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Climate Finance  
and Development  
Effectiveness in  
Africa

# RealityCheck

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Manoocher

## about this issue

*This edition of Reality Check provides an insight in the prospects and challenges for climate financing in Africa. It observes that though Africa is not the greatest emitter of greenhouse gas, these countries are most vulnerable to the effects of climate change such as extreme weather changes, agricultural productivity loss, and rising sea levels. The primary objective of climate finance therefore is to provide financial flows from industrialized to developing countries to both mitigate and adapt their economies to climate change.*

*African countries will be affected differently, depending on the region. The worst impacts of climate change will be felt in Sub-Saharan Africa, where the vast majority of the population is dependent on rain-fed agriculture. Agricultural production is projected to fall 50% by 2050 due to a reduction in rainfall and*

*increase in temperatures, while the majority of African states will be faced with water scarcity and water stress by 2050. The reduced income will certainly undermine the achievements made towards the realization of the Millennium Development Goals.*

*It concludes by observing that in designing the Green Climate Fund, it is worth reviewing the short-comings and challenges experienced by the implementation of the Aid Effectiveness agenda as well as implementation of the more successful global funds, like the Global Fund on HIV/Aids, TB, and Malaria.*

## Climate Finance and Development Effectiveness in Africa

Nancy Dubosse, PhD



“Though there is great variation in the costs of adaptation, the estimates are monumental, ranging between US\$75-\$100 billion annually; for Africa, approximately US\$18 billion annually.”

### SUMMARY

The aid effectiveness campaign has succeeded in offering a set of operating principles and a process framework for making development assistance more transparent, effective, accountable and consultative. However, as climate change poses to be a significant threat to African countries, the prevailing modality to address adaptation and mitigation is the global fund, which is delivered directly to projects, bypassing partner countries' public finance management systems and institutions.

Though there is great variation in the costs of adaptation, the estimates are monumental, ranging between US\$75-\$100 billion annually; for Africa, approximately US\$18 billion annually. There is an urgent need to fuse the gains made by the aid effectiveness movement with the goodwill and enthusiasm of global funds.

The number of vertical funds operating in the environment sector is astounding, considering the lag time with which both civil society and developing country governments were struggling to grapple with in the issue of climate change. As of December 2009, there were 22 funds with USD\$18 billion in commitments. Two institutions have emerged as administrators of these funds: the Global Environment Facility Trust Fund and the World Bank. The emerging centrality of the supply side of these global funds is appealing as it will ensure coherence, reduce transaction costs and facilitate accountability. But the emerging supplier is less appealing: the World Bank, with its record on funding projects which exacerbated environmental damage and displacement of people and the lack of transparency around its operations. The most recent global fund to be created is the Green Climate Fund (GCF), established at the 16<sup>th</sup> COP in Cancun, with initial commitments of US\$30 billion in 'fast-start finance'.

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### Emerging issues

#### ▪ **Additionality**

It is difficult to separate aid which addresses mitigation and adaptation and traditional aid (ODA), as the OECD has issued reporting directives to its member countries, which make it virtually indistinguishable from ODA. Currently, the percentage of total bilateral ODA addressing bio-diversity, climate change mitigation, and desertification is, on average, 7.1%. This appears to be in contradiction to the 2005 Gleneagles commitment made by donors of 0.7% of their GNI to development assistance. Recent evidence reveals that donors have been counting pledges made to climate change as ODA.

#### ▪ **Absorption capacity**

One of the reasons most often given as to why development finance is increasingly coming in the form of vertical funds is because of the absorption constraints of poor countries. Yet the persistent by-passing of the budget and, by derivation, the state's institutions, contributes to absorption constraints. Paying lip service to reinforcement of the institutional capacity of developing countries and the Paris principles of ownership and alignment despite the proliferation of vertical funds is an illustration of the policy incoherence in the aid architecture.

#### ▪ **National Adaptation Programmes of Action**

There is evidence that national adaptation programmes of Action are narrowly-focused on environment sectors. Rather than be directed at environment, rural development, and agriculture ministries, adaptation must be mainstreamed into development programmes, as climate change could destabilize existing achievements and undermine ongoing efforts. Adaptation also implies that current national development policies must be revised.

#### ▪ **The right of access to information**

The existing climate funds have been accused of opacity in their administration. It is difficult to obtain information on disbursements, terms and concessionality, and per project information. The absence of the relevant information obstructs meaningful engagement of civil society.

### **Recommendations towards improved effectiveness**

Among the recommendations made include:

- The use of public finance systems that have

been reinforced by the aid effectiveness principles, so as not to undermine partner country institutions and capacity.

- The sectoral fragmentation that currently exists between development practitioners and civil society erects barriers to learning and sharing. One of the areas in which the climate change/environment/aid community of practitioners needs to collaborate is the access to information movement.
- In designing the Green Climate Fund, it is worth reviewing the short-comings and challenges experienced by the more successful global funds, like the Global Fund on HIV/Aids, TB, and collapsing existing funds so as to reduce simply administration.
- National implementing agencies (NIA), a promising feature of global funds, should be adjusted to have mandated public consultation mechanisms with civil society organisations and parliament, and report directly to national parliaments.
- Attention needs to be devoted to the composition of climate finance. The countries most at risk are the poorest (income-wise) and least-developed in the world. Loans to address a situation for which these countries have no culpability are unacceptable. Any gains made in successful climate adaptation would be comprised by unsustainable debt burdens of future generations.

The multi-dimensional nature of climate change, and the actions required to address it, requires a coordinated approach. It requires cross-sector coordination, insofar as national strategies reflect the most urgent needs of the country as well as those of traditionally marginalised groups. It requires international coordination, ensuring that the requisite resources are made available. It requires inclusive planning, underpinned by broad consultations. Finally, it requires a culture of information-sharing, with a view to ensuring transparency of process and accountability of outcome.

## 1 INTRODUCTION

The Paris Declaration (2005) effectively ‘verticalized’ what was a chaotic field of aid donor and recipient countries, local government and departmental ministries, private entities, non-governmental organizations, and civil society. Guided by certain principles<sup>1</sup>, it placed government at the centre of aid disbursement and management by committing the signatories to a number of reforms, which included directing development assistance to the budget; making provisions for national consultations on its destination, use, and evaluation; committing to aid targets and also to use partner country procurement systems (on the part of donors). The Paris Declaration (PD) essentially created a process framework for development finance.

This was followed by the Accra Agenda for Action (2008), which reaffirmed the principle of ownership (on which stakeholders had not observed sufficient improvement). It underscored the need for more

inclusive partnerships, in particular with the private sector, global funds, middle-income countries, and civil society. It also emphasized the achievement of development results and ‘value for money’, as the desired outcome of poverty eradication had been somewhat cast aside in the concentration on process.

The identification of other stakeholders in the AAA, who had largely not been signatories in the PD, was essentially an indication that there was still unresolved competition on the supply side of the aid value chain. The participants at the 3<sup>rd</sup> High Level Forum (in Accra) encouraged all development actors to use the PD as a point of reference in development cooperation. A part of the AAA was devoted to global funds:

Global funds and programmes make an important contribution to development. The programmes they fund are most effective in conjunction with complementary efforts to improve the policy environment and to strengthen the



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institutions in the sectors in which they operate. We call upon all global funds to support country ownership, to align and harmonize their assistance proactively, and to make good use of mutual accountability frameworks, while continuing their emphasis on achieving results. As new global challenges emerge, donors will ensure that existing channels for aid delivery are used and, if necessary, strengthened ***before creating separate new channels that risk further fragmentation and complicate coordination at country level.*** (Emphasis by

author)

Generally, it can be stated that there remains a disconnection between international development goals and prevailing aid modalities. The much maligned international reserve requirement and the limitations on civil service employment of the International Monetary Fund (IMF) for countries under its Poverty Reduction and Growth Facility against the ‘big push’ for aid and spending towards achieving the Millennium Development Goals (MDGs) is just one example. With a range of development targets in focus, the world required a systematic assessment of how to attain them, as previous financing strategies had obviously failed poor countries, which remained poor despite having received nearly US\$400 billion in aid. In the ten years before the Paris Declaration (1995 – 2004), the average aid to GDP ratio for developing countries was US\$14.3; in Africa, US\$26.7; among Highly Indebted Poor Countries, US\$31.3.<sup>2</sup> The PD/AAA agenda, seen in this context, offered a set of operating principles, with respective indicators and



targets, in order to reform the chaotic, non-accountable, non-participatory aid value chain.

The next ‘big push’ is to address climate change: in the case of Africa, it is mainly on funding for adaptation



strategies. Though there is little unanimity on the costs of adaptation, estimates of annual adaptation costs range between US\$75-100 billion.<sup>3</sup> Rather than be directed at environment, rural development, and agriculture ministries, adaptation must be mainstreamed into development programmes, as climate change could destabilize existing achievements and undermine on-going efforts. Adaptation also implies that current development programmes must be revised (e.g. climate resilient roads and irrigation systems).

According to its guiding policy document on aid for climate change, the Organisation for Economic

Cooperation and Development (OECD), observes that the national level is critical for mainstreaming climate change adaptation.

At this level, strategic decisions are taken which create the enabling environment for public and private-sector actors as well as communities and households. It is also at this level that medium to long-term development and poverty reduction strategies and objectives are established, through national visions, national development plans and strategies. At the

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national level, several types of initiatives can be undertaken to enable the integration of adaptation into development processes. A “whole of government” approach needs to be adopted. This involves the engagement of key stakeholders, improving the coordination with existing mechanisms for disaster risk reduction and the implementation of relevant multilateral and regional environmental agreements. In addition, an important prerequisite for informed decision making on adaptation is that it should be based upon the best available information on the implications of both the current and the future climate in the country. To this end, the availability and quality of climate information needs to be improved.<sup>1</sup>

not to increase the fragmentation of aid. There is also the argument to be made that development assistance prior to the PD undermined and retarded the development of African institutions, those associated with public finance management in particular. Yet the climate finance modality du jour is the vertical fund in the form of global funds, which perpetuates this trend.

Climate finance is coming on fast and furious in African countries. In 2003, aid to address climate change in Africa was \$173 million, US\$63 million from DAC donors. In 2008, it was \$489 million to African countries by DAC, doubling the next year to US\$815 million.<sup>4</sup> But that is just in the form of Official Development Assistance (ODA). The proof is in the vertical funds pudding. The number of vertical funds operating in the environment sector is astounding, considering the lag time with which both civil society and developing country governments were struggling to grapple with the issue of climate change. As of December 2009, there were 22 funds with US\$18 billion in commitments.<sup>5</sup> One of the funds, the Global Environment Facility has disbursed US\$1 billion, just in the last four years.<sup>6</sup> Another, the Climate Investment Fund, despite having only disbursed US\$35 million to date, has pledges from DAC donors of US\$6 billion, all recorded as ODA.

This apparent schizophrenia<sup>7</sup> is unsettling. There is some tension between vertical funds and the PD/AAA agenda, as the overarching principle in the PD is that the sovereignty and supremacy of the state must be respected, and, in so doing, donors agreed to support and use partner country public finance and procurement systems, and these same donors agreed

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## 2 CLIMATE FINANCE ARCHITECTURE

### 2.1 Background

The Rio Declaration on Environment and Development (1992) sets the overall conceptual framework of environmental sustainability and how the threats posed from climate change will be dealt with. It states inter alia that:

- Human beings are at the centre of concerns for sustainable development. They are entitled to a healthy and productive life in harmony with nature.
- The right to development must be fulfilled so as to equitably meet developmental and environmental needs of present and future generations.
- States shall cooperate in a spirit of global partnership to conserve, protect and restore the health and integrity of the Earth's ecosystem.
- In view of the different contributions to global environmental degradation, states have common but differentiated responsibilities. The developed countries acknowledge the responsibility that they bear in the international pursuit to sustainable development in view of the pressures their societies place on the global environment and of the technologies and financial resources they command.

- Environmental issues are best handled with participation of all concerned citizens, at the relevant level.

This was followed by the United Nations Framework of the Convention on Climate Change<sup>8</sup>, originally ratified in 1994, and, to date, has 195 parties. Governments committed to sharing information, launching national strategies to address greenhouse gas emissions, and cooperate with each other in preparing for adaptation. The Conference of the Party (COP) is the supreme body of the convention, which meets once per year to review the progress of the convention.

The UNFCCC recognized the special situation of least developed countries (LDC); that is, though not emitters of greenhouse gas, they are most vulnerable to the effects of climate change such as extreme weather changes, agricultural productivity loss, and rising sea levels. The 7<sup>th</sup> COP resolved to establish guidelines for National Adaptation Programmes of Action (NAPAs), which LDCs could use to seek funding. The purpose of a NAPA is to identify the urgent and immediate needs of a country to adapt to the present threats from climate change. To date, 45 countries have prepared NAPAs and have made them available to the UNFCCC. Thirty (30) are African.

The Kyoto protocol, emerging from the 11<sup>th</sup> COP, is a legally-binding agreement to reduce greenhouse gas emissions, which entered into force in 2005. There were specific mechanisms established for reporting,

“Increased frequency of climatic disasters can force children out of school due to increased poverty, food shortage, remoteness and isolation, and child abandonment, which may affect the achievement of Goal 2 of the MDGs.”

the managing of information and ensuring compliance. There were also specific targets regarding the reduction of emissions.

African countries have been affected differently, depending on the region. The worst impacts of climate change have been in Sub-Saharan Africa. Here, 96% of the sub-continent’s population is directly dependent on rain-fed agriculture. Agricultural production is projected to fall 50% by 2050 due to a reduction in rainfall and increase in temperatures, while the majority of African states will be faced with water scarcity and water stress by 2050. The land suitable for agriculture will be reduced by 6% and the subcontinent’s total agricultural GDP will go down by 9% during the same period. Due to their direct dependence on natural resources sensitive to changes in climate, rural livelihoods will be the hardest hit by the impacts of climate change. Declining economic growth in the wake of global warming will result in reduced income for the rural poor, worsen poverty and directly undermine the achievement of the Millennium Development Goals.<sup>9</sup>

A study by the Center for Global Development has undertaken an econometric analysis in order to calculate the percentage risk faced by Africa with respect to the adverse impacts from climate change. For example, with respect to the probability that countries will experience extreme weather impacts in 2015, African countries are number eight of the top twenty. These include Djibouti, Kenya, Somalia, Mozambique, and Ethiopia. With respect to forecasts of percentage of agricultural productivity loss by region, Africa is the continent that will be most affected: Central Africa, 19.8%; Southern Africa, 18.9%; North Africa, 18%; Madagascar alone, 13.1%; Eastern Africa, 10.25.<sup>10</sup>

The Southern Africa Development Community (SADC) has also noted the potentially adverse impacts on the region and the attainment of the MDGs.

These can be illustrated by, amongst other things, reduction in soil moisture and water runoff to rivers caused by a warmer and drier climate, which may affect crop production, which is critical in ensuring food



N. Colombant - VOA

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security and poverty reduction (Goal 1 of MDGs). Loss of biological diversity, land degradation and desertification can also occur as a result of increased aridity, which could impact on environmental sustainability (Goal 7 of the MDGs). The realization of Goal 6 of the MDGs may be affected through the increase in water and vector-borne diseases as a result of long term rise in temperatures and occasional flooding. Increased frequency of climatic disasters can force children out of school due to increased poverty, food shortage, remoteness and isolation, and child abandonment, which may affect the achievement of Goal 2 of the MDGs.<sup>11</sup>

Therefore, adaptation measures in the water sector would entail, for example, measures to address both its supply and demand. They include the extraction of groundwater, desalination of sea water, expansion of rain water storage, removal of invasive non-native vegetation from riparian areas, reduction in water demand for irrigation, and the promotion of indigenous practices for sustainable water use.<sup>12</sup>

### 2.2 Climate finance mechanisms

As stated above, there is no shortage of climate adaptation financing instruments. The vast majority of funds are multilateral initiatives, among which include the Adaptation Fund, the Global Climate Change Alliance, the MDG Achievement Fund, the Pilot Programme on Climate Resilience (PPCR), the Special Climate Change Fund (SCCF), the Strategic Priority on Adaptation Fund, the Global Environment Trust Fund (GEF), the Least Developed Countries Fund (LDCF), and the Strategic Climate Fund.

The last four are administered by the Global Environment Facility, set up in 1991. UNFCCC stipulates that developed country Parties commit to providing financial assistance to developing countries to facilitate the implementation of the convention. To facilitate this transfer of funds, the Global Environmental Facility (GEF) serves as the operating entity of the financial mechanism under the UNFCCC.<sup>13</sup>

A team from the World Resources Institute undertook an assessment of the Global Environment Facility.<sup>14</sup>

In many ways the GEF was a watershed in institutional design. Its founding document, the GEF Instrument, provides for universality of participation of all Parties through its Participants Assembly, and an equitable, balanced representation of participants through a constituency system in the GEF Council, which divides seats roughly evenly between developed and developing country members. GEF decision-making in both the Assembly and the Council is by consensus.

The GEF engages civil society on policy issues through the GEF-NGO network of accredited NGOs, managed by local focal points. The meetings of the GEF Council themselves are open to civil society observers. The GEF strategy and programs are also informed by a Scientific and Technical Advisory Panel (STAP); notably, the STAP reviews proposals for GEF funding and offers recommendations on their suitability to the GEF Council.

However, the GEF is plagued by the lack of formalization between itself and the COP, putting into question issues regarding roles, responsibility and, ultimately, accountability. Another of the critiques of the GEF is the slowness with which it disburses funds, linked to what has been described as a 'cumbersome project cycle'.

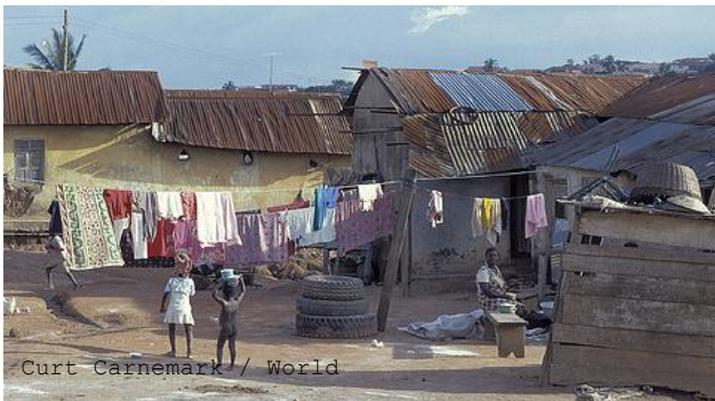
One study calculates that in 2005 the average time for projects to qualify for funding was between four and five years. Even after reforms were adopted in 2007 to expedite processing, the project cycle for full programs can take up to 22 months before approval.

A testament to this is the amount of disbursed funds from those approved. Between 2005 and 2009, this amounted to only US\$43.4 of US\$382.7 million.

The fourth independent evaluation of the GEF was completed in 2010. Among the findings include the fact that it is under-funded. The Small Grants Programme continues to be an effective tool for the

GEF in achieving global environmental benefits while addressing the livelihood needs of local populations, with special attention to reaching the poor. However its Monitoring, tracking tools, and impact indicators are not yet fully integrated into a results-based management framework for the GEF. Furthermore tensions in the GEF partnership arise from programming and project identification issues; these in turn mostly stem from the fundamental questions on the appropriate roles of the GEF partners.

The main administrator of funds outside the UNFCCC system is the World Bank, using the multilateral development banks as implementers. It currently administers two funds, the Climate Investment Fund, which can be further sub-divided into five funds and the Forest Carbon Partnership Facility. It also administers large trusts set up by Germany and Japan.



In 2010 the World Bank provided US\$6.5 billion of finance to the fossil fuel industry and increased its funding for coal fired power stations by over 350 per cent in just one year, reaching a total of US\$4.4 billion. With such a skewed governance structure, a history of failed projects and a key role in financing projects that have caused climate change, the World Bank is a completely inappropriate institution for managing and delivering international climate finance.<sup>15</sup>

The emerging centrality of the supply side of these global funds is appealing, as it will ensure coherence and facilitate accountability. But the emerging supplier is less appealing: the World Bank, with its record on funding projects which exacerbated

environmental damage and displacement of people and the lack of transparency around its operations.

A joint study<sup>14</sup> by the Jubilee Debt Campaign and the World Development Movement on one of the funds managed by the World Bank uncovered some disturbing findings. It found that half of the funds from the Pilot Programme on Climate Resilience (PPCR) are scheduled to be disbursed as loans, which, in essence, does make it eligible to be classified as ODA (which requires a grant element of at least 25%) and, as such, subject to the principles and targets of the PD/AAA. The study questions the governance model in use, classifying it as top-down in which the World Bank engages experts to identify eligible countries. It was also documented that there are some legitimacy concerns regarding consultation. In one instance, civil society organisations, which were listed as having been consulted, were unaware of the programme. There is also the ethical consideration of developing countries taking on loans for financing that is specifically for adaptation, as opposed to traditional development outcomes like education and health. The study gives an example of Niger, which currently has an annual debt service of US\$200 million and is scheduled to take on a loan of US\$72 million through the PPCR programme.

However, the most salient aspect of the study was the level of detail in tracking donations made by the UK to the PPCR fund; the implication being that broad generalisations concerning a distinction between climate finance and ODA are impossible. The study's findings underscore the fact that an international mechanism to coordinate and classify climate finance and aid is sorely needed.

## 2.2.1 The Green Climate Fund

The 15<sup>th</sup> COP resulted in the Copenhagen Accord, which was a pledge of funds of \$10 billion a year from 2010 to 2012, increasing to \$100 billion per year by 2020.<sup>16</sup> In order to formalise this finance goal, a collective agreement was made by developed countries 'to provide new and additional resources through international institutions, approaching US\$30 billion in fast start finance for the period 2010-2012'.<sup>17</sup> Thus, the most recent global fund to be created is

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the Green Climate Fund (GCF), established at the 16<sup>th</sup> COP in Cancun. Funding for adaptation will be prioritized for the most vulnerable developing countries, which includes LDCs, Small Island Developing States (SIDS) and countries in Africa. It is meant to be governed by the Green Climate Board of 24 with equal representation from North and South. The World Bank was named as the interim trustee for three years. The GCF is being designed by a transitional committee, headed by the former South African finance minister Trevor Manuel, which will submit a proposal at the 17<sup>th</sup> COP, to be held in Durban, South Africa in November-December 2011.

### 2.3 Climate Finance: Scope and Magnitude

It is difficult to separate aid which addresses mitigation and adaptation and traditional aid (ODA), as the OECD has issued reporting directives to its member countries, which make it virtually indistinguishable from ODA. However, as ODA is classified by destination, it allows for tracking by sector.

Aid to “general environmental protection” by DAC members was on average US\$2.1 billion over 2004-2007, which represented 3.1% of DAC members’ total bilateral sector allocable aid. In addition, aid activities classified outside the “general environment protection” sector but that targeted the environment as a policy objective amounted to US\$10.5 billion (US\$3.2 billion for activities that had environment as a “principal objective”; US\$7.3 billion for “significant objective”). In 2007, DAC members allocated approximately US\$3.5 billion for biodiversity-related aid, US\$4.3 billion for climate-change-related aid (mitigation) and US\$1.7 billion for desertification-related aid.

Between 2005 and 2007, the percentage of total bilateral ODA addressing bio-diversity, climate change mitigation, and desertification was, on average 7.1%<sup>18</sup>, with Germany and Japan ahead of the pack; US\$1.4 billion and US\$2.048 respectively. The average remained the same between 2008-09, with Japan increasing its aid to mitigation in particular to US\$3.5 billion and France and the EU featuring as emerging

large donors at US\$912 million and US\$743 million. Africa received approximately 20% of this form of ODA.<sup>19</sup>

Bilaterally, Japan and Germany have emerged as major donors. Since 2008, Japan has disbursed US\$4 billion and Germany US\$270 million. Norway, through a



multi-agency UN initiative called the UN Collaborative Programme on Reducing Emissions from Deforestation and Forest Degradation in Developing Countries (UN-REDD Programme), has disbursed \$83 million.

Through the multilateral global funds, the levels of financing are much higher. According to a report jointly commissioned by Eurodad and ActionAid<sup>20</sup>, the United Kingdom is the top donor to World Bank Group-administered trust funds, having contributed a total of almost US\$4 billion. It is followed by the United States with US\$3.47 billion, the European Community with US\$2.81 billion, the Netherlands with US\$2.7 billion, and Japan with US\$2.22 billion. The funds from SCCF and LDCF, managed by the Global

Environment Facility Trust Fund, are also considered as ODA. Since 2002, SCCF has disbursed US\$98 million, and the latter, US\$92 million.

Though it will be the most affected in regards to agricultural productivity loss by region and a number of individual states will suffer from extreme weather impacts, there appears to be a mis-alignment in the destination of climate finance in terms of recipients most in need. Of total adaptation finance available from both bilateral and multilateral climate funds, sub-

Saharan Africa has received only 5%, \$168 million. It



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## 3 EMERGING ISSUES

### 3.1 Additionality and Concessionalality

There is the perception among that adaptation projects will eat into current development projects, both in terms of policy space and resources. However, estimates of the costs of adaptation needs, at least with respect to Sub-Saharan Africa, dwarf current aid levels.

#### Comparison of current ODA and climate adaptation needs for sub-Saharan Africa<sup>21</sup>

| Sector                           | ODA, <b>USD million</b>                      | Average annual adaptation cost, <b>USD billion</b> |
|----------------------------------|--|--|
| Agriculture, forestry, fisheries | 2005: \$1227<br>2006: \$1341<br>2007: \$1688 | \$3.45   |
| Water                            | 2005: \$958<br>2006: \$1081<br>2007: 1378    | \$6.2  |
| Health                           | 2005: \$2069<br>2006: \$2388<br>2007: \$2737 | \$0.7  |
| Coastal zone protection          |  | \$4.2  |
| Infrastructure                   | 2005: \$2513<br>2006: \$2652<br>2007: \$3826 | 3.4  |
| Extreme weather events           |  | 1.18   |

That said, the scale of financing needed doesn't negate the 2005 Gleneagles commitment made by donors of 0.7% of their GNI to development assistance. Recent evidence reveals that donors have been counting pledges made to climate change as ODA. For example, it was revealed that the UK's contribution of \$2.5 billion pledged at the 15<sup>th</sup> COP in Copenhagen for short term climate finance was entirely from its already announced development aid budget, with half of its previously allocated and at least a third of the money in the form of repayable loans.

The desire to keep climate finance separate is tied to the belief that adaptation funding should be entirely grant funding and should not have a loan component at all, as per the Rio Declaration that developed countries bear the burden of responsibility for climate change. However, a EUROAD study<sup>22</sup> found that, *at most*, one-sixth of the financing from the Climate Investment Fund will be disbursed in the form of grants. The largest

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share will be in the form of concessional loans. The maturity for the majority of loans is 40 years, violating also the principle of intergenerational equity.

Part of the problem lies in the definition of ODA. It is defined as that which is provided by official agencies, state and local governments, and each transaction of which is administered with the promotion of the economic development and welfare of developing countries, and is concessional in character, conveying a grant element of at least 25%. This essentially removes climate finance from being examined through the aid effectiveness lens as the blending component will require private sector active participation.



### 3.2 Absorption capacity

One of the reasons most often given as to why development finance is increasingly coming in the form of vertical funds is because of the absorption constraints of poor countries. Yet the persistent by-passing of the budget and, by derivation, the state's institutions, contributes to absorption constraints.

Absorption in development finance jargon refers to the capability of receiving aid in a way that will not inhibit the production possibilities of the local economy nor disturb macroeconomic equilibrium.

Absorptive capacity has several dimensions<sup>23</sup>: macroeconomic, structural, and institutional.

The macroeconomic aspect of absorption refers to the

monetary and fiscal effects of how aid is used while the state is pursuing the goals of price stability, economic growth, and domestic investment. Adverse effects include inflation and exchange rate fluctuations. However, this aspect also includes the a priori conditions of donors regarding monetary and fiscal policy.

From a macroeconomic perspective, absorption can be detected by the widening of the balance of payments' current account deficit (an increase in imports), and its success depends on exchange rate policies and other policies that influence the demand for imports. If ODA is spent on imports (assuming there are no substitutes locally available), economic theory states that the current account deficit widens, but there is no change in relative prices within the sector targeted and certainly no economy-wide inflationary effects experienced. Additionally, there is the possibility of experiencing long-term productivity gains as a result of the imports (e.g. the purchase of ARVs resulting in longer working lives and thus increased tax revenues to the government).

Spending is considered the alternative to absorption, implying that governments have increased the domestic money supply by consuming locally. It is observed by the widening of the fiscal deficit.<sup>24</sup> Aid that is spent could have detrimental effects on the value of the recipient's currency. Since aid will be spent mainly by the public sector, there are certainly implications towards fiscal policy.

If the aid is spent on locally-procured goods and services, the initial effect is an increase in the money supply and then an increase in demand of the goods/services, followed by inflationary pressure. The assumption here is that the economy is operating at full capacity and the spending is on trade-able goods/services. Most African countries, however, at operating way below full capacity and have identified education, health and infrastructure as the main sector which will receive additional financing. Governments being the main providers of these services imply that concerns about stifling local competition are unwarranted. However, as these sectors are severely under-resourced, increased flows only result in bottlenecks, slowing absorption. Of course, if the increased consumption of goods/services has the longer-term effect of increasing supply capacity, allowing the main service provider to meet the

increased demand, then the price increases, if any, are only temporary.

The nature, composition, and destination of aid will determine its effects on the national economy, and the examination of the potential macroeconomic impacts of increased fiscal spending is a fruitful enquiry. However, absorptive capacity is not necessarily limited to financial flows: there is a structural dimension pertaining to the lack/scarcity of resources (e.g. shortage of human capital like teachers or health workers and infrastructure). It also includes the non-use of developing country systems by donors and the unpredictability of aid flows.

From a practitioner's perspective, absorptive capacity also entails the human capacity to coordinate, manage, monitor and evaluate the effectiveness of aid. The macroeconomic indicators aside, large amounts of aid can create bottlenecks, as it places pressure on scarce resources (e.g. road and transportation infrastructure, health workers, etc).

Well targeted aid can relieve these bottlenecks. If there are too few refrigerated warehouses for essential drugs, aid flows can help build new ones, at least to some extent. Strong monitoring and evaluation of aid flows, with specified benchmarks can help identify when resource constraints are making additional flows less effective, and how aid might help relieve some of those constraints.

1

In this context, aid that is directed towards the improvement of infrastructure services would constitute the sort of aid that could ease the absorption of additional funds. However, ODA to social infrastructure and services has far outpaced that to production infrastructure.

## Comparison of ODA sector flows to Africa, USD millions, DAC donors only

| Sector                             | 2003  | 2005  | 2008   | 2009   |
|------------------------------------|-------|-------|--------|--------|
| Social infrastructure and services | 5,297 | 7,120 | 12,422 | 13,206 |
| Production infrastructure          | 1,005 | 983   | 1,432  | 1,703  |
| --Transport                        | 251   | 503   | 836    | 1,084  |

Source: OECD Creditor Reporting System

Recent examinations of aid spending reveal that it has heavily swung towards social services rather than the reinforcement of productive capacities. Though social spending will increase productivity in the long-run, "the issue is about balance in the composition of investment, a balance which not being well achieved at present. The macroeconomic absorption problem is eased if aid-financed expenditures increase the output potential of the economy"<sup>25</sup>. After all, what is the point to building schools or hospitals if there are no roads for people to get there?

Current absorption constraints are as much outcomes of previous flows of aid, its modality, composition and destination, as they are hindrances to the improving the impact of aid. That is, the absorption constraints are endogenous to aid flows themselves. One of the characteristics that marked the pre-Paris period is the cumbersome administrative and reporting requirements of donors, including the number of projects and donor missions, the use of parallel implementation mechanisms, the non-use of partner procurement systems, the unpredictability of disbursement and the percentage of aid allocated off budget. The non-use of partner country systems can impact the capacity to absorb aid for the reason that if it isn't in the system, it simply can't be accounted for.

In light of the above mixed responsibilities borne by both donors and partner countries and the scale of funding that is being proposed to combat climate change, it is worth posing the question: what aspects of aid effectiveness was the Paris Declaration meant to improve?

Paris-Accra deals essentially only with process and not with the substance of

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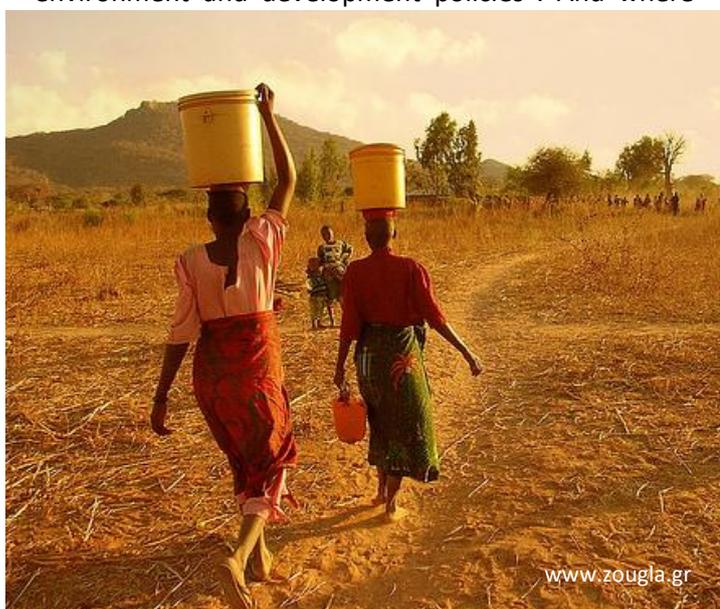
what needs to be done. They at times focus so heavily on the principle of alignment to country programmes that important issues, such as quality or severe risk of corruption, do not get the attention they deserve. They seem to forget that modalities, dialogue and allocations should be adapted to the needs of individual developing countries and that the objective is not better processes *per se* but better development outcomes.<sup>26</sup>

Paying lip service to reinforcement of the institutional capacity of developing countries and the Paris principles of ownership and alignment despite the proliferation of vertical funds is an illustration of the policy incoherence in the aid architecture.

### 3.3 National Adaptation Programmes of

#### Action

National Adaptation Programmes of Action (NAPA) are instruments of planning used by developing countries to seek finance to address climate change, mainly for adaptation. Heinrich Boll Stiftung (2011) undertook an enquiry into the NAPAs within SADC. Of the 30 African countries that have NAPAs, seven<sup>27</sup> belong to SADC. In the countries in which they do not exist, “adaptation tends to be addressed by a plethora of fragmented environment and development policies”. And where



they do exist, they tend “to be narrowly-focused, follow sectoral and project approaches to adaptation”. After review of national policy frameworks, the study also revealed that climate change is addressed mainly within the environment sector, though it threatens to destabilize existing development trajectories, and that the understanding of climate change and adaptation in particular is limited.

In 2008, the Collaborative African Budget Reform



Initiative and the African Development Bank commissioned a study on the quality of public finance management in 26 African countries.<sup>28</sup> The research reviewed a number of aspects (budget formulation, transparency, and execution), one of which was aid management. This section of the research was meant to gather information on how African governments organise themselves to deal with donor-funded programmes and projects, and incorporate them in their policy and budget processes. The study identified three fundamental issues affecting the management of ODA, from a partner country’s perspective:

The first one relates to the structure of government *institutions* that have responsibility for dealing with the donor community. The second one deals with the *policies* that governments put in place to actively manage and coordinate donor activities, while the third one is based on the *information* flows that allow the government to better capture aid flows at different stages of the

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budget process. More effective aid management systems help uphold key budgeting principles such as comprehensiveness, transparency and accountability.<sup>29</sup>

Though there was revealed a great degree of fragmentation with respect to the number of agencies involved in aid management, the research also concludes that countries are “reasonably well placed in terms of the necessary institutions and to a lesser degree as far as information flows are concerned. The main missing ingredient seems to be a clear policy statement that guides the overall relationship between the government and the donor community.” It would appear that African countries face the same challenge with respect to climate finance.

### 3.4 Access to Information and Transparency

The existing climate funds have already been accused of opacity in their administration. The Climate Investment Fund, for example, has US\$6 billion in pledges, all of which was recorded as ODA. As of March 2010, only US\$35 million had been disbursed. For one of the sub-funds, the objective is to integrate climate resilient aspects into development financing. There are only 3 African countries

currently tapping into this fund: Mozambique, Niger, and Zambia. Another track aiming to curb deforestation is only being implemented in Ghana, DRC and Burkina Faso. Yet another is meant to create new economic opportunities and increase energy access through the use of renewable energy and other low carbon technologies. Only Ethiopia, Kenya and Mali are receiving funding. Both the World Resources Institute and Eurodad studies have found that (as of Feb 2011), the financing agreements for the disbursed CIF funds have not been publicly disclosed. There is no information on disbursements, terms and concessionality, and per project information. In fact, the CIF does not disburse by project, but to the MDB, which then channels to projects.



## The Reality of Aid



Curt Carnemark / World

### 4 ENSURING EFFECTIVENESS OF CLIMATE FINANCE: RECOMMENDATIONS AND CONCLUSION

Given the emerging issues addressed above, the following are some recommendations towards the improvement of climate finance effectiveness:

- One of the challenges with ODA was that it was delivered at programme/project levels. The change in delivery of the bulk of aid to the general budget was meant to minimize the contestation for resources, support the public finance institutions, and improve the alignment of ODA to national plans. Because of the scale of financing being proposed for climate change adaptation, attention must be drawn to whether the appropriate participatory and accountability mechanisms are in place for this modality, especially with respect to the allocation of resources. The political economy of climate finance – as well as some potentially nefarious or at least ruthlessly self-serving local interests – will

impact on the process: the question of who gets what, when and how.<sup>30</sup>

- The sectoral fragmentation that currently exists between development practitioners and civil society erects barriers to learning and sharing. One of the areas in which the climate change/environment/aid community of practitioners needs to collaborate is the access to information movement. The principles that have been developed are useful in considering what is needed to enable poor people to participate in broader, national government-led planning processes and monitor the investments that have been made on their behalf. Some of the principles include the fact that information should be published proactively; it should be timely, accessible and comparable; everyone has the right to request and receive information; the right of access to information should be promoted.
- In designing the Green Climate Fund, it is worth reviewing the short-comings and challenges

experienced by the more successful global funds, like the Global Fund on HIV/Aids, TB, and Malaria and the GAVI. The UN Adaptation Fund has also been quicker at delivering money to projects and recipient governments. Despite receiving less than 10 per cent of the financial contributions the PPCR has received, the UN Adaptation Fund has already disbursed nearly US\$20 million, 50 times the amount the PPCR has given out in the same amount of time<sup>31</sup>.

- Citizens have the legislative branch as one limited means of participating in the evaluating policy and its associated financing. National implementing agencies (NIA) appear to be a promising feature and perhaps may be replicated. If so, these NIAs should have mandated public consultation mechanisms, open meetings, and report directly to national parliaments.

The benefits of participatory governance are innumerable. The efficacy factors of participatory governance stem from the possibility to profit from the knowledge and experience of all relevant stakeholders, which enables the design of rules better adapted to the environmental reality and therefore endowed with a higher degree of practicability. Furthermore, participation, which leads to the empowerment of the participants by facilitating dialogue (or at least offering the opportunity to make one's voice heard), may thereby prevent conflicts and enhance the legitimacy and, thence, the acceptance for the rules adopted, which in its turn paves the way for easier implementation of the rules by the governing stakeholders. Additionally, public participation contributes to raising the awareness in environmental issues among the different actors, not least among the general public, which may serve to

ensure a social consensus about the action that should be taken in the public interest.<sup>32</sup>

- Attention needs to be devoted to the composition of climate finance. The countries most at risk are the poorest (income-wise) and least-developed in the world. Loans to address a situation for which these countries have no culpability are unacceptable. Any gains made in successful climate adaptation would be comprised by unsustainable debt burdens of future generations.
- Climate finance need not be in the form of a unique modality, but all forms must be in alignment with national climate change strategies. For example, foundation-to-private sector financing for mitigation purposes can develop its own disbursement and evaluation mechanisms; however, it remains the responsibility of the parties to ensure that the project is in alignment with and serves the national interest, which could be one of the mandates of the NIAs.

The multi-dimensional nature of climate change, and the actions required to address it, requires a coordinated approach. It requires cross-sector coordination, insofar as national strategies reflect the most urgent needs of the country as well as those of traditionally marginalised groups. It requires international coordination, ensuring that the requisite resources are made available. It requires inclusive planning, underpinned by broad consultations. Participation includes both the right to be consulted and to participate in the decision making process. Finally, it requires a culture of information-sharing, with a view to ensuring transparency of process and accountability of outcome.

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## TABLE OF ACRONYMS

|        |   |
|--------|---|
| AAA    | Accra Agenda for Action                               |
| ARV    | Anti-retroviral                                       |
| COP    | Conference of the Party                               |
| CSO    | Civil Society Organisation                            |
| GCF    | Green Climate Fund                                    |
| GEF    | Global Environment Facility                           |
| GFATM  | Global Fund for AIDS, TB, and Malaria                 |
| HLF    | High level forum                                      |
| MDG    | Millennium Development Goal                           |
| NAPA   | National Adaptation Programmes of Action              |
| NGO    | Non-governmental Organization                         |
| ODA    | Official Development Assistance                       |
| OECD   | Organisation for Economic Cooperation and Development |
| PD     | Paris Declaration                                     |
| PPCR   | Pilot Programme on Climate Resilience                 |
| SADC   | Southern African Development Community                |
| UNFCCC | United Nation Framework Convention on Climate Change  |
| US\$   | United States Dollar                                  |

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