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## Policy pointers

**For climate finance to tackle the triple challenge of poverty, climate and deteriorating nature, primary donors, global funds and intermediaries need to dramatically increase the volume of finance to the local level and set targets for which they can be held to account.**

**Primary donors and global funds must prioritise intermediation through credible and innovative institutions with a track record of brokering local institutions and national mechanisms that also reach the climate frontier until they can access finance independently.**

**Funders must increase simple and patient incubation funding for frontier funds and other institutions with community reach, granting outside government systems where needed, to stimulate innovation that holds government to account.**

**Funders work with national governments to build understanding of the potential for local action, developing platforms that build bridges between actors at national and local levels.**

## Financing local responses to poverty, climate and nature

Only US\$1 in every US\$10 committed from global climate funds between 2003 and 2016 was for local-level climate action.<sup>1</sup> Too often, donors and global funds make decisions far away from communities and provide climate finance through layers of intermediaries — missing vital local experience and insights. The investment that does get through can be of inconsistent quality and goes to short-term projects with limited legacy in terms of capabilities. This briefing outlines IIED's vision for a reimagined climate finance landscape based on IIED's Money Where it Matters framework.<sup>2</sup> The framework aims to get more money to the households, cooperatives, federations, social movements and local governments best placed to absorb and disburse high-quality and high-quantity finance. Through local action this finance can support societies and ecosystems to thrive; here we set out how donors, global funds and intermediaries can help make this happen.

Urgent action is needed across societies and the environment to advance social prosperity and resilience and enable natural ecosystems to flourish. Delivering this would achieve a triple win for poverty, nature and climate. Households are affected by climate shocks in different ways depending on their location, networks, livelihoods, assets and the services they can access. And so community members and indigenous peoples, with their wealth of lived experience and local understanding, are best placed to make choices around protecting nature and building resilience where they are. Interventions that enable local people to make decisions are more relevant, cost-effective and long-lasting, and they provide greater financial accountability.

The current climate finance system is failing to support this triple win (shown on the left of Figure 1); donors too often make decisions in distant headquarters. By excluding local people from the process, they reduce the potential for innovation and dialogue to resolve challenges and

trade-offs. This approach prevents the build-up of trust that money will be well spent, so funders invariably impose heavy financial controls and reporting requirements. This results in upward rather than downward accountability and low-risk, late-stage climate financing, offering limited support to bottom-up community-led climate action.

Our reimagined end-to-end climate finance system aims to get money where it matters, reaching the people and places that need it most (shown on the right of Figure 1). We envision a system delivering finance more directly with fewer losses to intermediaries' administrative functions, maximising the utility of finance as activities on the ground receive more and better targeted funds. Decisions are more inclusive of local people, leading to better, tailor-made responses.

To deliver the triple win, this reimagined climate finance landscape will need to use a suite of financial and planning mechanisms to support ambitious climate action for all people and places.

This could include:

- Devolved climate finance for local government and communities' public good and landscape investments<sup>3</sup>
- Climate innovation centres for cooperatives' and enterprises' value-chain investments<sup>4</sup>
- Adaptive social protection for household-level risk reduction<sup>5</sup>
- Frontier (local) funds that are owned by and empower social movements and communities.<sup>6</sup>

*If we get the climate and development finance system right, those at the frontier of climate change will be empowered to thrive*

### A new framework for effective climate finance

The Money Where it Matters framework's fundamental aim is to show how the business-as-usual approach to climate and development financing can be reformed. The framework is composed of three elements: four **building blocks** for effective local finance; ten **good practices** to ensure frontier funds are effective and trusted; and the **journey** (Figure 2) of a frontier fund towards a mature financial mechanism able to deliver climate finance at scale.

#### Building blocks and good practices. Building block 1. Aggregating local climate action to

investable volumes and disaggregating finance down, delivered through:

1. Bespoke and flexible finance reflecting local needs, knowledge and changing opportunities, keeping local administrative costs low and allowing communities to shape funds. Appropriate subsidiarity supports more inclusive governance and helps tailor solutions for communities.
2. Collecting and reporting results to tell a compelling story for communities and donors. A theory of change logically telling the story of how the triple win is delivered at scale guides data collection and enables stronger reporting.

#### Building block 2. Building trust and shared understanding of risk upwards to investors and downwards to local communities, delivered through:

3. Devolved, multi-stakeholder governance. Inclusive decision making and advisory bodies with meaningful community representation provide local credibility and downward accountability. Collective voices provide the pragmatic imperative to solve local challenges.
4. Transparent and accountable systems and procedures, focusing on the needs of the communities they are created to support. Strong transparency gives external credibility and builds accountability to the constituency.

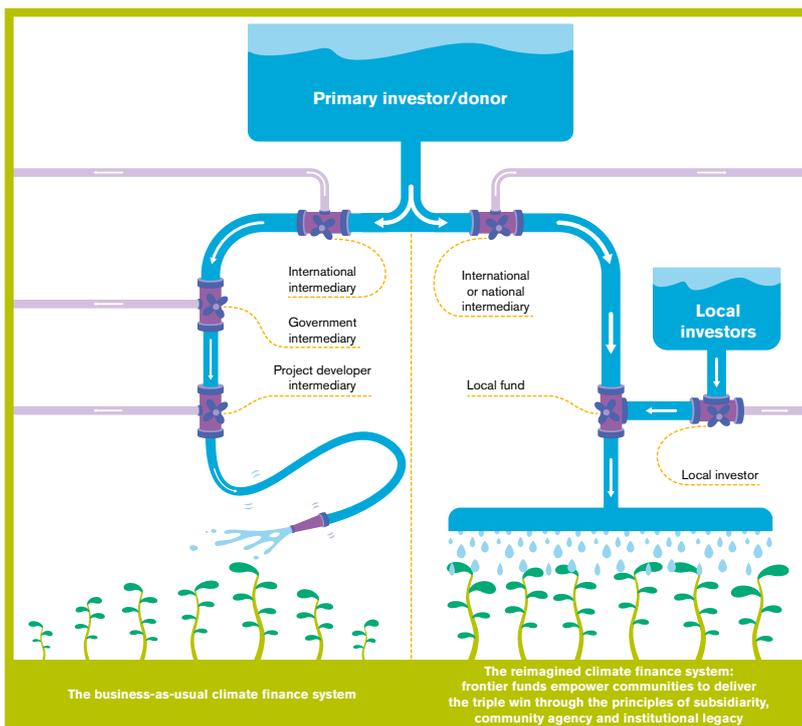
#### Building block 3. Shifting incentives by setting the direction and rules that encourage more sustainable livelihood choices and increased local level investment, through:

5. Building a shared purpose around predictable, sustained, longer-term investments, helping shift action from immediate needs to strategic opportunities over time. Building strategic vision and improving resource rights shifts incentives for communities.
6. Collective agency for influence, through representative decision-making bodies and strategic investments at different scales. This may evolve over time, improving capability and networks and enabling greater influence.
7. Strategic collaboration for influence — with local or national government, for example. Funds should carefully consider these partnerships to ensure they benefit rather than inhibit their influence.

#### Building block 4. Building capabilities for the long term while recognising the need for local actors' short-term capabilities, delivered through:

8. Prioritising iterative learning and adjustment through finance that creates space to develop incrementally, learning from what works while

Figure 1. The business-as-usual (left) and reimagined (right) climate finance landscape



remaining grounded to deliver local priorities through collective action.

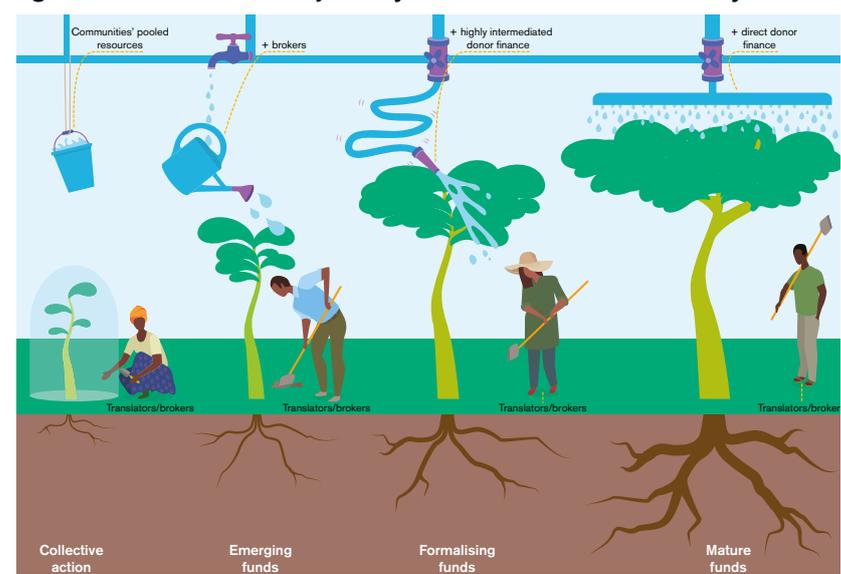
9. Early investment in local capabilities such as project management and monitoring, delivering returns in impact and efficiency. Although this may initially take up disproportionate funds early on, it is critical for establishing effective systems and learning from experience.
10. Peer-to-peer learning. Strategic exchanges with organisations dealing with similar challenges and wider stakeholders at local to national levels help build networks to influence investment and policy and helps identify and take strategic opportunities.

### Journey towards maturity

Over the course of this journey, frontier funds are striving to become mature, credible and agile institutions that are able to access large and varied sources of climate, development and private finance. With support from their donors, funds build skills to identify the type of finance they need at each stage. The journey is faster when they have patient, risk-tolerant support from **brokers**, who provide early-stage finance, and **translators**, who help build trust up the climate finance chain by translating objectives and bureaucratic requirements into understandable language. The journey has four stages:

1. **Collective action:** communities organise and establish local groups to develop grassroots responses to their development and climate challenges, securing access to services and resources. Community members contribute their time, labour and savings to form a frontier fund, increasing their impact. The Babaçu and Dema Funds in Brazil,<sup>7</sup> for example, had significant early support from allied NGOs and the Ford Foundation during this part of their journey.
2. **Emerging funds** begin to formalise governance, develop fiduciary systems and hone their strategic focus by influencing, networking, strengthening resource rights and building collaborative relationships. **Translators** help communities understand their options; **brokers** help them build systems and provide some external, early-stage, risk-tolerant finance. Despite its many successes, the Babaçu Fund still struggles to articulate climate benefits in donors' language and needs support from translators.
3. **Formalising funds** strengthen their procedures as their track record in delivering impact grows. They may still need ongoing support from **brokers** and **translators** to build capability in dealing with development and

Figure 2. A frontier fund's journey: from incubation to maturity



climate finance bureaucracy to meet primary donors' requirements – not all elements of a formalising fund are necessarily at the same stage of progress. The Dema Fund now gets scaled-up finance from the Amazon Fund and a network of foundations. Another fund — the Gungano Fund in Zimbabwe<sup>8</sup> — has channeled money from the Bill and Melinda Gates Foundation to loans for housing.

4. **Mature funds** access and combine a range of financing sources and distribute money effectively to local groups. With established strategic partnerships, they contribute to local or national strategic objectives such as national climate plans. With large donors and global funds ready to invest directly, they are building financial sustainability.

The journey to maturity is not quick and many critical choices must be made along the way for the funds to remain agile, responsive and relevant.

But as the funds progress, their good practices will grow. Supporting institutions can help them progress more quickly to become fully mature funds, accessing and absorbing low-risk finance at scale.

### Emerging good practice

Credible, agile and mature frontier funds that empower local communities to act can help deliver the triple win of advancing resilient and prosperous societies and vibrant ecosystems. Primary donors, global funds and their intermediaries need to improve the suitability of the finance they provide to nurture these funds, encourage good practice and support their progress towards maturity.

The Amazon Fund supports the Dema and Babaçu Funds to tackle the underlying drivers of deforestation, highlighting the value of a national

platform that understands local context and drivers. Other funds — including the Forest Investment Programme's dedicated grant mechanism, the UN's Adaptation Fund, the Green Climate Fund and the Forest and Farm Facility — also provide examples of innovation to increase accessibility of finance. But to provide truly accessible funding, which reaches the local level, they need to overcome several challenges. For example:

- To get Adaptation and Green Climate Fund accreditation, institutions need to show a track record of fiduciary, environmental and social standards equivalent to UN and multilateral development bank (MDB) standards; as a result, most of this finance goes through international intermediaries
- Hefty procurement and risk-management requirements of MDBs — key players in channelling global funds — prevent many intermediaries that are better equipped to build local capabilities and tackle the risks of local investment from providing small and flexible early-stage grants
- Global funds and major intermediaries do not prioritise local finance; their scaling-up strategies for climate change interventions focus on regional and national — rather than local — interventions
- To access global funds, frontier funds commonly depend on national government actors, which are not legally obliged to empower local actors when they prioritise investments
- Capacity-building finance is often too short term, hindering institutions' ability to develop appropriately for their context. This kind of finance is often not accessible to local partners or suited to building local capacity — for example, programme guidance is often only available in English, limiting its value.

## What development partners can do

A critical factor in the speed at which the funds studied developed was the role foundations played in providing early-stage risk finance, technical advice and brokering access to wider scaled-up finance. But not many donors provide early start-up finance and support to young institutions. Current development partners can and should play a vital

role in nurturing young funds, drawing together learning and building greater ambition and mutual accountability across society by:

1. Providing local finance with accountable targets and strategies, improving support and scaling up finance through a clear roadmap with concrete goals for getting finance to local actors.
2. Ensuring any intermediaries are credible and innovative institutions with a track record of brokering and strengthening national funding mechanisms that reach the frontier.
3. Providing clear rules of engagement, including stricter time-bound roles for any intermediary partners to support local institutions until they can access finance independently and then withdraw.
4. Using participatory processes to develop and report project indicators and results-management frameworks that incentivise outcomes and attract more strategic investments.
5. Increasing small, simple and patient funding to incubate frontier funds and other national institutions with real reach to communities, measuring success in terms of their ability to scale up and access lower-risk funding over time.
6. Supporting national governments to recognise the potential of subsidiarity and develop platforms for building bridges between communities, national policymakers and other actors, creating an enabling environment nationally.

Reimagining the business-as-usual climate finance system will maximise the impact of every penny and unlock the huge adaptation, mitigation and poverty reduction potential of local communities and enterprises. If we get the climate and development finance system right, those at the frontier of climate change will be empowered to thrive in a rapidly changing world, enabling the triple win of addressing poverty, protecting and restoring nature, and delivering climate resilience.

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## Knowledge Products

The International Institute for Environment and Development (IIED) promotes sustainable development, linking local priorities to global challenges. We support some of the world's most vulnerable people to strengthen their voice in decision making.

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## Notes

<sup>1</sup> IIED estimates less than 10% of the US\$17 billion climate finance committed from international climate funds between 2003 and 2016 was prioritised for local-level activities. Committing these funds to every level — national, regional and local — is key. The imbalance needs to be addressed with more of this money channelled to the local level. This analysis is of dedicated climate funds, which is only 7% of total climate finance over this period, as the rest of the climate finance is not sufficiently transparent to be analysed. So greater transparency is also needed to be able to track the effectiveness of climate finance. See: Soanes, M, Rai, N, Steele, P, Shakya, C and MacGregor, J (2017) Delivering real change: getting international climate finance to the local level. IIED, London. [pubs.iied.org/10178IIED](https://pubs.iied.org/10178IIED) / <sup>2</sup> Soanes, M, Shakya, C, Walnycki, A and Greene, S (2019) Money where it matters: designing funds for the frontier. IIED, London. [pubs.iied.org/10199IIED](https://pubs.iied.org/10199IIED) / <sup>3</sup> Greene, S (2019) Lessons from piloting the decentralised climate finance programme, Tanzania. Decentralised Climate Finance Project. [pubs.iied.org/G04398](https://pubs.iied.org/G04398) / <sup>4</sup> Macqueen, D, Benni, N, Boscolo, M and Zapata, J (2018) Access to finance for forest and farm producer organisations (FFPOs). FAO, Rome and IIED, London. [pubs.iied.org/13606IIED](https://pubs.iied.org/13606IIED) / <sup>5</sup> Soanes, M, Kaur, N, Venkataramani, V, Shakya, C and Kaur, D (2019) Financing a climate-resilient MGNREGS. IIED, London. [pubs.iied.org/10201IIED](https://pubs.iied.org/10201IIED) / <sup>6</sup> [www.iied.org/delivering-climate-finance-local-level](https://www.iied.org/delivering-climate-finance-local-level) / <sup>7</sup> [www.iied.org/delivering-climate-finance-local-level-babacu-fund](https://www.iied.org/delivering-climate-finance-local-level-babacu-fund) and [www.iied.org/delivering-climate-finance-local-level-dema-fund](https://www.iied.org/delivering-climate-finance-local-level-dema-fund) / <sup>8</sup> [www.iied.org/delivering-climate-finance-local-level-gungano-urban-poor-fund](https://www.iied.org/delivering-climate-finance-local-level-gungano-urban-poor-fund)