Briefing Paper

Climate Finance for a Just Transition: A Forum on Blended Finance and Catalytic Strategies

***Chemonics UK** and the **Impact Investing Institute** convened a diverse audience of investors, policymakers, researchers, and practitioners at their hybrid event, Climate Finance for a Just Transition: A Forum on Blended Finance and Catalytic Strategies, on 27 June 2023. The event featured a panel discussion on the challenges and opportunities for blended finance in the context of the global movement for a just transition. The panel was chaired by **Louise Quy**, Managing Director, Chemonics UK and speakers included **Gergo Mathe**, Climate Co-Finance Associate at the European Bank for Reconstruction and Development (EBRD); **Maria Teresa Zappia**, Chief Impact and Blended Finance Officer and Deputy CEO at BlueOrchard Finance, Head of Sustainability and Impact at Schroders Capital, and Global Head of Impact at Schroders; **Bella Landymore**, Policy and Strategy Director at the Impact Investing Institute; **Tracey Austin**, Sector Director, Financial and Professional Services at the UK Department for Business and Trade; **Tara Sabre Collier**, Director of Impacting Investing and Sustainable Finance at Chemonics UK, and Visiting Fellow at Said Business School, University of Oxford; and **Ben Cotton**, Head of Capital Markets at Matrix Global.*

While still falling short of the $3.5 trillion annual investment needed[1] to reach a net-zero future, global climate finance is accelerating and has more than doubled over the past decade. Yet ensuring this capital flows to the most vulnerable often requires intentionality. Currently, the majority of large-scale climate finance and impact capital focuses on developed markets, and even the share targeting lower- and middle-income countries tends to concentrate upon the emerging middle class. This imbalance is further compounded by the additional costs or risks, perceived or actual, in reaching historically disadvantaged groups or regions when unproven business models or markets are involved. Blended finance is thus a vital solution for unlocking climate finance in ways that ensure a just transition.

More information on the EBRD's Just Transition Initiative: The EBRD's Just Transition Initiative

More information on this topic: Blended Finance: Bridging the Sustainable Development Finance Gap

Key Takeaways

1 Just transition finance brings challenges and opportunities, which can build upon similar movements

Globally and nationally, more economically vulnerable communities and countries are often most at risk from the humanitarian and socio-economic burdens of climate change, despite often having made lesser historical contributions to emissions. This discrepancy can be observed across several intersectional lenses: geographic, urban-rural, gender, racial, socio-economic, among others.

Because women comprise 50% of the population globally, the evidence and progress of the gender lens investment makes it a useful entry point for examining just transition challenges and opportunities.

Challenges: In both advanced and developing economies, women are under-represented relative to men in almost every aspect of financial markets, particularly in terms of leadership and ownership. From asset ownership to venture capital, to commercial banking to small to medium sized enterprise finance portfolios themselves, women are disproportionately low both in access to, and management of, financial assets. This under-representation is also visible within climate finance. Ensuring that women are equally represented in every aspect of climate finance is challenging because it can implicate upending long-established frameworks and practices. For example, equalising access to climate finance for micro and small businesses to become more carbon neutral in lower-income countries would demand recognising that women in these markets often have less collateral than men, which affects credit scoring. Likewise, attempting to ensure women-led funds reach parity in climate finance would involve a re-think of established due diligence practices and track record preferences by their limited partners (LPs).

Opportunities: Gender lens investing has accelerated from under $200 million in 2010 to over $20 billion as of 2021. The world's largest development financial institutions (DFIs) committed to gender lens investing in 2018, giving birth to the 2X Challenge, launched at the G7 Summit 2018 as a pledge to collectively mobilise $3 billion in private sector investments in developing country markets over three years. This commitment from donors also creates opportunities for emerging and frontier market climate funds which integrate a gender-smart approach. At the same time, women represent a critical customer base for many climate finance and climate-smart agriculture solutions to be commercially viable and meet climate targets.

Realising the potential of gender lens investing often requires blended finance and, particularly, catalytic capital. Key examples range from warehousing facilities to support women fund managers, to grant funding to increase women-led ventures in access to energy, to donor-funded research to unpack how gender-smart business model design can improve commercial performance.

More information on the gender-climate nexus: 2X Global Gender and Climate Finance Toolkit

More information on women consumers and electrifications: Powering Households and Empowering Women: The Gendered Effects of Electrification in sub-Saharan Africa

More information on how LP investment frameworks can become more inclusive: Due Diligence 2.0 Commitment

2 Blended finance and insurance solutions exist and need scaling

Public and development financial institutions continue to take the lead in catalysing private capital through de-risking investments with seed capital, grants, concessional loans, and technical assistance. DFIs are in a strong position to integrate the additionality requirements in projects while working with governments at all levels on enacting appropriate policies, reforms, and strategic investments. Case studies cited at this event include EBRD's investments in the decarbonisation strategy for Wałbrzych, a Polish city.[2] The investment extends to mobilising technical assistance to develop a just transition action plan for the city, supporting the city with investments in energy efficiency, and helping to improve infrastructure.

Government-funded development projects like the USAID Climate Finance for Development Accelerator (CFDA)[3] help address the financing gap with catalytic capital intended to mobilise private capital for the sustainable development goals (SDGs). At the same time, government-backed investment need not always be concessionary to be catalytic. For example, the Foreign, Commonwealth & Development Office's (FCDO) MOBILIST programme provides equity in order to usher more SDG-aligned products into public markets, where private institutional capital can also be unlocked at a greater scale.

A pioneering example of blended finance with economic inclusion at the core is the Orange Bond,[4] considered the world's first asset class built as a solution to financing gender equality. The fund is supported by a 50% credit guarantee on the underlying loan portfolio by the U.S. International Development Finance Corporation and the Swedish International Development Cooperation Agency.

This Orange Bond case study is unique in showing a new approach to scaling gender finance (through public markets) but also highlights the important role of guarantees in blended capital structures. In fact, guarantees have been found to be one of the most important blended finance tools for climate action and the broader Global Goals, mobilising up to 5x more capital than other DFI instruments.

Just as guarantees are relatively under-utilised relative to their potential for achieving a just transition, the broader set of insurance products needs to evolve as a critical yet under-exploited instrument for both adaptation and mitigation.

The BlueOrchard InsuResilience Investment Fund (IIF)[5] is structured in an attractive way for private investors while still reaching underserved and vulnerable populations across emerging and frontier markets through a first loss tranche from KfW, on behalf of the German Federal Ministry for Economic Cooperation and Development (BMZ). The IIF is an umbrella fund structure combining a private debt Sub-fund (IIF Debt Sub-fund) and a private equity Sub-fund (IIF Equity Sub-fund).

The fund has a strong just transition focus as it seeks to build out an insurance ecosystem that protects vulnerable people and microentrepreneurs in emerging and frontier markets from the effects of climate change. The strategy is implemented through the provision of growth capital (equity) and debt investments with a focus on seeding and scaling local insurance providers.

The fund pays attention to reflecting the needs of end beneficiaries in its investments. To ensure that this is embedded in its strategy, a dedicated Grant Facility, which provides grant funding for Technical Assistance and

Premium Support projects (separately funded by BMZ), is made available to the Fund investees. One example is represented by the education workshops organised for (prospect) investees to improve the understanding of climate insurance and enabling communication between key stakeholders. This in turn helps accelerating investments and scaling up climate insurance.

Repository of blended finance data and deals: Convergence – Blending Global Finance

More information on scaling up blended finance in developing countries: OECD – Scaling Up Blended Finance in Developing Countries

More case studies on DFI-backed blending of concessional finance: DFI Working Group on Blended Concessional Finance for Private Sector Projects

More information on insurance products as SDG catalysts: A2ii – Insurance and the Sustainable Development Goals

3 Both global and local institutional investors have appetite, and both have an important role to play in driving a just transition

Institutional investors circulate over $100 trillion through private and public markets, more than enough to address the SDG finance gap, contingent on finding appropriate mechanisms that fit an array of risk-return profiles. While it is true that most large institutional investors prioritise commercial return, there is a proven and growing wave who are embracing the convergence of financial, social, and environmental performance. The Just Transition Finance Challenge, led by the Impact Investing Institute, is emblematic of this trend. The Challenge brings together global financial institutions with over £4 trillion of assets, or assets under management, who are committed to financing a just transition in the UK, other develop and emerging markets. Participants, which include the likes of HSBC, ResponsAbility, Fidelity, and Schroders, push forward investment products which advance the following three principles:

- Advancing climate and environmental action – for example, through greenhouse gas emission mitigation, reduction, and removal.
- Improving socio-economic distribution and equity – for example, through inclusive opportunities for decent jobs or local regeneration.
- Increasing community voices – through, for example, social dialogue and with affected communities that are often excluded and marginalised.

While the Challenge has already been embraced by some of the largest international investors from higher-income countries, it is essential that such approaches also embody partnership with local institutional investors in lower-income countries.

Not only are local institutional investors protected from currency risks, they bring market knowledge, expertise navigating regulatory and contextual hurdles, and the ability to deploy their expertise to manage risk and extract better returns. While partnerships between international and local institutional investors are still growing in number and scale, donors, such as USAID, have already begun to bring catalytic capital to harness this potential towards the Global Goals.

The Impact Investing Institute will also release, in Q4 2023, a guide to support catalytic capital providers in advancing a just transition, including by supporting the development of just transition-aligned blended finance vehicles, and by partnering with investors and other ecosystem players in the lower-income countries.

More information on Impact Investing Institute – Just Transition Finance Challenge: Impact Investing Institute – Just Transition Finance. See also the Just Transition Criteria developed by the participants in the Challenge, which provide a practical tool to help investors integrate just transition considerations into their products, solutions and portfolios.

Event recording – Climate Finance for a Just Transition: A Forum on Blended Finance and Catalytic Strategies: Chemonics UK – Climate Finance for a Just Transition: A Forum on Blended Finance and Catalytic Strategies

Endnotes

[1] Financing the Transition: How to Make the Money Flow for a Net-Zero Economy. Energy Transition Commission, 2023, https://www.energy-transitions.org/publications/financing-the-transition-etc/

[2] https://www.ebrd.com/what-we-do/just-transition-projects-financed

[3] https://chemonics.com/projects/mobilizing-finance-to-respond-and-adapt-to-climate-change/

[4] https://iixglobal.com/orange-bond-initiative-sign-up/

[5] https://www.insuresilienceinvestment.fund/

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Published in October 2023 by Chemonics International.