QUALITY MATTERS

Strengthening climate finance to drive climate action

Enhancing concessionality, access and impact in the new collective quantified goal on climate finance

Environmental Defense Fund

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About Environmental Defense Fund

Environmental Defense Fund (EDF) is one of the world's leading environmental nonprofit organizations. EDF's mission is to preserve the natural systems on which all life depends. Guided by science and economics, EDF finds practical and lasting solutions to the most serious environmental problems.

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FRONTPAGE/ SHUTTERSTOCK

EXECUTIVE SUMMARY

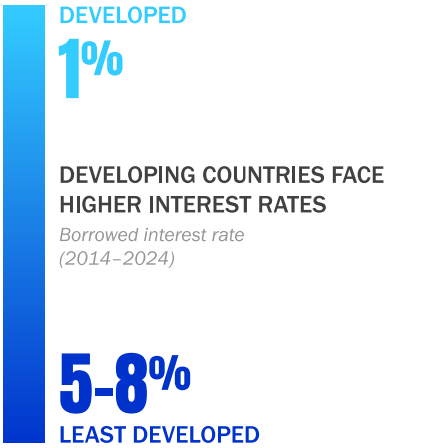
As the global community works toward finalizing the New Collective Quantified Goal (NCQG), it is critical to look beyond scaling the quantity of climate finance. This report outlines why strengthening the quality of international climate finance is essential and calls on multilateral institutions to address structural challenges and create strong enabling environments, to maximize the impact of resources in developing countries and improve the overall effectiveness of climate finance.

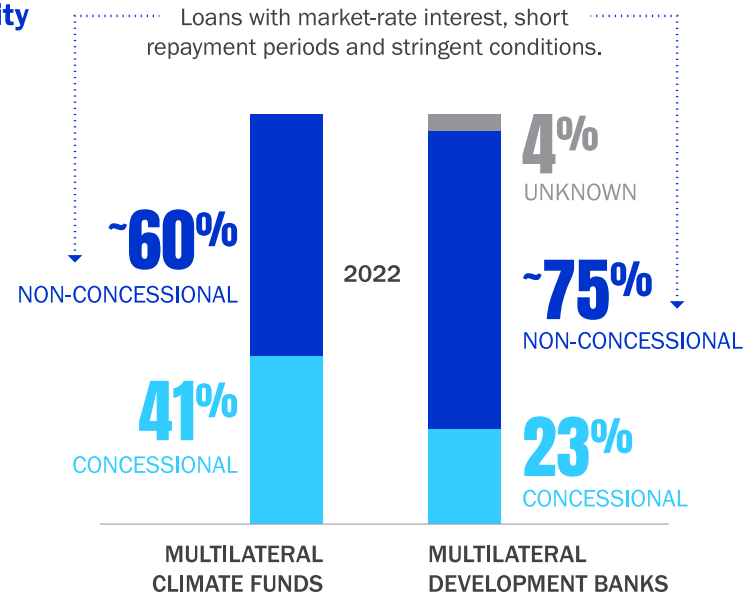
- We focus on **three key aspects** of climate finance quality—**concessionality, access and impact**—all of which are critical to ensuring that climate finance truly meets the needs of developing nations and supports effective, meaningful climate action.
- Developing nations face **significant obstacles** that prevent them from accessing the climate finance they require to achieve the objectives of the Paris Agreement. High investment costs, fiscal constraints and regulatory hurdles can make it difficult for these countries to secure and effectively deploy climate funding. These barriers often prevent funds from reaching the communities most in need or lead to ineffective, inaccessible and burdensome financing.
- As efforts begin to scale finance through the NCQG, improving the quality of finance will be essential to ensure that it can meet its full potential. We define high-quality climate finance as:
  - effective in driving positive climate change mitigation and adaptation outcomes;
  - accessible to the countries and communities that need it most; and
  - capable of catalyzing sustainable, long-term change.
- Several **innovative initiatives** are already making progress by breaking down barriers to financing and enhancing the effectiveness of climate projects where they are needed most.

FIGURE 1

Our global finance system is not ready for climate change

1 An overall lack of concessionality in global climate finance flows to developing countries.





2 Climate finance is difficult to access.

MANY DEVELOPING NATIONS REPORT THAT THEY FACE SIGNIFICANT OBSTACLES

- FUND-SPECIFIC REQUIREMENTS
- EXCESSIVE PAPERWORK
- UNPREDICTABLE TIMELINES
- DELAYS IN DELIVERY OF FINANCE

INTERNATIONAL CLIMATE ADAPTATION FUNDING

ONLY 46% allocated to Least Developed Countries was aimed at empowering local actors.

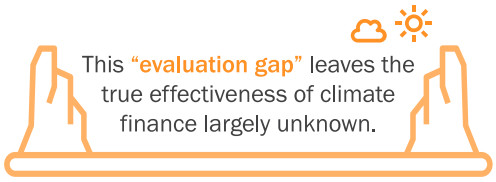
A 2021 study

3 The impact of climate finance is often not measured.

OUT OF MORE THAN **10K EVALUATIONS**, THERE WAS MINIMAL FOCUS ON:

CLIMATE MITIGATION **0.23%**

CLIMATE ADAPTATION **0.5%**



Evaluations collected by the International Initiative for Impact Evaluation

- To address systemic issues in climate finance, we offer **detailed recommendations** focusing on three key metrics: concessionality, access and impact.

Concessionality

1. Advance the reform agenda of multilateral development banks (MDBs) to strengthen concessionality windows and reform debt sustainability frameworks.
2. Increase transparency and scale of climate-specific concessional facilities, with clear targets for the proportion of concessional climate finance, particularly for highly vulnerable countries.
3. Address sovereign credit ratings and risk barriers to unlock more affordable financing options.

Access

1. Adopt the Multidimensional Vulnerability Index (MVI) to better measure climate risk in financing decisions.
2. Simplify and streamline bureaucratic procedures for accessing climate finance.
3. Establish more comprehensive disaster response financing mechanisms.
4. Encourage multilateral climate funds (MCFs) to invest more in readiness initiatives to enable countries and stakeholders to optimize instruments for impact and financial engineering.

Impact

1. Improve coordination between multilateral climate funds to enhance complementarity to enable countries to maximize options across the landscape for impact.
2. Develop stronger reporting measures to better assess the impact of climate projects to enable learning and innovation in future projects.

- We urge negotiating Parties to maintain NCQG text references to leveraging concessional finance to mobilize private investment, enhancing channels of access, reforming MDBs and improving coordination between climate funds.
- We propose **additional language** to ensure that the NCQG prioritizes enabling environments and addresses systemic issues related to climate finance quality, including strengthening language on quality considerations and language urging multilateral institutions to take steps to promote quality finance and reduce barriers to access.
- As we work toward the NCQG targets, it is vital to keep quality at the forefront of climate finance discussions. By focusing on concessionality, access and impact, we can ensure that climate finance goes beyond meeting quantitative goals and drives transformative, equitable and sustainable climate action in developing countries. Through ongoing research, methodological rigor and innovative breakthroughs, we can close the gap between ambition and action—leading the world toward a more resilient, low-carbon future.

FIGURE 2

Dimensions of quality

Concessional

DEFINITION

Finance is offered with favorable and transparent terms, not contributing to further financial burden.

SOLUTIONS

- Greater utilization of non-debt financial instruments
- Expand concessional finance capacity
- Leverage concessional public finance to mobilize new sources of private finance and blended finance projects
- Improve and enforce the transparency of terms

EXAMPLE

The World Bank adopted the use of climate resilient debt clauses to help make loans less burdensome for small states and small islands in the face of natural disasters. CRDCs allow countries to defer payments on loans for up to 2 years following an extreme disaster. In 2023, the World Bank broadened the scope of CRDCs such that they cover all new and existing loans in eligible countries, and will allow for the fees associated with CRDCs to be covered by concessional resources. While these measures don't eliminate debt, by postponing payments they allow for vulnerable states to focus on disaster response and ensure that existing loans – including for climate finance projects – are not creating extra burden during particularly challenging moments.

Accessible

DEFINITION

Finance is available to developing countries with relative ease, at amounts that are fit-for-purpose, and without undue delay.

SOLUTIONS

- Streamline bureaucratic processes for accessing finance
- Improve the flow of finance in disaster situations
- MCFs and MDBs should voluntarily adopt the Multidimensional Vulnerability Index as improved way to measure and understand climate risk
- Support countries in establishing NDC investment planning approaches

EXAMPLE

The Jurisdictional REDD+ Technical Assistance Partnership (JTAP) initiative, which EDF helped launch last year. JTAP will provide technical assistance to support forest country jurisdictions and their key partners, to strengthen local capacity and support them in participating in high integrity voluntary carbon market, to unlock finance for forest conservation and management. This initiative aims to support indigenous peoples and local communities in building local capacity and expanding access to tropical forest finance, which is critical as they are often overlooked.

Impactful

DEFINITION

The results and effectiveness of the finance are measured and evaluated under a clear, consistent methodology.

SOLUTIONS

- Improve complementarity between multilateral climate funds to maximize impact and support NDCs
- MCFs and MDBs should support stronger reporting measures to better understand climate impact of projects

EXAMPLE

Debt-for-nature and debt-for-climate swaps can help improve the impact of climate and environment initiatives by generating climate action while simultaneously freeing up fiscal space/reducing indebtedness. Swaps involve creditors (banks, governments) buying debt at a discount from a highly indebted government, in exchange for that government carrying out a conservation project with the purchased debt.

ROANNA RAHMAN

INTRODUCTION

As we approach the UNFCCC's COP29 in November, the world is at a critical moment for climate action. To enhance ambitious action and keep us on track to meet the Paris Agreement objectives, countries will need to reach agreement on a New Collective Quantified Goal (NCQG) on climate finance. Increased financial support will enable developing countries to step up their climate ambitions in the next round of Nationally Determined Contributions (NDCs) and channel significantly more funds toward urgently needed climate action.

Climate finance needs are significant, **estimated** to be $2.4 trillion per year by 2030 in developing countries alone. However, scaling the quantity of climate finance alone won't be enough. To maximize the effectiveness of climate funding, discussions must also consider the quality of finance. This report analyzes three aspects of climate finance quality: concessionality, access and impact. These factors are crucial to ensure that climate finance truly meets the needs of developing nations and drives meaningful climate action.

High-quality climate finance is characterized by its effectiveness in driving positive climate outcomes, its accessibility to countries and communities most in need and its ability to catalyze sustainable, long-term change. It encompasses not just the amount of funding provided, but also how that funding is delivered, utilized and measured for impact.

Throughout UN negotiations over the NCQG, many negotiators and stakeholders have stressed that shortcomings in quality represent a serious hurdle for the effectiveness of climate finance, and that quantity and quality must go hand in hand. Developing country representatives have highlighted quality issues such as limited availability of concessional and grant-based finance, the potential for climate finance to exacerbate debt burdens, difficulty in accessing finance and the need for stronger understanding of the impacts and outcomes of finance.

To ensure that new climate money is delivered efficiently and effectively, and at the needed speed, the NCQG must be more than an aspirational quantitative target. It is critical that the final text strengthens the important clauses on quality that are included in the current draft, and includes high-quality climate finance mechanisms to:

- foster measurable impacts and climate-positive outcomes;
- reduce unnecessary barriers and burdens for recipient countries;
- reduce investment risk for source countries;
- avoid exacerbating unsustainable debt loads; and
- ensure timely access.

This report details key issues of quality and solutions to address these structural challenges. Report findings were developed through reviewing and synthesizing literature on climate finance, engaging in MDB reform processes and UNFCCC negotiations, and consulting expertise within EDF.

- First, we explain how shortcomings in quality in existing finance flows diminish the impact of these investments and thereby the climate impact required to meet the Paris Agreement objectives.
- Next, we offer examples of initiatives that have helped to ease barriers and improve quality, demonstrating how strengthened quality in climate finance can enhance effective climate action.
- Finally, we suggest recommendations for the draft text of the NCQG to strengthen considerations of quality, and offer solutions that multilateral institutions can employ to enable a successful NCQG.

BARRIERS TO QUALITY CLIMATE FINANCE FOR DEVELOPING COUNTRIES

ERNEST ANKOMAH

Developing countries encounter major obstacles that prevent them from accessing the climate finance they urgently need. Key barriers, such as high investment costs, complex processes, fiscal limitations and regulatory challenges, make it difficult for these countries to obtain and effectively use climate funding. These obstacles can render climate finance inaccessible, ineffective and overly burdensome. They often prevent funds from reaching the communities most in need and can reduce the impact of investments. Recognizing these barriers is crucial to efforts to improve quality in climate finance systems and structures.

An unproductive cycle of debt and development losses

More than half of low-income developing countries are currently facing some degree of debt distress, an alarming trend with repercussions for climate action. Heavily indebted countries can become trapped in an unproductive cycle: Mounting debt payments limit their ability to invest in climate solutions, while extreme weather events cause severe economic losses, often forcing countries to borrow even more. This debt spiral is worsened by high borrowing costs and rising interest rates, which often make renewable energy projects more expensive than fossil fuel alternatives. As debt levels climb, the cost of financing energy projects rises further, leaving these nations unable to leave polluting approaches behind. If capital costs were lower, renewables could become more competitive, offering a pathway out of this destructive loop.

Sovereign credit ratings and perceived risks play a critical role in this dynamic. These ratings are influenced by economic, political and social factors and the particular preferences of rating agencies. Poor ratings lead to increased borrowing costs, as investors demand higher returns to offset perceived risks. One study by a group of UK universities found that 63 countries could see their credit ratings cut because of climate change by 2030. As rating cuts increase borrowing costs, the downgrade could add $137–$205 billion to countries' annual debt payments.

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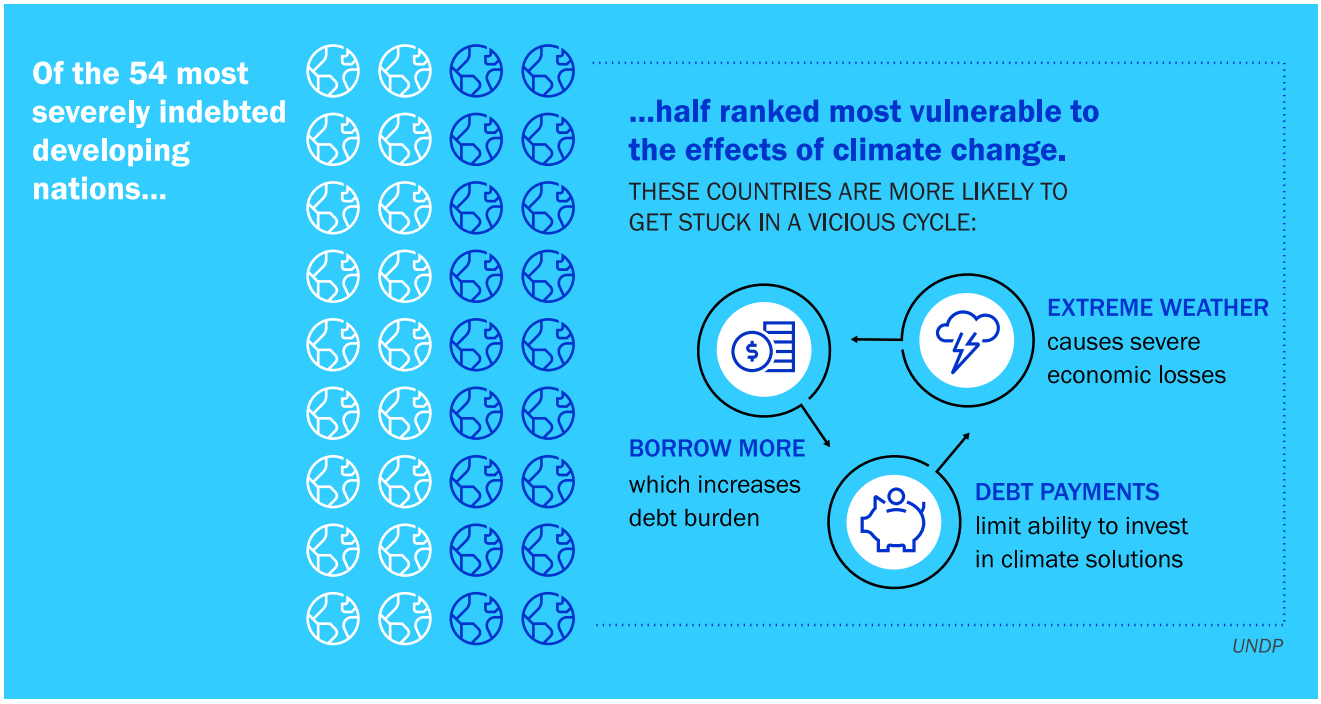
Developing countries also face a significant investment gap for financing renewable energy projects. According to a 2024 study by the Columbia Center on Sustainable Investment, a major contributing factor is the high cost of capital, driven by high perceived and actual risk, low sovereign credit ratings and the need to borrow in foreign currencies. Alarmingly, a significant portion of the funding provided to developing nations to finance climate-related and renewable energy projects is absorbed in excessive costs tied to the loans.

FIGURE 3

Developing countries face the barriers and burdens of climate finance



These challenges make it more expensive for developing nations to finance their energy transitions, compared to wealthier countries. For example, the real **cost of capital** for energy projects in African countries is two to three times higher than in advanced economies and China, according to the International Energy Agency. And a 2020 study found that the capital costs for solar and onshore wind in India are about twice as high as in Denmark (see case study on cost of capital).

The high cost of climate-related disasters

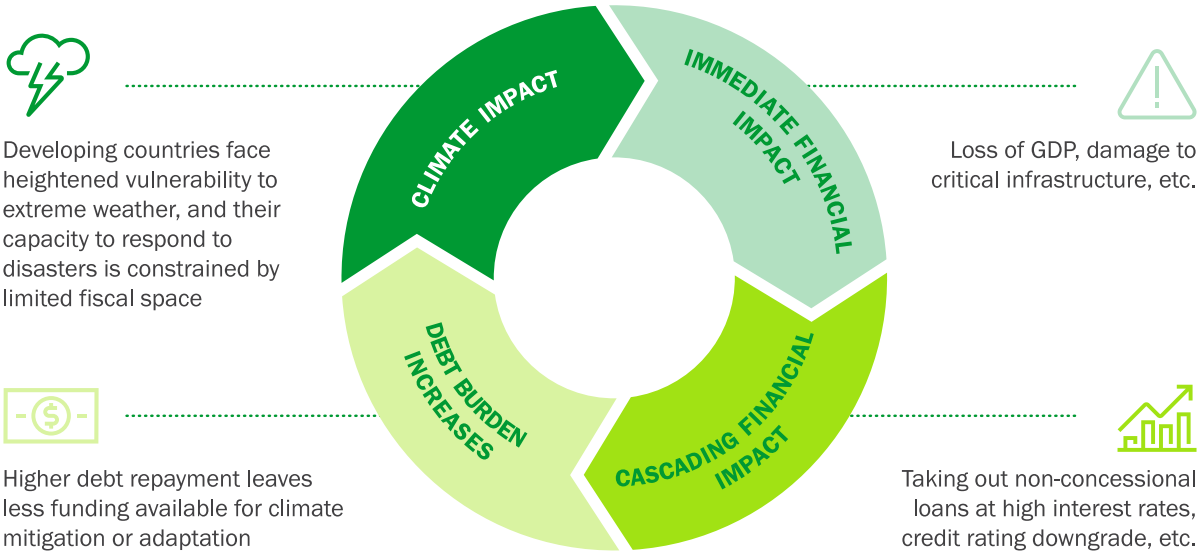
When climate-related natural disasters hit, many developing countries are forced to take out high-cost loans which must be repaid over a short period. It would significantly ease the burden if debt could be structured over a long period or enhanced with better terms and conditions that respond to climate stress. Unfortunately, the current global financial architecture largely offers market-rate loans and terms to these countries, failing to account for the unique challenges and timelines associated with their development and environmental goals.

This combination of high borrowing costs, unfavorable credit ratings and underlying economic weaknesses can trap developing nations in a cycle of unsustainable debt, which severely limits their ability to invest in renewable energy and other climate-focused initiatives. Tight public budgets and fragmented regulatory frameworks further complicate the situation, with land-use challenges—often involving agriculture and urban development—presenting additional obstacles.

According to the World Bank Group, external debt in low-income countries has risen at a pace exceeding economic growth over the past decade, with some 60% of these countries facing a high risk of debt distress or already in debt distress.

FIGURE 4

Climate crisis to debt crisis cycle



High financing costs in developing countries, driven by actual and perceived risks, make renewable energy projects more expensive than in developed countries, hindering effective climate action.

COST OF ENERGY

UTILITY-SCALE SOLAR PV PER MEGAWATT HOUR (MWH)

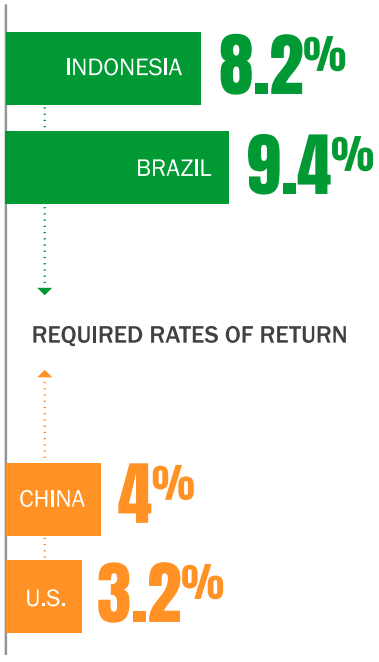
$40/MWh U.S.

$80/MWh DEVELOPING COUNTRIES

2X COST TO BUILD A WIND TURBINE IN INDIA THAN IN DENMARK.

COST OF CAPITAL

Investors need to see higher rates of return to finance renewable energy projects in developing countries.



In 2023, low-income countries allocated an average of 7.5 percent of their budgets to debt repayment—exceeding the combined expenditure on both health and education. Without more supportive frameworks for financing, many developing nations will remain trapped in this cycle, unable to access the funds necessary to successfully implement their NDCs.

Institutions, including the Multilateral Development Banks, are undertaking steps to address these compounding issues, including expanding the use of debt pauses following disasters.

In October 2023, reforms were adopted at the World Bank and IMF Annual Meetings in Marrakech, Morocco signaling progress towards reform. Environmental Defense Fund and *Foreign Policy* **convened** policy leaders during the 2023 meetings to further capture how these institutions can enable a just transition and the challenges remaining.

Yet there is much more to be done, especially to support vulnerable nations like Dominica, which have made significant strides toward resilience but remain in precarious situations.

Many of the countries most at risk of the impacts of climate change are also deeply indebted, as indicated by their public and publicly guaranteed (PPG) debt as a % of GDP, and have **limited ability** to respond without significant support through international climate finance.

CASE STUDY: THE EFFECT OF DISASTERS ON SMALL ISLAND NATIONS

Many developing countries, especially small island states like Dominica, are highly vulnerable to climate change due to economic weakness, limited resources and geographic constraints. These vulnerabilities often lead to cycles of unsustainable debt and underinvestment. In 2017, **Hurricane Maria**—a Category 5 storm—devastated Dominica, causing 30 deaths, displacing thousands and wiping out 226% of the country's GDP overnight.

Dominica has since aimed to become a leader as a **climate-resilient nation**, but remains at high risk of debt distress and future disasters. To strengthen its preparedness and reduce the impact of future storms, the country needs significant international financial support. By 2023, Dominica had established three early warning systems but **needs 50 more** to adequately cover the island. The lack of comprehensive early warning capabilities means that key economic sectors, such as agriculture and tourism, remain highly exposed to sudden climate shocks, potentially undermining Dominica's development goals.

Despite Dominica's commendable ambition to become a climate-resilient nation, the gap between intention and implementation remains substantial. Accessible, high-quality climate finance is key to bridge the gaps and support vulnerable nations in building genuine resilience to climate impacts.

ADDRESSING SYSTEMIC ISSUES IN CLIMATE FINANCE

IPLC EXCHANGE WORKSHOP 2023 - COSTA RICA

Developing countries encounter significant barriers that impede their access to essential climate finance and can lead to debt traps. These underlying conditions demonstrate the need for stronger considerations of quality in climate finance, to ensure that resources are used effectively and equitably.

International climate finance suffers from significant quality deficiencies, as structural barriers within institutions prevent funds from achieving their intended impact. There are many facets of quality to consider, from issues of effectiveness and efficiency to sustainability. This report focuses on three pillars of quality in particular—concessionality, access and impact—which have been touched upon in NCQG negotiations and can be catalytic for addressing other issues of quality as well.

- **Concessionality**: Debt concessionality, or concessional lending, refers to financial resources offered at more favorable terms than standard market rates. Concessional financing can be provided through mechanisms including loans, grants and equity. This could include lower interest rates, enhanced terms and conditions, longer repayment periods or even grant components. The key is to offer these benefits without disrupting market dynamics. Concessional financing improves the quality of climate finance by making projects more viable, enabling high-impact initiatives that might otherwise be inaccessible due to cost or high risk, and lessening the debt burden on recipients. This approach supports more sustainable and effective long-term outcomes.
- **Access**: Access refers to how easily eligible entities can secure and use climate finance. Improving access is essential to raising the quality of climate finance, as it promotes equitable distribution of funds, fosters a wider range of projects and solutions and empowers local actors to take meaningful action. Access in climate finance entails predictable and timely delivery of funding with reduced bureaucratic barriers for capacity-constrained countries, reaching local communities where they are most needed, and accommodating different contexts and capabilities.
- **Impact**: In climate finance, impact refers to the measurable, positive outcomes that result from funded interventions. Impact is a key indicator of quality climate finance, as it directly reflects how effectively the funding addresses climate change challenges. Impact measurement includes tracking emissions reductions, adaptation results and associated co-benefits, while considering the timeliness and effectiveness of fund disbursement. Impact is a key indicator of quality climate finance: it provides a measurable contribution to the implementation of NDCs, captures both immediate results and long-term transformational change, enables learning and improvement for future interventions and helps identify successful approaches that can be scaled.

CONCESSIONALITY

Concessional climate finance loans are essential because they offer more favorable terms that make it easier for low- and middle-income countries to invest in climate projects without being overwhelmed by debt.

And yet, according to the Organization for Economic Co-operation and Development, only 41% of loans from the Multilateral Climate Funds were concessional, and only 23% of loans from Multilateral Development Banks (MDBs) were **concessional**.

When a high proportion of climate finance loans are non-concessional, several issues arise:

1. Increased debt burden: Non-concessional loans, with higher interest rates and shorter repayment periods, increase the financial strain on recipient countries that may be already facing financial challenges. This can lead to unsustainable debt levels, diverting funds away from critical climate projects and economic development.
2. Reduced effectiveness of climate finance: If a larger proportion of funds are used to service debt rather than to finance climate-related interventions, the overall impact of climate finance diminishes, undermining global efforts to combat climate change.
3. Risk of economic instability: Non-concessional loans can worsen repayment difficulties and economic instability, particularly in countries that already face financial challenges. This could cause countries to cut back on essential services or climate initiatives, making them even more vulnerable to climate risks.

Perceived risk leaves high-impact projects underfunded

The relationship between perceived risk and concessionality is critical in climate finance. High levels of perceived political or market risk in developing countries often lead to low investment ratings, especially for transformational projects—those with the greatest potential to address climate change. Because these projects are seen as high-risk, they struggle to attract private investment. This is where concessionality plays a key role and highlights the need for de-risking climate finance.

Concessional finance can help offset these risks, making it more attractive for private investors to engage. By reducing the financial burden on borrowers and providing more predictable returns, concessional loans de-risk high-impact projects. However, when concessional finance is not adequately used, these high-risk, high-impact projects are left underfunded, which reduces the overall quality and transformative potential of climate finance. The higher the perceived risk, the more concessionality is needed to mobilize investment and ensure that critical, large-scale projects get off the ground.

HURRICANE IRMA CLIMATE CENTRE / NETHERLANDS / RED CROSS, 2017

Strings attached: Some loans funnel benefits back to lending nations

Many climate finance loans come with terms that disproportionately benefit the lending countries. Market-rate interest, short repayment periods and stringent conditions place significant financial strain on developing nations and underserved communities. In addition, wealthy countries often send climate funding to debt-distressed nations with strings attached that benefit the lending nations.

A **Reuters investigation** revealed that wealthy nations including Japan, France, Germany and the U.S. are profiting from climate loans and grants intended to help poorer nations, effectively funneling funds back into their own economies. At least $18 billion in market-rate loans have been issued, including $10.2 billion from Japan alone.

Another $11 billion in loans—largely from Japan—require recipient nations to hire companies or buy materials from the lending countries. Similarly, at least $10.6 billion in grants from 24 countries and the EU come with conditions forcing recipients to use firms or agencies from the donor nations, keeping money intended for climate action in poorer countries circulating back to the wealthier ones.

Andres Mogro, Ecuador's former national director for adaptation to climate change, described this as a "new wave of debt caused by climate finance."

Meanwhile, some analysts **argue** that wealthy nations are overstating their contributions to the 2009 pledge to provide $100 billion annually to help developing countries tackle climate change. Much of the money flows back to these wealthy nations through loan repayments, interest and exclusive contracts—undermining the true purpose of climate finance and deepening global inequality.

Under-use of blended finance models

Blended finance refers to the strategic use of public funds to attract private investment for climate projects by reducing the financial risks for private investors. This is done by "blending" public and private capital, often through concessional loans or guarantees, to make larger projects more financially viable. And yet, the use of public money to de-risk and mobilize the private sector to enhance concessionality is relatively infrequent—with an overall **downward trend** in blended climate financing between 2016 and 2020, and especially minimal blended finance for adaptation. These trends resulted from investors focusing on smaller projects with lower commitments, smaller public sector commitments to blended projects and shifting fiscal priorities during the COVID-19 pandemic. This underuse limits the potential for blended finance to drive significant investment in climate action.

Limited information to inform investment decisions

Transparency is essential for fairness, accountability and effectiveness in concessional climate finance, especially as developing countries work to address climate challenges under increasingly difficult financial conditions. High levels of transparency can encourage...

- Informed decision-making: Without clear and transparent terms, developing countries struggle to assess the true cost and benefits of concessional loans. Clear terms allow for informed decisions about whether financing is suitable for their climate projects and economic stability.
- Equitable access: Non-transparent terms can create an uneven playing field, where some countries may receive less favorable terms without realizing it. Clear, standardized terms help ensure that all countries, particularly low-income nations, can access fair and equitable financing.
- Accountability: Transparency holds lending institutions and donor countries accountable, ensuring that concessional financing truly serves its intended purpose—helping vulnerable countries invest in climate solutions without being burdened by unsustainable debt.
- Trust-building: Clear and open terms foster trust between donor countries and recipients. When terms are hidden or unclear, it raises suspicions about the true motivations behind the finance and can damage cooperation in climate action.
- Enhancement of finance quality: Transparent concessionality terms make it easier for countries to assess the extent of concessionality, ensuring that the loans are indeed designed to support transformative, high-impact projects rather than simply creating new financial burdens.

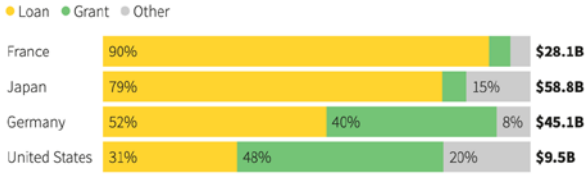
High-quality concessional loans are vital to ensure that climate finance remains accessible, impactful and supportive of sustainable development without pushing vulnerable nations into further debt. However, the landscape of climate finance is marked by significant disparities in how different contributors structure their support. This disparity is particularly evident in

the preference for loans over grants, a trend that has substantial implications for the debt burden of recipient countries, as illustrated in Figure 5.

FIGURE 5

Three of the top four climate finance contributors favor loans over grants

Japan, Germany, France and the U.S. reported the most climate finance contributions to developing nations between 2015 and 2020. Climate funding representatives from these top countries say loans are appropriate for large, revenue-producing projects in nations with strong economies.



Note: The "other" category includes financial instruments, such as bonds, equities, guaranties and contributions that included both grants and loans.
Source: Reuters analysis of climate finance data nations reported to the U.N.

This preference for loans, particularly by some of the largest contributors, has significant implications for the quality of climate finance, impacting debt burdens, long-term sustainability for countries already facing fiscal constraints, and access and equity deterring some of the most vulnerable countries from accessing climate finance, as they may be unable or unwilling to take on additional debt. It also shifts project selection towards those with clear revenue streams to ensure repayment, potentially neglecting critical adaptation projects or those with less tangible financial returns.

See: https://www.reuters.com/investigates/special-report/climate-change-loans/

ACCESS

Challenges of access to climate finance have increasingly entered the spotlight in recent years. While developed countries have reported increases in their provision of financial, technical and capacity-building support, developing countries have increasingly stated that resources have not reached their countries as indicated. Despite the creation of more multilateral and bilateral delivery channels and initiatives for climate finance support, many countries—particularly least developed countries (LDCs) and small island developing states (SIDS)—feel excluded from the larger resource streams that are urgently needed to address climate change and its impacts.

CASE STUDY: CONCESSIONAL FINANCE FOR SRI LANKA

Sri Lanka offers a valuable case study of a climate-vulnerable nation dealing with both high debt and limited concessional climate finance. The country is **ranked 110th out of 187 countries** in terms of vulnerability and readiness by the ND-GAIN Matrix of comparative resilience. **Risks** include sea-level rise, extreme heat and heightened natural disasters. At the same time, the country has been embroiled in a debt crisis since 2019. In 2022, debt reached 114% of Sri Lanka's GDP and it defaulted on its foreign debt.

Despite this precarious debt situation, most of the climate finance delivered to Sri Lanka has been in the form of debt instruments. Between 2015 and 2020, the country **received $1.6 billion** in climate finance, of which $1.5 billion (94%) was delivered through loans, while only $115 million was delivered through grants. These significant contributions to Sri Lanka's debt have led to higher interest payments, creating even less fiscal space for the country to pursue effective climate action in the future.

There has been some positive news in recent years. In recognition of Sri Lanka's ongoing financial crisis, the **World Bank** and the **Asian Development Bank** recently granted the country eligibility to access concessional financing, which can help to foster climate and development action without furthering its debt burden.

These countries continue to struggle with limited human and technical capacity to navigate the complex landscape of climate finance. The process, from project origination to implementation, is laden with bureaucratic barriers that are especially challenging for countries with constrained resources.

Multilateral institutions and donors often impose stringent and fragmented requirements, creating additional layers of difficulty. Many developing nations report that they face insurmountable obstacles due to

fund-specific requirements and excessive paperwork, and local communities often struggle to access meaningful support. Moreover, very little of this funding actually reaches local communities, where it is most needed. Recipients have frequently pointed out that that funding arrives unpredictably, later than promised, or is delivered in ways that bypass country institutions and systems.

A **2021 study** revealed that only 46% of international climate adaptation funding allocated to least developed countries was aimed at empowering local actors. Even more concerning, there was often minimal evidence of local actors taking the lead in crafting climate solutions. In fact, local non-state actors were involved in the decision-making process for less than 10% of verified adaptation funds.

Innovative and emerging financing tools could help open new pathways to access climate finance in developing countries, but often fall short of their full potential. For example, high-integrity voluntary carbon markets (VCMs) offer a unique tool to mobilize private sector financing for climate action. However, VCMs can be difficult to navigate, particularly for developing countries that often lack the resources and capacity to effectively participate in the VCM—including developing robust governance mechanisms and market infrastructure.

Stringent Standards and Complex Processes for Access

Accessing climate finance is often hindered by standards and complex processes imposed by multilateral institutions and donors, including the multilateral climate funds. These rigorous requirements, while designed to ensure accountability and effective use of funds, can create significant barriers, especially for institutions in vulnerable and capacity-constrained countries.

One prominent example of these high standards is the accreditation process. The accreditation process for climate funds, while necessary to ensure strong financial management and safeguard funded projects, presents significant challenges for institutions, especially in vulnerable and capacity-constrained countries. Deserving entities trying to access funds from multilateral institutions have few options, and often find that the wait to get into the project pipeline is very long.

One major issue is the high cost and extensive time commitment required to meet the complex fiduciary standards of global climate funds. These standards, while designed to ensure accountability, often demand extensive documentation, reporting capabilities and financial expertise that many smaller institutions or those in developing nations simply do not have. As a result, the process can become overly burdensome, discouraging potential applicants and limiting access to essential funding for the regions most impacted by climate change.

Moreover, the accreditation process often fails to account for the specific contexts of these vulnerable regions, where institutions may not have the same resources or infrastructure to meet the stringent environmental, social and risk-management standards imposed by climate funds. This one-size-fits-all approach creates a barrier to entry for many entities that, despite their local knowledge and commitment to climate action, struggle to navigate the technical and bureaucratic demands of the accreditation process. The result is a system that perpetuates inequality in the distribution of climate finance, favoring larger, more resource-rich institutions while leaving many frontline communities without the financial support they urgently need to address the climate crisis.

Fragmentation limits impact and access

The fragmentation of climate finance poses a significant challenge in the global fight against climate change. As countries continue to create new funds and initiatives, such as the Fund for responding to Loss and Damage and the Global Biodiversity Framework Fund, the landscape becomes increasingly fragmented, with financial resources scattered across multiple, uncoordinated channels.

This splintering of funds prevents the cohesive alignment of efforts needed to address the complex and interconnected nature of climate issues. It encourages siloed approaches, where specific problems are tackled in isolation, rather than through a holistic strategy that could generate far greater impact. In a realm where time is of the essence, the inefficiency created by this fragmented finance landscape hampers the ability to drive large-scale, transformative climate action.

IMPACT

In climate finance, impact refers to the measurable, positive outcomes that result from funded interventions. Impact is a key indicator of quality climate finance, as it directly reflects how effectively the funding addresses the climate crisis.

And yet, there is a glaring lack of high-quality evidence on the impact of climate finance. Compared to other areas of development finance, climate adaptation, mitigation and resilience are woefully under-evaluated. This "evaluation gap" leaves the true effectiveness of climate interventions largely unknown.

JOHNNY ANDREWS / UNIVERSITY OF NORTH CAROLINA CHAPEL HILL, 2021

According to the Center for Global Development, out of more than 13,000 evaluations collected by the International Initiative for Impact Evaluation, only 87 focused on climate adaptation and a mere 31 on climate mitigation. In contrast, sectors like nutrition, gender and air pollution have hundreds of evaluations. While the relatively recent rise of large-scale climate finance explains part of this gap, even newer efforts continue to see underrepresentation.

Compounding the problem is a "synthesis gap"—a shortage of systematic reviews that analyze climate finance across different sources and contexts. This absence of overarching insights hampers our understanding of what drives success in climate projects. The inconsistency of metrics, such as varying greenhouse gas accounting methods, adds another layer of complexity, as does the lack of transparency in reporting emissions reductions.

The Independent Global Stocktake **interviewed** expert practitioners in climate finance from regions including the Pacific, Latin America, Caribbean, Southeast Asia and Africa. The goal was to obtain these practitioners' perspectives on accessing climate finance from different UNFCCC-linked multilateral climate funds. The interviews highlighted shared perspectives on access to climate funding:

- Climate finance is creating unsustainable debt in their countries.
- Access to adaptation finance in particular is lacking, and the process of designing and submitting proposals for adaptation projects is too lengthy and difficult.
- There is unfair competition for resources between accredited entities.
- Smaller projects and programs with lower risk profiles receive more scrutiny than larger projects.
- Many developing countries do not have enough Direct Access Entities (DEAs) to meet their needs.
- No financial support is available for loss and damage needs under the UNFCCC-linked funds.

Ongoing efforts under the UNFCCC's Global Goal on Adaptation (GGA) have made progress in creating common frameworks for measuring results, but the need for standardized indicators remains to improve reporting and track collective progress in both mitigation and adaptation finance. Standardized metrics are particularly useful for understanding and demonstrating impact at the local level, which can in turn attract more finance. For instance, they help translate local climate resilience efforts into a language that international financiers understand in a "common currency" of impact measurement to make local projects more attractive to global investors. Standardized metrics can help financiers better assess the climate risks and potential for impact in specific local contexts, potentially lowering the perceived risk of investment in vulnerable areas.

Disbursement challenges

Further complicating these challenges, climate finance disbursement has consistently lagged behind other forms of official development assistance (ODA). This reflects a challenge as part of the process of accessing finance and the capacity of finance to make an impact in a timely manner. Since 2015, disbursement ratios for climate projects have trailed the ODA average, suggesting significant delays and, in some cases, outright non-implementation. By 2020, adaptation-related ODA had a **disbursement rate** of just 59%, and mitigation-related ODA reached 75%—both far below the 91% average for general ODA.

While the COVID-19 pandemic understandably delayed many projects, the disbursement gap predates it. Adaptation finance, in particular, has consistently seen slower disbursement compared to mitigation. Although quick disbursement doesn't guarantee success, timely and predictable funding is essential for recipients to plan and implement projects effectively.

Disbursement issues in climate finance are often complicated by the internal conditions of recipient countries, where on-the-ground realities do not always align with the theoretical project designs. Projects may seem feasible on paper, but in practice, local challenges such as inadequate infrastructure, cultural factors or logistical barriers can hinder successful implementation. Climate finance disbursement must account for these dynamic realities, and support reasonable project restructuring and adaptive management to ensure initiatives can evolve and succeed despite obstacles. By allowing for project adjustments and providing implementation flexibility, climate finance can better help countries transform funding into effective climate action, even as they strengthen their institutional capabilities.

Moreover, the limited absorption capacity of many developing countries can prevent them from effectively managing large sums of money disbursed all at once. Without the necessary institutional capacity, these countries may struggle to translate funding into tangible climate actions, resulting in delays, inefficiencies or poorly executed projects.

Additionally, coordination between different levels of government—local, regional and national—can be disjointed, further complicating the disbursement process. In many cases, climate finance is channeled through national governments, but the most pressing needs may be at the local level, where direct climate impacts are felt. The lack of coordination or misalignment between government bodies can delay funds from reaching the communities most in need, or even result in misallocated resources. These structural issues within recipient countries highlight the need for a more nuanced, context-aware approach to climate finance that takes into account local realities and fosters stronger coordination between various stakeholders.

Long-term adaptation projects are often neglected

Climate finance challenges are especially pronounced for adaptation projects, which are critical for countries vulnerable to rising sea levels, stronger storms and other climate-related disasters. The process of designing and submitting proposals for adaptation funding is both lengthy and complex, often requiring detailed justifications even when lives are at stake.

Practitioners frequently encounter a bias toward large-scale mitigation projects, which can offer more immediate and measurable returns, especially in the case of renewable energy where the power is sold to the grid. Adaptation projects often provide indirect financial returns by reducing risk and protecting existing investments, but financial returns in the form of avoided costs may be harder to quantify and are often realized over a longer time frame.

ERNEST ANKOMAH

This bias overlooks the urgency of adaptation projects—such as installing early warning systems or restoring mangroves to protect coasts - which often yield more localized social and economic benefits by protecting vulnerable communities and ensuring economic continuity in the face of climate risks. For islands and low-lying coastal states, investments in flood defenses may avoid billions in damage from extreme weather events over the next few decades. For many communities, adaptation is not just about minimizing climate impacts; it is about safeguarding their very existence.

High transaction costs, small project sizes and limited data can further complicate matters, making it difficult for smaller nations to attract investments or compete for funding. The one-size-fits-all approach of climate finance often leaves these countries sidelined, unable to access the resources needed to build climate resilience. Without reform, these nations remain trapped in a system that is ill-equipped to meet their needs.

Impact of innovative mechanisms

Innovative and emerging financing tools have the potential to mobilize climate finance and drive climate action in developing countries. However, these innovative mechanisms are often not as impactful as they could be. Voluntary carbon markets offer a useful case study, representing a tool which sometimes does not deliver emissions reductions or other promised environmental and climate benefits. The VCM has come under criticism about low-quality carbon credits driven by overexaggerated claims of emissions reductions and failure to deliver sustainable development benefits. For example, the VCM lacks any standardized revenue-sharing agreement to ensure that the host countries or communities for carbon credit projects or programs retain some of the profit.

TIMOR LESTE JAQUELINO MAGNOUNDP / 2024

VOICES FOR CLIMATE FINANCE REFORM

During the NCQG work program meetings in 2024, negotiators stressed the need to improve qualitative elements of climate finance, and the importance of incorporating quality considerations into the NCQG. **Here are some of their comments:**

> **The debt burden of developing countries must not be increased by the new goal. The NCQG must be delivered to the largest extent possible via the provision of public finance in a grant based or concessional equivalent manner.**
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> —
>
> **Negotiator for Group Sur**

> **We would like to see a reference that any market-rate loan is not counted as climate finance. We would also want to see a representation of the fact that any finance flowing to developing countries must consider the fiscal constraints of developing countries...**
>
> —
>
> **Negotiator for African Group of Negotiators**

> **The NCQG must address 'disenablers' of climate finance such as high cost of capital [and] high transaction costs associated with access and unilateral measures. Loans at market rates and private finance flows at market rate of return cannot be termed as climate finance under the NCQG. Rather, they represent a reverse flow from developed to developing countries if we consider the repayments.**
>
> —
>
> **Negotiator for LMDC Group (Like-Minded Developing Countries)**

> **On the qualitative side, access and predictability are important. For instance, addressing access modalities, cost of capital [and] high transaction costs...is crucial. Grant-based finance, especially for adaptation and loss and damage, will be critical for our growth. We are very concerned [about] debt burden and indebtedness.**
>
> —
>
> **Negotiator for Least Developed Countries Bloc**

Notably, developed countries are also calling for greater consideration of climate finance quality within the NCQG:

> **For us, investing in climate action is really a means to an end....and making sure that there's a strong focus on effectiveness is actually really the critical thing here, rather than the dollars or cents invested.**
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> —
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> **Negotiator for the United States**

> **We've also heard a lot about the challenges related to debt and the cost of capital, and we recognize these challenges that countries with high levels of debt and vulnerability face when addressing climate change. It is because of this that quality of finance is key. Grant based and concessional finance must have a role in the NCQG.**
>
> —
>
> **Negotiator for the United Kingdom**

> **We're well aware that investment flows are currently not at scale flowing to developing countries, and we think that this goal offers opportunity to work on that, and to get the international financial system in shape to allow more funds to flow where it's most needed...highlighting the role of MDBs, IFIs, the role of enabling conditions that come with that.**
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> —
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> **Negotiator for the European Union**

ANNA JIMENEZ CALAF / UNSPLASH

EFFORTS TO IMPROVE CLIMATE FINANCE QUALITY

Improving the quality of climate finance for developing nations involves addressing the key challenges of concessionality, access and impact. Innovative initiatives are already addressing these key areas, helping to break down barriers to financing and enhancing the effectiveness of projects in the countries that need them most.

By reforming financial mechanisms, building local capacity and creating more effective ways to measure results, these initiatives demonstrate that it is possible to create a more equitable and efficient system of climate finance—one that truly empowers developing nations to meet the climate challenge head-on.

CONCESSIONALITY

A number of initiatives are working to address concessionality challenges, aiming to make funding more affordable, de-risk projects and provide flexibility when needed.

Multilateral development bank reform

At the 2024 World Bank spring meeting, the bank approved the **Framework for Financial Incentives (FFI)**, an initiative aimed at expanding concessional finance flows to projects tackling global challenges, including climate change. The **FFI** relies on the newly established Livable Planet Fund to mobilize concessional resources and grants. By making funding more affordable, this framework is intended to encourage countries to take on ambitious climate projects without the financial burdens that traditional lending imposes.

Multilateral support for local private sector climate finance

Multilateral climate institutions are increasingly recognizing the importance of creating tailored spaces for private sector engagement that are relevant to developing countries' local contexts. These efforts aim to catalyze private investment in climate action while addressing the unique challenges and opportunities in different regions. The Green Climate Fund's Private Sector Facility (PSF) exemplifies this approach, with promising examples such as **CRAFT - Catalytic Capital for First Private Investment Fund for Adaptation Technologies in Developing Countries** and the **Acumen Resilient Agriculture Fund** (ARAF). Similarly, the Global Environment Facility has launched its Non-Grant Instrument Program, which uses equity, guarantees, and concessional loans to attract private sector investment in areas such as land degradation, biodiversity and climate change. The Climate Investment Funds, through its Private Sector Set-Asides, also provides concessional financing to encourage private sector involvement in clean technology, forest conservation and climate resilience projects. These initiatives demonstrate a growing trend among multilateral institutions to create flexible, context-specific mechanisms that bridge the gap between global climate finance and local private sector engagement in developing countries.

Climate resilient debt clauses

The World Bank's Climate Resilient Debt Clauses were adopted to allow vulnerable low-income countries to defer their repayments for up to two years if they are hit by a severe hurricane, flood or other natural disaster. While these measures don't eliminate debt, they allow for vulnerable states to focus on disaster response and ensure that existing loans—including for climate finance projects—do not create extra burdens during particularly challenging moments. These clauses were **expanded** in 2023 to cover all eligible countries.

HURRICANE IRMA CLIMATE CENTRE / NETHERLANDS / RED CROSS, 2017

Debt-for-nature and debt-for-climate swaps

Debt-for-nature and debt-for-climate swaps offer an innovative approach for funding effective climate action while directly addressing countries' debt burdens. These **swaps** allow highly indebted countries to engage in conservation or climate-action projects in exchange for debt relief. This fiscal space will serve to reduce debt while also helping to deliver an innovative pathway to address two urgent challenges simultaneously. This kind of dual benefit for climate actions is another reason why thinking about climate finance in other economic contexts and silos makes so much sense: it has the potential to deliver more meaningful and transformative climate impacts.

Donor country efforts

While **the use of market rate loans for climate finance remains high** among many donor nations, some developed countries are taking steps to increase the use of grants and other concessional instruments within their public climate finance commitments. For example, in 2021, Canada **committed** to increase the proportion of grants in its climate finance mix from 30% to 40%. Additionally, the other 60% of Canada's climate finance is being delivered in the form of Unconditionally Repayable Contributions—a form of concessional financing where repayment terms are negotiated between the parties. Delivering finance through a greater mix of grant and concessional tools can help limit additional debt burdens, and mitigate the potential for net outflow of funds from developing countries.

ACCESS

These initiatives are working to address complex bureaucratic barriers and stringent accreditation processes, and improve coordination and capacity-building to improve the flow of resources to where they are needed most.

The taskforce on access to climate finance

In 2021, the COP26 Presidency established the **Taskforce on Access to Climate Finance**, an initiative intended to develop principles and recommendations to improve climate finance access, use and programming. The Taskforce has worked to strengthen awareness of access considerations among MDBs and MCFs, including working to integrate principles within the institutions' strategic planning efforts, and is engaged in pilot programs in several developing countries to build climate financing plans and approaches.

Greater access through MDBs

As part of their reform agenda, the World Bank and the International Monetary Fund are cooperating to channel more climate finance to countries in need. The World Bank **delivered** $42.6 billion in climate finance in FY2024 - a 10% increase over the prior year - and plans to dedicate 45% of its total lending to climate finance in FY2025. Additionally, the groups have also **committed** to establishing country-led platforms to support in mobilizing additional finance.

Jurisdictional REDD+ Technical Assistance Partnership (JTAP)

The **JTAP initiative** was launched as a global initiative of five international NGOs, including Environmental Defense Fund, to provide technical assistance to forest jurisdictions that aspire to participate in the high-integrity voluntary carbon market, unlocking finance for forest conservation and management at scale. By focusing on local capacity building, JTAP empowers those on the frontlines of deforestation and climate impacts, ensuring they have the tools and resources needed to secure climate finance.

Community of practice for direct access entities

Supported by two Multilateral climate funds—the Adaptation Fund and the Green Climate Fund—the **Community of Practice for Direct Access Entities** brings together national and direct-access entities to share knowledge and strengthen institutional readiness for accessing climate funds. By improving coordination between these entities and enhancing their capacity to plan for and utilize funding effectively, this initiative helps to ensure that resources flow to where they are needed most.

Green climate fund's simplified approval process

The Green Climate Fund instituted a **simplified approval process** to reduce bureaucratic hurdles, streamline approval and speed up access for certain projects. The simplified process is designed to support small, low-risk projects, allowing funding to more quickly and easily traverse the system.

STOKPIC/ PIXABAY

IMPACT

Several innovative initiatives exemplify how climate finance can be structured to drive real, measurable change. These examples demonstrate how well-designed financing can deliver tangible, long-term benefits by standardizing assessments, improving transparency in outcomes and accelerating the disbursement of funds.

Common approach to measuring climate results

To improve how the success of climate projects is tracked, multilateral development banks agreed at COP28 to develop the **Common Approach to Measuring Climate Results**, a scorecard that will be used across the MDB system. The new framework seeks to standardize and improve measurement of both mitigation and adaptation outcomes, mobilization of private finance and co-benefits for other sustainable development goals. The MDBs intend to share an updated set of indicators to inform this approach at COP29.

Energy Access Relief Facility

The **Energy Access Relief Facility (EARF)**, supported by the Green Climate Fund during the COVID-19 pandemic, provides an example of how concessionality, access and impact can be addressed simultaneously to achieve comprehensive improvements in the quality of climate finance. The GCF approved EARF almost instantaneously, at a level of concessionality that few other climate funds can reach, providing extremely fast, significant assistance to energy-access companies across sub-Saharan Africa. By ensuring that these companies would survive the crisis, the facility ensured that they could continue to deliver access to energy, a service that is especially important to vulnerable populations. On top of this relief, it incorporated clear impact metrics ensuring that the concessional resources would produce longer-term benefits, too. EARF shows exactly why well-designed climate finance can be mobilized quickly, reach those who need it most and create life-changing, measurable impacts.

Linking finance to verified impact

One effective way to incorporate impact considerations into climate finance is by directly linking payments to verified outcomes, using results-based payments (RBPs). This approach has become a key tool for REDD+ initiatives (efforts to reduce emissions from deforestation and forest degradation), offering financial rewards in exchange for proven reductions in emissions. A notable example is the Amazon Fund, managed by the Brazilian Development Bank, with funding from countries like Norway and Germany. The fund provides RBPs to Brazil, incentivizing efforts to curb deforestation in the Amazon.

Rapid disbursement windows

The new Fund for responding to Loss and Damage (FRLD) is exploring innovative access modalities and disbursement windows. The fund's **governing instrument** suggests that it could utilize a rapid disbursement window to quickly get money out the door following an extreme weather event, fast tracking the process to ensure that loss and damage finance can be impactful in a timely manner. **Similar rapid disbursement mechanisms** have been utilized through specialized disaster response funds at the World Bank and other MDBs, but are not in use from the other multilateral climate funds.

Integrity Council for the Voluntary Carbon Market

The **Integrity Council for the Voluntary Carbon Market (ICVCM)** has established a set of ten Core Carbon Principles (CCPs) to identify high-quality carbon credits that create real, verifiable climate impact. These principles aim to ensure that carbon credits are governed effectively by carbon crediting programs; represent real, additional and permanent emission reductions; and contribute to positive environmental and social outcomes, including by providing sustainable development benefits and strong safeguards. This helps to prevent the issuance of low-quality or fraudulent credits and ensures that the finance generated by the carbon credits is used to generate positive climate impact.

ROANNA RAHMA

QUALITY CLIMATE FINANCE FOR FOOD SYSTEMS AND AGRICULTURE

Building quality in climate finance is important across sectors, including for food and agriculture. Climate finance for agrifood systems is critically underfunded, making up just 4% of total climate finance, even though the sector contributes nearly one-third of global emissions and has a pressing need for adaptation. By improving the design and delivery of climate finance, we can support a more sustainable, climate-resilient food system that benefits both farmers and the environment. Here are some key recommendations:

CONCESSIONALITY

- Financing must address existing inequities in farmers' access to funds.
- Public and philanthropic funding should play a role in blended finance solutions for the long term.
- Concessional, catalytic capital is essential to fill financing gaps and support collaborations between farmers, financial institutions and market partners.

ACCESS

- Financial solutions must be designed to meet farmers' specific needs, considering the unique farming region, production system, climate risks and socioeconomic conditions.
- Finance should directly reach farmers to help them invest in on-farm practice changes and technology for climate adaptation.
- Funding should be easy for farmers to access by reducing application burdens and delays, ideally distributed through trusted local partnerships.

IMPACT

- Farmers need a comprehensive set of incentives, including both financial and technical support, for climate-resilient agriculture.
- Financing strategies should be scalable and developed with a landscape-level approach.
- Systems for measuring, monitoring, reporting and verifying environmental impacts must be both accurate and practical for farmers and their partners.
- The private sector, including food and agriculture value chains and the finance sector, has a key role in driving systemic change by collaborating and creating new financial models.

EXAMPLES OF INNOVATION IN CLIMATE FINANCE FOR AGRIFOOD SYSTEMS

- **One Acre Fund** provides high-quality farm products and services in rural areas of Africa, offering affordable, flexible payment options. Through their full-service program, they support farmers year-round by providing farm inputs on credit, delivering products close to home before planting and training in effective farming techniques. This comprehensive approach helps farmers overcome barriers to climate-resilient agriculture.
- **Aceli Africa** incentivizes local banks to lend more to small- and medium-sized agribusinesses in East Africa, especially those meeting climate resilience criteria. Since 2020, Aceli has mobilized $152 million, with an average loan size of $97,000, supporting businesses too large for microfinance but too small for traditional bank loans.
- **AGRI3** Fund mobilizes public and private capital to reduce deforestation in agricultural value chains by partnering with local financial institutions. Through financial guarantees and grants for technical assistance, it supports sustainable practices. In Brazil, the Responsible Commodities Facility provides low-interest loans to farmers who commit to zero deforestation and conservation of native vegetation, with WWF Brazil involved in oversight.
- The Field to Market **Climate-Smart Agriculture Innovative Finance Initiative** leverages $176 million from government, corporate and industry sources to support 10.6 million acres of climate-smart farming, and reduce 2.8 million metric tons of GHGs in the United States. The project connects innovative financial products like the **Regenerative Agriculture Financing Program**, which provides farmers who reach environmental targets with an interest rate rebate, with demand and incentives from value-chain companies.

ASIAN DEVELOPMENT BANK, 2019

BUILDING QUALITY CONSIDERATIONS INTO THE NCQG

The New Collective Quantified Goal will be a milestone and guiding framework for climate finance in the coming years. To be truly effective, it must prioritize high-quality standards in climate finance flows, focusing on key issues such as concessionality, accessibility and measurable impact. Additionally, it should urge decisive action from multilateral institutions and donor governments to ensure these goals are met.

The substantive framework for a draft negotiating text for the NCQG includes qualitative elements. **We urge that negotiating Parties retain this language in the final NCQG text,** including specific language on leveraging concessional finance and other innovative tools to mobilize new sources of finance, enhancing channels of access for climate finance, reforming the multilateral development banks, strengthening complementarity between climate funds and improving financial disclosure measures.

In addition to this language, the following proposed text can be used by negotiating parties to ensure that the NCQG promotes efforts to improve enabling environments and tackle systemic issues related to quality in climate finance.

PROPOSED TEXT

We suggest that the NCQG text to include the following:

In "Context and Scene Setting"

- *Agrees* to strengthen quality considerations in the provision and mobilization of climate finance, including enhancing the use of concessional and grant resources, improving channels of access and better measuring the impact of finance.

In "Goal Formation including quantitative and qualitative elements"

- **In Section 5 - Sources, channels and instruments:** *Calls upon* Multilateral institutions, including multilateral climate funds to foster stronger complementarity and channels of cooperation, such as through establishing flexible co-investment mechanisms or developing integrated capacity building programs.

- **Section 8 - Reducing barriers, addressing disenablers and increasing opportunities to enable climate finance and enhance quality:**

  1. *Urges* the multilateral development banks and multilateral climate funds to:

     (a) Increase their concessional finance capacity and leverage it to mobilize new sources of private finance, with the aim of doubling the ratio of private capital mobilized for every dollar of public financing;

     (b) Expand the use of blended finance models to de-risk projects and attract private investment;

     (c) Support developing countries in building frameworks to align climate objectives with national planning and budgeting processes, to foster successful and equitable engagement with the private sector.

  2. *Urges* multilateral climate funds and multilateral development banks to improve the measurement and understanding of climate risk when making financing decisions, particularly for small island developing states and other vulnerable countries.

ROANNA RAHMAN

RECOMMENDATIONS

To successfully implement the NCQG and make progress on the Paris Agreement objectives, multilateral institutions and other climate finance providers are central to address structural challenges in climate finance and create strong enabling environments—as identified within the draft NCQG text. The following section offers recommendations for **what** policies these institutions should pursue to enable a successful NCQG, with specific steps for **how** they can improve the quality of climate finance and maximize the impact of resources in developing countries.

CONCESSIONALITY

To ensure that concessional instruments can continue to bolster global climate efforts and support countries in implementing their NDCs, multilateral development banks and donor countries must take tangible steps to strengthen the role of concessionality in international climate finance.

1. **Expedite the reform agenda of multilateral development banks with a focus on strengthening concessionality.**

- Expand the use of blended finance models, similar to the Green Climate Fund's Private Sector Facility, to de-risk projects and attract private investment.
- Implement more flexible loan terms, such as the World Bank's **Climate Resilient Debt Clauses**, across a wider range of climate finance instruments. CRDCs support vulnerable countries that are facing economic shocks, including fiscal crises due to natural disasters.

- Explicitly consider debt burden when structuring climate finance solutions and expand the use of non-debt financial instruments.
- Expand concessional finance capacity and leverage it to mobilize private finance. Currently, MDBs leverage about $0.60 in private capital for every $1 of MDB financing. The G20 has called on MDBs to double this ratio. By improving their leverage of private finance and facilitating blended finance projects, MDBs can unlock significant additional resources for climate investments.
- Develop new financial products that offer more favorable terms for high-impact climate projects, especially in least developed countries (LDCs) and small island developing states (SIDS).

2. **Improve transparency in concessional finance.**

- Establish clear, standardized reporting on the terms of concessional loans from MDBs and other multilateral institutions, ensuring that countries understand the precise financial conditions of these loans.
- Establish an aligned set of terminology around access to climate finance to reduce confusion and improve communication between providers and recipients.
- Develop basic guidance for equitable bilateral and multilateral climate finance, including a roadmap for a long-term shift to institutional and programmatic approaches to climate finance and comparable platforms with terms and conditions available across channels.

3. **Address undue barriers created by sovereign credit ratings and risk.**

- Provide partial guarantees for MDB loans, which can help improve sovereign credit ratings and make it easier for developing countries to access affordable finance.
- Offer currency hedging mechanisms, to allow countries to borrow in local currencies while protecting against exchange rate risks.
- Improve credit rating accuracy and fairness and update methods for assessing debt ceilings to ease financial pressures on developing countries. Rating agencies should reform their methodologies to provide transparent, longer-term (30–40 years) assessments of creditworthiness, focusing on growth potential rather than short-term projections. Additionally, the adequacy of credit-risk management systems and regional monetary arrangements should be factored into ratings.
- Apply alternative risk measurement methods. For example, the Global Sustainable Competitiveness Index (GSCI) ranks countries on their ability to achieve long-term, inclusive and sustainable economic growth. Unlike traditional credit ratings, the GSCI focuses on sustainability and considers factors beyond financial metrics, providing a long-term perspective on future growth potential for both society and the environment.

ACCESS

With adequate access to climate finance, developing countries can catalyze a broader range of projects, particularly those tailored to local needs and conditions, thereby increasing the overall effectiveness of international climate efforts. Ensuring that climate finance is accessible is key to making climate justice a reality, empowering vulnerable nations and communities to lead their own climate responses.

1. **Adopt the Multidimensional Vulnerability Index (MVI), as an improved way to measure and understand climate risk when making financing decisions.**

- Replace gross national income (GNI) with MVI as a means of accounting for factors such as exposure to environmental disasters, the capacity to recover from shocks and social vulnerability. Adoption of the MVI should enable more funding to reach countries and communities that are most vulnerable to climate impacts, even if their income levels might otherwise disqualify them under traditional metrics. (In September of 2024, the UN General Assembly adopted a resolution advancing the use of the MVI, though its implementation remains voluntary.)

2. **Streamline procedures for climate finance access**

- Simplify and standardize climate finance procedures to reduce barriers and accelerate access across funding sources.
- Establish clear and stable policy frameworks in recipient countries to provide certainty for private investors.
- Offer capacity-building programs to help private sector entities understand and navigate the climate finance landscape.
- Accelerate the implementation of standardized metrics for measuring climate finance impact, ensuring that these metrics capture access-related issues.

3. **Establish comprehensive disaster response finance**

- Transform disaster response financing from reactive to proactive by creating pre-arranged mechanisms that enable rapid, predictable access to funds.
- Reduce paperwork, simplify eligibility criteria and cut approval times to accelerate access to financing in disaster-response situations.
- Develop risk-sharing mechanisms, such as first-loss guarantees or insurance products, to encourage private sector investment in climate projects in developing countries.

4. **Stimulate greater investment from MCFs in readiness initiatives towards an NDC investment planning approach.**

- Create platforms for public-private partnerships in climate finance, facilitating collaboration between multilateral institutions, governments and private sector entities.
- Support programs such as the Climate-Smart Agriculture Innovative Finance Initiative that connect innovative financial products with demand from value-chain companies.
- Help developing countries build the skills and expertise necessary to engage with private investors, allowing countries to unlock new sources of climate finance and amplify the impact of international funding. Empowering local actors to take ownership of climate projects can ensure that climate initiatives are aligned with national and local priorities.
- Enhance NDCs through comprehensive mainstreaming and stakeholder engagement to create more fundable climate projects. Countries could integrate climate objectives directly into national planning and budgeting processes, while mapping and realigning existing finance flows toward climate action. This integration should be paired with robust stakeholder engagement that systematically includes subnational authorities, marginalized groups and potential implementing entities in the planning process.

ERNEST ANKOMAH

IMPACT

Boosting the effectiveness of climate finance ensures that resources are used efficiently to drive meaningful progress toward a sustainable, climate-resilient future. By focusing on high-impact interventions that deliver tangible benefits—such as reduced emissions and strengthened resilience—developing countries and funders can better meet their goals. These recommendations on impact complement a **recent** report by the Independent High-Level Expert Group appointed by the Brazilian G20 Presidency, which called for stronger collaboration among the Multilateral Climate Funds.

1. **Enhance complementarity between climate funds to maximize the impact and quality of climate finance in support of more ambitious and effective NDCs**

- Foster Flexible Co-Investment Mechanisms:
  - Develop adaptable frameworks that enable various climate funds to co-invest in projects and programs, while also facilitating private sector participation.
  - Create guidelines for flexible co-financing arrangements that can accommodate different fund mandates and private sector requirements.
  - Implement a streamlined due diligence process that reduces redundancy while meeting the needs of multiple funds and private sector partners
- Develop Integrated Capacity Building Programs:
  - Design and implement coordinated capacity building initiatives that leverage the strengths of different funds to comprehensively support countries in developing and implementing ambitious NDCs.
  - Create a common capacity needs assessment tool used across funds Establish a shared pool of technical experts accessible to all funds.
- Launch a Multi-Fund Blended Finance Initiative:
  - Establish a collaborative program that combines resources from multiple climate funds to create innovative blended finance instruments and scale up successful projects.
  - Develop standardized criteria for blended finance projects across funds and a shared pipeline of bankable projects eligible for multi-fund support.

2. **Develop stronger reporting measures to better understand the climate impact of projects.**

- Consider the co-benefits for biodiversity, development and other issues, given the compounding nature of challenges and limited global resources available to tackle them.
- Establish categorizations and guidelines for investments aligning with climate objectives to offer direction for private investors.
- Create incentives, such as tax breaks or preferential treatment in public procurement, for private-sector entities that invest in high-quality climate projects.
- Support initiatives that improve the quality and availability of climate-related financial data to inform investment decisions.

CONCLUSION

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The High-Level Expert Group on Climate Finance **estimates** that developing countries need $2.4 trillion annually by 2030 to combat climate change effectively. However, our analysis reveals that current climate finance often fails to reach its intended recipients or achieve meaningful impact due to issues of concessionality, accessibility and effectiveness.

For instance, only 41% of loans from Multilateral Climate Funds and 23% from Multilateral Development Banks are concessional, while bureaucratic hurdles leave many vulnerable communities unable to access funds. Furthermore, the lack of enhanced impact metrics make it difficult to assess the true effectiveness of climate investments. These concrete challenges underscore the urgent need to prioritize the quality of climate finance, not just its quantity, as we work towards the NCQG.

By deepening our focus on these key dimensions of quality, we can ensure that financial resources are allocated effectively to meet the climate goals of developing nations, and better engender transformative outcomes.

To achieve these goals, multilateral development banks and donor countries must prioritize **concessionality**. By offering more favorable loan terms and expanding blended finance models, MDBs can make high-risk, high-reward projects more feasible. Ensuring that developing countries are not burdened by unsustainable debt loads is critical to avoiding a debt spiral that hinders climate action. Further, concessional loans must be coupled with risk mitigation strategies, such as guarantees and currency hedging mechanisms, to reduce the perceived and actual risks for investors.

Improving **access** to climate finance is another key dimension. Streamlining bureaucratic processes and offering tailored capacity-building programs can empower developing countries to attract more investment while reducing reliance on external intermediaries. For example, adopting the Multidimensional Vulnerability Index offers a more nuanced approach to allocating finance based on a country's vulnerability to climate risks rather than traditional income-based metrics. Such measures can enable a more equitable distribution of climate finance, ensuring that the most vulnerable nations receive the support they need.

In terms of **impact**, this report highlights the importance of creating a coherent and complementary system of multilateral climate funds, with clear reporting and accountability mechanisms to track the outcomes of financed projects. Effective measurement and reporting frameworks are essential to evaluating the true effectiveness of climate finance, while aligning incentives for private investors—such as tax breaks or standardized reporting—can drive more investment in impactful climate projects.

Efforts to date, including initiatives from MDBs, have shown promise in addressing these barriers. However, scaling such solutions across different financial channels and regions remains a significant challenge, as do systemic issues like high borrowing costs and unfavorable credit ratings for developing nations.

Current efforts have seen advancements in tackling challenges regarding funding terms and accessibility in climate matters, and ongoing attention to these issues is vital for optimizing the benefits of investments in climate actions. There is also a need for exploration into how to ensure the effectiveness of climate financing quality standards. Future studies should look to create measures that assess the outcomes of climate funding beyond just reducing emissions. This might involve evaluating advantages for biodiversity and strengthening stability. We could also consider how various financial tools, like investing in stocks or funding based on outcomes, can help with a variety of climate solutions in countries with limited resources and small island nations.

To deepen understanding, future research should also focus on how local actors and communities can be more integrated into the climate finance process. Local ownership of projects has been shown to enhance their success, yet many developing countries lack the institutional capacity to engage effectively with international financial institutions. Research could explore strategies for building this capacity and developing frameworks that ensure climate projects are responsive to local needs and conditions.

Taking an approach to assessing the quality of climate finance would entail developing common metrics and reporting structures that are widely recognized and agreed upon by all parties involved. This would involve aligning the terminology and definitions related to concessionality, accessibility and impact, across organizations and countries to minimize any confusion.

As the global community strives to meet the NCQG targets, quality must remain at the heart of climate finance discussions. By focusing on concessionality, access and impact, we can ensure that climate finance does more than simply meet quantitative goals. Instead, it can catalyze transformative climate action that is equitable, sustainable and aligned with the urgent needs of developing countries. By strengthening our focus on delivering high-quality climate finance, we can bridge the gap between ambition and action—driving the world toward a more resilient and low-carbon future.