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POLICY **BRIEF**

The Climate Finance Landscape: Barriers and Opportunities to Uganda's access and utilization of climate finance

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Photo Credit: Author

Photo taken in Kilembe Sub County, Kasese District.

1.0 Introduction

Uganda, like other developing countries, is one of the lowest emitting countries accounting for less than 0.1% of the global emissions (UNDP, 2020) yet very susceptible to the impacts of climate change. People and ecosystems countrywide are already feeling the impacts of these changes, as warming has contributed to more frequent and extreme weather events such as floods and droughts, pests, and diseases, among other calamities. Climate change damage estimates in the agriculture, water, infrastructure, and energy sectors in Uganda could collectively amount to US$273–437 billion (2.8–4.5% of cumulative prospected GDP) between 2010 and 2050 (MWE, 2015). These are exacerbated by the dwindling natural resources such as forests and wetlands that have declined from 24% in 1990 to 13.3% currently and 15.6% in 1994 to 8.9% in 2021 (MWE, 2022) respectively (Figures 1&2).

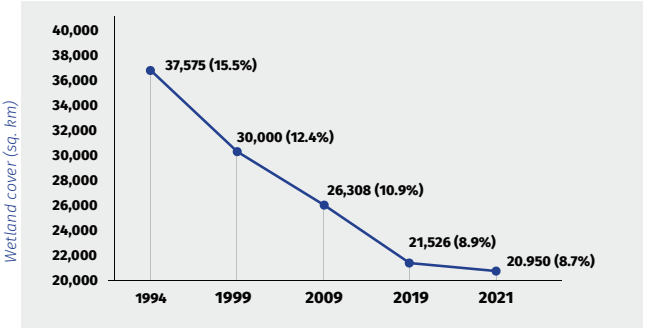
Combating climate change impacts comes at extraordinary costs because of the scale, urgency, and complexity of the climate crisis.

The Climate Policy Initiative (2022) estimates that at least $4.3 trillion is required annually by 2030 to meet the Paris Agreement targets at a global level. According to the recently updated NDC, Uganda will need to invest approximately USD 28.1 billion by 2030 to meet the ambitious economy-wide mitigation target of 24.7% emissions reduction.This is a warning that the impacts can be economically significant, especially for the poor and marginalized that heavily depend on natural resources for their livelihoods (Bakika et al., 2020). Uganda's priority is to reduce the vulnerability of its population, environment, and economy by implementing climate adaptation and mitigation actions. This requires a massive scale up in resource mobilization and investments in climate resilient and low carbon development pathways.

This brief provides a snapshot of the climate financing landscape in Uganda examined through a comprehensive literature review, and generation and analysis of secondary data. Using a mixed methods approach of qualitative and quantitative analysis, the review focused on the state of climate financing in Uganda, barriers, and opportunities in accessing and utilizing climate finance.

Figure 1: Trends in forest cover.

Figure 2: Trends of wetland loss.



Source: MWE Annual Performance Report (2022) & MFPED BMAU Briefing Paper (2022).

2.0 Uganda's Climate Finance Landscape

Adaptation is the priority climate action response for Uganda and the implementation cost of the adaptation actions in the National Climate Change Policy was estimated at US$ 194.5 million annually over the next 15 years (EMLI & CARE, 2020).

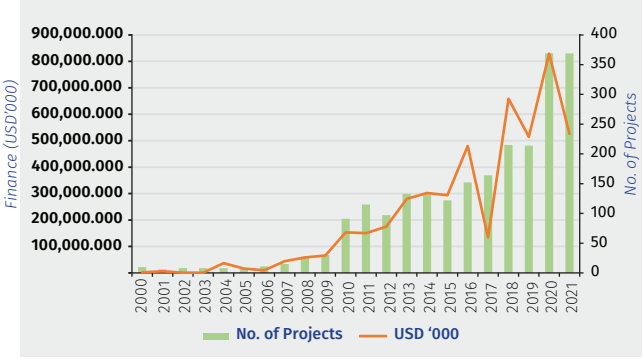
Due to data limitations, public (domestic) climate finance has not been fully quantified to date. However, in the National Budget Framework Paper for 2023/2024, the votes mapped under the Natural Resources, Environment, Climate Change, Land and Water Management Programme have been allocated a total budget of UGX 547 billion, of which 269 billion is domestic funding and UGX 279 billion is external financing. The current funding levels are still significantly below the estimated annual targets.

In the climate finance tracking database maintained by the Organisation for Economic Co-operation and Development (OECD, 2023), a total of 2,303 climate-related projects were committed to Uganda over the last two decades (2000-2021) with related total climate finance commitments of USD$ 4.74 billion from international sources (Figure 3). This aligns well with the findings of the Stock Take Report of Uganda's Nationally Determined Contributions (NDCs) and NDC Partnership Plan Implementation for specific periods that were analysed.

Most of the resources were mobilized in the form of grants (64.7%) and debt (35%). As per the OECD-DAC statistics, the ratio of climate financial flows to Uganda during the two decades has been well balanced with 52% committed for adaptation and 48% committed for mitigation projects. Uganda's largest providers of climate finance are bilateral donors with multilateral providers also significantly contributing.

In terms of sectors, agriculture, forestry, and fisheries have been the largest recipients of climate financing (20.7%), followed by general environmental protection; water supply and sanitation; and energy at 19.0%, 10.0% and 9.8% respectively. This is also aligned with the desire to reduce emissions from the high impact sectors of the economy such as the agriculture, forestry and other land use which constitutes 77.4% of the share of emissions (MWE, 2023).

Figure 3: Climate related projects and financial commitments for Uganda.



Source: Author's analysis based on OECD Database (2023).

Financial Instrument	Climate-related Development Finance - Commitments - USD '000	%age
1. Grants	3,065,053.06	64.7%
2. Debt instrument	1,658,651.14	35.0%
3. Equity and shares in collective investment vehicles	14,558.98	0.3%
4. Unspecified	1,898.12	0.0%
Grand Total	**4,740,161.31**	**100.0%**

Source: Author's analysis based on OECD Database (2023).

3.0 Some of the Funding Opportunities

At the 15th Conference of Parties (COP15) of the UNFCCC in Copenhagen in 2009, developed countries committed to a collective goal of mobilising USD 100 billion per year by 2020 for climate action in developing countries, in the context of meaningful mitigation actions and transparency on implementation. The goal was formalised at COP16 in Cancun, and at COP21 in Paris, it was reiterated and extended to 2025 (OECD, 2021).

Several developed countries came forward at COP 26 with further climate finance commitments, and the Glasgow Climate Pact included an urgent call to double adaptation finance by 2023. Further to this, at the COP 27, Governments took the ground-breaking decision to establish new funding arrangements, as well as a dedicated fund – The Loss and Damage Fund, to assist developing countries in responding to loss and damage. Parties at the COP 28 agreed on its operationalization arrangements with pledges of over USD 661 million. This provides an opportunity to developing countries such as Uganda to strategize and benefit from these funds.

Considering the above, Uganda, like many developing countries, has unlimited potential to attract, mobilize and leverage climate finance from both private and public sources (domestic and international). The country has a strong and enabling policy, legal and institutional framework supported by the Climate Change Act, 2021, Uganda Green Growth Development Strategy, an Updated Nationally Determined Contributions Action Plan among other implementation plans. The implementation structures are situated under a dedicated Climate Change Department under the Ministry of Water and Environment. However, technical, and administrative capacity is key to developing financially attractive (bankable) and sustainable climate projects. Some of the opportunities for the provision of financial resources on a grant or concessional basis exist through several channels.

At COP 28 still, the Green Climate Fund (GCF) received a boost with six countries pledging new funding at COP28 with total pledges currently standing at USD 12.8 billion from 31 countries, while further contributions are still expected. The Adaptation Fund received new pledges totalling nearly USD 188 million, whereas the Least Developed Countries Fund and Special Climate Change Fund received new commitments totalling more than USD 174 million. This is in addition to COP 26 which realised record pledges of USD 356 million to the Adaptation Fund and USD 413 million to the Least Developed Country Fund including from new contributions, while around $240 million was newly committed to the Adaptation Fund at COP27.

At the COP 28, the UAE Declaration on Sustainable Agriculture, Resilient Food Systems, and Climate Action, alongside regenerative agriculture and climate-food innovation also received financing commitments of USD 2.6 billion.

The Climate Finance Delivery Plan Progress Report on Advancing the Ten Collective Actions highlights the diverse set of actions contributor countries are taking towards meeting the US$100 billion goal, including collaboration with other stakeholders to ensure the effective delivery and utilization of the funds. Below are some of the opportunities presented in the report from different parties globally:

- The EU and its Member States announced EUR 175 million in support of the Methane Finance Sprint, to boost methane reduction. These funds will help catalyse efforts from government, industry, and philanthropy to reduce methane emissions across the energy sector. The Global Forest Finance Pledge (GFFP) announced at CoP 26 the intention to provide USD 12 billion for forest related climate finance between 2021-2025.

- Under its Climate Change Action Plan (CCAP), the World Bank Group committed to provide $25 billion on average in annual financing between FY21-25, for initiatives that lower GHG emissions and foster adaptation, while reducing poverty and inequality and improving development outcomes. The World Bank Group delivered more climate finance USD 317 billion, which represents 36% above their target which informed the 2021 Delivery Plan.

- The European Investment Bank (EIB) committed to support €1 trillion of investments in climate action and environmental sustainability in the critical decade from 2021 to 2030. The European Commission committed approximately €28 billion for the period 2021-2027 to serve climate adaptation objectives. The African Development Bank (AfDB) committed US$ 25 billion towards climate action for the period 2020-2025.

- Italy recently established the Italian Climate Fund, with an endowment of 840 million euros annually from 2022 to 2026 for climate action in developing countries. The Netherlands announced a significant increase in its annual climate finance (public and private) from €1.25 billion to €1.80 billion in 2025.

- Japan committed to provide up to USD 10 billion in climate finance on top of the previous USD 60 billion, in the subsequent five years. In March 2022, Japan made a new contribution of USD 42 million to the United Nations Development Programme (UNDP) Climate Promise.

- Denmark committed USD 500 million annually from 2023 towards climate finance; Finland committed approximately €900 million during the period 2020-2025; France committed €6 billion annually between 2021 and 2025; and Germany committed €6 billion per year by 2025. Norway's Climate Investment Fund became operational in 2022 and was to be capitalised with NOK 2 billion annually in the subsequent five years.

- The Swedish International Development Cooperation Agency (SIDA) also provides concessions and guarantee resources to mobilize private investment for green projects in Africa. In October of 2021, the Swedish government announced plans to double its climate development assistance budget to SEK15 billion (US$1.6 billion in 2019 prices) by 2025, compared with 2019 levels. Sweden increased its environment and climate provision by SEK 1.5 billion for 2022 -2026.

4.0 Barriers to climate finance access and utilization

The different commitments made by different governments and institutions present vast opportunities for Uganda to mobilise climate financing for different sectors to deliver on their targets.

There is a significantly large pool of global capital and liquidity to close global investment gaps, given the size of the global financial system. However, there are key barriers in redirecting capital to climate action in the context of economic vulnerabilities and indebtedness facing many developing countries including Uganda (IPCC, 2023).

The barriers include inadequate enabling policy and regulatory frameworks to aid climate/green financing, limited access to financial and technical expertise, and weak risk management mechanisms (AfDB, 2023). These occur at the market, product, and project level. At the product level, financial institutions are not designing appropriate green financial products and hence not providing green project finance, and from the demand-side, the regulatory framework and skills constraints remain a barrier to the formulation of green projects (Fig. 4). The barriers include:

Regulatory uncertainties – the enabling framework and regulatory environment for the green/climate finance sector is often lacking for many financial institutions. The understanding of what defines and constitutes "green" in relation to specific financial products is still a challenge e.g., establishment and or expansion of the green bond markets is constrained by inadequate regulatory frameworks and a lack of bankable and standardized green projects.

Limited awareness of green/ climate funding options – there is a wide variety of financing options for climate action. However, most of the stakeholders often lack knowledge about the options available (Deng-Beck & Price, 2016). This makes it difficult to identify and choose the best financing instruments for supporting the planned climate action investments.

Complex fund application procedures – the stringent eligibility criteria or complex application procedures for gaining direct access accreditation to multilateral funds makes it difficult to access international climate finance. This limits the amount of financing available to implement the ambitious NDCs and plans formulated by the country.

Limited capacity in structuring green projects – the technical capacity to develop fundable green projects is inadequate and this is compounded by the lack of reliable data and evidence for the climate rationale for example, an analysis of proposals submitted to the GCF up to 2017 shows African countries had the lowest percentage of approvals (39%) compared to all other regions.

Figure 4: Climate finance challenges and constraints summarized.

Source: ADB. 2017. Catalyzing Green Finance: A Concept for Leveraging Blended Finance for Green Development.

Inadequacies in designing practical green/ climate finance models – there is limited ability by project financiers to structure financial models for green projects with leveraged financing plans aimed at catalysing finance from private or public investors, or risk-adjusted returns and end-user demands. This also limits the access to available funding for such projects.

Data intensive processes – securing financing for large climate investments usually requires the collection of technical information, risk assessment and preparation of detailed analyses (EU, 2017). Often, there is limited capacity to measure, report and verify (MRV) climate finance, and this results in lack of credible information to inform financial support to climate-related projects.

Low bankability of climate action projects – failure to demonstrate bankability of planned investments especially for non-grant instruments is often due to lack of sufficient data about future returns on investment, insufficient information about the amount of finance needed to support adaptation action or about the future benefits/savings from avoided damages that comes with resilience and adaptation measures (EU, 2017). Low bankability is also related to the lack of ability to monetize or value direct and indirect green benefits resulting from green projects that may not lead to increased revenues for the project.

Low quality pipelines of viable climate positive projects and lack of aligned regional green taxonomies – there is an ability by project developers to develop innovative technology projects, that can address higher-risk profiles of climate investments and attract finance into such investments. This is compounded by the lack of regional specific taxonomies to define what is and what is not green e.g., the available taxonomies are not tailored to the African context to guide project structuring, which increases the likelihood of green washing.

5.0 Strategies to scale up adoption of green practices

To facilitate shifts in private finance towards green/climate space, there is need to enhance low carbon development pathways focusing on the demand side, supply side and regulatory frameworks.

On the supply side, there is need for new systems and competencies in financial institutions to green markets through product innovation (e.g., green bonds), increase equity participation, provide derisking instruments such as guarantees and insurance schemes, subsidies such as grants, establish robust and unified standards, and tax incentives to advance long-term green investment flows and associated outcomes.

Financial institutions should consider establishing special facilities/ funds as innovative mechanisms to mobilize both national and international climate finance resources and ensure they are directed to low carbon and adaptation projects that are near-bankable and commercially viable with the highest impact possible. The Climate Finance Facility at the Uganda Development Bank is a good example, but more facilities are needed to meet the financial needs.

Technical Assistance and Project Development Assistance are among the most important approaches/ tools used to overcome the obstacles of insufficient technical and administrative capacity or expertise in developing successful applications for climate financing. This is key in growing a sustainable and good quality green investments pipeline to advance climate action.

On the regulatory side, it is necessary to ensure that fiscal policies are designed to provide targeted and efficient incentives to both financial institutions and implementation entities (such as subsidised interest rates) for investment in projects that will yield less risky but significant environmental/ sustainable development benefits and higher climate impact. Providing derisking instruments and instituting risk sharing schemes such as credit guarantees and insurance schemes e.g., agricultural insurance have proved to lower risks, reduced lending rates and increased access to credit.

Project developers and financiers should develop taxonomies and other guiding policies, strategies and as well as implementation frameworks to facilitate green financing. This supports improved assessment of climate-related risks and investment opportunities within the financial system, reduces sectoral mismatches between available capital and investment needs, improves the risk-return profiles of climate investments, and develops institutional capacities and local capital markets (IPCC, 2023).

6.0 Conclusion

The increase in climate financing opportunities makes it important for the country to consider how to attract and leverage different types of climate finance instruments, including that from private sources.

While there are immense climate financing opportunities, there exist key knowledge gaps as well as risks which impede not only the ability to structure green deals, but also the appetite to support green initiatives. There is, therefore, a need to enhance capacity building programs and to develop derisking instruments to enhance demand for and supply of green products.

The private sector has a critical role to play in unlocking financing for climate action and green growth. The private sector can mobilize finance, promote innovation, reduce climate risks, and promote public-private partnerships. Therefore, it is critical to leverage private sector financing and strategic public sector-driven collaborations to enable climate-resilient development and green growth in the economy.

Ministries, Departments and Agencies (MDAs) need to leverage the role of multilateral development banks in climate funding, notably through long-term or concessional resources that promote private sector involvement, while also encouraging private investors to provide "patient" capital to local businesses. The capacity of government owned enterprises needs to be strengthened to balance local and national development priorities in resource revenue generation and utilization (AfDB, 2023).

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