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Funding Proposal: Climate Finance Design Gap 2021

Note to Executive Board representatives

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For: Approval

Recommendation for approval

The Executive Board is invited to approve that:

US\$1.2 million from IFAD's regular grants resources be earmarked to meet a financing gap associated with the design of Green Climate Fund (GCF) projects in 2021.

I. Background and rationale

1. Access to concessional international climate finance at the national level is critical for countries to meet their commitments under Nationally Determined Contributions (NDCs) and their long-term goals for adaptation under the Paris Agreement and the Sustainable Development Goals.
2. However, at national level, capacity to: (i) achieve accreditation status with international climate finance donors; and (ii) develop robust climate finance proposals to achieve these commitments is limited. This is particularly a problem in the case of small-scale agriculture. At present, only approximately US\$10 billion of international climate finance flows target this sector, representing only 1.7 per cent of total climate finance tracked. It is only a fraction of the needs of vulnerable small-scale farmers¹—a critical gap since small scale farmers are responsible for more than one-third of the world's overall food supply. They also account for 5 per cent of all greenhouse gas emissions globally, and 32 per cent of emissions from the agriculture sector.^{2,3}
3. Consequently, many IFAD Member States are requesting support in accessing climate finance resources. They seek to leverage IFAD's accreditation status and technical experience with international environment and climate funds such as the Adaptation Fund (AF), the GCF and the Global Environment Facility (GEF). In this regard, IFAD uses its status with the funds to contribute to a global public good by helping countries access climate finance resources. This helps countries meet their climate commitments and enhances the climate resilience of the world's most vulnerable small-scale farmers, thus promoting global food security. Such support to IFAD countries aligns with IFAD's policies and strategies. Specifically:
 - (i) IFAD's 2019–2025 Environment and Climate Change Strategy, which increases IFAD's commitment to secure climate financing to support national partners.
 - (ii) The IFAD12 report calling for IFAD to leverage its own resources by mobilizing financing from thematic funds (i.e. GEF, GCF and AF).⁴

II. GCF portfolio opportunities

4. In 2019–2020, IFAD increased its engagement with the GCF, the world's largest multilateral funder of climate investment in developing countries.⁵ IFAD has a competitive advantage over other Accredited Entities of the GCF, being the only United Nations Agency that is also an International Financial Institution. IFAD is uniquely positioned to channel climate financing to support small-scale farmers in adapting to climate change. This is an urgent priority considering that less than 2 per cent of climate finance currently benefits small-scale farmers, one of the

¹ https://www.ifad.org/documents/38714170/42157470/climate-finance-gap_smallscale_agr.pdf/34b2e25b-7572-b31d-6d0c-d5ea5ea8f96f?t=1605021452000.

² Lowder, S.K., Sánchez, M.V. and Bertini, R., 2021. Which farms feed the world and has farmland become more concentrated?. *World Development*, Volume 142, June 2021, Article 105455.

³ <https://ccafs.cgiar.org/news/emissions-smallholder-farming-may-be-significant-mitigation-recommendations>

⁴ <https://webapps.ifad.org/members/gc/44/docs/GC-44-L-6-Rev-1.pdf>.

⁵ In 2019, the GCF received replenishment pledges totalling US\$9.8 billion to be programmed by 2023.

groups most affected by climate change. Consequently, IFAD has access to GCF loan resources that allow it to design highly innovative and sustainable projects targeting adaptation and the most vulnerable populations—key priorities for the GCF. In this regard, IFAD has over the past year, developed an ambitious pipeline of projects targeting the GCF. Once the pipeline is realized, the GCF portfolio will represent more than 20 per cent of IFAD’s current programme of work.

5. In IFAD’s GCF pipeline, designs being prepared in 2021 include strategically important regional programmes and single-country projects that will channel climate adaptation resources to some of IFAD’s most vulnerable countries. These projects, once approved by the GCF Board, will assist national partners in securing climate adaptation financing **totalling US\$549 million**. Support for, and engagement in, these designs is directly requested from our national partners to meet their international climate commitments while greatly boosting the resilience of vulnerable small-scale farmers to climate change at a local level.

III. Operationalizing the portfolio

6. Despite the high level of demand for GCF funding from Member States, IFAD’s ability to deliver is currently limited due to existing GCF fee restrictions. GCF’s Fee Policy specifies that GCF management fees can only cover costs directly related to project implementation, supervision and reporting. Thus, GCF resources *cannot* be used to finance the design costs⁶ of IFAD’s current pipeline. IFAD has identified **an urgent need to secure resources to cover the financing gap for ongoing designs to be submitted to the GCF Board at the end of 2021 or early in 2022**.
7. The GCF restriction on the costs of project design is applied by GCF across all its Accredited Entities, including IFAD. Other organizations have established specific financing mechanisms to cover design costs of GCF proposals that are in turn primarily financed through supplementary funds or sources that are determined by organization-specific legal restrictions. At IFAD, costs of GCF designs are categorized as supplementary Fund-related costs. This categorization further aligns with development effectiveness indicators and the harmonized United Nations cost classification categories, and it is therefore appropriate for IFAD costs for GCF projects to be funded by non-administrative budget funding sources, as suggested below.
8. Management proposes that a portion of the IFAD11 allocation for the regular grants programme be used to cover the urgent financing requirements of IFAD’s GCF projects currently being designed. Going forward, Management is also committed to finding ways to support these design costs in a predictable and efficient way over the years. In the interim, obtaining this urgent support for IFAD’s current design needs will place IFAD in a strong position to make key announcements related to the GCF at COP 26 in November 2021 and will position IFAD as a leading player in the international climate finance arena. If resources are not secured to cover this gap, IFAD will not be able to develop its GCF projects in 2021. This would present a reputational risk for both the GCF and IFAD, since their national partners rely on IFAD to secure GCF resources.

IV. Proposal to cover urgent GCF design costs

9. Management is seeking Executive Board approval **to urgently earmark US\$1.2 million** from IFAD’s regular grants resources to support Member Countries in the design of projects to be submitted for GCF’s consideration by the end of 2021 or early in 2022. Projects based on these designs will contribute directly to country-

⁶ <https://www.greenclimate.fund/sites/default/files/document/principles-list-costs-pm.pdf>.

led initiatives as well as national climate commitments and NDCs while boosting the climate resilience of the world's most vulnerable rural poor.

10. The proposed use of IFAD grant resources will not compromise the achievement of the regular grants programme. The proposed amount of US\$1.2 million accounts for only 0.6 per cent of the overall allocation to the regular grants programme for IFAD11 (4 per cent of the remaining allocation in 2021). Furthermore, the proposal fully aligns with: (i) the key principle of IFAD's recently approved Regular Grants Policy,⁷ namely enhancing on-the-ground delivery of IFAD's programme of work in a catalytic manner; and (ii) the Strategic Guidance Note for IFAD Grants 2019–2021, namely its Priority Area 2, Climate change, resilience and environmental sustainability. As mentioned in the Note, "grants under this priority area could be instrumental to leverage additional funds for climate change adaptation from the GEF, the Green Climate Fund and other sources".
11. Possible risks related to using regular grant resources were assessed prior to formulating the proposal. The primary risk is the possibility that the GCF Executive Board does not approve targeted proposals. This has been mitigated through:
 - (i) Robust screening of proposal ideas in-house to align with key GCF eligibility criteria prior to designing GCF proposals;
 - (ii) Discussions with the GCF Secretariat on IFAD's entity work programme for feedback on the GCF's priorities; and
 - (iii) Developing a detailed technical review process in-house to ensure optimal proposal quality.

⁷ EB 2021/132/R.3.