



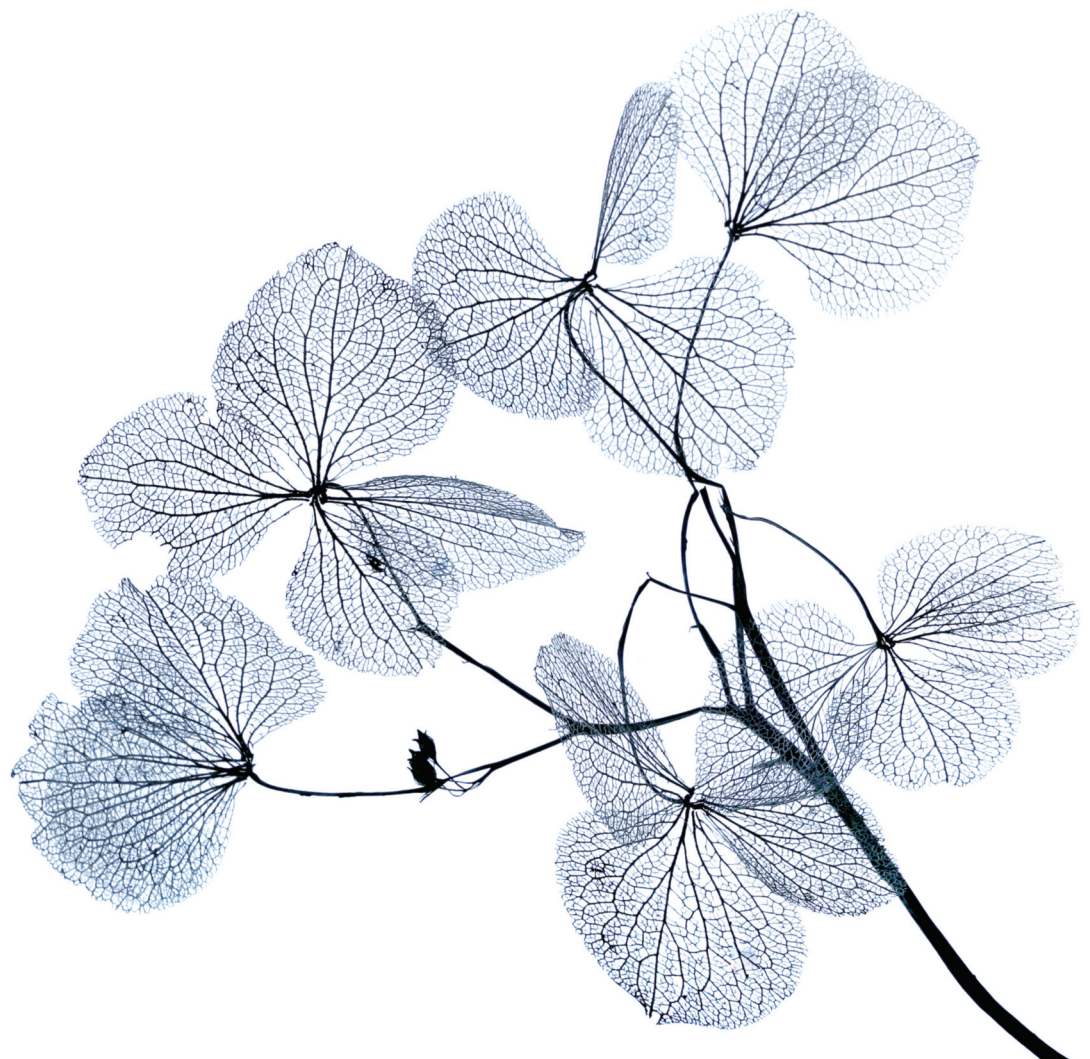
E3G

Strategic national approaches to climate finance

Report on scoping work in Peru, Chile and Colombia
on national climate finance pathways and strategies

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The financial support provided by CDKN during the course of 2013 has enabled E3G to further develop its conceptual framework. This work has included i) determining the current status of LEDS planning and processes; ii) evaluating the associated financing challenges and priorities; and iii) in-country engagement with government officials, civil society and other stakeholders involved in developing low emission climate resilient development plans and implementation strategies, including Nationally Appropriate Mitigation Actions (NAMAs) (where applicable).

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About E3G

E3G is an independent, non-profit European organisation operating in the public interest to accelerate the global transition to sustainable development. E3G builds cross-sectoral coalitions to achieve carefully defined outcomes, chosen for their capacity to leverage change. E3G works closely with like-minded partners in government, politics, business, civil society, science, the media, public interest foundations and elsewhere. More information is available at www.e3g.org

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List of Acronyms and Definitions

The report contains several acronyms which are named in full where they first appear in the document. The list below reflects the primary acronyms, including those relating to country spe-

cific acronyms for ease of reference. Where necessary, a short description has been added to the acronym to describe its meaning as used in the context of the report.

ADP	Ad Hoc Working Group on the Durban Platform, of the UNFCCC
AILAC	Independent Alliance of Latin American Countries
APPCAM	Action Plan for Climate Change Adaptation and Mitigation (Peru)
BAU	Business As Usual, a term used in the MAPS planning process described below and typically used in the context of non-action towards mitigation
CER	Centre for Renewable Energy (Chile)
CDKN	Climate & Development Knowledge Network (www.cdkn.org)
CDM	Clean Development Mechanism
CFU	Climate Funds Update, an independent website tracking international climate finance initiatives (www.climatefundsupdate.org)
CLCDS	Colombia Low Carbon Development Strategy
COFIDE	Cooperación Financiera de Fomento, a Peruvian national development bank
CONAMA	National Environment Commission (Chile)
CORFO	National Development Agency for Production (Chile)
CTF	Clean Technology Fund, a sub-fund of the Climate Investment Funds
GCF	Green Climate Fund, a financial mechanism of the UNFCCC
GEF	Global Environment Facility, a financial mechanism of the UNFCCC
GDP	Gross Domestic Product
GHG	Greenhouse Gases
IADB	Inter-American Development Bank
JICA	Japanese International Cooperation Agency
KfW	German government-owned development bank
LAC	Latin American Countries

LECB	Low Emission Capacity Building Programme, run by UNDP
LECR	Low Emission Climate Resilient, typically used when referring to the transition to a development path that mainstreams both mitigation and adaptation measures into national development priorities
LEDS	Low Emission Development Strategies, a development planning method to deliver measures that can help reduce emissions, and thereby mitigate climate change
LEDS GP	LEDS Global Partnership, a partnership of over 100 countries to enhance cooperation on climate resilient low emission growth (www.ledsgp.org)
LTMS	Long Term Mitigation Scenarios, used in the context of MAPs and by the South African government when determining mitigation options
MAPS	Mitigation Action Planning Scenarios, a process guidance methodology for developing a national approach to greenhouse gas reduction (www.mapsprogramme.org)
MADS	Ministry of Environment and Sustainable Development (Colombia)
MDBs	Multilateral Development Banks, referring collectively to the International Bank of Reconstruction and Development, Inter American Development Bank, African Development Bank, Asian Development Bank and the European Bank of Reconstruction and Development
MRV	Monitoring, reporting and verification, in the context of tracking of climate finance flows
NAMAs	Nationally Appropriate Mitigation Actions, used in context of programmes focusing on mitigation actions registered with the UNFCCC by developing country to attract resources
NAPAs	National Adaptation Programmes of Action, describing a process by which least developed countries can identify immediate and urgent priorities to adapt to climate change
NCCS	National Climate Change Strategy (Peru)
NCCRP	National Climate Change Response Paper (South Africa)
NGCCM	National Guidelines for Climate Change Mitigation (Peru)
NIE	National Implementing Entities, used in context of accreditation of national institutions to manage international climate funds
NDBs	National Development Banks
NFP	National Financing Pathways and Strategies, referring to the concept described in this report

PACC	National Climate Change Action Plan (Chile)
PNACC	Climate Change National Adaptation Plan (Colombia)
PPEE	National Energy Efficiency Programme (Chile)
PRONAMI	National Mitigation Programmes (Peru)
OECD	Organisation for Economic Cooperation and Development
OECD DAC	OECD Development Assistance Committee
ODI	Overseas Development Institute, a UK government think-tank focused on international development and humanitarian issues
REDD+	Reducing Emissions from Deforestation & Forest Degradation, a UN initiative to create financial value chains, conservation efforts and sustainable management of forest carbon stocks
SISCLIMA	National System of Climate Change (Colombia)
SMAPS	Sectoral Mitigation Action Plans, relating to Colombia's CLCDS
TPC	Tonnes per capita
UNEP	United Nations Environment Programme
UNDP	United Nations Development Programme
UNFCCC	United Nations Framework Convention on Climate Change

Key Messages

This paper describes the emerging strategic approach of National Financing Pathways and Strategies (NFP) for climate finance. In essence, this refers to **the outcome of a process whereby a country determines, defines and mobilises the financial and other resources necessary for its transition to a low emission and climate resilient development path**. The concept is explained in greater detail in *Chapter 4*, which also sets out E3G's perspectives on emerging diagnostic tools that may be applied, and core principles that may be relevant for developing countries to consider when developing a NFP. Different financing pathways may evolve for each country, and it may be useful to have these steered by establishing various milestones over the short, medium and long term. These milestones may in turn facilitate and promote the evolution of a national and international ecosystem for finance that is conducive to low emission and climate resilient development paths.

The concept of NFP emanates from an existing body of work by E3G which has yielded the following insights:

- > Recognition that at the international and national levels there is a **mismatch of resources and expectations** between providers and recipients of climate finance;
- > Implementation of low emission development strategies (LEDS) and climate resilience development plans requires a strategic approach to resource mobilisation that is **integrated with national development plans**; and
- > Appreciation of **differing national needs and circumstances** is essential for considering strategic approaches to climate finance, particularly with respect to assessment of

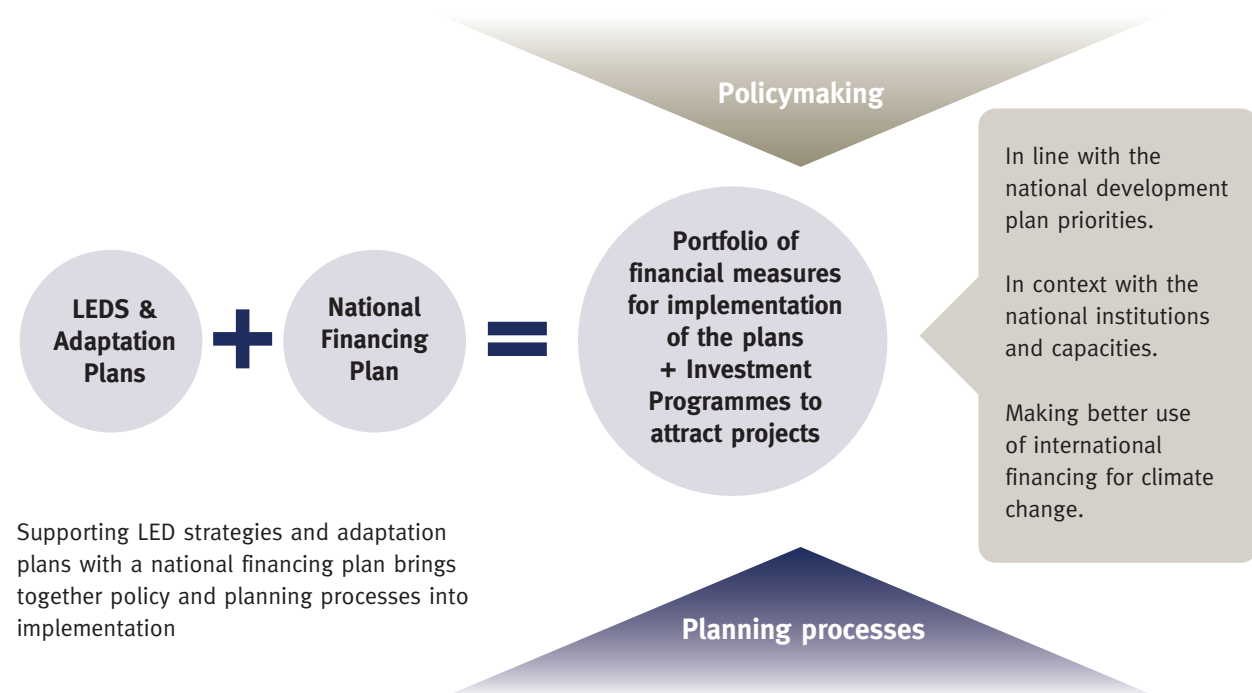
priorities and capacities to implement and effectively institutionalise climate finance.

Peru, Chile and Colombia expressed an interest in addressing the resourcing challenges necessary for the implementation of their ongoing work on LEDS and climate resilience development plans. Through the LEDS Global Partnership, and funded by Zennstrom, CIFF and CDKN, E3G has engaged with these countries to assess how a strategic approach to climate finance such as a NFP may apply within the context of each country's development and climate change priorities.

The scoping work within Peru, Chile and Colombia provided insights into the national development priorities of these countries, the status of their climate-related planning, and relevant institutional arrangements, coordination and engagement with respect to climate actions. *Chapter 3* of the report highlights these country specific findings, including: the current status of LEDS and climate resilience planning; emerging climate finance priorities; structure of the national finance sector; as well as a high level scan of international climate finance initiatives.

There are some important potential opportunities and benefits that a NFP may provide towards shaping an effective international ecosystem for climate finance. These are considered in *Chapter 5*. Notably, as countries develop NFPs these can be useful in helping to shape and determine resources required at the international level, or a long-term financing pathway to 2020 and beyond. The further development of NFP may also help to inform the design of the Green Climate Fund, the work of the UNFCCC Standing Committee on Finance, and the nature of the means of implementation within a new legally binding agreement.

Figure 4.1 NFP in context of policies and plans



Supporting LED strategies and adaptation plans with a national financing plan brings together policy and planning processes into implementation

Source: Authors' depiction

This scoping study has provided evidence of several important issues to consider in the design and development of national strategic approaches to climate finance and identified implications for the evolving international financial ecosystem. Of particular note are the following key findings::

1. In the current economic context, **developing and developed countries face similar challenges** in ensuring a rapid and smooth transition to low emission and climate resilient policy choices for infrastructure and economic growth. It is therefore becoming increasingly apparent that limited public resources (both national and international) need to be used effectively in order to attract private capital at the scale required for the global transition to a low emission climate resilient economy.
2. Due to the scale of investment required, it is important that low emission and climate resilient development plans result in **programmes that attract investment from the private sector. This may be particularly important for transformation within some key sectors.** Peru, Chile and Colombia, for example, are increasingly conscious of the need to mainstream both low emission and climate resilience into their national development plans and budgets, and create opportunities for private sector investment and participation in these plans.
3. There is presently **a mismatch between providers and recipients of climate finance**, with a predominance of a “supply-driven” approach towards climate finance. The plethora of differing approaches towards climate finance create fragmentation of the international climate finance ecosystem, poses challenges for institutional readiness for climate finance and may hinder programming of climate finance for transformational impact as well as inhibit financial innovation.
4. The **proliferation of international climate finance initiatives** available to developing countries addresses a wide range of activities, such as technical planning, institutional, technology and capacity assessments and support, as well as market and climate finance readiness programmes. As these initiatives are not effectively coordinated or harmonised at the international level, it becomes increasingly difficult to ensure coherence and effectiveness at the national level. For this reason, it is essential that developing countries foster a “demand driven” approach to these initiatives to ensure greater consistency and lasting benefits.
5. Evidence is mounting to support the adoption of **national strategic approaches to climate finance**, which can address various implementation challenges, including **broadening considerations beyond the short-term horizon** that may be typical of financial decision-makers.
6. One of the **benefits of national strategic approaches is the creation of platforms for ongoing dialogue** between national and international partners, as well as in-country engagements between the public and private sector. Importantly, a NFP will facilitate the design of effective investment programmes and project pipelines, as well as identify and promote market enabling conditions.
7. There has been growing recognition both in LAC and other developing regions of the need to integrate low emission and climate resilient growth strategies with wider development plans. **Many governments in LAC are taking a leadership role on climate action.** By way of example, the Independent Alliance of Latin American Countries (AILAC) is promoting ambitious mitigation and adaptation action at the national and international level.
8. As part of AILAC and in their national contexts, **Peru, Chile and Colombia are demonstrating significant leadership on climate change.** Each country has embarked on a robust national process to define their mitigation and adaptation options at a sectoral level. They are critically analysing the status of climate finance within their countries, in some instances with the support of their international development partners and in others, independently. The anticipated outcomes of these efforts has the **potential to provide clarity and transparency in terms of the national and international resources necessary for implementation**, and enable a more “demand-driven” basis towards climate finance.
9. Developing national financing strategies and pathways for climate finance may be sequenced according to **strategic milestones that are staggered over different time frames along the transition path.** The primary objective is to ensure that over the long term, the public and private sectors are both able to facilitate scaled up investment in climate-related sectors. This will require climate-related objectives being mainstreamed in national budgeting, risk management and investment processes, including within the private sector. The time scales and associated priorities may differ according to country contexts.
10. **Emerging diagnostic tools** that may contribute to the development of a NFP include: i) implementation of an iterative process of stakeholder engagement; ii) evaluation of national financing systems and capacity; and iii) development of scenarios to build financing pathways. There are several evolving core principles that may underpin NFP that E3G consider may be important for developing countries, namely: i) inclusivity; ii) equitable access to finance; iii) effectiveness; iv) predictability; and v) transparency.
11. The **consultative engagement of a broad range of stakeholders** has the potential to ensure a long term sustainable transition and the development of investment programmes which deliver a pipeline of projects to attract private capital at scale.
12. This signals a **new era in the application of international climate finance**, with recipient countries assuming leadership in the use of climate finance for greatest transformational impact within the context of their needs and circumstances. Such an approach will create **strong foundations for a smooth transition** to low emission climate resilient development paths, and holds valuable lessons for the evolution of the international climate finance ecosystem and long-term financing pathway.

1. Introduction

A rapid shift of investment to low emission and climate resilient infrastructure is required to meet the goal of limiting global average temperature increase to 2°C above pre-industrial levels¹. Approximately US\$1.3 trillion per year of additional investment in clean energy infrastructure, low emission transport, energy efficiency (EE) and forestry will be required to achieve this goal. The scale of response required in maintaining the stability of the atmosphere, and the resulting impact upon the global and domestic economies, entails transformation of the existing economic, social and institutional infrastructure upon which national and international systems are based.

In the current economic context, developing and developed countries face similar challenges in ensuring a rapid and smooth transition to cleaner and more resilient policy choices for infrastructure and economic growth. It is therefore becoming increasingly apparent that limited public resources (both domestic and international) need to be used effectively in order to attract private capital at the scale required for the transition to a low emission climate resilient global economy over the long-term.

Adopting a strategic approach to climate finance can address these challenges, including by broadening considerations beyond the short-term horizon that may be typical of financial decision-makers within the public sector. This document will describe the emerging strategic approach of National Financing Pathways and Strategies (NFP) for climate finance. In essence, this refers to **the outcome of a process whereby a country determines, defines and mobilises the financial and other resources necessary for its transition to a low emission and climate resilient development path over a period of time**. The concept is explained in greater detail in Chapter 4.

1.1 Evolving role of public finance

The scale and scope of the financing challenge entailed in the transition to low emission, climate resilient development requires governments to take a strategic approach to the allocation of public resources (whether domestic or international) to ensure that these lead to the greatest mobilisation of private resources through national policy and regulatory frameworks and mechanisms. Extensive research and case studies offer evidence that financing climate change interventions poses significant challenges on multiple levels. Such challenges require careful government attention to overcome barriers that may prevent the flows of finance required

for implementation (OECD, 2012; The Global Mechanism of the United Nations Convention to Combat Desertification, 2008; FONAFIFO, 2012; ODI, 2013; Asen, et al., 2011).

The introduction of new, and therefore unfamiliar, technologies and business models, which are commercially unattractive, generally requires financial incentives to mitigate the associated risks. This implies a role for public finance during the early stages of a new technology and/or business model to attract private capital. Whilst the type of financial support provided will be determined by technology, sector and country contexts, a common barrier is the lack of familiarity and related reluctance of public financial decision-makers to allocate public resources for such activities. Public resources for climate-related action is scarce, and climate projects have to compete with other national development priorities where the social and economic benefits are more widely accepted. Therefore a key challenge is to strengthen the understanding of the potential benefits and opportunities associated with new climate-related investments in both the public and private sector and to build confidence in the affordability of both abatement options and measures for increasing resilience.

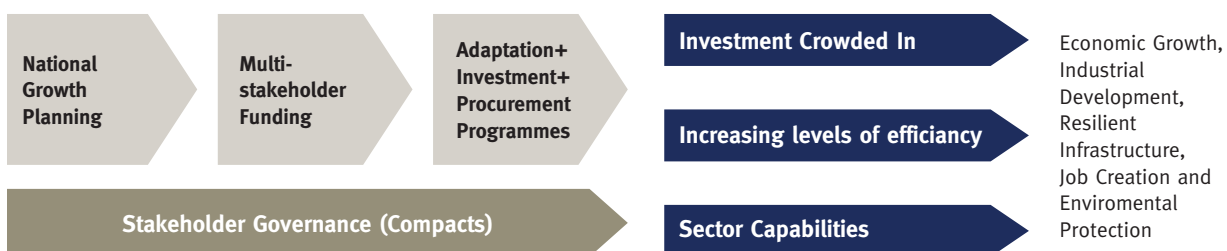
Dealing with conflicting goals and limited resources requires cohesive policy direction, clear implementation strategies, detailed resource mobilisation plans and procurement programmes (see Figure 1.1) to deliver benefits of economic growth, industrial development, resilient infrastructure, job creation and environmental protection.

Due to the scale of investment required, it is also important that plans such as those for low emission climate resilient development result in programmes that attract investment from the private sector in critical transformation sectors. Developing countries are increasingly conscious of the need for a balanced approach, including adaptation and climate resilience as a core priority to mainstream into national development plans and budgets.

1.2 Mismatch between providers and recipients of climate finance

International climate finance as provided for under the obligations of the United Nations Framework Convention on Climate Change (UNFCCC) has been criticised for its lack of effectiveness, relevance and accessibility to recipient countries (Ballesteros, Nakhoda, Werksman & Hurlburt 2009; Amin,

Figure 1.1 Building blocks for a climate resilient development path



Source: Naidoo, 2011 (Adapted from DPE Growth Paradigm 2011)

¹ IEA (2013). Redrawing the energy-climate map. WEO special report.

Naidoo & Jaramillo, 2013; Cloete, Ramgowlan & Tyler, 2011). Various causes are cited, including fragmentation of the international climate finance landscape, poor institutional readiness, inadequate programming and project planning and lack of financial innovation.

The narrative for climate finance has been largely supply driven, with programmes and demonstration projects based on the priorities of the providers of climate finance. Increasingly, attention is shifting towards understanding how best to ensure the most effective use of climate finance, resulting in a greater emphasis on the demand for climate finance. As developing countries are strengthening institutions and processes for financing LEDS and

climate resilience, this represents an opportunity for cultivating a demand driven approach towards climate finance.

This in turn should allow such countries to integrate LEDS and climate resilience more closely into national development priorities and plans, as illustrated in Figure 1.2 below. The Figure illustrates a systematic approach to integrating national and climate aims in the context of existing policies, and the identification of gaps that are not filled by national finance mechanisms. In essence, these gaps provide the basis for a discussion on how to bridge the demand and supply of international climate finance.

Figure 1.2 Integration of development and climate priorities

Sectors	Energy & Energy Efficiency (EE)	Natural Resource Management	Sub national Government
National development aims	Energy access & security	Sustainable land use, water security, biodiversity & conservation protections	Effective service delivery to citizens at local and provincial level
Policy frameworks	Integrated Energy Plan, Integrated Resource Plan & National EE strategy, Independent Power Producers Programme	National strategies and Acts for environmental management, waste, water etc	Municipal Finance Management Act, Municipal Services Management Act
Climate response	Shift fuel sources towards clean energy & reduce energy demand on national grid	Resilience and enhanced adaptive capacity of natural resources	Build climate resilient economic and social systems at grass root level
National finance mechanisms	Power Purchase Agreements, EE levies, Green Fund	Expanded Public Works Programme, Carbon offsets, Drylands Fund, Green Fund	Revenue allocations based on integrated development plans, Cities Support Programme, access to other national funds
Gap analysis (demand)	Project development, risk guarantees & SMME finance	Attracting private sector investment in response	Full integration into local and provincial budgets
International climate finance (supply)	Bilateral loans and guarantees Multilateral project development assistance Technical and technology capacity building	Adaptation Fund (NIE) Global Environmental Facility (NIE)	Sub-national focused efforts to ensure national to sub-national integration

Source: Adapted from Naidoo, 2012.

Evidence is mounting to suggest that a more strategic approach to climate finance is required, specifically to ensure that available national and international resources are effectively utilised to achieve large scale economic, social and environmental transformation. This suggests a need to build bridges between the available resources at the international level on the one hand with the demand for resources at the recipient level on the other.

Strategic approaches such as the NFP described in this report can enable the design and development of robust implementation plans for low emission, climate resilient development paths. The elements described in Figure 1.3 indicate that the benefits of strategic approaches can deliver platforms for dialogue between national and international partners, as well as in-country engagements between the public and private sector.

Importantly, an upfront strategic approach to climate finance has immense potential to facilitate the creation of investment programmes and project pipelines coupled with the appropriate market enabling conditions.

In doing so, there should be ongoing dialogue between stakeholders to ensure a dynamic and flexible approach to finance is maintained. The importance of public dialogue on financing priorities and challenges, instruments and institutions is essential and can support more effective utilisation of public, private and international cooperation. Evidence of the importance of dialogue can be found in the United Kingdom and South Africa, with respect to the preparation of their respective climate responses, and in the emerging dialogues in Colombia, Chile and Peru regarding the development of their Nationally Appropriate Mitigation Actions (NAMAs).

Figure 1.3 Bridging supply of climate finance with demand



Source: Amin, 2012

1.3 Integration of climate action with national development priorities

As substantial resources are necessary to enable a global transition, it is important that public resources and international cooperation are focused on mobilising private capital, assisting technology development and transfer, and developing technical and human capacity for suitable institutional and governance systems. The speed of transition is likely to be determined by several factors, including the structure of the economy, the degree of political support, existing development priorities, perceived risk and the domestic capacity to embrace change at minimal cost to jobs and industry, as well as the ability to mobilise appropriate resources. The strength of in-country coordinating and planning structures and institutions that can support implementation in alignment with existing development priorities is also critical.

The majority of developed and developing countries have acknowledged that “business as usual” (BAU) is no longer an option, and are working towards low emission, climate resilient development paths. The LEADS Global Partnership (LEADS GP) is an example of a partnership that provides a platform to draw together these requirements by supporting countries in their strategies to achieve low emission, climate resilient development. The Partnership consists of over 100 countries and international

programmes working to enhance coordination, information sharing and mutual learning. Participating countries are in various stages of developing LEADS as part of their national climate response plans. It is essential that plans such as these are supported by robust measures for implementation and the appropriate means for mobilising international and national resources, including attracting investment from private financial institutions.

1.4 Purpose of the report

The work presented here represents the convergence of several work streams by E3G relating to climate finance, which have culminated in the recognition that a strategic approach to climate finance is required at the country level. Specific country experiences, including the creation of the Green Investment Bank in the United Kingdom and South Africa’s articulation of the role of the finance sector in its National Climate Change Response Paper (NCCRP), support the growing view that national strategies for climate finance are useful to engage the domestic financial system (NCCRP, 2011). The concept emerging from this work is one of creating more strategic approaches to climate finance through NFP, which aim to improve the effectiveness of public and private climate finance at the national level. NFP is a concept that articulates interdependencies between public, private and international sources of finance as a means of delivering investment at scale to support implementation of low emission, climate resilient development.

Relevant insights generated through E3G’s international climate finance programme include:

- i) Recognition that at the international and national level there is a **mismatch of resources** and expectations between the providers and recipients of climate finance.
- ii) Implementation of LEADS requires a strategic approach to resource mobilisation that is **integrated with long term national development plans** in order to be sustainable.
- iii) Understanding of **different national contexts** when considering strategic approaches to climate finance is essential and enables critical assessment of priorities, capacities for implementation, and effective institutionalisation of climate finance.

This report describes ongoing work undertaken by E3G with government officials and stakeholders in Peru, Chile and Colombia on the resources and processes necessary for climate action implementation. The outcome of this ongoing engagement process over the course of 2013, with funding provided by the Climate and Development Knowledge Network (CDKN) and by Zennstrom Philanthropies, is contributing to an evolving concept of NFP being developed by E3G.

This report describes the context of the scoping mission (Chapter 2) and the different national contexts in which climate finance is being applied (Chapter 3). Chapter 4 builds on the outcomes of the scoping mission and offers an emerging conceptual framework to NFP. Chapter 5 offers reflections on the relevance of this strategic approach for the international and national financial ecosystem, while Chapter 6 describes potential next steps and conclusions.

13 WEF (2013) The Green investment Report: The ways and means to unlock private finance for green growth: A report of the Green Growth Action Alliance.

14 Jorge Núñez Ferrer and Arno Behrens (2011) Innovative Approaches to EU Blending Mechanisms for Development Finance.

2. Context of the scoping mission

Over the past decade Latin America has experienced relatively high levels of economic growth, due in part to the successful implementation of policies to promote investment, increasing productivity levels and favourable commodity prices. This has led to falling levels of poverty and unemployment, improvements in public services and increased investment in infrastructure. Most countries in the region have national development plans aimed at ensuring that this trend continues.

At the same time, there is widespread recognition that the region's relatively high vulnerability to the effects of climate change represents a direct threat to its development goals. This vulnerability is largely due to the region's reliance on agriculture and natural resources for economic growth. Key impacts are likely to include: significant dieback of the Amazon rainforest; disappearance of tropical Andean glaciers; increased flooding in coastal zones; and increase in extreme weather events². At the same time the region is expected to experience rapid increase in rate of energy consumption. Addressing this challenge will require a massive scaling up of investment. According to the Inter-American Development Bank (IADB), net additional annual costs of climate stabilization of 2 tonnes per capita (TPC) by 2050 would cost the region approximately US\$100 billion or 2.2% of Latin American Countries' (LAC) 2010 Gross Domestic Product (GDP).³

Thus there has been growing recognition both in LAC and other developing regions of the need to integrate low emission and climate resilient growth strategies with wider development plans. The LAC is taking a leading role in its climate action: by way of example, the Independent Alliance of Latin American Countries (AILAC) is promoting ambitious mitigation and adaptation action at the national and international level.

During discussions at the 2012 LEDES Global Partnership, Peru, Chile and Colombia expressed an interest in working with E3G on developing national financing strategies for LEDES implementation. During the course of the scoping study within these countries, the concept of National Financing Pathways and Strategies has evolved, as well as a focus on enabling policy and regulatory frameworks and mechanisms. The latter focus appears necessary to ensure public financial resources, including international climate finance, are used most effectively to overcome barriers to private sector investment and facilitate an inclusive transition to LEDES economies.

This study has identified the need for appropriate institutional and technical capacity, particularly to ensure decision-makers from finance ministries, planning entities and public agencies (including National Development Banks (NDBs), better understand the financing challenges and investment profiles associated with LEDES investments across different sectors. As introduced in Chapter 1, a NFP is an emerging strategic approach to climate finance, whereby a country develops strategies and pathways to determine, define and mobilise the appropriate financial and other resources necessary for its transition to a

LEDES development path over a period of time. The concept is explained in more detail in Chapter 4.

The concept of a NFP is potentially a useful tool for mainstreaming climate objectives into a country's financial systems and sector specific investment plans. This chapter aims to delineate the different categories of international climate finance initiatives that are available to developing countries, focusing on: planning and capacity building, and implementation and resourcing of national climate plans. These initiatives are often decoupled from each other, creating a fragmentation of efforts which may limit the collective impact they have at recipient level. These issues are more fully addressed in Chapter 5, but are important to note as context to the scoping report and the subsequent discussion in this Chapter on climate finance dynamics in LAC.

2.1 International climate finance initiatives

There are a wide range of international climate finance initiatives that support developing countries with LEDES development, financing and implementation. Table 2.1 overleaf groups the various initiatives by category, description, type of resource offered and time scale. This list is not intended to be exhaustive, but serves to illustrate, from a developing country viewpoint, the proliferation of existing initiatives, which presents both opportunities and challenges in terms of developing a strategic approach to climate finance at a national level.

These institutions and networks provide a range of finance or risk management products, technical assistance and research support, as well as platforms for sharing best practices. They form a solid foundation of support, which developing countries have been able to draw upon in order to begin implementing LEDES. However, to date there has been only limited coordination between the initiatives. The relatively large and diverse number of initiatives and institutions, combined with a lack of coordination, presents a significant challenge for developing countries' efforts to formulate LEDES plans.

2.2 LEDES planning in Latin America

Countries in Latin America are demonstrating immense commitment and support for LEDES development planning and can already point to important markers of progress in this area. Chile, Colombia and Peru represent some of the developing countries that are taking the lead and are looking to develop a deeper understanding of the financing measures needed to deliver desired outcomes. One example of this effort is the establishment of the LEDES Latin America Regional Platform, under the LEDES GP. This initiative mapped 98 LEDES-related support programmes in LAC and 16 regional networks. Examples of activities that have taken place in recent years include: development of tools for planning and LEDES processes; improved international cooperation and best practices; and capacity building for low carbon development.⁴ Chapter 3 of this report

2 IADB 2013 The Climate and Development Challenge for Latin America and the Caribbean

3 IADB 2013

4 <http://en.openei.org/wiki/LEDESGP/LEDESLAC>

Table 2.1 Summary of financial instruments and mechanisms used within green finance incentive schemes

Institution types	Examples	Resources on offer	Use of funds	Time scale
UNFCCC Mechanisms and initiatives	Global Environmental Facility (GEF), Green Climate Fund (GCF), Adaptation Fund, Nationally Appropriate Mitigation Actions (NAMAs), Clean Development Mechanism (CDM)	Grants, loans and technical assistance	Projects and programmes supporting climate action for adaptation and mitigation	Medium – long term
Other Multilateral Institutions	Organization for Economic Cooperation and Development (OECD), United Nations Environment Programme (UNEP), United Nations Development Programme (UNDP), World Economic Forum (WEF)	Knowledge sharing and technical assistance	Case studies and in country research and support on sector specific issues, MRV, finance, technology, institutional capacity and planning	Short term
Multilateral Development Banks and Funds	Inter-American Development Bank (IADB), World Bank, , European Bank of Reconstruction & Development, Climate Investment Funds (CIF), International Finance Corporation (IFC), Multilateral Investment Guarantee Agency (MIGA), Energy Sector Management Assistance Program (ESMAP)	Grants, loans, technical assistance, risk management products and research	Demonstration projects & programmes for private and public sector investment – sector specific and facilitation of UNFCCC mechanisms	Short term
Bilateral Finance Institutions	Agence Francais Developpement, European Investment Bank, Japan International Cooperation Agency (JICA), KfW, NEFCO, US AID, GIZ	Grants, loans, technical assistance, risk management products, climate finance readiness programmes	Sector specific investments, project development & direct technical assistance to environmental, finance and planning ministries	Short – medium term
Networks and partnerships	Climate Development Knowledge Network (CDKN), Partnership for Market Readiness, Global Green Growth Initiative, Green Growth Best Practice, International Development Finance Club, Capital Markets Climate Initiative (CMCI), LEDS Global Partnership, Mitigation Action Plans and Scenarios (MAPS)	Knowledge sharing and technical assistance	Long term planning using scenario analysis Institutional capacity assessments & readiness, financial innovation, financial markets transformation	Long term

Source: Adapted by authors from Amin, Mohanty & Tomlinson, S. (March 2012).

provides a more detailed overview of climate change activities in Chile, Peru and Colombia.

2.3 Climate finance dynamics in LAC

LAC has been attracting a growing share of global climate finance in recent years. The region accounted for 6% of total clean energy investment in 2012 and over US\$ 2 billion has been approved for 220 projects in the region since 2004⁵. The amount of financing directed towards REDD+ projects in 2012 totalled US\$ 3 billion in the region⁶. Investment, historically

concentrated in Brazil, has also been diversifying to other countries.

According to the Overseas Development Institute (ODI), 20 climate dedicated funds are active in the region, with the largest contributions coming from the Clean Technology Fund (CTF) and the Global Environment Facility (GEF). The ODI reports only on funds that they specifically monitor, which includes only partial bilateral contributions and not Official Development Assistance (ODA). From the bilateral information available through the Climate Funds Update, Japan and Norway

5 IADB (2012) Climatescope 2013. New Frontiers for Low Carbon Energy Investment in Latin America and the Caribbean.

6 Buchner et al. (2013) The Global Landscape of Climate Finance 2013 Climate Policy Initiative.

are the largest bilateral contributors, while the United Kingdom and Germany are also active in the region⁷. Just over half of climate finance in LAC goes towards mitigation activities.⁸ Mexico has by far the highest share of approved climate finance, followed by Guyana, Brazil, Chile, Colombia and Peru. However, disbursement of finance has generally been a slow process and so many low emission and REDD+ projects have stalled.

NDBs play a particularly important role with respect to financing infrastructure in a number of LAC countries. As of 2011, NDBs in the region had outstanding assets of approximately US\$1 trillion and a capital base of US\$ 100 billion.⁹ The IADB surveyed 9 NDBs in LAC and found that all of them were involved in climate finance to varying degrees. The unique role of NDBs relative to other institutions, such as Multilateral Development Banks (MDBs) or Bilateral Development Banks (BDBs), includes: deep local knowledge and relationships; understanding of local markets; and a higher threshold for taking risks than other financial intermediaries.¹⁰

The IADB lists several other advantages of NDBs, including:

- > Market development, for example in new sectors and emerging industries through capacity building;
- > Long-standing relationships with local private financial institutions, hence understanding the unique risks and barriers that they face (some NDBs have an explicit mandate of working with the private sector) and helping them to address many of these barriers;
- > Ability to aggregate large numbers of small-scale projects through a portfolio approach when assessing credit risk, which streamlines the application process, thereby minimising transaction costs and encouraging the participation of local financial institutions.

Mapping of climate finance in LAC demonstrates that there is a strong base of funding and activities on which to build. For the purposes of this scoping study it was necessary to conduct a more comprehensive analysis to investigate how climate finance is unfolding in the context of the current status of LEDS planning and implementation.

2.4 Summary – basis for country choices

Distinguishing features which supported the choice of Colombia, Chile and Peru as a basis to assess their strategic approaches to climate finance include:

- > There is a growing awareness in the LAC region of the linkages between LEDS implementation and the **need for a strategic approach to financing**.
- > **Countries in LAC want to lead the implementation** of their LEDS and the mobilisation of the associated resources.

- > These countries believe that they **need to strengthen their understanding of climate finance**, their capacity to utilise it effectively and ensure that appropriate institutional arrangements are in place.
- > These countries recognise the **need for coherency and for harnessing the advantages** of the different climate finance-related international development cooperation work streams that are being implemented at country level.

The experiences of countries that are involved in developing LEDS is directly relevant to other countries and may be shared within the region through the LEDS LAC Platform and to other regions through the LEDS GP. It is important to build linkages to the wider finance community by drawing on the experiences at country level.

7 Schalatek, L. et al (2012) Climate Finance Regional Briefing: Latin America and the Caribbean. Climate Finance Fundamentals. November 2012.

8 Ibid 2012

9 IADB (2012) Role of National Development Banks.

10 IADB (2013) The Role of National Development Banks in Catalyzing International Climate Finance. March 2013.

3. Country analysis

This section provides a summary of findings from the scoping mission for each of the three case study countries: Colombia, Peru and Chile. It includes a brief summary of relevant social and economic indicators, the results of mapping the climate finance and governance architecture and LEDS stakeholders and the structure of the domestic finance sector. A summary of findings and conclusions from the scoping work is also provided. The goal of this scoping exercise was to build a strong understanding of the current status of LEDS planning processes and implementation and to begin to identify policy, regulatory and institutional gaps, needs and priorities.

3.1 Colombia

Colombia is Latin America's third largest economy and one of its most populous, with 47.5 million people¹¹. The country has abundant natural resources and its economy is heavily dependent on oil exports¹². It is also a major producer of gold, silver, emeralds, platinum and coal. Colombia has a comparatively high unemployment rate of 11.1%¹³. Major industries include textiles, food processing, oil, clothing and footwear, beverages, chemicals, cement; gold, coal, and emeralds, platinum and coal. Colombia is highly vulnerable to climate impacts with a large proportion

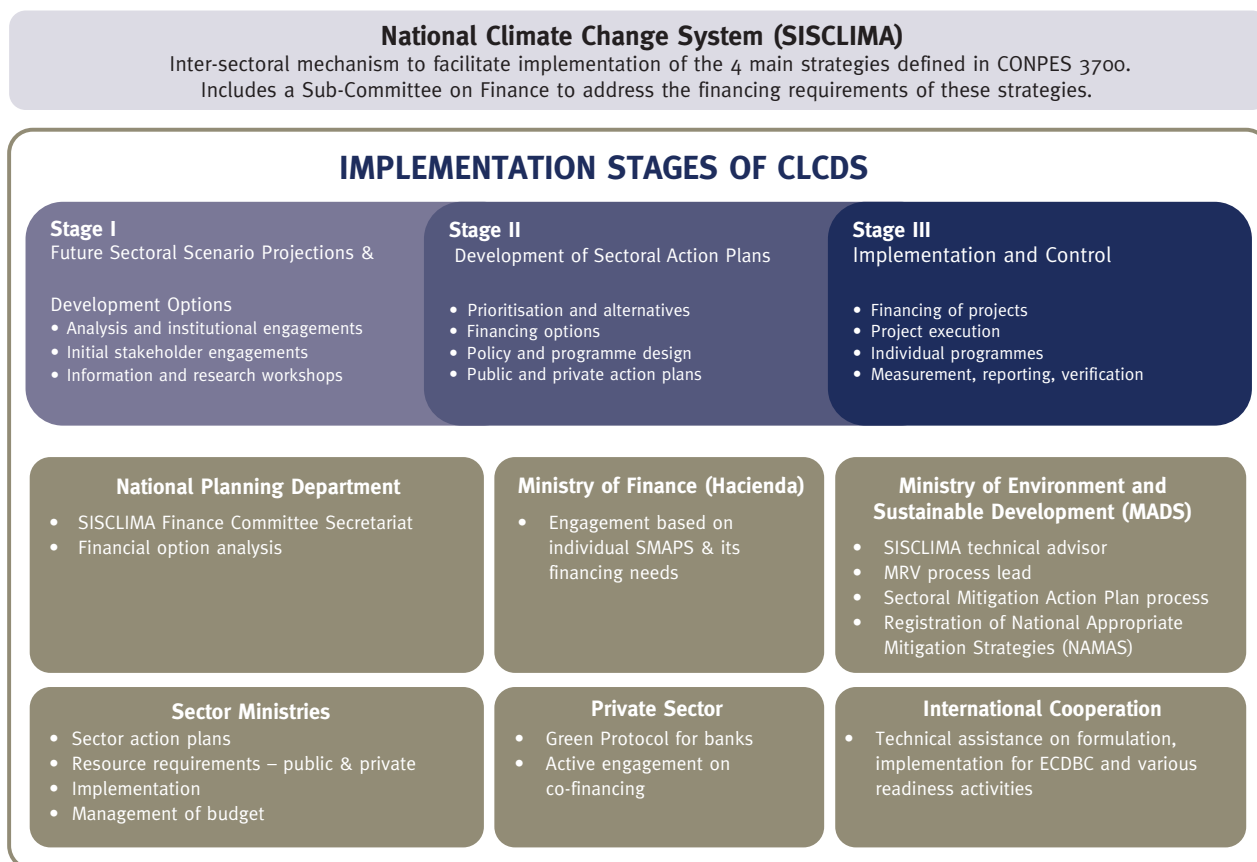
of its population living in the Andes at high risk of water shortages, or on the coast with high risk of flooding. Colombia's GDP corresponds to 0.5% of the global economy, however, the country emits only 0.37% of global GHGs due largely to reliance on hydropower. The energy and agricultural sectors contribute 37% and 38% of national emissions respectively.¹⁴

Climate finance governance and architecture

The Colombian government has created a platform called the National System of Climate Change (SISCLIMA) which includes a Finance Committee. SISCLIMA was articulated in a strategy document, entitled CONPES 3700 Plan, in 2007, with the aim of creating an intergovernmental platform of engagement. SISCLIMA is in the process of being officially recognised and approved within the Colombian government. The structure of SISCLIMA consists of an inter-sectoral commission of climate change; a finance committee; and four permanent committees (Sectoral, Territorial, International Affairs and Research), with production and communication of information on the climate change transversal committee.

Financing priorities and needs would be determined at a sectoral

Figure 3.1 – Colombian Low Carbon Development Strategy (CLCDS)



Source: Authors' depiction based on in-country discussions.

11 The National Administrative Department of Statistics (DANE) Statistics (accessed March 2014)

12 Central Bank of The Republic of Colombia, Trade Balance (accessed March 2014)

13 The National Administrative Department of Statistics (DANE) Statistics (accessed March 2014)

14 Lozano et al (2012), Colombia's 2nd Communication to the UNFCCC, IDEAM, Colombia.

level and embedded in the budget applications to the Ministry of Finance prepared by the National Planning Department (DNP). This is a direct approach, which requires holistic assessment of the fiscal measures, market mechanisms and financial instruments available from both the private sector and international sources in order to support implementation. Within these actions, SISCLIMA will coordinate the implementation of the four climate change priority strategies defined by the government, namely: the Climate Change National Adaptation Plan (PNACC); the Colombian Low Carbon Development Strategy (CLCDS); the National Strategy on Reducing Emissions from Deforestation and Forest Degradation (ENREDD+); and the Strategy for Fiscal Protection Against Natural Disasters. It is expected that these strategies will formulate their own finance strategies, including a component focusing on private sector investment.

The finance committee that has been provided for under SISCLIMA, which will interrogate and address the financing strategies of the four climate change priorities identified, as well as explore avenues for financial innovation. This Committee meets on a regular basis to discuss and engage on the specific and collective financing challenges associated with implementation, and ensures that the cooperation that Colombia is securing on climate finance is complementary and in line with national priorities. Representatives on the Finance Committee include the Colombian government, its national development banks and the private sector, with the DNP serving as the Secretariat.

The impact of climate change on economic development has been recognised by the Colombian Government, which called for the design of the four national strategies aimed at addressing climate change in Colombia's National Development Plan (2010 – 2014). This plan has a strong focus on economic growth and competitiveness, and introduced substantial environmental and climate measures that were influenced by the costly impact of La Niña, a hydro-climatic event, in 2010-2011. The Colombian Low Carbon Development Strategy (CLCDS) is led by the Environment and Sustainable Development Ministry (MADS), DNP and the Sectoral Ministries. The initiative seeks to develop a plan for the short, medium and long term that allows the identification and mitigation of GHG emissions without adversely affecting national economic growth. Figure 3.1 describes the developmental stages of Colombia's CLCDS strategy as they are unfolding and the partners being engaged as co-implementers of this strategy.

The CLCDS will chart a path to identify, evaluate, establish, promote and monitor sectoral actions/projects, including NAMAs, which can reduce emissions while keeping the sectors on track to reach their growth targets. Colombia is also engaged in strategic planning and in assessing the financing strategies for adaptation and climate resilience, which would form part of the strategies being managed under SISCLIMA and the Finance Committee.

Key stakeholders facilitating implementation of climate action plans

The core national departments coordinating and integrating LECR into Colombia's national development agenda are the

DNP, MADS, Ministry of Finance and Public Credit (Hacienda). MADS is the principal technical partner to DNP and Hacienda, as it is responsible for ensuring that climate change and sustainable development are integrated into the government's national priorities. The DNP is responsible for Colombia's national development plan which is updated every four years, and it also provides budget recommendations to the Hacienda. Together, MADS and DNP are supporting and engaging with the sectoral ministries to develop sectoral mitigation action plans (SMAPs), as well as NAMAs that aim to deliver the economic, social and environmental benefits of low emission climate resilient development.

Structure of domestic finance system

Colombia has a mature domestic finance sector. As of 2012 the banking sector had roughly US\$151 billion in assets¹⁵. The finance sector in Colombia is characterised by strong credit and profitable banks, some of which are at the top of the capitalisation market (e.g. Bancolombia and Banco de Bogota). Colombia's lending environment is one of the best in the LAC region, with the cost of debt (5.2%) and swap rate (4.7%) being at the lower level amongst its peers. Private equity funds are growing at an accelerated rate and are considered the key financing sources for Colombia's future entrepreneurs. Private pension funds are worth US\$80 billion.¹⁶ The stock market had a traded volume of US\$40 billion in 2012 and a market capitalisation of US\$254 billion at the end of March 2013. A strong financial regulatory environment as well as major improvements to Colombia's security and three investment-grade ratings helped attract a record US\$16.7 billion in foreign direct investment and cash to its stock and bond markets last year.¹⁷ On the other hand, the full potential of micro-finance institutions has yet to be unlocked, as few are supporting low carbon solutions, and generally there has been a downturn in the sector in recent years.

International climate finance initiatives

Colombia ranks third regionally in total international climate finance received with approximately US\$100 million¹⁸. As Table 3.1 demonstrates, it is already working with multiple bilateral and multilateral partners across various sectors of the economy. Initiatives listed in this Table are based on a literature review of publicly available information and interviews with stakeholders in Colombia during the course of the scoping work. This list is not exhaustive but is intended to illustrate the scale of climate finance related activity in the country.

There are a significant number of climate finance-related initiatives underway in Colombia covering both mitigation and adaptation activities. The extent to which these are formally coordinated within Colombia and lessons are exchanged among them was not evident during the scoping work. It appears that the Finance Committee is making efforts to ensure that synergies among some of these climate finance activities are realised. While improved coordination is likely to ensure greatest impact, these initiatives could provide a strong foundation for a comprehensive NFP in future.

15 <http://usbusiness-opportunities-embassybogota.com/2012/05/31/opportunities-for-u-s-commercial-banks-in-colombia/>

16 <http://www.bnamericas.com/news/insurance/colombia-private-pension-funds-reach-us81bn-in-2012>

17 <http://www.reuters.com/article/2013/05/20/us-latam-summit-colombia-stock-idUSBRE94J0X820130520>

18 ODI (2013) Climate Finance Regional Briefing: Latin America and Caribbean.

Table 3.1 International Climate Finance Initiatives in Colombia

Finance initiative	Focus	Resources	Project outcomes	Time scale
NAMA (5 projects)	Multiple sectors	Grants, loans and technical assistance	Demonstration results for future scaled up action	Short term
Clean Technology Fund (CTF) (3 projects)	Mitigation	Grants and loans	Scale up the demonstration, deployment, and transfer of low carbon technologies	Short – medium
Fast Start Funds (Japan)	Adaptation	Grants	Integral Management of Watershed with Emphasis in Sustainable Development of Rural Territory and Environment	Short – medium
Germany International Climate Finance Initiative (6 projects)	Mitigation and Adaptation	Grants	Development of NAMAs, efficiency from CHP, expansion of grid connected renewables etc.	Short – medium
Adaptation Fund UNDP (2 projects)	Reducing risk from floods	Grants	Reducing Risk and Vulnerability to Climate Change in the Region of La Depresion Momposina in Colombia	Short – medium
Forest Carbon Partnership Facility	REDD+	Grants and technical assistance	Reducing emissions from deforestation and forest degradation, forest carbon stock conservation, the sustainable management of forests, and the enhancement of forest carbon stocks in developing countries (activities commonly referred to as REDD+).	Short – medium
Clean Development Mechanism CDM (61 projects)	Mitigation, multiple sectors	Finance	GHG reduction	Short – medium
Global Environment Facility (approximately 11 projects)	Mitigation and Adaptation, Multiple sectors	Grants	Domestic implementation capacity	Long term
Partnership for Market Readiness (World Bank)	Public finance	Grants	Carbon tax modelling and climate change fund for transport projects	Long term
Climate Finance Readiness Programme. (BMU, Germany)	National and International climate finance mobilisation and coordination	Grant	Capacity building for accessing the GCF and project pipelines, strengthening institutions and developing CPEIR methodology.	Short – Long term

Source: Authors' analysis as of February 2014, based on engagement at country level and publicly available information.

Summary of key findings on climate finance

Colombia has a long standing commitment to environmental issues and through SISCLIMA and its Low Carbon Development Strategy it is a global leader in LEDS development and implementation. A systematic approach to climate change is being taken, based on comprehensive sectoral action plans that aim to mainstream low emission and climate resilient develop-

ment into national and state priorities. Colombia's specific climate finance efforts are described below.

- > Efforts are already underway to **ensure appropriate institutional arrangements for financing and implementation of climate change plans** are in place. Colombia can therefore point to important progress in terms of the activities involved in the short and medium term components of an NFP. The

existence of the Climate Finance Committee in SISCLIMA, tasked with identifying finance needs, is a potential stepping stone for an NFP and may facilitate ongoing dialogue with a broad spectrum of participants in the private finance sector (including banks, institutional investors, microfinance, and development agencies) to investigate their interest in, and impediments to, offering finance for climate related investments. Financing priorities are being identified at sectoral level and embedded in budget applications to the Ministry of Finance and National Development Plan. At this stage, financing priorities relate mainly to delivering strong business models to support implementation.

- > Various initiatives are currently in place to improve understanding of the nature of a strategic approach to financing climate change plans. These include: a climate finance readiness programme implemented by United Nations Environment Programme (UNEP); a study on barriers for access and management of climate finance; projects on carbon tax modelling and climate change fund for transport projects with the Partnership for Market Readiness; and an ODI-E3G led collaboration on National Financing Arrangements.
- > In an effort to bring private and public finance sectors more closely together in the financing of sustainable investments (including climate change) an important step was taken in 2012 when a number of financial institutions and the Colombian Government signed a Green Protocol. The Protocol aims to promote credit and/or investments in programmes that promote sustainable use of natural resources, and their protection and contribution to the life standards of the population. It also promotes sustainable practices among the signatories and stronger environmental and social safeguards.
- > Colombia's engagement process and focus on NAMAs and SMAPs in particular is a positive signal and is already providing a wealth of experience from which to draw lessons. There is a wide range of climate finance initiatives currently underway.
- > Colombia has significant experience in implementing initiatives that seek to mobilise financial resources for environmental management. Fiscal incentives have been used to leverage private sector investment, and the retributive charge for hydrologic resources was widely recognised as an innovative mechanism. Lessons can be drawn from these experiences and the potential for scaled up programmes based on similar principles could be studied.

Colombia's regulatory and legislative experiences in the environmental sector, healthy private sector institutions, and the holistic approach to the national financial ecosystem represented by the mandate of the SISCLIMA Finance Committee offer a wide range of financial tools and mechanisms that could help drive the implementation of national climate change strategies.

Achieving this outcome will, however, require better strategic coordination, such as the formulation of a National Financing Plan. Colombia has recognised this, alongside other priorities in terms of financing its NAMAs and assessing the potential for existing national financing mechanisms to coordinate climate finance. In summary, Colombia has established a sound platform and is on a clear trajectory to develop a robust national climate financing strategy.

3.2 Peru

With a population of about 30 million, Peru has been experiencing rapid growth in recent years and is one of the most stable economies in Latin America (IMF 2013). Its economy has almost doubled in size since 2002; real GDP has grown at an average annual rate of 6.5%.¹⁹ Three quarters of the population work in services and one quarter work in industry, and the unemployment rate of 6.4% is comparatively low.²⁰ Peru has a high dependence on exports of minerals and metals and produces a wide range of agricultural products. It is included among the ten countries in the world that are most vulnerable to climate change (Tyndall Centre, 2004), having four out of the five vulnerability characteristics recognised by the UNFCCC, namely: low coastal zones; arid and semiarid zones; zones exposed to floods, drought and desertification; and fragile mountainous ecosystems. Local economies are heavily based on climate dependent activities (e.g. mining, agriculture, fishing and forestry).

According to the Ministry of Environment, Peru is "one of the 10 mega diverse countries in the world: it has the second largest Amazon forest, the most extensive tropical mountain range, 84 of the 104 life zones identified in the planet and 27 of the 32 world climates. Of the four most important crops for human nutrition (wheat, rice, potato and corn), Peru holds high genetic diversity for the last two. It is also rich in the glacier areas (71% of the tropical glaciers of the world) that are of utmost importance for providing water for human consumption, agriculture, mining, and electric power generation" (MINAM, 2010). If global average temperature were to rise 2°C and rainfall variability were to increase by 20%, by 2050 there would be a 6% loss of the potential GDP in 2030; by the year 2050 such losses could exceed 20%. The adoption of global measures to stabilise climate variables in 2030 would allow the reduction of such losses to less than one third (BCR, 2009). The "Investment and Financial Flows for Climate Change Study"²¹ calculated that Peru will require more than US\$2.4 billion dollars until 2030²² to implement priority adaptation measures in the agricultural, water and fisheries sectors (UNDP, 2011). While Peru's current contribution to global emissions is less than 0.5% (PLANCC, 2013), the country is maintaining sustained economic growth which is currently highly linked to emissions.

Climate finance governance and architecture

To date, there has been no single concrete policy effort to integrate economic and social development, environmental management,

19 World Economic Forum: http://www3.weforum.org/docs/LA13/WEF_LA13_PeruTravelTourismSummit_Report.pdf

20 Trading Economics (based on Central Reserve Bank of Peru).

21 Conducted by Libelula in 2011 and supported by UNDP

22 Includes the regions of Junin and San Martin for agriculture, human consumption and sanitation for urban areas in coastal regions for water, and indirect human consumption and aquaculture for fisheries.

emission reductions and climate resilience goals into a single LEDS. However, there are several initiatives that push towards low emission objectives, and a framework for a comprehensive approach that considers climate change as intertwined with the country's main objectives has already begun to emerge.

The National Climate Change Strategy (NCCS) is the instrument that guides climate change management in Peru. The NCCS is a reference framework for all central government entities and for regional and local governments. One of its strategic lines is “the development of policies and measures oriented to manage GHG emissions to reduce the impact of climate change” (MINAM, 2011a). The NCCS in Peru is currently under review.

The Action Plan for Climate Change Adaptation and Mitigation (APPCAM) and the National Guidelines for Climate Change Mitigation (NGCCM), both developed within the Climate Change Directorate in the Ministry of Environment (MINAM), demonstrate the approach taken to mitigation actions. These instruments, while useful, only serve as guidelines and recommendations. The NGCCM proposes a national mitigation effort through the use of National Mitigation Programs (PRONAMI). PRONAMI covers forestry and land use; waste; energy; agriculture; transportation; industry; and buildings/housing sectors. Each PRONAMI should be coordinated by the respective sector and/or MINAM, and have a registry to account for mitigation actions and emission reductions.

A recent initiative, although sectoral in nature, is also clearly in line with a future LEDS. The Ministry of Energy and Mining (MINEM), with the help of the Inter-American Development Bank (IADB) has worked on a “New Sustainable Energy Matrix”.

A multi-sectoral Commission was created in 2012 to improve environmental management. Nine heads of ministries participated: Agriculture (MINAG), Culture, Energy and Mines (MEM), Economy and Finance (MEF), Health (MINSa), Production (PRODUCE), Development and Social Inclusion (MIDIS) and Environment (MINAM). As a result of the work of the Commission, four strategic pillars for environmental management were established. One of these aims to secure a sustainable natural heritage. Its objectives include the incorporation of climate considerations in development strategies, and the conservation and sustainable use of biological diversity as a development opportunity. This pillar proposes to strengthen and develop governmental and societal readiness for climate change adaptation and mitigation needs. The report of the Commission also highlights PLANCC as a national priority project, together with the definition of adequate institutional arrangements for climate change management and adequate climate finance (also referred to as PRONAGECC) (MC, 2012).

Key stakeholders facilitating implementation of climate action plans

Notwithstanding the importance of the many different stakeholders involved in this preparatory process for LEDS development, it is worth highlighting the crucial role that three ministries play, namely:

- > the MINAM, entrusted with climate change management and the focal point of two of the three sectors covered by Peru's international voluntary mitigation pledges (forests (in coordination with Agriculture) and waste management);
- > the Ministry of Economy and Finance, as main authority for economic, fiscal and tax policy; and
- > the MINEM, as the main authority for the sectors that account for most of the GDP growth, foreign direct investment and also the sectors most related to rising social environmental conflicts.

The national development bank, *Cooperación Financiera de Fomento (COFIDE)*, is also building an evidence base of innovative financing instruments for energy efficiency and renewable energy projects without existing international climate finance support (2 specific programmes). Civil society plays an important role in climate change, particularly *Libelula*, a Peruvian based NGO that provides technical coordination for *PLAANCC* and serves as an advisor to MINAM on *Interclima*.

Structure of domestic finance system

The banking and financial sector showed steady growth over the past decade. Total assets of the Peruvian banking system reached US\$70.4 billion at the end of November 2011.²³ According to the Central Reserve Bank, credit flow from financial institutions to the private sector has more than tripled since 2003. The Peruvian economy has strong capacity to allocate resources for important investments, which has given the economy the necessary dynamism to sustain a continuous rate of economic growth.

Positive features of the financial system in 2012 included: a) growth in loans; b) reversal of the influence of short-term foreign capital; c) improved liquidity in the financial system; d) low levels of unpaid debt; e) intervention of new participants; f) increased transparency; g) improvements in the quality of customer service; h) increasing trend of the micro finance sector, creating increased competition; i) adaptation to Basel III; and j) regulatory changes to *Superintendencia de Banca (SBS)*. On the other hand, negative features included: a) negative effect of the European crisis on export financing; b) possible slowdown in deposits; c) exchange market interventions by the Central Bank, to maintain low volatility of local currency; and d) slowing growth in consumer and commercial loans (COFIDE, 2013).

COFIDE is a mixed economy bank with 98.7% of capital owned by the Peruvian State. NDBs have been recognised as key stakeholders for national climate finance. COFIDE is seeking to play a strategic role in climate finance in Peru, supported by the IADB, with whom it is conducting a study regarding its potential role. COFIDE has developed the *COFIGAS* product that is closely related to climate change mitigation, by promoting the extensive use of natural gas by taxi drivers in Lima. In addition, COFIDE manages credit lines from JICA (the Japanese development agency) and KfW (the German development agency) for renewable energy development.

Table 3.2 International climate finance initiatives in Peru

Finance initiative	Focus	Resources	Project outcomes	Time scale
NAMAs (4 projects and 4 feasibility studies)	Multiple sectors including agriculture, energy, housing and waste management	Grants, loans & tech assistance	Demonstration results for future scaled up action	Short term
Climate Finance Corporation	Solid waste	Grants	Cooperation project grant to facilitate the design of a NAMA for the capture and utilisation of methane emissions from solid waste.	Short term
Germany's International Climate Initiative (8 projects)	Adaptation and mitigation, in the REDD+ and agriculture sectors	Grants	Adapting public investment to climate change in Peru	Short – medium
Fast start finance (Japan, 3 projects)	Mitigation and Adaptation, REDD+ and solar energy	Grants	Forest Preservation Programme (s)	Short – medium
MDG Achievement Fund	Adaptation	Grants	Integrated and adaptive management of environmental resources and climatic risks in High Andean micro-watersheds	Short – medium
Forest Carbon Partnership Facility	REDD+	Grants and technical assistance	Reducing emissions from deforestation and forest degradation, forest carbon stock conservation, the sustainable management of forests, and the enhancement of forest carbon stocks in developing countries (activities commonly referred to as REDD+).	Short – medium
KfW (with Betty Moore Foundation)	REDD+	Grants	Strengthening scientific technical capabilities for implementing REDD +	Short – medium
MDB (Inter-American Development Bank and World Bank)	Multiple sectors	Financial and technical assistance	Rural electrification from renewable sources, energy efficiency programme and REDD+ financing strategy.	Short – medium
Clean Development Mechanism CDM (63 projects)	Mitigation, multiple sectors	Finance	GHG mitigation	Short – medium
Global Environment Facility (GEF) (approximately 13 projects)	Mitigation, multiple sectors	Grants	Domestic implementation capacity	Long term
Partnership for Market Readiness (World Bank)	Public finance	Grants	Diagnostic for country use	Long term
Climate Finance Readiness Programme (BMZ – Germany)	Accessing International Climate Finance	Capacity Building	Institutional support, National GCF investment plans and corresponding project pipelines, study on options for supporting a national fund.	Short – Long term

Source: Authors' analysis as of February 2014, based on engagement at country level and publicly available information.

International climate finance initiatives

A wide range of international climate finance initiatives are already underway in Peru, as Table 3.2 demonstrates. Initiatives listed in this table are based on a literature review of publicly available information and interviews with stakeholders in Peru during the course of the scoping work. This list is not exhaustive, but is intended to illustrate the scale of climate finance-related activity in the country.

While there are a few examples of support for energy efficiency or renewable energy projects, for example cooperation with the GEF and Peru's efforts on NAMAs, the majority of international climate finance seems to be directed towards REDD+ or other forestry-related activities. At present, there is no formal climate finance coordination or tracking system within Peru, however, PRONAGECC aims to achieve this once implemented.

Summary of key findings on climate finance

The scoping study identified some modest efforts underway in Peru to push forward a low emission and climate resilient agenda. The Peruvian government is working with industries to deepen understanding of sustainability issues. Similarly, COFIDE is funding green investment programmes for small and medium sized businesses. A key focus moving forward is to continue deepening engagement with the private sector to build capacity and champions from business to engage with government to promote understanding, identify priorities and consider financing impacts and needs of programmes/strategies that emerge. Regarding climate finance specifically, the following findings have emerged:

- > Several key barriers were identified to LEDS in Peru and the country is still in the pre-investment or "readiness" phase. There is a strong focus on economic development and poverty reduction and to some extent a scepticism that this can be reconciled with national climate action plans. Interviews conducted during the country visit indicated concern from developmental banks that NDBs are not necessarily being market catalysts but rather creating distortions in the market. Country partners also identified capacity constraints within institutions in their management of risk and their ability to conduct environmental impact assessments. There is a clear need to build better understanding of the value of green investments.
- > Some important progress is being made regarding NAMAs: proposals are being prepared in the transport, waste, bioenergy, construction, housing and buildings sectors. During the course of 2014, various consultations may be arranged on a sector specific basis to refine the technical and resource requirements of the proposed NAMAs.
- > A fragmented regulatory framework poses a further challenge. The current "rules of the game" for Peru, both for environmental management and climate change manage-

ment, lack the needed clarity and organisation, sending incorrect signals to key stakeholders that environmental management is about permitting and is an obstacle to investment. A harmonised, coherent and clear regulatory framework would have great impact both on public and private finance.

- > Improving liquidity of the financial system is an opportunity: by the end of 2012, private sector liquidity registered an increase of 14.5%. There are resources that could be channelled for climate-related programmes.
- > It is also important to recognise financial capacity constraints: multiple sources - ranging from international support, public finance, financial markets and private sector investment (in its multiple forms) - need to be structured and assembled adequately to enable effective climate finance. At this stage, Peru is lacking the correct financial architecture to efficiently channel resources into climate change needs.

Despite the fact that Peru has no overarching LEDS in place, Peru's readiness for addressing the complex climate change challenge is increasing steadily. It is encouraging that many smaller scale instruments have been established to advance climate change mitigation. Climate change has been considered within Peru's legal and policy framework since the beginning of the last decade. Current initiatives, such as PLANCC and the Multi-sectoral Commission, show an increase in climate awareness among relevant authorities, and that the country is willing to improve its information and evidence base, and include sharing, reporting and priority setting. Growing international cooperation and an increase in public expenditure has resulted in more institutions outside the "environmental arena" looking into climate action. A good example is COFIDE, which has been identified as a key institution for catalysing climate finance. While it could be considered both a threat and an opportunity, continuous economic growth and improving development indicators increase Peru's ability to raise and relocate resources and efforts towards climate change.

3.3 Chile

With a population of 17 million Chile is among Latin America's fastest growing and most stable economies. During the past 20 years, the country recorded an average annual growth of 3.5% and per capita income almost doubled in real terms (World Bank 2014). The mining industry is critical to Chile's economy, particularly copper, lithium, and gold²⁴. Chile has a relatively low unemployment rate of 5.9%.²⁵ Exports account for approximately one-third of GDP, with commodities comprising approximately three quarters of total exports.²⁶ Over half of Chile's power generation comes from fossil fuel sources, with more than 80% of such fuel being imported. Energy demand is growing and is estimated to double from 2010 to 2020, and triple from 2010 to 2030 (NRDC, 2011). Accordingly, Chile's energy sector is at the centre of discussions for defining a new sustainable path.

24 KPMG 2014: <http://www.kpmg.com/Ca/en/industry/Mining/Documents/KPMG-Mining-country-guide-Chile.pdf>

25 OECD 2014

26 Economy Watch: http://www.economywatch.com/world_economy/chile/export-import.html

27 Gobierno de Chile National Climate Change Action Plan (2008-2012). Available at: http://www.mma.gob.cl/1304/articles-49744_Plan_02.pdf

Chile is highly vulnerable to extreme weather events and climate change poses high risks to its water resources. The southern region is particularly affected by reduction in glacier volume.²⁷ Chile has seven of the nine characteristics indicated in the UNFCCC vulnerability framework. Chile is only responsible for 0.2% of the world's total emissions of greenhouse gases although the country has relatively high per capita GHG emissions for the region (second in South America)²⁸.

Climate finance governance and architecture²⁹

The government of Chile created the National Advisory Committee on Global Change in 1996, with the presidency given to the National Environment Commission (CONAMA) and the vice presidency to the Ministry of Foreign Affairs. The Committee not only advises on national communications to the UNFCCC, but studies and proposes actions for mitigation, adaptation and finance mechanisms, such as the CDM. One of the key outcomes of the Committee was the formulation of the National Climate Change Strategy for Chile, which was approved in 2006 by CONAMA (the Ministry of Environment replaced CONAMA in 2010). This is structured around three key axes: adaptation; mitigation; and formulation and strengthening of national capacity, which acts a transversal area.

In 2008 the National Climate Change Action Plan 2008-2012 (PACC) was approved to implement the strategy. PACC was designed to address the identified axes using a participative process, including various national academic and research bodies and the articulation of the policies across governmental bodies around climate change. PACC's main objective within the designated four year period is to generate the information required to define the national and sectoral plans for adaptation and mitigation to climate change for the long term. PACC has 22 action lines and 103 specific actions, involving 13 sectors and 32 national entities.

Progress in PACC on the mitigation and adaptation axes includes the formulation of the National Action Plan for Adaptation and Sectoral Adaptation Plans. The forestry, agriculture and livestock plan was launched in 2013; the biodiversity action plan is expected in 2014; fishing and health sector action plans are expected in 2015; adaptation plans for infrastructure, hydro and energy sectors will be ready in 2016 and the tourism sector plans ready in 2017. In mitigation, the focus has been on developing a national inventory system and formulation of mitigation scenarios through the MAPS-Chile initiative, as well as in evaluating the mitigation potential of different sectors and specific actions, which has been undertaken through sectoral NAMAs and energy efficiency programmes as well incentives to renewable energy. National mitigation activities are ongoing and currently being developed under the Low Emission Capacity Building Programme (LECB) – Chile project.

The third axis focusing on capacity building has seen, among other outcomes, the implementation of the Climate Change

Office within the Ministry of Environment and climate change advisory committees across various ministries. The project provides support for the design and implementation of a low emission development strategy and sectoral mitigation actions in the public and private sectors through: defining and operationalising a national GHG inventory system; designing and undertaking a voluntary carbon management programme; and developing a MRV system for national NAMAs. The Ministry of Environment is leading the project, acting in a coordinating role with other ministries through the “Ministries Committee on Climate Change” (which includes Energy, Agriculture, Transportation, Mining, Public Works, Industry, Foreign Affairs and Finance). In addition, a National Project Steering Committee comprises representatives from key ministries and institutions³⁰.

Another example of the coordination among governmental bodies is the National Green Growth Strategy³¹, which was presented by the Ministry of Finance to the OECD in December 2013³². This takes a general vision of environmental policy in Chile and is in accordance with the specific adaptation and mitigation plans. The strategy includes the implementation of environmental management instruments; development of the national market of environmental goods and services (eco innovation and entrepreneurship, green employment and training); and monitoring and measuring the strategy through green growth indicators, environmental behaviour indicators and a wellbeing indicator.

In 2013 the Climate Change Advisory Committee composed of 14 ministries was introduced, replacing the National Advisory Committee on Global Change. This Committee is responsible for the implementation of national policies, plans and programmes for climate change response, as well as monitoring and coordinating the various initiatives that fulfil national commitments to the UNFCCC.

There are also a number of national initiatives driving investments towards climate change actions outside PACC. For example, the National Development Agency for Production (CORFO) programme provides direct support, including competitive funds and pre-investment studies for renewable energy projects and energy efficiency. The Centre for Renewable Energy (CER) was created in 2009 under CORFO and includes the establishment of an information centre, pilot programmes and other knowledge sharing activities. The Ministry of Economy established the National Energy Efficiency Programme (PPEE) in 2005, which became the responsibility of the National Energy Commission in 2008. The programme's budget has risen from US\$1 million in 2006 to close to US\$40 million in 2009³³. The Chilean Energy Efficiency Agency was created in 2010, which is the successor to the PPEE. The new mandate is to design and establish public policies for energy efficiency. In addition, Chile has experience with the CDM, with 141 projects approved by the Chilean Designated National Authority. It

28 <http://cdkn.org/regions/chile/>

29 Resources: Ministry of Environment of Chile and CONAMA

30 UNDP Low Emissions Capacity Building Programme, Chile

31 Government of Chile National Green Growth Strategy December 2013. Available at: <http://www.hacienda.cl/english/press-room/news/archive/national-green-growth-strategy.html>

32 <http://www.oecd.org/chile/countries.htm#chi>

33 2nd National Communication of Chile to the UNFCCC. Ministerio del Medio Ambiente. 2011.

is also exploring carbon market mechanisms and has acquired relevant energy policy experience through regulations such as Law 20.257, which was introduced in 2007 to support development of non-conventional renewable energy (NCRE). This law requires energy companies to ensure that a portion of the energy they supply comes from NCRE, or otherwise pay a penalty. Although the policy does not seem to have generated the impact expected (NRDC, 2011) these are valuable experiences to build upon.

Key stakeholders facilitating implementation of climate action plans

In 2010, law 19.300 article 70 defined the Ministry of Environment as the body responsible for policy proposal, plans and programmes to address climate change. In order to fulfil this mandate, the Ministry has created the Climate Change Office under the Sub-secretariat of the Ministry of Environment. This Office has a stream of work dedicated to LED strategy to facilitate this process across government and is now considering Chile's post 2020 targets. In addition, the cross-sectoral Climate Change Advisory Committee also has an important role in LEDS implementation.

At a technical level, the Government of Chile also specified in the PACC the bodies responsible for the execution of each of the priority areas defined for the three axes, which includes 13 ministries and 23 organisations (mix of academic and scientific institutions, ONG's and committees). The Ministry of Energy and Agriculture are some of the leading bodies in climate change matters, with the Ministry of Energy having strong interest in promoting investment in renewables.

Finally, a key role is played by the Ministry of Finance (the Hacienda). The Hacienda has a deep understanding of the LEDS³⁴ process and supports developing a national financing plan towards implementation, subject to economic and social objectives being articulated. It requires such objectives to be framed within the context of economic growth, competition, and seeks to avoid market distortions through the proposed interventions.

Structure of domestic financial sector

The country's financial system is large and well diversified compared with other countries in the region. In a report in 2013, the OECD³⁵ found that banks have a strong financial position and adequate liquidity ratios despite the difficulties presented by the international context. Solid capital buffers and lower and more diversified external financing (less than 10% of its liabilities) limit vulnerabilities. However, in the third quarter of 2013, the cumulative current account deficit was 3.4% of GDP, which implies a slight reduction compared to that observed in 2012 and a third consecutive year with a deficit. This result was influenced by the largest deficit of the balance of trade and services, which was offset by lower income referral abroad, particularly mining. International reserves fell slightly, from US\$41,650 million in December 2012 to US\$41,149 million in November 2013.

Bank lending eased in the second half of 2013, which is consistent with the slowdown in economic activity. Financing conditions remain favourable in the local market, long-term rates have been stable, and money market spreads are around the system's historic average. The solidity of the banking sector explains the high international credit ratings of the larger institutions at the global level and their ability to access external debt and credit markets.

Commodity export investment contributed 50% of GDP growth between 2010 and 2012³⁶. Investments in the mining sector between 2010 and 2012 represented an average of US\$3,700 million with gross figures over US\$6,000 million, representing 45% of total investment in 2012, up from a 13% share in 2000. Non-mining investments represented US\$ 7,200 million in the same period. In a report in 2013, the BBVA forecasted that projects related to mining, energy and real estate will represent about 70% of the total investment portfolio with a significant increase of private investment in large energy projects in 2013, and an increase in the total investment in 2014 led by energy projects, with a moderate increase in mining investment.

In terms of investments in renewable energy, the Climatescope 2013 report indicates that the average costs of debt for renewable energy projects ad swap rate are the third lowest among the region's countries. This enabled US\$2 billion investment in Chile's clean energy sector in 2012, of which local financial institutions were responsible for financing US\$300 million. 67% of the total investment went to wind projects.³⁷

International climate finance initiatives

A number of important climate finance initiatives are underway in Chile, as demonstrated in Table 3.3. Initiatives listed in this Table are based on a literature review of publicly available information and interviews with stakeholders in Chile during the course of the scoping work. This list is not exhaustive but is intended to illustrate the scale of climate finance related activity in the country.

Chile has made good progress in developing NAMAs and is working with UNDP to develop a LEDS, including sectoral mitigation actions in the public and private sector and a MRV system for national NAMAs. Chile is in the process of ramping up efforts to identify priorities and articulate national objectives for international climate finance, including conducting a landscape study of ongoing climate actions and resources. This study may lead to the development of a larger suite of potential initiatives.

Summary of key findings on climate finance

Chile has articulated an extensive national action plan for climate change, which has engaged cross-sectoral ministries, academics and NGOs. This plan is currently allowing evaluation of the baseline in which the country stands in relation to climate change and its translation into the cross-sectoral mitiga-

34 Recently led the National Green Growth Strategy presented to the OECD <http://www.oecd.org/chile/countries.htm#chi>

35 OECD (2013) Estudios Economicos de la OECD: Chile. Available at: <http://www.oecd.org/eco/surveys/Overview%20Chile%20spanish.pdf>

36 BBVA Research Observatorio Economico: Chile. November 2013.

http://serviciodeestudios.bbva.com/KETD/fbin/mult/BBVA_SEEChile_ObservatorioInversi_n_1311_tcm346-411470.pdf?ts=2522014

37 Climatescope 2013 New frontiers for low carbon energy investment in Latin America and the Caribbean. Bloomberg New Energy Finance.

Table 3.3 International climate finance initiatives in Chile

Finance initiative	Focus	Resources	Project outcomes	Time scale
NAMAs (4 registered projects, 1 in process, 3 feasibility studies)	Multiple sectors including transport, energy efficiency and agriculture	Grants, loans & tech assistance	Demonstration results for future scaled up action	Short term
NAMA Facility	Mitigation	Grants	Displacing around 2 million tonnes of CO ₂ by implementing 60 MW in projects from technologies such as biogas, biomass and photovoltaic, for energy self-supplying systems in Chile's commercial-industrial sector.	Short term
UK Prosperity Fund	Mitigation	Grants	To finance the Santiago Transport Green Zone (STGZ) NAMA research	Short term
Canada Fast Start	Financing Mitigation	Grants	NAMA readiness support	Short term
Clean Technology Fund (CTF) (2 projects)	Mitigation, renewable energy	Grants and loans	Scale up the demonstration, deployment, and transfer of low carbon technologies	Short – medium
Clean Development Mechanism CDM (105 projects in CDM registry; 141 projects validated by Chilean state)	Mitigation, multiple sectors	Finance	GHG mitigation	Short – medium
Global Environment Facility (approximately 14 projects)	Mitigation, multiple sectors	Grants	Domestic implementation capacity	Long term
Low Emission Capacity Building Programme (LECB) – UNDP	Mitigation	Capacity building	Support for the design and implementation of a low emission development strategy and sectoral mitigation actions strategy.	Long term
Partnership for Market Readiness (World Bank)	Public finance	Grants	Diagnostic for country use	Long term
Readiness Fund of the Forest Carbon Partnership Facility	Forestry	Grants	Strengthening technical and institutional capacities to participate in a future REDD+ mechanism	Long term

Source: Authors' analysis updated February 2014 based on a literature review and interviews with stakeholders in Chile

tion and adaptation actions required. In addition, there is relevant experience in the following areas:

> Chile has made important progress by setting up institutional arrangements for coordination and implementation of mitigation and adaptation actions, including the structural arrangements for the delivery of the LECB-Chile projects with a robust framework. Evaluating the capacity of the current arrangement for effective finance coordination will be required once Chile starts moving into the implementation phase of the climate change actions currently being defined.

> As the actions for mitigation and adaptation across various sectors are defined between now and 2016, it is critical to develop a congruent national vision for financing these activities. Efforts have begun with the establishment of a public working group on NAMAs and capacity building workshops on this subject as well as MRV. Chile understands the importance of having a strategic view for financing these activities, and is also seeking the formulation of a national financing pathway for implementation of the defined actions.

> Wider stakeholder engagement will be needed when defining a credible finance strategy that can help to deliver

transformational change. Key actors inside the government, such as the Hacienda, and other actors in the private sector need to be brought closer to the processes around defining a NFP. Their input and buy-in on the need for investments in developing such planned actions will be vital. This need is well understood within climate change authorities in the government and activities to engage both actors will take place in 2014.

Chile ranks third in investment on renewable energy in the region and has relevant experience in putting in place energy policy for encouraging the switch into renewable energy sources as well as in exploring innovative financing instruments which may be attributed in part to a strong financial system. The current efforts to better understand and define its climate change programmes, barriers to investment and financing needs sets a positive landscape for development of a coherent NFP to mobilise resources for the country's climate action plans.

3.4 Key findings of the scoping work

Emerging themes across the case studies reveal some valuable insights:

- > LEDS governance and the coordinating and engagement structures for climate action vary within countries. The effectiveness of these structures determines the quality of intergovernmental engagement, which in turn has an important role when developing robust and strategic approaches to climate finance.
- > There is an agreement in principle on the integration of LEDS and climate resilience (adaptation) with national development priorities. To ensure that the proposed plans and programmes also contribute to the economic transformation of these countries, broad and dynamic engagements between the public and private sector is necessary when addressing issues such as appropriate regulatory environment and financial models.
- > The structure and maturity of the domestic financial sector is a key factor in countries taking leadership in the implementation of climate action, guided by economic priorities. The depth and capacity of the financial sector may determine its ability to develop strategic approaches to climate finance and in the long term, contribute to mainstreaming climate action into broader investment and risk decisions. There is also growing discourse on the role of NDBs and other key financial stakeholders in creating the appropriate environment for climate investment, instilling market confidence to support the efforts of the national government.
- > Developing a cohesive storyline for a country's climate action (through plans such as NAMAs, LEDS and NAPAs) is critical to ensure an investable programme and project pipeline that delivers the desired transformative effect on the economy, social systems and environmental impact.
- > International climate finance is not regarded as a panacea for national climate action plans. Each country is adopting

a proactive and dynamic approach to mobilising both national and international sources and seeking ways to effectively utilise such finance. Having said that, Peru, Chile and Colombia represent middle income developing countries, with Chile an OECD country and Colombia in the process of accession, which have strong internal governance, mature domestic financial markets and institutional capacities upon which to draw for climate action. These characteristics are not necessarily applicable for least developed countries.

3.5 Concluding statements

This scoping work has revealed a deep commitment by the governments of Peru, Chile and Colombia to further their understanding of the financing challenges associated with their climate change action plans through a process of national self-evaluation. In addition, they are seeking a balance between financing approaches for mitigation and adaptation actions, and ways to attract private sector investment to support governmental efforts in both responses. It is also clear that these countries view international climate finance as a contributory (rather than sole) source of funding, which they can utilise to advance their national efforts. These countries also recognise the importance of identifying and defining complementary roles for the private and public sector in advancing short, medium and long term climate change action plans. In addition, consideration is being given to the appropriate institutional arrangements and coordination mechanisms necessary for financing and utilising climate finance more effectively at country level. Each of these three countries is at some stage of developing a national financing pathway or strategy for their climate change plans.

4. Emerging conceptual frameworks

This scoping work has helped identify issues of relevance to the emerging concept of a NFP. Reflecting on the developments described in Chapter 3, this Chapter aims to organise E3G’s observations into process learnings and emerging concepts that may be useful for other countries to consider as they navigate similar challenges.

4.1 Developing a working definition for “National Financing Pathways”

The ability to mobilise and leverage different forms of finance, both public and private from domestic and international sources, will be key to delivering the steady transition to a LECR development paradigm. For this reason, NFPs are put forward in this paper as a concept that articulates the interdependencies between public, private and international sources of finance when delivering scaled investment to support the implementation of low emission and climate resilient development. The interplay between national policy objectives and institutional frameworks with various sources of finance can be considered as constituting a national finance ecosystem, and so influencing the shape and pace of the NFP.

A NFP can be considered as the strategic outcome of a process whereby a country determines, defines and mobilises the financial and other resources necessary for its transition to a LECR development path over a period of time.

In the context of the climate change action plans developed by countries, such as LEDS, NAMAs and NAPAs or green economy strategies, NFPs may provide strategic direction to support implementation of these and other relevant climate-related

plans. Such plans are intended to be fully integrated into national development priorities; the reality in the case of Peru, Chile and Colombia is that national planning departments, environmental and finance ministries are working closely together to determine how best to achieve this integration.

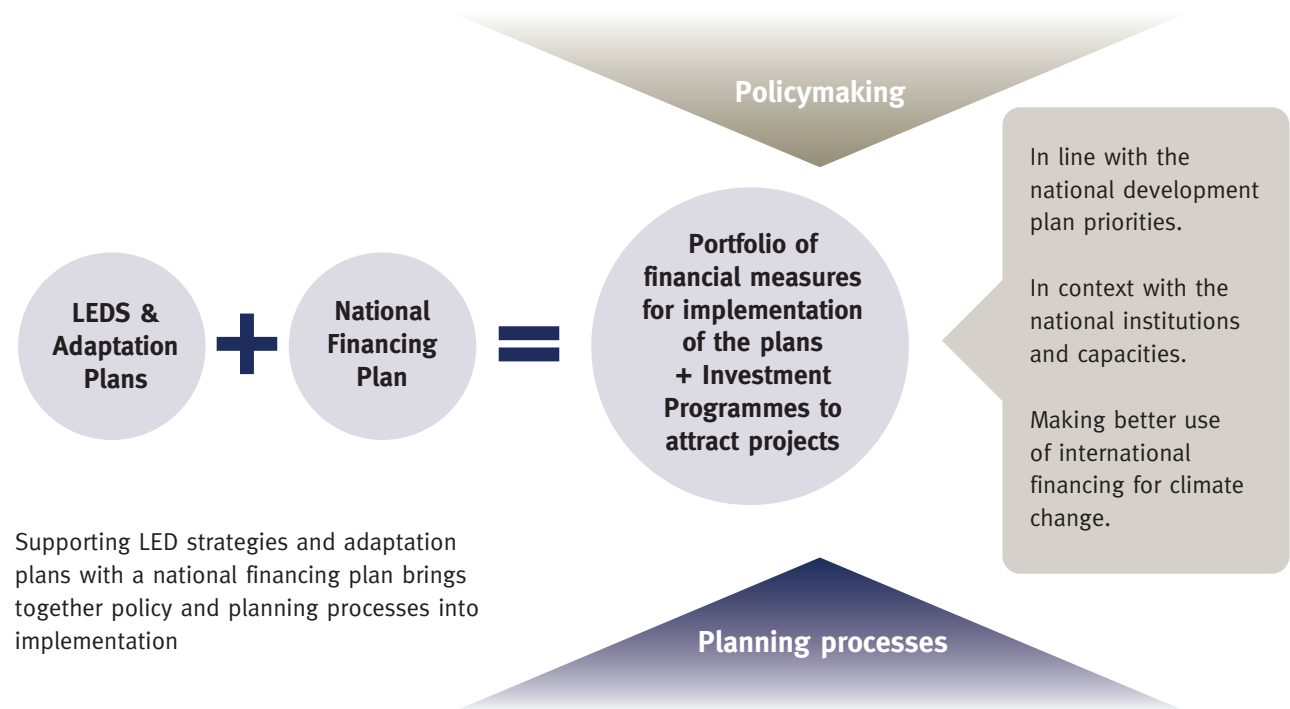
A key outcome of ensuring that the plans have a clear financing strategy is being able to deliver investment programmes and projects (Figure 4.1). This pipeline in turn would provide private and international climate finance providers with clarity regarding the priorities and actions of the national government over a period of time. Such clarity instils investor confidence, and based on the NFP, the defined role for private, public and international climate will be identified and harmonised. The unique and complementary roles of different stakeholders in the financial system, including engagement with international providers of climate finance, would ideally be articulated in the NFP. Such roles would reflect their individual and collective ability to most effectively facilitate the implementation of a country’s climate action plans.

This process will necessarily involve robust and inclusive engagement with key stakeholders to understand their roles and capacity requirements for delivering appropriate, adequate and predictable financial resources for the long term transition to a LECR economy.

4.2 Iterative approaches with key stakeholders and processes

The development of climate action plans (e.g. LEDS, NAMAs and NAPAs) has involved iterative cycles of engagement with public, private and international stakeholders to ensure that they

Figure 4.1 NFP in context of policies and plans



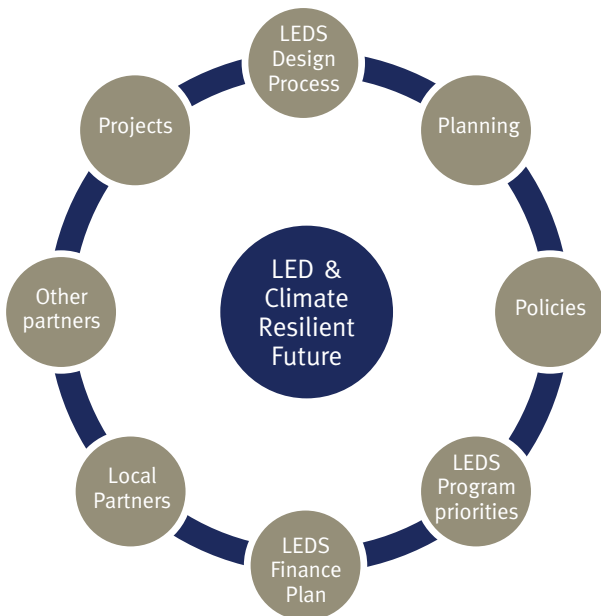
Source: Authors’ depiction

address the development objectives of each country. It is a complex process to ensure that the plans are implementable and are at sufficient scale to advance a country's efforts towards LECR development. The implementation of these climate action plans is dependent on the appropriate resources, capacity and institutions for a sustainable transition.

As the concept of NFPs emerges, it becomes apparent that financing is not a linear approach, but will be an iterative process involving multiple policy and sectoral decisions (see Figure 4.2). The NFPs can help bridge the gap between the design of climate change action plans, development processes and national budgeting and financial decision-making processes. NFPs can assist in focusing efforts on mobilising local and international partners and catalysing private sector capital over time. Ongoing and structured engagement with non-governmental stakeholders, including the finance sector (e.g. regulators and providers), can deepen the analysis and facilitate understanding and mitigation of barriers to scaling up investment.

Through this iterative and consultative process, countries may become increasingly confident in developing a target investment range on either a sectoral or national basis (e.g. renewable energy investment targets or setting a national target for carbon emission reductions). Delivering on these investment targets will involve public support that may be channelled through a range of policy and regulatory support measures, risk mitigation mechanisms and institutional strengthening programmes, for example to develop markets that capture the benefits of technology transfer.

Figure 4.2 Iterative cycle linked with NFP



Source: Authors' depiction

Resource mobilisation is likely to follow a similarly iterative process of engagement with different stakeholders at the national and international level. Depending on the unique circumstances of each country and building upon the existing local work by government or through its partners, such cycles of engagement

will follow specific routes. For example, in Colombia, SISCLIMA's Finance Committee represents a platform where such iterative engagement can occur, drawing together the sectoral plans and their related financing challenges. Given its mandate to consider innovative approaches for finance, the inputs of the different sectoral departments are interrogated and the aggregate impact is being considered holistically to ensure the overall financing frameworks for implementation of their climate change responses are in place. The iterative process means that the programmes are scrutinised in depth and a robust proposal is likely to emerge that helps to ensure sustainability.

Resource mobilisation is a critical outcome of a strategic approach to climate finance and will require an assessment of the appropriate financing structures at programme and project level, prior to the climate action plans being launched.

Existing efforts at the country level that support an iterative process of engagement are:

- > Country workshops on NAMAs in Colombia and Chile, focusing on the technical and financial components of these NAMAs to facilitate commercial interest in the proposed actions.
- > Annual national workshop in Peru (Interclima) showcasing Peru's climate change efforts and challenges and inviting commentary and engagement from a host of national and international experts to refine response strategies. This promotes transparency, enables country leadership and creates a sense of ownership in both public and private sectors.

4.3 Evaluation of national financing systems and capacity

A deep understanding of the national financing systems and capacity is essential to developing NFPs for implementation of climate change plans. Each component of the national finance system, i.e. public budget, private finance institutions, capital markets, commercial and retail banks, microfinance institutions and development agencies, have a role to play in the creation of economic growth in the country. Framing national development and climate change priorities as investment opportunities creates the scaled up demand for investment that facilitates the transfer of capital, in turn securing implementation of both mitigation and adaptation priorities.

Several key questions emerge which are essential considerations in developing an NFP to implement a country's LECR plans. These include:

- > What economic incentives and risk mitigation mechanisms are required to trigger behavioural changes and redirect investment flows into new sectors and business models?
- > How can these incentives be integrated with other development and budget priorities, and what are the opportunities for integrating these?
- > What is the role for specific policies and regulations for incentivising low emission and resilient investments?

Depending on the answers to the above, the residual national public financing challenges can be identified and address further questions which would represent the core of an NFP:

- > Who are the key domestic financial players that will need to take action?
- > What is the role of existing or new domestic and international public financial mechanisms for mobilising investment for financing the pathway to LECR development?
- > How are existing or new financing mechanisms and instruments to be deployed, and what is the interaction with public policy and regulatory frameworks for catalysing the scale and pace of investment required?

The responses of Chile, Colombia and Peru to these questions has led to the commissioning of studies³⁸ of the domestic climate finance landscape to determine the:

- i) environmental and climate change measures in the national budget;
- ii) regulatory environment and existing environmental measures in the national finance institutions;
- iii) absorption capacity of the private finance institutions, capital markets and institutional investors for climate investment;

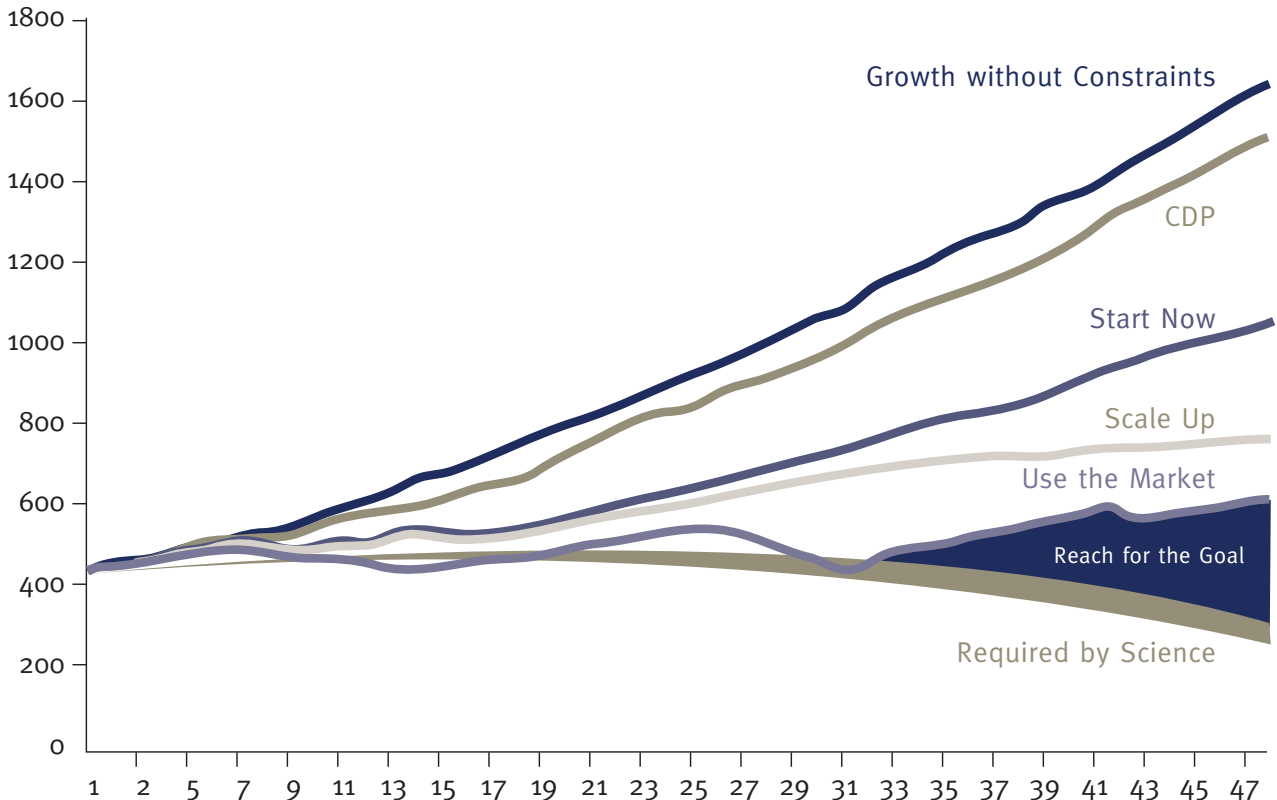
- iv) context and impact of international climate finance efforts, including assessments at programme and project level in certain instances where such information is available;
- v) institutional and coordination mechanisms necessary to facilitate higher access to climate finance; and
- vi) priority areas for a national climate finance pathway and strategy.

A national strategy which articulates the role of public and private capital enables governments to consider upfront an entry and exit strategy more effectively. In addition, the long term policy and financial mechanisms that governments may introduce can be assessed in the context of the life span of new and existing incentives and subsidies, providing appropriate signals to attract private capital at scale. As a first step towards design of a strategy, governments can also benefit from a self-evaluation of their technical, financial, institutional, policy and other capacities needed for implementation and thereby choose their climate finance providers more effectively and efficiently.

4.4 Scenarios to develop pathways

Countries such as Peru, Colombia, Brazil and Chile have been developing mitigation and adaptation scenarios through programmes such as Mitigation Action Planning Scenarios (MAPS) to enable them to develop scientifically based options from which to chart a course of action. In the case of South Africa, on which the MAPS programme has been modelled, Long Term

Figure 4.3 Long Term Mitigation Scenarios for South Africa



Source: Energy Research Centre, 2007

38 To add specific mention of UNEP (Barrier analysis), UNDP (SMAPs), World Bank (PMR), GIZ (climate readiness) and CPEIR, CCAP (NAMAs)].

Mitigation Scenarios (LTMS) were developed by the government as part of planning its response to climate change (Figure 4.3). The scenarios are premised on bridging the gap between two scenarios reflecting “Growth Without Constraints” (i.e. no GHG concerns) and “Required by Science” (i.e. South Africa reduces emissions by 30 to 40% by 2050). The LTMS provided a platform to determine and prioritise South Africa’s mitigation options (Energy Research Centre, 2007).

In a similar manner, financing scenarios can be developed depending on a country’s chosen climate objectives and likely trajectory for delivering these priorities. Developing similar scenarios linked to finance and resource mobilisation more broadly can provide various options for countries to consider, based on three critical areas:

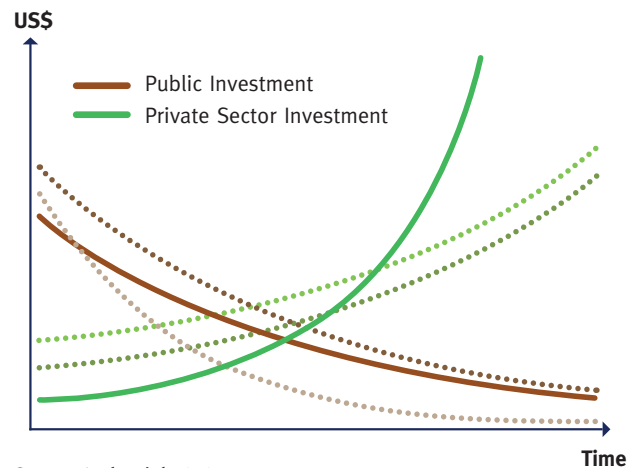
- i) policy incentives, direct public finance support through taxes and subsidies as well as allocations to NDBs, including the duration of support provided by the national budget to implement these priorities;
- ii) ability of private finance institutions to invest in prioritised actions; and
- iii) certainty and predictability of the investment flows from the international sources of finance.

An additional factor to build into such financing scenarios is the relative contribution of public, private and international cooperation during periods of low to high economic growth. For a sustainable transition to a low emission and climate resilient development path, it is essential that a base level of certainty, predictability and access to finance is maintained throughout implementation. Otherwise efforts may be undermined, resulting in a loss of investor confidence.

A number of tools may be useful in helping to analyse the responses to the questions raised in section 4.3 above. The scenario analyses should be adapted to individual country circumstances based on the interplay of public and private capital within their economies. Figure 4.4 illustrates how pathway scenarios can be developed to identify potential flows of public finance versus private finance. The illustration in Figure 4.4 assumes that public finance is best utilised to reduce risks of climate investment in the initial stages of implementation. Public finance would progressively attract private sector investment as the risk profile of particular actions reduce over time and thereby become more attractive to private investors. This in turn provides a natural exit for government for certain types of interventions where public finance has served a catalytic role. However, certain types of investments may require longer term public support especially those linked to socially driven measures and adaptation efforts. As public finance declines over time, private finance would therefore progressively assign more capital to climate actions and facilitate the transition towards LECR economies.

Developing different financing scenarios for the implementation of climate action plans in close consultation with national stakeholders, particularly the private sector, can create greater

Figure 4.4 Potential Financing Scenarios to determine National Financing Pathways



Source: Authors' depiction

transparency and confidence regarding the country’s investment pathway, increasing the confidence of private sector investors. The financing scenarios can therefore provide a useful basis to assess different ways in which to allocate public resources, both domestic and international, and as well potential roles for the private sector in programmes that integrate climate change priorities into key sectors of the economy. NFPs can also serve as a tool for identifying and facilitating a dynamic pipeline of scalable and replicable projects for financing. As emphasised in section 4.2, an NFP would be an iterative process of “learning-by-doing” amongst all key stakeholders involved in the financing and implementation of climate change strategies and plans.

4.5 Assessing resource needs for climate action plans

Discussions with country partners highlighted the value of developing a diagnostic tool to assist them in considering the different financing aspects of their climate change action plans. This need is particularly relevant as different ministries are engaged in the developing of mitigation scenarios, climate vulnerability and risk assessments, climate resilience plans, determining priorities and translating these into specific programmes of action and determining the associated budget allocations. Typically, the capacities to develop the technical components of the mitigation scenarios and climate resilience plans reside in the environmental and sectoral ministries (and in the case of Colombia, the planning ministries as well), whereas the assignment of budget involves mainly the national finance, and in some instances, the economic planning ministries (e.g. Peru and Colombia). By the time it reaches the national finance ministries, there is normally an expectation for a clear and crisp budget application for consideration.

Therefore, in an attempt to develop a crisp budget application for the climate change action plans, a series of questions (per Table 4.1) have been developed to assist in refining the resource components of climate change programmes and consider the different sources of funding in a holistic manner (Naidoo, 2011). These questions were developed as part of research to develop policy recommendations for climate finance for South

Africa's National Climate Change Response Plan and contributed to the design architecture of its national Green Fund.

Table 4.1 Evolving diagnostic to aid development of National Finance Strategies

- > What are the constituent elements of the LECR plans and their financing needs?
- > What resources are required and available for the different stages of implementation?
- > What specific resources are needed to finance these sectors, i.e. where are financing gaps?
- > Which national and international development partners are best suited for implementation?
- > What is the desired role of the financial intermediaries?
- > How should risk be allocated between these intermediaries to catalyse investment?
- > What are the support structures and institutional mechanisms available and required?
- > How do existing international climate finance mechanisms, such as NAMAs, GCF Readiness programme and similar initiatives, bridge existing gaps within national finance landscape?
- > How are these resources accessed by those that require them most?
- > What monitoring mechanisms would be best suited to track country's progress?
- > What are the key variables that may influence different financing scenarios for LECR implementation relative to competing national priorities?

4.6 Proposed core principles underpinning a NFP

Countries are mainly concerned with integrating their development and climate priorities to achieve economic, environmental and social objectives. Based on these concerns, the authors have proposed the following set of working core principles that could underpin a country's NFP, focusing on a "demand driven" approach to climate finance:

- > **Inclusivity** means creating the enabling conditions across the financial system to support climate investment, including financial policies and regulation, investment and risk appraisal, portfolio management and appropriate mechanisms to support programme and project development. For example, in Colombia the President and the Chairperson of the Banking Association have committed

to the Green Protocol, which focuses on developing enabling conditions within the banking system to advance environmental, social and governance factors in investment decisions.

- > **Equitable access to finance** means facilitating access to appropriate resources for transformational change through large scale investment and small to medium term enterprises. Therefore the finance strategy should focus on utilising the unique roles of all key financiers involved in both large and small scale financing, including commercial and development banks as well as microfinance and trade organisations. The resources harnessed should contribute to job creation and new business development for both large and small scale investments. A particular country's focus on either large or small scale investment would be dependent on the structure of its economy, its finance system and national priorities. In the case of Peru, this is particularly pertinent as the majority of the country's GDP is based on small businesses and therefore access to finance at national, sub-national and rural level is critical, as well as the need to create economic opportunities for small businesses.
- > **Effective** means mobilising the appropriate national and international resources to eliminate and/or significantly reduce the financial barriers associated with implementation of the climate change action plans. The NFP should promote a holistic resource package for the implementation of such plans and facilitate the delivery of outcomes that are aligned with country priorities and the necessary institutional, technical and other capacities. A key element of effectiveness in the context of a NFP is ensuring that the demand for finance is matched to the most pressing and urgent need, thus enabling transformational change by supporting a sustainable transition.
- > **Predictable** means securing resources from different sources to support a long-term implementation and transition to a LECR economy. In practice this means that the country should have certainty of the resources that are available over a defined time horizon, as well as define upfront the role of its public finances to promote and catalyse investment to support the transition. In addition, a country should be assured that the stakeholders within its financial system and its development partners are committed to delivering on their respective financial mandates.
- > **Transparency** means ensuring that the country has clear definitions and systems that allow for tracking and evaluation of the financing flows, in terms of the four core principles above (effectiveness, sustainability, equity and inclusivity). These systems should track necessary information that provides valuable feedback for future policy, planning and resource mobilisation efforts on a "learning-by-doing" or iterative basis. This will not only have a dimension for self-evaluation at national level but will also support the international finance dimension (i.e. MRV needs).

4.7 Mapping a NFP over different timeframes

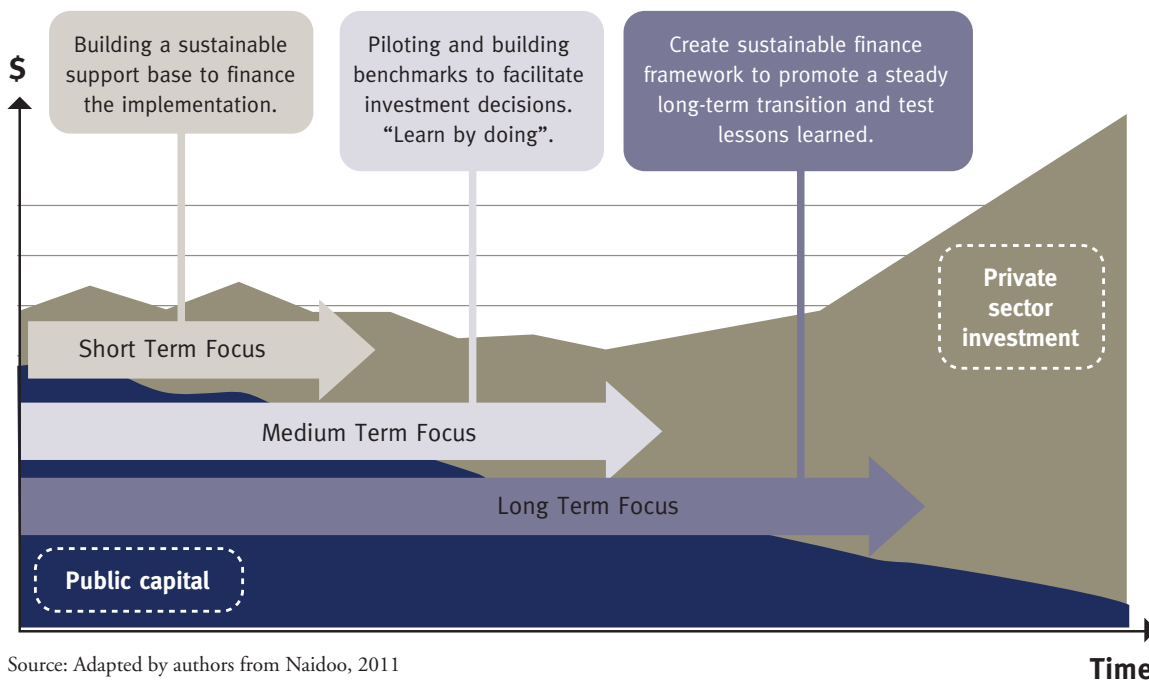
Based on the processes observed in Chile, Colombia and Peru, it is evident that a fluid approach is necessary when developing a NFP, which can evolve over time as new priorities, circumstances and resourcing requirements emerge. In addition, provisions for evaluating and integrating lessons learnt, particularly those generated through pilot and demonstration activities, should be explicit. As such it is useful to consider three main stages for developing a NFP as depicted in Figure 4.5 below. These timeframes are based on i) immediate/short-term outcomes (0 – 2 years); ii) medium term outcomes (1 - 5 years) and iii) longer term outcomes (5 + years).

Figure 4.5 illustrates the potential relationship between public and private sector investment in the course of the transition to a LECR economy. A potential role for public finance is to invest in the enabling policy, regulatory and investment environment to build the basic economic foundations that progressively attract private capital. Ideally, public finance should reduce over time, as the private capital absorbs the new investment opportunities in the course of the transition, e.g. renewable energy, energy efficiency, low emission transport systems. This depiction may not hold true for all public finance incentives and interventions.

A primary goal across these times scales is to create an enabling environment for climate investment and robust financing frameworks that ensure public finance (both national and international) is used effectively to:

- i) mobilise private finance, including different sources of finance across debt and equity capital markets, institutional investors and others; and
- ii) scale up climate investment in critical areas of climate action.

Figure 4.5 Milestones for NFP over time scale



Source: Adapted by authors from Naidoo, 2011

The activities associated with these different time scales may proceed in parallel, although they are likely to be overlapping and contribute to each other.

Shorter term focus (0 – 2 years):

Building a sustainable support base to finance the implementation

A cornerstone of the short term focus is for consensus-building among national treasuries, central banks and national planning agencies through a process of learning and reflection. This will help to identify financing approaches that may be necessary over the medium to long term so that “sustainability” factors are increasingly prioritised. Such consensus-building also enables a “reality check” on the opportunities, barriers, restrictions and resource requirements for both public and private finance. Ultimately, this process should facilitate discussion on priority mitigation and resilience measures to be financed.

An open and transparent dialogue with government, business, investment and commercial institutions, long term investors, microfinance and development institutions is also important to create a unifying vision of the financing challenges. This should also form the basis of a deep and long-lasting partnership with financiers, and identify potential roles for different financial actors and maintain their engagement in the implementation over time. Establishing effective dialogues with multiple stakeholders will also help to ensure a broad understanding of national climate objectives and financing requirements in a way that can deliver wider social, economic and environmental benefits.

Therefore, this component would entail:

- i) engaging Ministries of Finance and Planning, Environment and specific sectoral ministries on integration of low emission and resilience objectives;

- ii) strengthening and/or establishing institutional arrangements for consideration of financing issues;
- iii) developing a structured dialogue across the public and private finance sectors to create a unifying vision and identifying opportunities, financing instruments and risk mitigation mechanisms, early demonstration of LEDS and climate resilient plans.

Medium term focus (1 – 5 years):

Piloting and building benchmarks to facilitate investment decisions

Prior to mainstreaming LECR into broader development, financial decision-makers will wish to see a period of demonstration to learn about the feasibility of new types of investments as well as to generate understanding of their risk-reward profiles. This is a prudent response, as it would be premature to embed within national systems poorly understood options and alternatives. Hence, the medium term focus should be on developing and piloting sectoral plans and programmes that can demonstrate potential for scaled up and transformational investments. Collectively, these initial lessons would “feedback” into the ongoing processes and contribute towards the longer term focus and strategy to mobilise new resources.

Therefore, this component would entail:

- i) a learning-by-doing approach towards attracting and deploying climate finance, for example through sector-focused NAMAs;
- ii) creating monitoring and evaluation processes for tracking finance and assessing progress;
- iii) creating a platform for continuous and deep dialogue with domestic and international financial actors from both the public and private sectors, on priorities for investment and match-making with resources (i.e. enhancing coordination between different financial stakeholders and creating greater visibility of financeable pipeline of projects); and
- iv) capturing learning within the policy design process and ensuring effective channels for communicating these widely across relevant stakeholders.

Longer term focus (+5 years):

Create sustainable finance framework to promote a steady long-term transition

Parallel to the consensus-building, demonstration and continuous learning processes, it will also be important to draw together different finance providers through a dialogue designed to attract sources of long-term capital. In particular, decision-makers within Ministries of Finance and Planning should take the lead in bringing national and international development banks, commercial and investment banks together with institutional investors, financial regulators and the central bank.

Early and appropriate engagement of institutional investors in order to identify potential barriers and solutions for ensuring

long-term finance may facilitate long term finance for scaled-up investments in LECR development. Working jointly with financial providers, the government can ensure that the NFP presents a vision and measures for a comprehensive long-term investment strategy that will be necessary to leverage relatively low cost capital from institutional investors.

Therefore, this component would entail:

- i) building on stakeholder dialogue to partner with investors on a critical analysis of the ability of the domestic financial sector to finance the pathway;
- ii) financial regulations that may hinder or foster the financing of long-term objectives;
- iii) allocating resources to facilitate private sector opportunities in underfunded areas (e.g. natural resource management); and
- iv) identifying and testing risk-sharing instruments based on learning generated during the short-medium term phases.

4.8 Role of monitoring and evaluation in the context of NFP

From these time scales, it is evident that in developing a NFP, continuous evaluations and iterations are necessary for countries to assess and reassess their resource requirements and importantly, consider the impact of their financing interventions. For this reason, it is also essential that countries develop monitoring and evaluation frameworks to support the implementation of their climate action plans and to identify the appropriate and effective access modalities within the context of their national circumstances.

4.9 Summary benefits of NFP

To summarise, adopting a strategic approach to climate finance through a NFP offers several benefits, including a continuous learning mechanism for countries to test what resource requirements are needed for implementation of their climate change objectives and to identify those access modalities that are most effective within the country context. This process empowers countries to define their financing priorities, which enables more effective allocation of resources and helps in bilateral discussions between countries. These discussions with international providers of climate finance can then focus on specific resource requirements in line with country needs, circumstances and priorities.

Using this approach, developing countries may provide clearer “demand” signals for climate finance as compared to the current status quo, which relies on international cooperation partners proposing certain courses of action based on their cooperation priorities. As clearly articulated pathways develop, mechanisms such as national green funds or other coordination mechanisms can be created to coordinate and mobilise resources for the identified climate change priorities. Whilst there is no blueprint for a NFP, it is clear that various tools may be useful for assisting countries in the design of strategic approaches to climate finance as presented herein.

5. Relevance to the evolving international ecosystem for climate finance

The international ecosystem for climate finance has constantly evolved with new opportunities for countries to access climate finance and related resources emerging over time. At the Cancun UNFCCC COP17 governments agreed to create a new Green Climate Fund (GCF), and the governing instrument for this was adopted at COP18 in Durban. This marked a significant development within the existing international ecosystem of climate finance, with many considering that the GCF would become the leading source of international climate and green finance. In section 1.2 the mismatch between recipients and providers of climate finance was highlighted with national strategies and pathways, as the focus of this paper, suggested as a means for bridging the gap. This chapter focuses on the international climate finance ecosystem and considers the implications of a NFP from such an international perspective.

5.1 Elements of the international ecosystem for climate finance

The plethora of multilateral and bilateral climate finance initiatives bring with them a multitude of differing procedures for accessing, deploying and reporting of climate finance which makes it challenging for countries to benefit from the range of resources available (as illustrated in Table 2.1).

As discussed in Chapter 3, a number of initiatives are supporting decision-makers within developing countries with the design and development of their LEDS, climate resilience and green growth policy agendas. Whilst various international initiatives span a wide range of activities, an E3G study in 2012 identified³⁹ a gap in support for governments aiming to increase their understanding of how best to deploy domestic public finance and related institutional capacity for effective implementation countries strategies and plans. In response to this gap, E3G proposed the concept of a National Financing Strategy which would ensure the necessary country ownership and leadership for achieving the maximum transformational impact of climate finance, whether from national or international sources.

Since 2012 a number of other initiatives have emerged, particularly relating to support for readiness for accessing the GCF. These have a strong focus on ensuring country ownership of, and access to, international climate finance, and can largely be considered as relevant components that would form part of a National Financing Strategy. Examples include the GEF, which is providing support to strengthen countries' national institutions, specifically in the accreditation of national implementing entities (NIEs). Governments, notably Germany and South Korea, have made significant resources available for supporting readiness for climate finance. These are implemented through a range of institutions such as GIZ, KfW, UNDP, UNEP and WRI. The Climate Investment Funds have also been providing concessional finance and support for delivering transformational change and investments within a handful of countries. The

IADB has focused on strengthening NDBs' capacity for financing of climate related investments and programmes.

On an individual basis, these efforts each have their merits and are valuable. However, in the context of developing countries where the climate change plans and resources span across both the private and public sectors, these efforts may create unnecessary complexity or even present competing pressures or objectives.

As the international ecosystem evolves to present a more coherent framework for climate or green related investments, it is important that international measures of support are utilised as a coherent and comprehensive package of support at the national level. As discussed in earlier sections, a NFP, which engages the necessary national stakeholders from the outset, can help ensure coherence and work to direct international measures of support so that they have greatest catalytic impact and benefit.

5.2 Challenges of fragmentation

As international climate finance is currently provided via a wide range of multilateral and bilateral measures, the multiple sources of international climate finance, and related capacity-building measures, do not present themselves as a coherent "package" from which developing countries can access the required resources. This is partly due to the dispersed institutional framework and in some cases differing priorities of those providing climate finance and related support.⁴⁰

The many different definitions of climate finance which are emerging such as LEDS finance, NAMA finance, Green finance and South-South green finance place greater burdens on the capacity of the national finance system to absorb, apply and monitor such funding. The term "climate finance" in itself attracts enquiry and there is no single definition which developed and developing countries are able to apply. While these narrower definitions may be useful in differentiating between types of support being provided by developed countries, from a recipient country perspective they are likely to inhibit the effective use of finance. For most developing countries, it is more important to secure predictable financial support and cooperation, with criteria and rules that are understood.

Generally the capacity of national finance systems to absorb climate finance is dependent on the strength of the local institutions shaping the national finance system, i.e. human and technical capacity to identify and analyse potential climate investment opportunities and respond with appropriate financial products and services that appropriately mitigate the risk profile of investments whilst avoiding potential for market distortions. Using climate finance to mitigate risks is necessary for mainstreaming climate change actions across the economy and for facilitating scaled up investment for a sustained long-term, low emission and resilient transition.

39 Amin, A, Mohanty, R. and Tomlinson, S., Report to CIFF: Leveraging LEDS, March 2012, unpublished.

40 For example, in the case of Germany GIZ provides technical assistance and capacity building for various development initiatives and KfW offers limited technical assistance and concessional finance. However at country level, these two core parts of Germany's commitments to developing countries are not viewed as a "package of support" in practical terms – although this may be drafted as such in terms of the bilateral agreements between countries.

Ensuring the transparency and predictability of the provision of climate finance has been recognised as important issues within the UNFCCC long-term finance agenda⁴¹. The Standing Committee on Finance created under the Convention now has the role for considering how to improve the transparency, efficiency, and effectiveness in the delivery of climate finance.⁴² Failure to deliver on these criteria will undermine the extent to which resources for means of implementation⁴³ are perceived as a credible “package” of support for developing countries mitigation and adaptation actions. This will compound the existing challenges for actively engaging public financial decision-makers of developing countries, thereby reducing the potential for increasing domestic expenditure for climate change action.

The scoping work confirmed some of the challenges that countries are facing as a result of a fragmented⁴⁴ international ecosystem for climate or green finance. These range from a multitude of rules and criteria for accessing climate finance; to lack of a common approach towards the definition of climate finance and indicators for reporting or tracking of climate finance; to more systemic challenges of the financial system, which deter long-term institutional investors from investing at scale. When considering these common challenges, the value of countries taking a more strategic approach towards climate finance is underscored. Similarly the importance of feeding lessons from the national to the international ecosystem whilst it remains fluid and subject to evolution is time critical. A number of issues are considered here as important issues of relevance to the interface between national and international ecosystems for climate finance.

5.3 Country Ownership and Access

In a recent submission⁴⁵ to the Ad Hoc Working Group on the Durban Platform (ADP) AILAC calls for a new legally binding agreement in 2015 under the UNFCCC that ensures means of implementation are designed to reflect each country’s specific circumstances, priorities, development needs, capabilities, responsibilities and vulnerability to the impacts of climate change. As the GCF is expected to play a central role in channelling international climate finance from development partners, including the private sector, to recipient countries, its design will be important for achieving such an objective. As the structure and mechanisms of the GCF are being defined for operationalisation of the fund, the issue of country ownership and access to resources is critical. Effective country ownership and arrangements that reflect this are therefore important for ensuring the GCF can fulfil its mission of supporting countries with a paradigm shift towards low emission and climate resilient development.

Current discussions around country ownership in the GCF have primarily focused on a “No-objection procedure”. However, it has been recognized that there is a need to define country ownership beyond this parameter to ensure that resources from the GCF are directed to projects that best address the specific mitigation and adaptation needs of a particular country for

maximum impact. Furthermore, if the GCF is to support a paradigm shift, this will necessarily need to take place over the medium and longer-term. Hence, identifying and implementing climate financed activities within the context of a strategic long-term plan will be important in delivering this key objective. This also underscores the role of a NFP in helping countries to identify how best to enhance arrangements for effective country ownership. The very process of developing a NFP will help identify gaps and opportunities for strengthening institutional arrangements; which in turn can ensure international climate finance is integrated into the domestic budget and planning processes for maximum catalytic impact of such funds.

5.4 Readiness Activities

Readiness activities related to accessing international climate finance, particularly the GCF, are underway. Most evident are the initiatives of bilateral agencies, as well as the activities of UN agencies and MDBs. These are assisting developing countries with preparations for accessing international climate finance. A new GCF readiness support programme, currently under design, will also provide resources that should complement and build on readiness activities already begun by development partners.

These programmes represent a significant opportunity for developing countries to prepare and build capacities for capturing and implementing the larger volumes of international finance expected to flow once the GCF is capitalised later in 2014. The success of these in delivering a sustained and long term impact is likely to involve a demand-driven approach, whereby strong country ownership underpins specific country context measures to enhance readiness. Measures will likely focus on strengthening capacities of public financial institutions, including NDBs, and will require engagement with a wide range of stakeholders, including national designated authorities and national implementing entities. In this context, a NFP can help developing countries to better understand their needs and in identifying a long-term roadmap for enhancing their ability to access international climate and other sources of finance. Furthermore, a NFP will have long-term vision for the transition to LECR development that can translate into the transformational impact required for a paradigm shift.

Readiness activities identified in this report include, for example, the German agency GIZ readiness programme in Peru, which is intended to serve as a basis towards accreditation with the GCF, and entails a study of the institutional landscape with a particular focus on establishing a national implementing entity (NIE), as well as supporting a national fund.⁴⁶ In Colombia, UNDP has started a comprehensive readiness plan that aims to build national capacity, evaluate needs for a NIE, implement monitoring processes, support project development and strengthen financial institutions⁴⁷. In addition, all of Chile, Colombia and Peru are part of the Partnership for Market Readiness initiative.

41 <http://unfccc.int/resource/docs/2013/cop19/eng/07.pdf>

42 <https://unfccc.int/focus/finance/items/7001.php#intro>

43 Means of implementation refers to the provision of financial, technology transfer and capacity-building support to developing countries as objectives under the UNFCCC.

44 Amin, A Dimsdale, T, and Jaramillo, M. (April 2014): Designing smart green finance incentive schemes: the role of public sector and development banks

45 AILAC Submission to the ADP, 2014: http://unfccc.int/files/documentation/submissions_from_parties/adp/application/pdf/adp_ailac_workstream1_20130830.pdf

46 GIZ 2013 Climate Finance Readiness Programme: Early Action for Ambitious Goals

47 DNP 2014 Climate Finance Readiness Propuesta cooperación E3G - National Financing Pathways in LAC

5.5 Monitoring, reporting and verification

Successful resource mobilisation is increasingly linked to being able to demonstrate the effective utilisation of the funds previously received. To date this has been a difficult for both developed and developing countries to contend with. Positive aspects of MRV enable a country to utilise the information to, among other things, determine the effectiveness of its interventions relative to the resources being mobilised; consider the extent to which additional finance has been leveraged; and assess the impact of public finance interventions. In turn, this provides helpful insights regarding future resource requirements and as a valuable policy and planning feedback tool. One of the shortcomings of tracking climate finance has been due to a predominantly supply-driven process, which includes the measurement criteria and frequency of reporting based on the priorities and time scales of the provider of funds. Until recently the majority of recipients of climate finance have not been able to articulate specific needs for climate finance and have a limited understanding of how a national MRV system can serve as a strategic tool to determine the effective deployment of both national and international resources.

A range of different initiatives that are currently developing their own approaches towards tracking climate finance are of relevance to the MRV of international climate finance. These include the MDBs' collaboration on tracking, work by the International Development Finance Club, the Climate Policy Institute, work of ODI and Heinrich Boell Foundation, as well as an OECD research collaborative on tracking private climate finance. The OECD DAC has also created a Task Team to consider options for enhancing the use of the Rio Markers so that they remain relevant for tracking climate finance. Efforts are underway to bring relevant initiatives together to consider some form of harmonisation or reconciliation between different approaches. This can be useful in supporting the work of the Standing Committee on Finance as it develops guidelines for Parties' biennial reports on climate finance as well as the MRV of finance provided by developed countries.

One potential approach to MRV taken from other areas of development finance is "results" or "performance-based" funding, whereby finance is linked to the achievement of pre-defined set of objectives or outcomes.⁴⁸ Results-based financing approaches and payment for verified results are being considered in the contexts of the GCF, particularly as relates to the REDD+ agenda, and the new market mechanisms.⁴⁹

The scoping study revealed that developing countries like Peru, Chile and Colombia are keenly focused on the integration of climate into their national development priorities, ensuring that there are economic, social and environmental benefits derived from any interventions. Therefore, the strategic approach proposed in the context of developing a NFP may support a country in articulating its resource mobilisation priorities and facilitate traction towards achieving the desired impact of such resources.

5.6 GCF Results Management Framework

The emerging GCF Results Management Framework will be important for ensuring the transparency of funding flows and the actions that they deliver. However, they can also be useful tools for increasing country ownership, stakeholder engagement and learning if developed in the right way. It is likely that an iterative approach will be required as countries continue to develop objectives and priority investments within their national plans. Simplistic results-measurement systems (e.g. based only on tonnes of carbon) will incentivise a project portfolio and culture in delivery organisations that may be misaligned to broader sustainable development objectives of countries as well as the GCF objective for delivering a paradigm shift.

Activities developed through a NFP can therefore help support countries national results management systems by establishing country systems for tracking financing flows for mitigation and adaptation activities and their evaluation in terms of effectiveness, sustainability, equity and inclusivity. These activities would in turn help to inform the GCF Results Management Framework, ensuring a balanced approach towards monitoring the transformational impact of the GCF funded activities.

5.7 Bridging the gap between national and international climate finance systems

As an NFP can help identify financing needs over the short, medium and longer-term this can be an important country-owned approach towards influencing what may be required from an international financing pathway. During the Long-term Finance 2013 Work Programme, Colombia put forward the idea that the international pathway towards US\$100 billion per year by 2020 could be shaped in line with countries' expected requirements for finance. It was recognized that such projections would likely involve an iterative approach, which would help to ensure better matching of supply of finance with demand for finance. Countries' NFPs could therefore be a useful means of shaping an international long-term financing pathway.

As highlighted throughout this report, a NFP can also serve as a valuable platform for ensuring differing sources of finance are most effectively combined with domestic resources, as well as each other, in support of country specific priorities and needs. This can therefore help overcome some of the challenges associated with the fragmented nature of international climate finance. However, transparency of country requirements for climate finance – which a NFP can help to articulate – is widely recognised as fundamental for increasing the effectiveness of climate finance.

In their submission AILAC also proposes that it is the national responsibility of all countries to mobilize and invest resources in climate friendly actions at the national level and to mainstream climate change in national spending. This approach can set the conditions for a global economy of growth that is climate sensitive and for which AILAC stresses, there is need to focus on defining options and actions that all countries can pursue in

48 ECN (2012) Annual Status Report on Nationally Appropriate Mitigation Actions

49 GIZ (2012) Nationally Appropriate Mitigation Actions: A Technical Assistance Source Book for Practitioners

order to follow sustainable development pathways compatible with climate protection.

These developments and proactive calls by developing countries represent a paradigm shift within the dynamics of the international ecosystem for climate finance. Such a shift, coupled with increased country leadership through an NFP, will help bridge the supply-demand divide whilst signalling that effective use of climate finance is the responsibility of both developed and developing countries.

5.8 Concluding remarks

The fragmented nature and typically supply-driven focus of international climate or green finance will likely undermine the potential for, and continue to present challenges to, developing countries wishing to access and deploy climate finance for transformational impact. As this scoping work has identified, differing criteria for accessing and deploying climate finance, as well as differing methods for monitoring and evaluation creates additional burdens on the relatively limited institutional capacity of most developing country governments and relevant public finance agencies. Such fragmentation also reduces transparency and predictability for private investors, hence undermining efforts to delivering scaled up climate investments and development of strong domestic markets. Addressing this problem would help ensure resources are used more effectively in the creation of national and global investment frameworks and markets.

As the GCF business model evolves, it is hoped it will promote coherency amongst different sources of international climate finance whilst retaining flexibility for ensuring the ongoing provision of finance and related support. The GCF could therefore set the norms and rules by which climate finance is provided whether this comes directly from the GCF, or indirectly via other multilateral, bilateral and national funds and mechanisms. Countries that are developing a NFP will therefore need to consider the emerging GCF operational guidelines, criteria for investment and mechanisms for accessing and MRV of financial flows. The work of the Standing Committee on Finance will also be important in shaping the criteria and MRV of climate finance. However, it is equally important that country experiences in developing a NFP can feed in relevant experiences and lessons to considerations of design of the GCF business model as well as the work of the Standing Committee on Finance.

A UNFCCC agreement on a long-term financing pathway and the definition of climate finance, as well as a corresponding MRV system, may emerge in the next couple of years. This would also help promote coherency within the international ecosystem for climate finance. Other initiatives underway, such as the Expert Committee on Sustainable Development Financing which will make recommendations to the UN Secretary General in September 2014, the OECD led Partnership for Climate and Development, or the post-2015 focus on Sustainable Development Goals may all help to create a more coherent approach towards financing for sustainable development. It is also anticipated that many climate finance initiatives will be launched at the Secretary General's Summit on the 24th September 2014, although most of those under consideration represent

voluntary actions rather than convergence towards more of a normative framework for the international ecosystem for climate finance.

6. Conclusions and next steps

The concept of NFPs for climate finance as proposed herein would be determined by country specific priorities and circumstances. A “rule book” to create a NFP is therefore unlikely; however, countries can nevertheless benefit from sharing their responses to certain common challenges. Analysing these common challenges and responses in differing country and sector contexts can be valuable information for all, particularly as the international ecosystem for climate finance is evolving and showing greater convergence towards the integration of climate and sustainable development, in investment, risk and regulatory frameworks.

6.1 Key conclusions emerging from research study

Notwithstanding their differences, some common challenges are likely to feature across most if not all countries. Drawing out these common challenges, as well as what has worked in differing country and sector contexts, can be valuable information for all. An overarching feature of NFP is the leadership emerging from developing countries in drawing upon available sources of international climate finance more dynamically. In the past, the narrative for international climate finance has largely been “supply” driven, based on the priorities of providers of climate finance and criteria for accessing these resources. The NFP represents a “demand” driven approach, whereby recipients identify and communicate how international climate finance can best support the implementation and financing of their transition to a LECR development paradigm.

NFP can bridge a gap by providing a country-led approach for ensuring that differing international initiatives and sources of finance deliver national priorities for LECR development. A NFP can also be useful in identifying and articulating roles of different financial actors including how the Green Fund, NAMAs and readiness support can complement and catalyse public and private sector resources from the wider domestic financial system.

6.2 Country leadership in national climate finance approaches

Reflecting on the experiences of Chile, Colombia and Peru, an overarching theme is a commitment to strengthen their understanding of the financing challenges and ways of mitigating risks for private sector investment. All are recognising the importance of identifying and defining complementary roles for the private and public sector, and of ensuring appropriate institutional arrangements for financing the implementation of LECR plans are in place. There are common trends across these countries which will ultimately define a series of actions to be taken in financing their climate action plans. These include:

- > Recognition that LECR should be framed in the context of national development priorities, specifically job creation, economic growth, maintaining market competitiveness, poverty reduction and energy security in order to attract requisite intergovernmental support for implementation.

- > Focused efforts to create appropriate governance to facilitate implementation and financing of LECR, including new government forums and capacities being created.
- > Recognition that ongoing engagement with national industries and private institutions will build support to implement LECR plans over the long term, including understanding the structure and capacity for investment by existing commercial and development institutions as well as building up the scale of existing interventions (e.g. organisations in Peru are working with industries to deepen their understanding of sustainability issues and COFIDE is already funding green investment programmes focusing on SMEs).
- > Adoption of voluntary initiatives in the banking sector that ensure that there are sustainable banking practices to improve the quality of investment decisions by factoring in environmental, social and governance factors (e.g. the Green Protocol adopted by Colombia’s banking sector; and the sustainability training initiatives by Peru focused on its business leaders).
- > Recognition that an enabling environment with risk mitigation mechanisms is essential and that this can be framed through programmes that create an investable pipeline of projects, capable of delivering a transformative impact with private sector participation (e.g. Colombia’s active engagement on financing challenges and possible financial structures for NAMAs and its Sectoral Mitigation Action Plans).
- > Interrogation of good practices in specific sectors and internal assessment of how these may be transferred and shared on an intergovernmental basis with other sectors (e.g. Chile’s Ministry of Energy has extensive experience in facilitating renewable energy and energy efficiency investment and has created institutions to promote ongoing investment).
- > Appreciation that international climate finance should be utilised more creatively in addressing country specific market gaps, including to catalyse domestic investment and to build absorption capacity and the potential for scaled up investment by the private sector.
- > Recognition that the evolving international ecosystem for climate finance should be shaped by country circumstances and national approaches for use of climate finance. In this context the relevance of national strategic approaches for climate finance should be reflected within the new legal binding agreement on climate change, the evolving design of the GCF as well as the work of the Standing Committee. Countries’ NFPs may also be useful in deliberations on a long-term financing pathway to 2020 and beyond.

6.3 Limitations of the research study

The scoping mission was conducted between April and May 2013 and followed up with visits in September and December 2013 for country specific hosted workshops on NAMAs (Colombia) and Interclima (Peru). The report benefited from the contributions of several key partners as described in the Acknowledgements section above. The primary limitations of the research study were access to key engagement partners, due to various resource challenges and electoral priorities at country level. Nevertheless, these limitations were insignificant when compared to the wealth of information provided through in country engagements.

Information relating to international climate finance initiatives in Colombia, Peru and Chile were primarily gleaned from in-country discussions and publicly available information. These data sets are not exhaustive due either to the absence of comprehensive tracking and mapping at country level of international climate finance initiatives or to a lack of access to such information during the course of the scoping work.

The authors are appreciative of the transparency and willingness of our partners in Colombia, Peru and Chile to share and engage on climate finance. The progress being made at country level and the commitment to defining a robust national climate finance position is commendable and the authors are confident that many other countries will benefit from the ground breaking efforts of these countries.

6.4 Ongoing work related to an NFP

The scoping work has initiated an ongoing process of engagement and study within Peru, Chile and Colombia related to strategic approaches to climate finance, through a NFP. These include a paper describing the landscape of Peru's public and private sector in relation to climate change and a paper on the institutional options for resourcing NAMAs in Colombia, as well as ongoing country engagement to develop and apply relevant tools, diagnostics and approaches described herein. Further work to consider more the specific lessons and implications of a NFP for the evolving international ecosystem for climate finance is also underway, as well as consideration of how NFPs can shape an international long-term financing pathway.

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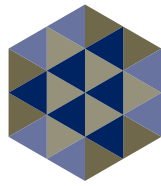
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