Empowered lives.
Resilient nations.

Policy Paper

A Faremwork to Strengthen Climate Change Finance Readiness in Yemen

Published in December 2013 and updated in June 2014

United Nations Development Programme

ENVIRONMENT AND ENERGY

Policy Paper

A Faremwork to Strengthen Climate Change Finance Readiness in Yemen: An Interim Mechanism under the Social Fund for Development (SFD)

Walid Ali
Climate Change Policy Advisor
Poverty and Sustainable Development Unit
UNDP Yemen

Fuad Alkadasi
Team Leader, Poverty and Sustainable Development Unit, UNDP Yemen

Summary

Climate change is not only an environmental issue but rather an environmental and development challenge. Although, Yemen is one of the countries which is highly vulnerable to projected climate change impacts, it has not yet designated a dedicated national institution like National Climate Fund (NCF) for administrating climate change polices and strategies through which a broader mandate and capacities are necessarily systematized to capture and address the multidisciplinary, and inter-sectoral developmental challenges induced by climate change. Nevertheless, as far as this concept noted is concerned, the other conclusion around can be re-emphasized in that the Social Fund for Development (SFD) has the potentiality to host an interim national mechanism to increase the likelihood of attracting and using climate finance. Capitalizing on the SFD's relative development finance readiness including improved project management, delivery, MRV capacities, and hosting of an interim NCF mechanism under the SFD is a feasible strategy. By so doing, putting in place the necessary dedicated national institutional capacities to use climate finance more effectively, the likelihoods of attracting potential domestic, and international climate finance in Yemen will significantly improve than otherwise would. Put this way, the opportunity cost of no action (i.e. weak readiness to climate finance as in business-as-usual scenario) will likely be running higher than expected. In other words, the likelihoods of attracting potential climate finance will significantly diminish so that foreseeable climate finance capital investment opportunities will highly be unfeasible due to unsatisfactory and weak national capacities. In fact there is a lack of understanding among policy-makers in Yemen regarding climate finance readiness, and how to go about it. Therefore, this concept note aims to contribute by attempting to strengthen understanding of policy-makers about the concept of climate finance readiness, out its different policy implications together into a national perspective in order to advocate and promote scaled-up efficient, and cost-effective climate-related national priority actions in Yemen. This concept note has drawn on a couple of related UNDP publications, and experience which capitalize on knowledge and technical expertise in climate change-related actions across about 140 countries around the world.

1. Understanding of Climate Finance: Concept, Sources, and Channels

Climate Change Finance, also known as Climate Finance is a term used extensively in climate talks, policy-makers, media and practitioners to describe the use of the present, and innovative financing sources to make transformative change in the production and consumption patterns in ways that catalyze low-emission, and climate resilient development (LECRD) paths. Climate finance sources are diverse such as government budgets, capital markets (carbon markets, venture capital), and international funding. With the projected climate change impacts, development will experience further complication, and consequently countries all over the world will require substantial supplies of climate finance in order to make the transformative change in response to a changing climate. On the other hand, countries around the world will experience varying levels of climate change impacts based upon their respective vulnerabilities. In addition, national response to the project climate change impact mainly relies upon the level of a country's adaptive capacity.

In general, developed countries are characterized of being technologically advanced, with high levels of living standards including world-class infrastructure, welfare, and social security as well as access to well-established capital markets among others. So, adaptive capacities of these countries to cope with and adapt to climate change including capacities to use climate finance for catalyzing capital investments pertaining to climate-related actions is by far better off. Whereas, at least in present, developing countries and Least Developed Countries (LDC) have relatively limited adaptive capacities to undertake actions including catalytic climate finance interventions which puts the transformative change in place. As such, the estimated demand for climate finance by developing countries, and LDCs is as many times as greater than the present levels of Official Development Assistance (ODA) to promote low-emission and climate resilient development patterns.

Under the different development priorities, and barriers experienced by developing countries, and the extremely vulnerable LDCs, domestic public climate finance is to invest and catalyze in response to the projected climate change impacts has been unsatisfactory or in some countries unidentified. Among others, lack of classified public budgetary, and expenditure codes, many LDCs including Yemen have not undergone specific national processes such as Investment And Financial Flows Assessment (I&FF), and Climate Public Expenditure And Institutional Review (CPEIR) to assess their respective public on-budget climate expenditures and established a baseline and identify the need and gap in terms of climate finance.

Nevertheless, under increasing climate-related priorities, lack of public climate finance in many developing countries, and majority of LDCs around the world, the transfer of international climate finance to these countries has been growing. This regards international climate finance usually channelled to developed countries and LDCs in particular through various multilateral and bilateral agencies, the United Nations Framework Convention on Climate Change (UNFCCC) and a number of private financial intermediaries. However, under the UNFCCC, Clean Development Mechanism (CDM) and Bilateral frameworks, the following are among the prominent global institutions through which climate finance are channelled including for instance:

1. The Global Environment Facility (GEF);
2. Adaptation Fund (AF), Least Developed Countries Fund (LDCF);
3. Climate Investment Funds (CIF);
4. Green Climate Fund (GCF);
5. Performance-based payments for reducing emissions from deforestation, degradation, and forest

conservation (REDD+);
6. (CDM) based Certified Emission Reductions (CERS); and
7. Capital markets, etcetera.

With this respect, it worth-noting that there are usually two main modalities for developing countries as well as LDCs including Yemen to access international climate finance. These modalities include direct and indirect access. Direct access is enabled if a national entity is certified through specific accreditation process to become the national implementing agency or institution for international climate financing. This modality requires building of proper and satisfactory national capacities including fiduciary management qualities to the expected international standards. For instance, National Climate Funds (NCFs) are one of the mechanisms through which a formal entity is mandated to manage access and implement climate-related priority actions (for further information, please refer to the UNDP publication entitled as Blending Climate Finance through National Climate Funds). In addition, it can serve as the national implementing entity of accessing and delivering domestic and international climate finance). The advantage of this modality includes existence of national mechanism and capacity to plan, access, and deliver nationally climate-related priority actions from a diverse of sources including international climate finance.

Furthermore, these modalities secures additional capacities to access, and implement large-scale climate finance while at the same time reducing transaction costs, and creates greater efficiency than otherwise would. However, proper planning and capacity building should be undertaken to establish the national implementing entity in charge of managing and implementing climate-related priority actions. On the other hand, an indirect modality which usually requires intermediary multilateral, and/or bilateral agencies to support the request of national counterparts accessing certain climate finance is becoming less engaging compared to direct access. The opportunity cost involved in the indirect modality usually is relatively higher including the forgone value of building national capacities to access, and implement large-scale climate-related actions financed from domestic and international finance sources.

2. Understanding of Climate Finance Readiness: the likelihoods of Attracting Finance

This section adapts a framework to establish a common understanding about the concept of readiness to climate finance through which to advocate, promote scaled-up efficient, and cost-effective climate-related national priority actions in Yemen. This concept note reflects on related UNDP publications which capitalize on an in-depth knowledge and technical expertise in climate change-related actions across about 140 countries around the world.

A generic framework for understanding of climate finance readiness is well lay out and elaborated in the UNDP publication entitled as “Readiness for Climate Finance: A framework for understanding what it means to be ready to use climate finance”. In short, to be ready to use climate finance to make a transformative change, a nationally appropriate mechanism is to be designated factoring on national contexts including priorities, capacities, barriers, and etcetera. In general, readiness for climate finance is meant to refer to a set of four national capacities in place to plan for, access, deliver, and monitor and report on international and domestic climate finance to make transformative change in ways that catalyze low-emission, and climate resilient development (LECRD) paths. It should be noted that the outlined framework’s components are not prescriptive but rather intends to provide a conceptual tool for analysis to help advice on proper national action to strengthening national climate finance readiness. In other words, the cost-effective entry point for strengthening of national climate finance readiness in Yemen has to strategically synergize along with the existing institutional capacities rather than starting from

scratch. Therefore, the following is not meant to be as a prescriptive but rather it introduces a perspective through which to further analyze existing national institutional capacities (strengths, weaknesses, threats, and opportunities) related to a due process aiming at strengthening of Yemen's readiness to climate finance through an Interim Mechanism under the Social Fund for Development (SFD) as indicated later in Section 5:

1. **Planning for Climate Finance:** First, national capacities in development of low-emission, and climate resilient policies, strategies, action plans, and the underlying investment programmes are the core of this component. For instance, this includes capacities to assess national climate-related needs, and priorities. In addition, identification of barriers for climate-related capital investment, appropriate policy-mix and sources of financing are among the key capacities under this component.

2. **Accessing Finance:** under this component, national capacity to formulate project, programme, and sector-wide approaches proposals and documents in line with national priorities to the expected international standards of bilateral and multilateral donors is a key to access international climate finance

3. **Delivering Climate Finance:** Technical, administrative, project, programme management policies, and operational and fiduciary capacities to implement and execute project, programme, and coordinate implementation are necessarily critical to be ready to access climate finance. Fiduciary management is the key for designation of national mechanism to deliver international climate finance. On the other hand, capacities to coordinate project and programme implementation through proper oversight and directing mechanism is also a key capacity under this component.

4. **Monitoring, Reporting & Verification (MRV) of Climate Finance Results:** The capacity to monitor progress towards planned results within timeand budget, verify realization of results, and reporting is among the key qualities to access, and deliver climate finance by nationally implementation mechanism.

Climate change is not only an environmental issue but rather an environmental and development challenge. Although, Yemen is one of the countries which is highly vulnerable to projected climate change impacts, it has not yet designated a dedicated national institution (i.e. NCF) for administrating climate change polices and strategies through which a broader mandate and capacities are necessarily required to capture and address the multidisciplinary, and inter-sectoral developmental challenges induced by climate change. However, at present, the Environmental Protection Authority (EPA) is the focal point of UNFCCC, and in charge of coordinating donor-finance climate change interventions. EPA is the national institution in charge of coordinating, oversight, and enforcement of Environmental law, and international environmental conventions. On the other hand, EPA has no relevant project, programme management, and delivery capacities to effectively use (i.e. plan for, access, delivery, and MRV) domestic and international climate finance.

Furthermore, it worth-noting that such capacities are not only lacking within EPA, but rather across the various national institutions in Yemen with the exception of SFD, and PWP cases. Following this analysis, it can be concluded that there is a critical need to designate a dedicated national institution mandated with administration of climate change polices and strategies. Its mandate has to be broad, and capacities to be strengthened enough to use climate finance to manage and address climate change considerations as effectively as possible. To recap, this section reiterates that the likelihoods of attracting and using potential domestic, and international climate finance in Yemen will significantly improve by putting such dedicated national institutional capacities in place.

3. Climate Finance Readiness in Yemen: Insights from Development Finance Experiences

This section will explore Yemen experience from development assistance's perspective to provide insightful implications for strengthening readiness of climate finance. To avoid confusion between climate finance and ODA, it is useful to make a distinction by pointing out to the point in that climate finance is mobilized to specifically address the underlying causes (known as climate change mitigation actions), and/or impacts of climate change (adaptation). Although both of climate finance and ODA contributes to achievements of sustainable development goals, the Cancun Agreements specify that climate finance should be new and additional to the ODA. On the other hand, the Copenhagen Accord suggests mobilizing about US$ 100 Billion US$ on annual basis by 2020 to support climate-change mitigation and adaptation activities in developing countries, with the funds coming from "public and private, bilateral and multilateral, including alternative, sources of finance".

The present levels of the ODA allocated to developing countries and LDCs is insufficient to bridge the development finance gap. On the other hand, many of the ODA recipient countries including Yemen have weak absorptive capacity and accountability mechanisms as to use such funds effectively. Yemen's donor funding experience suggests that Yemen has weak absorptive capacity to use development finance assistance, and catalyze transformative change towards achievement of economic development, poverty reduction, Millennium Development Goals (MDG), and sustainable development. For instance, Yemen's experience indicates that enormous funding opportunities which have been pledged by bilateral and multilateral donors in 2010, and recently in 2012 are not fully exploited due to many reasons and mainly the weak national and sectoral absorptive capacities. Similarly, as climate change is projected to pose serious threats across the globe, developing countries in general, and LDC in particular are projected to be experiencing growing vulnerabilities.

Growing of climate change-related vulnerabilities will likely to continue due to increasing levels of exposure induced by the Green House Gas Emission (GHG) trends, and sensitivity to new and multiplying climate change related risks as well as lack of adaptive capacity including the necessary capacities especially financial resources, institutional, regulation, policy, and technical, as well as technological capabilities to use climate finance for coping with, and adapting to its potential impacts. A key lesson learnt from lost opportunities of capitalizing on donor pledges in the past, and at the present suggests that a lack of nationally reliable designated mechanisms with supportive development finance-based planning, access, delivery, as well as measurement, reporting and verification (MRV) capacities, are among the relevant main causes of a weak absorptive capacity in Yemen. Yemen otherwise could have been supported to strengthen its responsive capacities related to development finance absorptive capacity. Enabling environment including of removing of barriers and strengthening of development finance readiness to, at least, access, and deliver significant development results through effective and efficient use of such funding opportunities.

Similarly, as noted above, although the ODA finance is thematically different in terms of agenda, the capacity barriers context remains applicable, and hence reduces potentiality of Yemen to use climate finance effectively. Nevertheless, it is worth-mentioning that unlike most of the national institutions and funds in Yemen, the Public Works Project (PWP) and SFD's records in terms of efficiency, effectiveness are relatively better off. This has been recognized by several international organizations and donors (Chatham House 2010, DFID 2013, WIDER 2013, World Bank 2014) operating in Yemen. Although PWP and SFD apparently have relatively encouraging achievements, appropriate project and programme delivery mechanisms in addition to relevant development and

community-based development experience. The UNDP Yemen Country Office has also publicised a policy note in 2011. The initial findings of the analysis focused on the potentiality of these two institutions in general and the SFD in particular to attract climate finance through establishing an interim mechanism to serve as a NCF under the SFD.

As far as this note is concerned, Yemen is particularly constrained by the mentioned earlier capacity barriers (informally, known as absorptive capacity) to attract capital investments to finance national climate-related priority actions. As indicated earlier, removing of national capacity barriers is critical to use (from either sources; domestic or international, and public or private) climate finance effectively. In addition, public on-budget climate related expenditures is necessarily a key for removing climate finance capacity barriers, as well as catalyzing climate related capital investments. Following this understanding, and reading through the country's socio-economic and institutional outlook, a pessimistic scenario of losing climate finance opportunities in Yemen to produce low-emission and climate resilient development paths will likely repeat itself unless proper interventions to strengthen readiness to climate finance are initiated.

4. The opportunity cost of lacking a national climate finance mechanism in Yemen

This section reflects on the analysis of the earlier sections. Given that:

- Yemen is an LDC, and a low-income country with an average national income per capita of US$950;
- Yemen also has the lowest Official Development Assistance (ODA) of per capita at US$12.7 or just 2.2 percent of Gross Domestic Product (GDP), compared to US$33.4 per capita (18.7 percent of GDP) for other least developed countries in the world which is due to many reasons but include as an LDC, its weak absorptive capacity;
- Foreign Direct Investment (FDI) in Yemen is relatively low, but Oil, and Liquefied Petroleum Gas (LPG) stands as the prominent FDI investments in the country, representing about 80 percent of national exports, accounting for about 70 percent of Government revenues. In other words, reliance on one economic sector increases the risk of maladapation.
- Yemen is already one of the most water-scarce countries in the world, lacking rainfall and surface water;
- Yemen's economy largely depends on its rural natural resources.
- More than 75 percent of the population is rural-based engaged in farming, pastoralism, fishing and hence highly reliant on climatic conditions for their livelihoods.
- Rural livelihoods which secure minimum food and/or income is extremely sensitive to exposure to unfavourable climate conditions
- In absolute terms, around 10 million of population in Yemen are food insecure, and live below the poverty line of 2$/a day.

It can be noted that the majority of population in Yemen including vulnerable communities and groups, such as the poor, and especially women and youth will therefore likely to experience greater livelihood impact hardship and complications. Put into a context, without proactive national policy action, the aforementioned vulnerability context, and capacity barriers, sustainable livelihoods upon which to make means and ends available for national economic development, as well as poverty reduction, sustainable human development in Yemen will likely to be experiencing many more challenges under changing climate. Yemen needs substantial resources to implement adapation and mitigation programmes. In nutshell, the opportunity cost of no action (i.e. weak readiness to

climate finance as in business-as-usual scenario) will likely be higher than expected. Moreover, the likelihoods of attracting potential climate finance will significantly diminish so that foreseeable climate finance capital investment opportunities are highly being unfeasible due to unsatisfactory and weak national capacities.

5. The potentiality of SFD to attract climate Finance in Yemen

As mentioned earlier, the findings of the publication by UNDP Yemen Country Office in 2011 concluded that, the SFD has the potentiality to host an interim national mechanism to increase the likelihood of attract climate finance. Please refer to the publication in its two visions (A shortened and detailed copies). The analysis of the indicated publication is consistent with the aforementioned discussions about readiness to climate finance.

6. An Interim NCF Mechanism under the SFD: Role of Potential Partners

- **SFD:** Hosting of an interim NCF mechanism to attract climate finance by capitalizing on the SFD's relative development finance readiness including improved project management, delivery, and MRV capacities.

- **NCF:** In the interim, and after maturity, the NCF mechanism will serve as the national implementing entity of climate change policy. This mechanism will significantly improve the likelihood of Yemen to directly access, and deliver potential domestic, and international climate finance more effectively than otherwise would.

- **UNDP:** Provide advisory services, and start-up support until maturity of the interim NCF mechanism; establishment of an independent NCF entity

- **EPA:** Beneficiary of the interim NCF mechanism in line with climate change policy

- **Other Governmental Institutions:** Beneficiaries of the interim NCF mechanism in line with climate change policy

Acknowledgment

The authors would like to express thanks and appreciation to UNDP Yemen CO senior management particularly Mikiko Tanaka for advice and support, the Boots on the Ground's regional advisor for continuous advise, support, valuable discussions, consultations, and knowledge sharing, and the Boots on the Ground's team, and Environmental and Energy Team in HQ for continuous support, facilitation, and knowledge sharing. The authors would like also to express thanks to the Environment Protection Authority (EPA, Yemen) and the SFD for valuable consultations and discussions, facilitations, and knowledge sharing.

List of References and Sources

A. List of national sources

1. Yemen's Second National Communication (SNC 2013)
2. Governance and Climate Change in Yemen: A Policy paper (UNDP Yemen 2012)
3. Yemen's National Agriculture Sector Strategy (NASS 2012)
4. Joint Social and Economic Assessment for the Republic of Yemen (2012)
5. Yemen's National Water Sector Strategy and Investment Programme (NWSSIP 2012)
6. Climate Change, Agricultural Production and Food Security: Evidence from Yemen (Kiel Institute for the World Economy 2011)
7. Climate change impact assessment on the agriculture and water sectors, Republic of Yemen (World Bank 2010)
1. Comprehensive Food Security Survey, Yemen (WFP 2010)
2. Yemen's Initial National Communication (INC 2001)
3. Yemen's National Adaptation Programme of Action (NAPA 2008)
4. Yemen's Pilot Program for Climate Resilience (PPCR 2010)
5. Yemen's National Environmental Action Plan (NEAP 2005-2015)
6. National Strategy for Environmental Sustainability (NSES 2007-2015)
7. Fourth National Plan for Development and Poverty Reduction (DPPR 2007-2011)
8. Yemen's National Biodiversity Strategy and Action Plan (NBSAP 2005)
9. Yemen's National Capacity Self Assessment (NCSA 2008)
10. Yemen's National Fishery Sector Strategy (NFSS 2012)
11. Yemen's National Disaster Management Plan
12. DFID Operational Plan 2012-2015 (DFID 2013)
13. An Overview of the World Bank in Yemen and Civil Society's Role (World Bank 2014)

B. List of references

1. Readiness for Climate Finance: A framework for understanding what it means to be ready to use climate finance (UNDP 2012)
2. National Climate Funds: A Guidebook for Decision-Makers (UNDP 2012)
3. Catalyzing Climate Finance: A Guidebook on Policy and Financing Options to Support Green, Low-Emission and Climate-Resilient Development (UNDP 2011)
4. Human Development in a Changing Climate: A Framework for Climate Finance (UNDP 2010)
5. Adapting to climate change-UNDP-GEF Initiatives Financed by the Least Developed Countries Fund , Special Climate Change Fund and Strategic Priority on Adaptation (UNDP 2011)
6. Mapping Climate Change Vulnerability and Impact Scenarios: A Guidebook for Sub-National Planners (UNDP 2010)
7. International Guidebook of Environmental Finance Tools: A sectoral Approach (UNDP 2012)
8. Local governance and climate change: a discussion note (UNDP 2010)
9. Climate Change Governance: Background Paper to the 2010 World Development Report
10. Climate Economics: The State of the Art (2011)
11. Impact of Climate Change on Arab Countries
12. Social Dimensions of Climate Change
13. National Communications mainstreaming guide
14. Mainstreaming Climate Change Adaptation into Development Planning: A Guide for Practitioners (2010)

15. Effective Resourcing to Address Climate Change
16. Expert views of climate change adaptation in least developed Asia
17. Regional Perspectives of Climate Change
18. Practitioners and Policy Makers Exchange on Climate Change Adaptation in Agriculture (2011)
19. Delivering good aid in hard places- Working Paper (WIDER 2013)
20. Yemen: Political Dynamics and the International Policy Framework (Chatham House 2010)