improvement would be a prerequisite for an effective implementation of PBF.

- Finally, PBF to date is provided by multilateral and bilateral development banks, generally with national and regional offices to ensure a close relationship for its development and implementation. Based on this local knowledge and general experience in policy reforms, these institutions provide support in the form of short-term consultancy inputs and policy dialogue. Given the GCF’s mandate, its still-growing experience since it began operations in 2015, and its still limited presence at a country and regional level, the GCF may not be able to provide or ensure the necessary field presence.

Table 3 summarises the opportunities and challenges in introducing PBF under the current Governing Instrument and investment opportunities of the GCF.

**Table 3: Opportunities and challenges in introducing PBF in the GCF**

<table>
<thead>
<tr>
<th>Common PBF features</th>
<th>Opportunities</th>
<th>Challenges</th>
</tr>
</thead>
<tbody>
<tr>
<td>Conditionality</td>
<td>Conditionality can (technically) be implemented in FPs or RPSP</td>
<td>Limited experience with conditionality</td>
</tr>
<tr>
<td></td>
<td>Result-based payments for REDD+ already exist for FPs and they have conditionality aspects</td>
<td>Result-based payment schema differs by nature from the result-based approaches within PBF</td>
</tr>
<tr>
<td></td>
<td></td>
<td>PBF touches on politically sensitive topics which might cause conflicts of interest with country ownership</td>
</tr>
<tr>
<td>Programme structure along a policy matrix</td>
<td>NDAs as partners could potentially have the legitimacy, mandate, knowledge, strong institutional relationships, and extensive knowledge of the sector in which the programme will be implemented</td>
<td>Partners for PBF need to be governments. Structuring FP/SAP as PBF requires AE as partner, which might lack legitimacy, mandate and knowledge, or have an accreditation with low fid. Standards or small project size</td>
</tr>
<tr>
<td></td>
<td>Policy matrix can be a part of the country programme</td>
<td>Lack of GCF’s experience in developing policy reforms/matrix</td>
</tr>
<tr>
<td></td>
<td>PBF could aid in carrying forward the main mandate of the GCF</td>
<td>Lack of local and regional GCF presence</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Policy structure is typically negotiated with governments</td>
</tr>
<tr>
<td>Length</td>
<td>No problem</td>
<td>No problem</td>
</tr>
<tr>
<td>Disbursement and implementation</td>
<td>Targets could trigger the next disbursement</td>
<td>Challenges in disbursing and implementing funds quickly (based on current delays)</td>
</tr>
<tr>
<td></td>
<td>Can be accompanied by technical assistance</td>
<td></td>
</tr>
<tr>
<td>Preference for middle income</td>
<td></td>
<td>Does not correspond to the GCF priority group</td>
</tr>
<tr>
<td>Country Ownership – government institutions</td>
<td>Country ownership deeply embedded in governance structure of the Fund</td>
<td>PBF might raise concerns with country ownership aspect due to the conditionality of payments</td>
</tr>
<tr>
<td>--------------------------------------------</td>
<td>--------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>Finance instrument</td>
<td>Flexibility along all GCF financing instruments for FP</td>
<td>Limited on grants for RPSP</td>
</tr>
<tr>
<td>Financing volume</td>
<td>Technically no limitation on the project size for FPs</td>
<td>Indirectly affected by the project size for which the AE is accredited for FPs</td>
</tr>
<tr>
<td></td>
<td>Up to USD 1 million per country per year for support related to institutional capacity building, coordination, policy and planning, and programming for investment; or up to USD 3 million per country for the formulation of NAPs and/or other adaptation planning processes</td>
<td>Project volume limited for RPSP</td>
</tr>
</tbody>
</table>
5. Conclusions

Policy development and implementation in developing countries can be financed in multiple ways. PBF is a dedicated instrument for developing policy frameworks, aiming for a holistic approach to support systems change and to contribute towards a low-carbon, resilient economy. This report analyses whether PBF could aid in carrying forward the main mandate of the GCF.

This report demonstrates that the GCF is contributing to strengthening institutional and regulatory frameworks for low emission climate-resilient development pathways within approximately half of its projects and programmes (FPs). In addition, the GCF supports the strengthening of institutional and regulatory frameworks through the small grants provided as part of the Readiness and Preparatory Support Programme (RPSP), in particular for adaptation. Within both of these funding channels, PBF could potentially be included as a new financing instrument in the long term. However, in the short to mid-term, this report identified significant operational, political, and logistical challenges that reduce the potential of PBF for the GCF.

Regarding operational challenges, PBF within FPs would face obstacles through the current low number of available national AEs, given that country ownership and institutional capacity are important factors in achieving positive outcomes through design of policies, use of instruments. An alternative is to facilitate PBF in cooperation with international institutions. As illustrated in Section 2, PBF is already offered by various MDBs. Many of them are accredited as international AEs under the GCF, such as AFD, AfDB or ADB. PBF could therefore also be indirectly addressed in GCF co-financed projects. Targeted exchange and sharing lessons on PBF among development partners would be a critical starting point.

PBF could also be provided through the RPSP. However, the RPSP only provides grants of limited volume, and total grants per country are also limited, depending on whether the funding is for adaptation planning. The opportunity could be considered and elaborated on by including a focus on this topic when developing the next readiness strategy.

For both projects and readiness activities, political challenges would be mainly related to the sensitivities around PBF’s focus on changing policies in recipient countries. For example, the conditionality that is inherent to PBF should not go against the fundamental issue of country ownership. Discussions on imposing more conditions on potential PBF projects or programmes could turn tense within the Boardroom, especially if some would consider them to be hindering developing countries in accessing finance for climate challenges.

Regarding logistical challenges, unlike many MDBs, the GCF does not have regional offices and hence lacks the closer physical proximity to the governments in need of policy support. Such proximity facilitates dialogue between the institutions and governments, allows for closer relations and deeper understanding of country contexts, which enables the use of the PBF instrument. The GCF could also capitalise on such benefits, if a strengthening of the regional presence were to be realised in the coming years, which would then further increase the likelihood of PBF to be implemented within its funding frameworks in the mid- to long-term.

Including PBF in the mid- to long-term as a financing instrument within the GCF financing structure could contribute to the overall alignment of national, institutional and regulatory frameworks with the goals put forth in the Paris Agreement. Moreover, once the IRMF is successfully implemented, the way in which the GCF supports policy development and implementation and the proportion of this support compared to
other climate finance approved and disbursed by the Fund will become more transparent, making it clearer how the GCF actively supports policy in developing countries.

Finally, climate funds such as the CIFs and the GEF currently do not use PBF as a financing instrument in order to develop and implement policies in developing countries. Successful integration of PBF within the GCF’s financing structure could incentivise other climate funds to do the same, formalising the financing of policies specifically for addressing the issue of climate change.
References


