CIF CLIMATE INVESTMENT FUNDS

PRINCIPLES FOR TRANSFORMATIONAL CLIMATE FINANCE TO ADVANCE JUST AND EQUITABLE SOLUTIONS

// June 2023

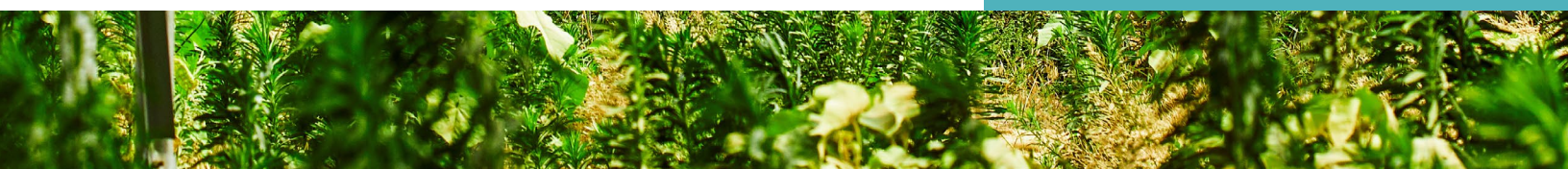
TRANSFORMATIONAL CHANGE LEARNING PARTNERSHIP//

Paper

CIF Programs: **All**

TOPICS

- Climate Finance
- Transformational Change
- Innovation
- Blended Finance



ACKNOWLEDGMENTS

www.climateinvestmentfunds.org

This paper captures insights from a number of Transformational Change Learning Partnership (TCLP) virtual and in-person events focused on Transformational Climate Finance. The writing team comprised Tim Larson, Nacibe Chemor, Janelle Roberts, Mike Ward, and Sarah Moin. The team drew on the insights from presenters (Shilpa Patel, Archi Rastogi, Christopher Head, Camilla Roman) and participants in the 12 May 2022 Webinar: How can Multi-stakeholder Finance Models Drive Rapid and Just Responses to the Climate Crisis. These insights were further developed through breakout group discussions during the in-person workshop hosted in Washington, DC by the TCLP from 4-6 October 2022. Special thanks to Sandra Guzman who helped facilitate the in-person events and shape the emerging text. A draft paper was widely circulated between December 2022 and May 2023, and benefitted from comments and suggestions by many TCLP participants, including a webinar discussion on 28 March 2023 around principles and their operationalization, exemplified by Gareth Phillips and Joan Prats. Special thanks to Gemma Norrington-Davies (and the team at Agulhas Applied Knowledge), Rob van den Berg, Aaron Werikhe, Danny Morris, Abhi Bhaskar, Paul Hartman, Neha Sharma, and Geir Hermansen for their insightful input. The revised draft of the paper was used to inform discussions during a hybrid event hosted by the TCLP on Transformational Climate Finance from 10-11 May 2023. Contributions by the presenters (Ethan Zindler, Mauro Soares, Dinara Akhmetova, Andy Norton, Lydia Muithya, Ahmed Ibrahim, Peter Odhengo, Victor Orindi, Liz Curmi, Leonardo Beltran) and all the participants both affirmed and refined the contents of the draft paper. These workshops were made possible through the support team including Dana Stefan, Angela Cruz, and Priscilla Shyam. Finally, the writing team would like to thank Marion Davis for an in-depth edit and insightful suggestions.

Photo Credits
All photos by CIF or under license to CIF unless otherwise noted.

Design
Art Direction: Andrea Carega
Graphic Design: Karlien Truyens

TABLE OF CONTENTS

ACKNOWLEDGMENTS 2

SUMMARY 4

1. **Introduction** 5
2. **What is transformational climate finance?** 6
   2.1. Normative goals for transformational climate finance 7
3. **Current barriers to transformational climate finance** 8
4. **Principles for transformational climate finance** 11
5. **Exploring the principles through the lens of the TCLP concepts** 13
6. **Developing pathways to achieve transformational climate finance** 15
   6.1. A Call to Action 17

ENDNOTES 18

SUMMARY

There is growing recognition that tackling the climate crisis and related social and environmental challenges will require fundamental changes in human systems. Since 2017, the Transformational Change Learning Partnership (TCLP) has advanced thinking and practice on transformational change in the context of climate change programs and projects. This paper focuses on the role of the climate finance community. Concerted efforts are needed to make climate finance a catalytic force in mobilizing large-scale investment in climate action, while also ending subsidies on fossil fuel use and other destructive activities and realigning global financial flows with a vision for inclusive, equitable, resilient, and sustainable development.

Building on the five dimensions of transformational change highlighted by prior TCLP work—relevance, systemic change, speed, scale, and adaptive sustainability—the paper identifies seven guiding principles for transformational climate finance: 1) focus on varied needs and contexts; 2) be actively inclusive; 3) unlock systems change; 4) provide de-risked, small, and decentralized solutions; 5) streamline processes; 6) work collaboratively to mobilize finance; and 7) create robust systems for monitoring, evaluation, and learning. The document also frames key pathways for action to advance transformational climate finance, setting the stage for expanded activities by TCLP and other partners.

GUIDING PRINCIPLES

- Focus on varied needs and contexts
- Be actively inclusive
- Unlock system change
- Provide de-risked, small and decentralized solutions
- Streamline processes
- Work collaboratively to mobilize finance
- Create robust systems for monitoring, evaluation and learning

1. INTRODUCTION

A growing array of science-based assessments of climate change, biodiversity loss, environmental degradation, and associated social impacts point to the need for profound and rapid changes in the fundamental economic, technological, social, and political systems that mediate the relationships between people and planet.[1] Last November at the Sharm el-Sheikh Climate Change Conference (COP27), countries reaffirmed the urgent need for transformational change across key systems and sectors if we are to fulfill Article 2 of the Paris Agreement and limit the global average temperature increase to 1.5° C.[2]

The COP27 outcome also reiterated the vital role of climate finance—investment levels of at least US$4–6 trillion per year—to support a global transformation to achieve net zero emissions by 2050 in ways that are socially just.[3] Scaled-up investment is also needed to enable societies to adapt quickly and build resilience to accelerating climate change impacts, and to address the losses and damages already being experienced by many countries.

There is a pressing need to apply transformational change thinking and practice to climate finance and global financial systems and investment flows.[4] Concerted efforts are needed to make climate finance a catalyst for mobilizing large-scale climate investments around the world, shifting public and private capital flows within countries and globally to advance climate solutions and deliver them to the people who need them most. Recent studies have found that 10- to 20-fold increases in annual financing are needed to successfully transition to low-carbon, climate-resilient economies.[5]

At the same time, it is crucial to halt the massive subsidies and financing flows that perpetuate the use of fossil fuels and other economic activities that harm natural systems. The recent *State of Finance for Nature* report found that public expenditure on environmentally harmful subsidies is three to seven times greater than public and private investment in nature-based solutions.[6]

More broadly, we must align climate finance and broader global financial systems and flows to simultaneously advance pathways supporting inclusive, equitable, resilient, and sustainable development that centers on the needs and well-being of all people, with particular attention to vulnerable populations, Indigenous communities, children, and women.

This is a major endeavor and requires a clear vision for enabling and managing transformational change within financial systems toward sustainable development pathways. This paper proposes seven guiding principles for transformational climate finance. It takes stock of ongoing discussions and provides a structure for more detailed exploration of challenges, barriers, and solutions.

The ideas and analysis presented here build on concepts developed by TCLP to support partners of the Climate Investment Funds (CIF) and other stakeholders. TCLP brings together a broad community of experts to advance thinking and practice on transformational change in the context of the global climate crisis.

Recognizing the urgent need for transformation in climate finance, TCLP has launched a workstream on transformational climate finance, in line with CIF's mandate and ambition for transformational change. This paper, which is informed by CIF and TCLP knowledge-building activities on climate finance, provides a foundation for collaboration and discussions on transformational climate finance with CIF's multilateral development bank and country partners and across the TCLP network. It is intended for the climate finance community, but materials will be developed in the future to foster engagement with other stakeholders.

2. WHAT IS TRANSFORMATIONAL CLIMATE FINANCE?

The term "climate finance" spans a broad range of financial flows—public and private, from the local to the global scale—to support actions to mitigate and/or adapt to climate change.[7] In order to be transformational, it must also align with TCLP's working definition of transformational change for climate action: "a fundamental change in systems relevant to climate action with large-scale positive impacts that shift and accelerate the trajectory of progress toward climate-neutral, inclusive, equitable, resilient, and sustainable development pathways."

Transformational climate finance must thus do more than support effective climate action: it must be **catalytic**, mobilizing much larger financial flows to match the scale of the climate crisis, and it must **break through entrenched systems** to shift financial flows away from harmful practices and toward climate-neutral, inclusive, equitable, resilient, and sustainable development pathways. The resulting investments will themselves be transformational if they **address the root causes** of climate change and the socio-economic structures that drive marginalization, inequality, and vulnerability.

Our resulting definition of transformational climate finance is:

An approach to financing climate action that prioritizes catalytic investments, promotes systemic changes in financial systems to align financial flows with the Paris Agreement, and delivers resources to climate investments that are climate-neutral, resilient, inclusive, equitable and sustainable.

2.1. Normative goals for transformational climate finance

Before we can promote transformational change, we must first have a clear objective: What are we changing toward? The definition above incorporates several normative goals; it is important to examine each in turn and ask:

- What would climate finance look like if we took these normative goals seriously?
- Do current or proposed investments support these normative goals?
- How do financial flows need to change to align with these goals and address the underlying causes of climate change, exclusion, inequality, vulnerability, and environmental harm?

Climate-neutral: The Paris Agreement aims to reduce greenhouse gas emissions to net zero by mid-century. Actions to achieve net zero must avoid other negative environmental impacts, and the effort must be shared with recognition of differences in needs, responsibility, and capacity both between countries and within countries.

Inclusive: Climate action—from planning, to implementation, to evaluation—must include all affected people. Less powerful populations are often harmed more severely by climate change impacts and responses, may have insight into more regenerative solutions, and play key roles in combatting climate change. Inclusiveness should enhance both justice (e.g., social justice, intergenerational justice) and efficiency (e.g., greater levels of support).

Equitable: Climate change and associated responses affect people differently, based on power dynamics and intersecting factors such as gender, race or ethnicity, caste, and socio-economic status. Some interventions can be "threat multipliers," worsening existing vulnerabilities and inequalities. Equity therefore requires differentiated interventions based on both need and justice (including restorative justice) to ensure that all countries, and all segments of society, can equally participate and benefit.

Resilient: Climate action must not only help ensure that people and natural systems can "bounce back" after a shock (e.g., a storm or flood), but also be proactive and anticipate risks. Recognizing that many situations are already untenable—and others may be after the next crisis—climate action must also help people "bounce forward" to create new pathways for change and regeneration.

Sustainable development pathways: It is crucial to align climate action with the Sustainable Development Goals (Agenda 2030), while also progressively moving toward more inclusive, equitable, and resilient human systems that thrive within healthy and productive ecosystems.

3. CURRENT BARRIERS TO TRANSFORMATIONAL CLIMATE FINANCE

Recent TCLP discussions and many studies have identified a wide array of challenges and barriers that inhibit the transformational potential of climate finance.[8] This section provides an overview, pointing to specific needs that we must address if we wish to realize that potential.

Limited mobilization of financial flows towards the goals of the Paris Agreement: Progress to channel financial resources towards the goals of the Paris Agreement remains slow.[9] Developed country efforts to jointly mobilize US$100 billion per year in climate finance by 2020 have fallen substantially short.[10] Many low- and middle-income countries' own capacity to invest in climate action is severely constrained by debt, including from development finance, which limits the availability of public sector resources.

Mechanisms to support the alignment of multilateral, public, and private sector investments with climate goals are in the early stages of development and implementation. For example, the past absence of established green taxonomies for climate action has been a barrier for identifying and aligning investment opportunities.[11] Public and private sector systems for disclosure and reporting on climate-related risks and opportunities are disjointed and complex and have a way to go to fundamentally shift global investment flows.[12]

Historically fragile enabling environments, including policy and regulatory frameworks: Aligning financial flows with climate goals will require substantial work to strengthen country-level and subnational enabling environments.[13] Centuries of exploitation and the legacy of colonialism in many developing nations have historically hindered efforts to establish strong political, social, and economic institutions. Powerful vested interests continue to benefit from extractive economic systems that often thrive in the context of limited institutional capacities and weak policy and regulatory frameworks and may actively promote instability.

This can create a negative feedback loop, where weak enabling environments in many developing countries have heightened perceived risks of investing and increased risk premiums for climate solutions, thus driving investment flows to developed countries.[14] Weak and misaligned policies and regulations, including financial regulations, legal frameworks, information transparency and disclosure instruments, and permitting requirements, make it difficult for climate-aligned projects to compete with conventional projects that benefit from the short-term bias of mainstream economic and financial decision-making.

Limited capacity at multiple levels to support transformational climate finance: Experts often observe that there is insufficient capacity within many institutions to effectively support needed transformations in financial structures and markets to support climate action.[15] Capacity challenges extend to financial sector actors and intermediaries and down into local jurisdictions and communities. Capacity challenges often include limited or changing personnel, insufficient skills, knowledge, or training, as well as the presence of weak institutional structures that inhibit people's ability to perform in environments that are safe, predictable, secure, and free from corruption.

Local stakeholders may be challenged with complicated requirements for accessing financing

mechanisms (if there are financing mechanisms that adequately respond to their needs), or to develop the financial skills needed to meet certain standards of financial management. In this light, perhaps the most significant overall "capacity challenge" is that we expect a diverse set of agents in developing countries to align themselves to standards and practices prescribed by donors and investors in developed countries. These actors in developed nations also need to enhance their capacity to be flexible, agile, and more attuned to local contexts.

Perceived risks that constrain investment in new pathways and actors: CIF program experience has demonstrated that there are many untapped opportunities to de-risk investments in climate solutions in ways that attract commercial and private finance.[16] However, risk management in climate-related projects often lacks adequate mechanisms to mitigate risk aversion from national and international donors, reinforcing the focus on "bankable" opportunities.

Perceptions of risk lead investors to favor larger projects—and, in the power sector, on-grid, not off-grid renewable energy projects or other decentralized solutions. The risk perceptions of powerful stakeholders also reinforce their technological preferences, stifling innovation and excluding smaller decentralized projects and developers that could be more transformative in the long term.[17]

Concerted efforts to mitigate perceived and actual risks related to financing climate solutions are imperative to unlocking much larger public and private investment. At the same time, expanded grant funding is needed to address needs that market-based financing will not take up and to strengthen capacities and track records that can attract broader investment over time. Risk and uncertainty also limit financial flows to resilience- and adaptation-focused programs. For example, the lack of adequate credit rating systems for adaptation and resilience interventions limits their ability to compete for financing, as illustrated by the large financing gap for adaptation-focused solutions relative to mitigation solutions.[18]

Insufficient attention to justice, equity, and gender in climate finance: COP27 affirmed global commitments to implementation pathways for just transitions that are attentive to sustainable economic development and poverty eradication.[19] However, attention to inequities in power, justice, equity, and gender in climate finance is emergent, is not a core driver of decisions, and lacks broadly held principles and practices to guide needed transformations at scale.[20]

The fact that developing countries with very limited historical responsibility for climate change are disproportionately suffering from its impacts is a powerful framing concept in climate justice discussions and underlying calls to rapidly scale climate finance flows to developing countries. However, climate finance for just, equitable, and gender-responsive solutions goes further, recognizing that more resources flowing through the current mechanisms will not fully achieve just and equitable low-carbon transitions.

In fact, injustices may be exacerbated by current climate finance investment flows at all levels—from the macro-level capital flows to different countries and sectors down to the micro-level ways in which ownership decisions are made. Existing power structures can constrain procedural justice and inclusion as well as equitable distributional outcomes, including by favoring certain financing mechanisms, business models, technologies, and projects.[21] A growing number of studies have elevated the importance of a gender lens and gender responsiveness in investments and financial policies for transformational climate action, both in terms of equity and increased impact.[22]

Governance trends and practices that concentrate decision-making power and limit inclusion: Governance structures for climate finance mechanisms at the global, country, and subnational levels often struggle to include many types of actors—particularly subnational and non-state actors—who could benefit from access to climate finance. This can give outsize influence to actors with power and resources.

As climate finance investments are deployed to leverage broader financial markets and flows, governance structures and decision-making processes often further weaken inclusion and influence of actors who can champion just and equitable climate action. For example, research indicates that the expansion of climate finance into market-mediated forms of blended finance, as well as debt-based financing, can shift and concentrate decision-making power with financial fund managers.[23] Innovative, decentralized, polycentric governance structures, which can more effectively reach actors who are directly implementing climate solutions, are nascent and need field-testing, particularly for adaptation and nature-based solutions. Recent discussions, such as those resulting in the 2022 Bridgetown Initiative for the reform of the global financial architecture, are also drawing attention to reforms that include governance dimensions at international financial institutions.[24]

Ongoing subsidies for fossil fuel assets: The financial sector continues to fund and is highly exposed to carbon-intensive assets in the energy and industrial sectors.[25] Direct fossil fuel subsidies amount to about US$340 billion per year, and when all costs and forgone revenues are considered, may reach US$5.9 trillion per year—completely eclipsing subsidies for renewable energy and other climate solutions.[26] Fossil fuel subsidies distort markets and price signals, making it more difficult for climate solutions to compete for public and private financing. This has created a path dependency, since many developing countries still rely on fossil fuels to generate revenues and subsidize their production, perpetuating the activity. This has allowed the planning of new fossil fuel assets that are likely to be stranded in the future, which will undermine the economic and political feasibility of low-carbon transitions over the coming decades.

Insufficient attention to mechanisms for financing transformational resilience, adaptation, and nature-based solutions: Climate finance and other investments to resilience, adaptation, and nature-based solutions substantially lag behind investments in low-carbon energy. For example, the United Nations Environment Programme (UNEP) estimates that international adaptation finance flows to developing countries are one-fifth to one-tenth of the estimated need, and the gap is widening. Estimated annual adaptation needs are US$160–340 billion by 2030 and $315–565 billion by 2050.[27] More interest and innovative mechanisms are needed to attract and channel investments to diverse projects across many landscapes. There is also a need for willingness to include other indicators beyond profitability to ensure the sustainability of adaptation and nature-based solutions projects.[28]

Limited transparency and accountability to support rapid learning and improvement: Monitoring, evaluation, verification, reporting, and disclosure mechanisms connected with climate finance and broader financial flows are often insufficient to support transparency, accountability, and learning. Information and transparency gaps can prevent investment from flowing to climate solutions outside of traditional, larger-scale projects. Opaque financial flows can also hinder visibility to investments that undermine low-carbon and resilient development transitions. Improvements are needed to enhance transparency and consistency in measurement; enhance consistency and coverage in reporting; and support both formal and informal (including both quantitative and qualitative) verification.[29] Finally, the urgency of transforming climate finance will require new and strengthened mechanisms to support rapid learning and diffusion of insights and compelling financing models which can support adaptive management and innovation.

The wider community working with climate finance will agree that these challenges are not new and there is still much to be done to tackle them. The following sections in this working paper explore how to address this need by proposing a set of principles to drive transformational change to climate finance, linking them to the dimensions of transformational change proposed in the TCLP framework, and using these principles and dimensions to chart new pathways to tap into the transformational potential of climate finance.

4. PRINCIPLES FOR TRANSFORMATIONAL CLIMATE FINANCE

With our normative goals in mind, we present seven guiding principles for transformational climate finance. As noted at the outset, the purpose of these principles is to support further thinking, discussions, and actions to advance transformational climate finance supported by CIF, its partners, and the broader climate finance community.

1 **Focus on varied needs and contexts:** Keeping the global temperature increase below 1.5°C, as envisioned by the Paris Agreement, will require reducing global greenhouse gas emissions by 43 percent by 2030.[30] However approaches must take cognizance of the historical emissions and wealth accumulation of developed countries, and the national and subnational development needs and contexts of low- and middle-income countries. Focus centers on addressing the root causes of climate change and vulnerability.

2 **Be actively inclusive:** Proactively engage with marginalized communities and vulnerable groups to incorporate their ideas, needs, and priorities in meaningful and sustained ways into the design and implementation of climate finance programs. Expand and shift finance to enable access by local communities, supporting radically different ownership models, promoting long-term support, promoting effective participatory approaches, addressing power dynamic imbalances, and strengthening governance and capacities. Programs should work to build and aggregate demand for climate solutions and assert power dynamics that emphasize local ownership and keep resources circulating in local communities in regenerative ways.

BOX 1. PRINCIPLES IN PRACTICE:

The Dedicated Grant Mechanism for Indigenous People and Local Communities (DGM) is a US$80 million CIF initiative that supports community-led, context-specific programs that draw on local expertise to advance sustainable forest management and elevates local voices in climate action.

The County Climate Change Funds in Kenya are a pioneering mechanism to facilitate climate finance to county governments while empowering local communities. It is a practical example of how climate finance can support climate-resilient development and effective participation as set out in the Paris Agreement.

The Adaptation Benefits Mechanism from the African Development Bank is an innovative mechanism for mobilizing new and additional public and private sector finance for enhanced climate change adaptation action. It has the potential to speed up transformation to low carbon resilient and sustainable development by giving value to resilience.

The International Guarantee Trust Fund for Renewable Energy (iTrust) is an innovative and customizable guarantee package solution to de-risk private investment in renewables in developing countries. The funds come from donors, multilateral development banks, and institutional and private investors, as well as the countries supported.

The Southeast Asia Clean Energy Facility (SEACEF) is an innovative blended finance facility that provides catalytic capital and development support to early-stage clean energy projects and businesses in a market-responsive manner across the region.

The IDB and The Nature Conservancy supported a debt conversion in Barbados, backed by a US$150 million guarantee, allowing the country to reduce borrowing costs and use savings to finance a long-term marine conservation program. The unique deal underscores the country's innovation in mainstreaming climate sustainability and biodiversity into its fiscal management agenda.

3 **Unlock systemic change:** Instead of making one-off investments, take a programmatic approach to strengthen the enabling environment for change and to overcome barriers. A programmatic approach also makes it more feasible for climate finance to catalyze and support action to tackle the root causes of environmental harm, inequality, and vulnerability, such as power inequities, entrenched poverty, and marginalization.

4 **Provide de-risked, small, and decentralized solutions:** Finance programs clarify and mitigate perceived and real risks associated with innovative climate solutions. Perceptions of risk and higher transaction costs associated with community-based initiatives need to be reconsidered in relation to the value created by responsive and inclusive climate action and how this addresses power inequities.

5 **Streamline processes:** Given the urgency of the climate crisis climate finance programs need to mobilize and shift mainstream investment flows faster and more efficiently towards relevant sectors and areas. This will require reducing access and implementation barriers, using innovative approaches that balance established financial practices with measures designed to address systemic injustices that inhibited access to climate finance.

6 **Work collaboratively to mobilize finance:** A key way to scale up climate finance flows and maximize their impact is to bring together public, multilateral, private, and philanthropic capital through innovative partnerships and other mechanisms for cooperation. Such approaches also benefit from the different partners' unique strengths and networks, while building power and influence for transforming finance for climate solutions.

7 **Create robust systems for monitoring, evaluation, and learning:** Transformational climate finance requires transparent, easy-to-use, and robust systems for monitoring, evaluation, reporting, and learning. These are essential both for accountability and to enable continuous improvement, drawing on new insights to identify ways to improve programs, close capacity gaps, and address the needs and concerns of stakeholders.

5. EXPLORING THE PRINCIPLES THROUGH THE LENS OF THE TCLP CONCEPTS

Mapping the transformational climate finance principles to the transformational change dimensions developed by TCLP can be helpful for understanding how the principles may relate to one another and how they can be mutually reinforcing to enhance their transformational potential.

Relevance

This dimension invites us to compare what is needed with what is planned to ensure that the two are aligned and we are on track to achieving our desired outcomes. In the case of transformational climate finance, principles focused on ***responsiveness to needs and context,*** and inclusiveness help to align financial systems with the Paris Agreement commitment to keep the global temperature increase below 1.5°C while responding to the social and economic needs of all people.

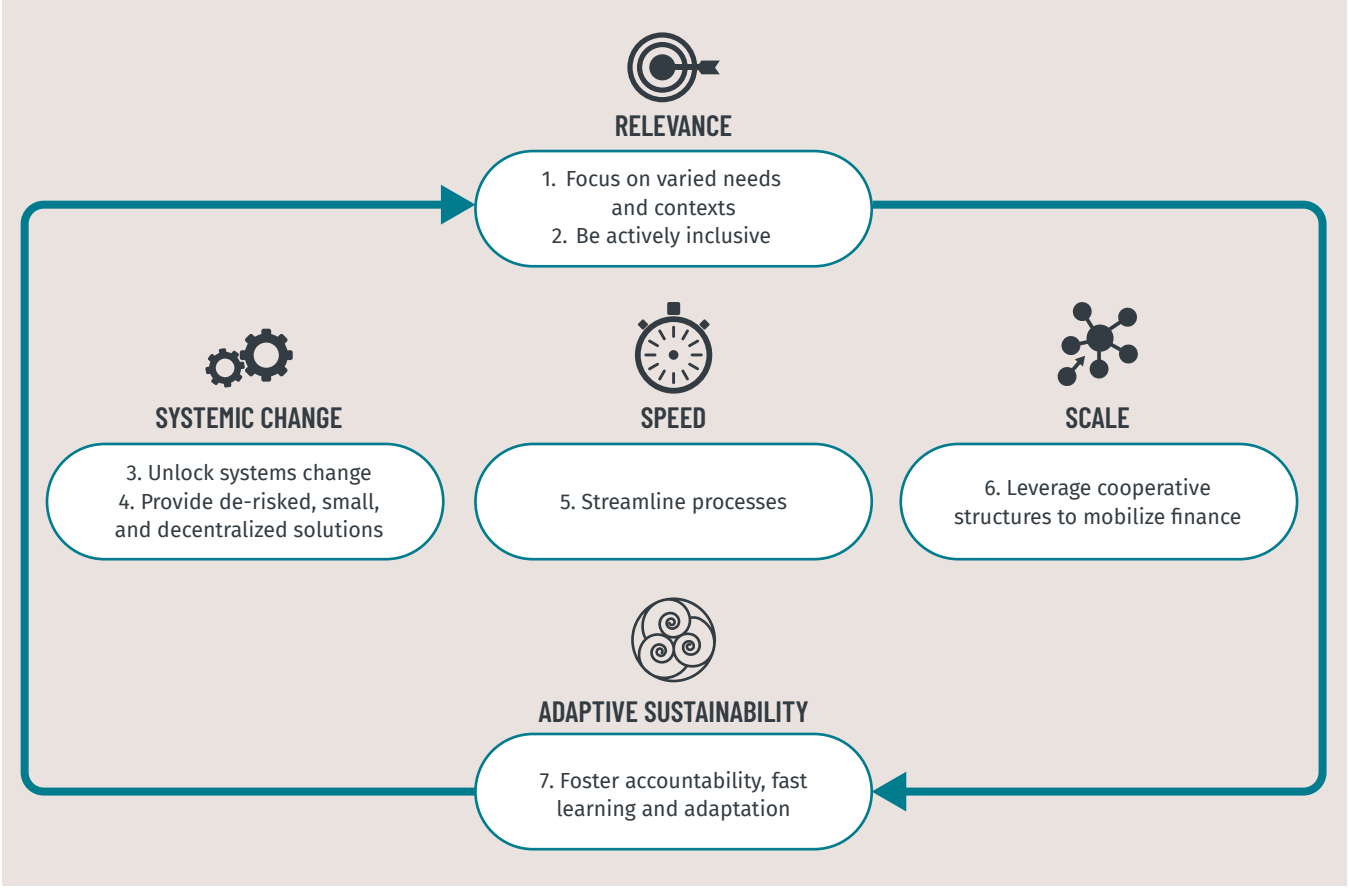
Systemic change

This dimension helps us to consider the fundamental change needed across interconnected environmental, social, and economic subsystems. It also highlights the need to consider whose interests are served by these systemic structures. A systems-change perspective—including ***de-risking smaller and decentralized solutions***—should contribute to climate-neutral, inclusive, equitable, resilient, and sustainable development pathways. This also requires new socioeconomic models, where value is given to sustainable industries, such as the protection of biodiversity and forests.

Speed

This dimension recognizes that, given the urgency of the climate crisis, time is of the essence in climate finance. If emissions must be at or near net zero by 2050, then investments in fossil fuels and harmful environmental practices must be rapidly curtailed and investments in clean, renewable, and sustainable solutions must be rapidly scaled. The costs and challenges of these transitions will grow substantially as climate impacts intensify, heightening the need for speed. To accelerate these transitions, it is crucial to ***streamline climate investment processes and mechanisms*** to deliver finance more quickly to where it is needed and support transition processes that are equitable and just.

FIGURE 1. Transformational Climate Finance Principles and the Five Dimensions of Transformational Change



Scale

This dimension calls for ensuring that the magnitude of action and impact of climate finance match the scale of the challenge. Shifting financial flows away from harmful activities, as noted above, is an urgent priority, as they remain far larger than investments in climate solutions. This requires that subnational, national, and international structures, policies, and actors (in terms of both numbers and orientation) need to be realigned to deliver progress relative to the Paris Agreement. Transformational climate finance requires a fundamental change in the core ***cooperative structure and operations of local, national, and international financial institutions and systems*** to reach sufficient scales of impact.

Adaptive sustainability

This dimension highlights the need for climate action—and finance—to continue to evolve and improve as we face climate change and learn from experience. ***Faster learning*** based on higher degrees of disclosure, ***transparency,*** and cross-sectoral engagement is required. Governments need to be explicit about how their financial policies and investment decisions achieve climate goals, while simultaneously requiring that financial actors report on progress in ways that are time-bound and in line with the trajectory of limiting climate change to 1.5°C. This will require building the capacity of the financial sector, business, civil society, government, and labor to allocate and track investment flows in ways that align with climate science, both in terms of impact and timelines, and drive ***accountability*** for progress.

6. DEVELOPING PATHWAYS TO ACHIEVE TRANSFORMATIONAL CLIMATE FINANCE

What will it take to operationalize the transformational climate finance principles outlined above? What will it take to break the inertia of the current system that is failing to deliver on commitments and to jump start new patterns of transformational finance and action? These questions are vital to guide the work ahead as the TCLP and its partners forge new pathways to achieve transformational climate finance. The opportunities outlined below will likely be important to this journey.

BRIGHT SPOTS: Find bright spots to rapidly learn from and scale. Recognize that compelling solutions, mechanisms, models, and practices exist already. For example, the Adaptation Benefits Mechanism (ABM) being pioneered by the African Development Bank and partners may offer a compelling model for connecting finance with local climate resilience and adaptation projects. Work to identify, characterize, assess, and learn from them, communicating how these models are working to advance transformational change. Engage champions from these bright spots to support learning, diffusion, and scaling opportunities.

CREATIVE INNOVATION: Foster innovation, creativity, and unconventional partnerships. Catalyze breakthrough ideas and approaches by encouraging innovation, new thinking, and partnerships that connect with new actors and in new ways. Creative innovation is needed on many levels, including the governance and processes of global and national financing institutions and cross-sectoral investment models that recognize and strengthen mutually beneficial outcomes. New approaches to financial intermediation for climate solutions and financing mechanisms that strengthen local ownership and move resources to vulnerable and underserved communities and households are also needed. Focus innovation efforts on areas of emergent need, such as financing for labor force transitions and addressing the social and economic implications of just transition initiatives and financing for resilience and adaptation solutions.

ACTIVE INCLUSION: Take bold steps to engage and include diverse stakeholders and to broaden and shift climate finance beneficiaries to include vulnerable and underserved groups. Focus on rapid expansion of inclusion in both procedural and distributional benefits of climate finance in a way that local communities and Indigenous peoples benefit directly and support change. Deeply internalize the phrase "nothing about us without us," and take bold steps to include relevant constituencies in planning, design, and selection processes relevant to climate finance. Be particularly attentive to creative approaches to involving local-level and community actors. Map and communicate on progress on inclusion in processes and distributional outcomes of climate finance and related investment programs to foster accountability and incentivize change.

ALIGNMENT: Ensure rapid alignment of financial flows with the Paris Agreement goals. Support and accelerate current efforts by climate and development finance institutions to work with stakeholders to clarify the amount of finance required and the potential sources of funding (including their respective roles). Develop a clearer line of sight between investments and climate change benefits and risks. Support recent COP27 commitments by governments and international financial institutions to align all investment programs with Paris Agreement goals through both technical assistance and accountability pressures. Consider alignment across a range of areas, such as policy (development and implementation, which enables vertical scaling); geographic expansion (linkages and expansion across developed and developing nations to support horizontal scaling of financing for solutions); and support for institutions and individuals (education on impact of investment decisions and opportunities for transformation to deeper understanding and support ("depth scaling"). Embed transformational change thinking into all climate finance, with an eye towards influencing broader financial flows.

ALLIANCES FOR SYSTEMS CHANGE: Build alliances and partnerships that approach financing for climate solutions with a systems change perspective. Encourage climate and development finance and investment actors to take more programmatic, holistic, integrated, and systemic approaches to interventions and investments. Encourage and incentivize financial actors to participate in coordinated alliances and partnerships with diverse actors to plan these programmatic approaches to investments. Work collaboratively to strengthen enabling environments that incentivize economy-wide climate-smart investments by enhancing predictability, efficiency, and access. Enhance the use of blended finance structures, where appropriate, that braid different types of capital in ways that leverage their unique attributes and risk tolerances. Build and strengthen mechanisms that allow donors and international financial institutions to collaborate in an organized and efficient manner, contributing towards systemic change that does not saddle low- and middle-income countries with unsustainable debt burdens.

PROCESS OPTIMIZATION: Streamline climate finance processes to move resources quickly and efficiently while being inclusive and sensitive to complexity and the need for just transitions. Develop processes and mechanisms that are sufficiently flexible to accommodate national and local capacities and that reinforce the development of stronger enabling environments over time. Remove obstacles to process streamlining and develop inclusive participation opportunities that are more strategic and influential than transactional. Explore innovative approaches to aggregate demand and projects to reduce transaction costs and attract affordable investment at scale.

LEARN AND ADAPT: Invest in monitoring, reporting, accountability, and learning as the foundation for ongoing adaptation and transformation towards increasingly sustainable development pathways. Connect and align monitoring and evaluation activities to support transparency, accountability, and learning within and across countries. Build nimbleness and adaptive capacity into climate finance programs and mechanisms to allow iterative cycles of improvement based on learning. Use evidence, data, and transparency to build political will for change and action.

6.1. A Call to Action

Adequate financing for climate solutions at all levels is vital to addressing the climate crisis and building robust and resilient sustainable development pathways. However, humanity is not currently on track to mobilize and shift the financial investment flows away from destructive, extractive practices towards generative climate solutions at the pace and scale needed. Incremental changes will not get us where we need to be.

Transformative climate finance is needed to disrupt existing patterns and practices and to jump-start new ways to finance climate solutions and align financial systems with sustainable development pathways. We need innovation, meaningful inclusion, and a focus on systems change in how we fund and what we fund to advance climate solutions.

This paper aims to generate discussion within the TCLP and beyond, and to catalyze broad and accelerated principles and practices to characterize and advance transformational climate finance. As we strive towards the ambitious goals set for climate finance in the Paris Agreement, as well as in the COP27 Sharm El-Sheik Implementation Plan, collaboration is key to create powerful and innovative pathways that align climate finance—and global financial systems—with the needs of people and planet.

We plan to continue building on this foundational piece by developing:

- **Examples and insights:** Continue to identify examples that illustrate the principles in practice and what would it take to operationalize them;
- **Recommendations:** Develop specific recommendations for CIF, its partners, and other climate funds;
- **Tools and resources:** Develop products, tools, and resources to both communicate bright spots, foster learning, and catalyze change among broader actors, such as philanthropy, governments, and the private sector;
- **Strategic convenings:** Bring together change makers within and adjacent to the climate finance community to explore solutions, advance thinking, and catalyze change.

ENDNOTES

CLICK ON ANY NOTE TO GO BACK TO THE REFERENCED PAGE

→ 1 For example, see: IPBES. 2019. *Global Assessment Report on Biodiversity and Ecosystem Services.* Edited by S. Díaz, J. Settele, E.S. Brondízio, H.T. Ngo, M. Guèze, J. Agard, A. Arneth, P. Balvanera, K.A. Brauman, and S.H.M. Butchart. Bonn: Secretariat of the Intergovernmental Science-Policy Platform on Biodiversity and Ecosystem Services. doi:10.5281/ZENODO.3553579.

Global Commission on the Geopolitics of Energy Transformation. 2019. *A New World: The Geopolitics of the Energy Transformation.* Abu Dhabi: International Renewable Energy Agency. https://www.irena.org/publications/2019/Jan/A-New-World-The-Geopolitics-of-the-Energy-Transformation.

→ 2 UNFCCC. 2022. "Second periodic review of the long-term global goal under the Convention and of overall progress towards achieving it." Section 13. Bonn: United Nations Framework Convention on Climate Change. https://unfccc.int/sites/default/files/resource/cop27_auv_CP%2013_PR2.pdf.

→ 3 UNFCCC. 2022. "Sharm el-Sheikh Implementation Plan." Section IX. Bonn: United Nations Framework Convention on Climate Change. https://unfccc.int/sites/default/files/resource/cop27_auv_2_cover%20decision.pdf.

→ 4 UNFCCC. 2022. "Second periodic review of the long-term global goal under the Convention and of overall progress towards achieving it."

→ 5 UNEP. 2022. "Emissions Gap Report 2022: The Closing Window – Climate Crisis Calls for Rapid Transformation of Societies." Nairobi: United Nations Environment Programme. https://www.unep.org/resources/emissions-gap-report-2022.

→ 6 UNEP. 2021. "State of Finance for Nature 2021: Tripling Investments in Nature-Based Solutions by 2030." Nairobi: United Nations Environment Programme. http://www.unep.org/resources/state-finance-nature.

→ 7 This is a simplified wording of the definition used by the United Nations Framework Convention on Climate Change (UNFCCC) Secretariat: "local, national or transnational financing—drawn from public, private and alternative sources of financing—that seeks to support mitigation and adaptation actions that will address climate change." See https://unfccc.int/topics/introduction-to-climate-finance.

→ 8 For an example of a study analyzing barriers to investment in climate solutions, see: Hafner, S., O. James, and A. Jones. 2019. "A Scoping Review of Barriers to Investment in Climate Change Solutions." *Sustainability* 11 (11): 3201. doi:10.3390/su11113201.

→ 9 Kreibiehl, S., T. Yong Jung, S. Battiston, P. E. Carvajal, C. Clapp, D. Dasgupta, N. Dube, R. Jachnik, K. Morita, N. Samargandi, M. Williams. 2022. "Investment and finance." In *Climate Change 2022: Mitigation of Climate Change. Contribution of Working Group III to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change* [P.R. Shukla, J. Skea, R. Slade, A. Al Khourdajie, R. van Diemen, D. McCollum, M. Pathak, S. Some, P. Vyas, R. Fradera, M. Belkacemi, A. Hasija, G. Lisboa, S. Luz, J. Malley, (eds.)]. Cambridge, UK, and New York: Cambridge University Press. doi: 10.1017/9781009157926.017.

→ 10 See UNFCCC. 2022. "UNFCCC Standing Committee on Finance: Report on progress towards achieving the goal of mobilizing jointly USD 100 billion per year to address the needs of developing countries in the context of meaningful mitigation actions and transparency on implementation." Bonn: United Nations Framework Convention on Climate Change. https://unfccc.int/sites/default/files/resource/J0156_UNFCCC%20100BN%202022%20Report_Book_v3.2.pdf.

→ 11 OECD. 2020. *Developing Sustainable Finance Definitions and Taxonomies.* Paris: Organisation for Economic Co-Operation and Development. https://www.oecd-ilibrary.org/sites/f903685d-en/index.html?itemId=/content/component/f903685d-en. (See Section 3, "Key issues for sustainable finance definitions and taxonomies").

Also see: Pettingale, H., S. de Maupeou, and P. Reilly. 2022. "EU Taxonomy and the Future of Reporting." *The Harvard Law School Forum on Corporate Governance* (blog), April 4. https://corpgov.law.harvard.edu/2022/04/04/eu-taxonomy-and-the-future-of-reporting/.

→ 12 For information on the state of public and private Paris-aligned investment flows, see Kreibiehl et al., 2022. "Investment and finance." Promising initiatives to advance disclosure and reporting related to climate risks and sustainability impacts include the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) and the Task Force for Climate-Related Disclosures (TFCD). In 2022, the International Sustainability Standards Board (ISSB) launched an effort to help evolve the currently fragmented environmental, social, and governance (ESG) disclosure landscape, which currently lacks connectivity and has conflicting concepts, to a truly global common language of sustainability-related financial disclosures (see https://www.ifrs.org/news-and-events/news/2022/12/issb-describes-the-concept-of-sustainability/). In addition, recent EU decisions to pursue mandatory corporate sustainability reporting over the next several years signals evolution in the field.

→ 13 Kreibiehl, S. et al., 2022. "Investment and finance."

Also see CIF and KPMG. 2022. *Enablers: The Role of Enabling Environment in Scaling Up Climate Finance.* Washington, DC: Climate Investment Funds. https://www.cif.org/news/enablers-role-enabling-environment-scaling-climate-finance.

→ 14 See UNEP, 2022. "Emissions Gap Report 2022," p. 67.

→ 15 For example, research by CIF and KPMG finds the importance of capacity building of national and subnational agencies to manage climate investment mechanisms. See CIF and KPMG, 2022. *Enablers: The Role of Enabling Environment in Scaling Up Climate Finance.*

→ 16 For example, see BNEF and CIF, 2021. *Multiplying the Transition: Market-based solutions for catalyzing clean energy investments in emerging economies.* Washington, DC: Bloomberg New Energy Finance and Climate Investment Funds. https://www.cif.org/sites/cif_enc/files/knowledge-documents/cif_bnef_multiplying_the_transition.pdf.

→ 17 Anantharajah, K. and A.B. Setyowati. 2022. "Beyond Promises: Realities of Climate Finance Justice and Energy Transitions in Asia and the Pacific." Energy Research & Social Science 89 (July): 102550. doi:10.1016/j.erss.2022.102550.

→ 18 UNEP. 2022. "Adaptation Gap Report 2022: Too Little, Too Slow – Climate Adaptation Failure Puts World at Risk." Nairobi: United Nations Environment Programme. https://www.unep.org/resources/adaptation-gap-report-2022.

→ 19 UNFCCC, 2022. "Sharm el-Sheikh Implementation Plan," Section VIII.

→ 20 Many recent initiatives and studies have focused on the growing attention to the nexus of climate finance and equity, justice, and gender issues. For example, see the Just Transition Initiative and related research and concepts developed by the Center for Strategic and International Studies (CSIS) and CIF at https://justtransitioninitiative.org/about-just-transitions/. Also see: "Climate Finance Justice: International Perspectives on Climate Policy, Social Justice, and Capital." 2020. *Climatic Change* 161 (2): 243–49. doi:10.1007/s10584-020-02790-7.

→ 21 Anantharajah and Setyowati, 2022. "Beyond promises: Realities of climate finance justice and energy transitions in Asia and the Pacific."

→ 22 For example, see: Bosone, C., S.M. Bogliardi, and P. Giudici. 2022. "Are ESG Female? The Hidden Benefits of Female Presence on Sustainable Finance." *Review of Economic Analysis* 14 (2): 253–74. https://openjournals.uwaterloo.ca/index.php/rofea/article/view/5005.

Clancy, J., G. Özerol, N. Mohlakoana, M. Feenstra, and L. Sol Cueva, eds. 2020. Engendering the Energy Transition. Cham: Springer International Publishing. doi:10.1007/978-3-030-43513-4.

→ 23 Bracking, S. and B. Leffel. 2021. "Climate Finance Governance: Fit for Purpose?" *WIREs Climate Change* 12 (4). doi:10.1002/wcc.709.

→ 24 See the Bridgeton Initiative recommendations at https://gisbarbados.gov.bb/download/the-2022-barbados-agenda/. Also see news coverage of efforts to reform international finance institutions: Gelles, D. and M. Bearak. 2022. "Poor Countries Need Climate Funding. These Plans Could Unlock Trillions." *The New York Times,* November 9, sec. Climate. https://www.nytimes.com/2022/11/09/climate/imf-world-bank-climate-cop27.html.

→ 25 UNEP, 2022. "Emissions Gap Report 2022," p. 67.

→ 26 While explicit fossil fuel-related subsidies amount to about US$340 billion annually, a recent International Monetary Fund analysis estimated that implicit fossil fuel subsidies (undercharged environmental costs, including climate change, and forgone consumption taxes) amount around US$5.9 trillion per year globally. See Vernon, N., S. Black, and I. Parry. 2021. "Still Not Getting Energy Prices Right: A Global and Country Update of Fossil Fuel Subsidies." IMF Working Paper WP/20/236. Washington, DC: International Monetary Fund. https://doi.org/10.5089/9781513595405.001.

→ 27 UNEP, 2022. "Adaptation Gap Report 2022.

→ 28 Muller S. and Robins N. (2022). "Just Nature: How finance can support a just transition at the interface of action on climate and biodiversity." London: Grantham Research Institute on Climate Change and the Environment and Centre for Climate Change Economics and Policy, London School of Economics and Political Science. https://www.lse.ac.uk/granthaminstitute/publication/just-nature-finance-just-transition-climate-and-biodiversity-2022/.

→ 29 Atteridge, A. 2012. "Monitoring, Reporting and Verifying Climate Finance: A Framework for Transparency of Support Provided to Developing Countries." SEI Policy Brief. Stockholm: Stockholm Environment Institute. https://www.sei.org/publications/monitoring-reporting-and-verifying-climate-finance-a-framework-for-transparency-of-support-provided-to-developing-countries/.

→ 30 Scientific estimates from the IPCC released in 2022 use 2019 as a baseline, indicating that GHG emissions need to be cut 43% by 2030. See https://unfccc.int/news/climate-plans-remain-insufficient-more-ambitious-action-needed-now.

THE CLIMATE INVESTMENT FUNDS

The Climate Investment Funds (CIF) is one of the largest multilateral climate funds in the world. It was established in 2008 to mobilize finance for low-carbon, climate-resilient development at scale in developing countries. 15 contributor countries have pledged over US$11 billion to the funds. To date CIF committed capital has mobilized more than $64 billion in additional financing, particularly from the private sector, over 70 countries. CIF's large-scale, low-cost, long-term financing lowers the risk and cost of climate financing. It tests new business models, builds track records in unproven markets, and boosts investor confidence to unlock additional sources of finance. Recognizing the urgency of CIF's mission, the G7 confirmed its commitment to provide up to $2 billion in additional resources for CIF in 2021.

CIF CLIMATE INVESTMENT FUNDS

The Climate Investment Funds
c/o The World Bank Group
1818 H Street NW, Washington, D.C. 20433 USA

Telephone: +1 (202) 458-1801
Internet: www.cif.org

@CIF_action
CIFaction
CIFaction
CIFaction
CIFaction
@CIF_action