



FMO

Entrepreneurial
Development
Bank

SNV Netherlands
Development
Organisation

CLIMATE
FUND MANAGERS

**DUTCH FUND
FOR CLIMATE &
DEVELOPMENT**

Bid Application
Public Version



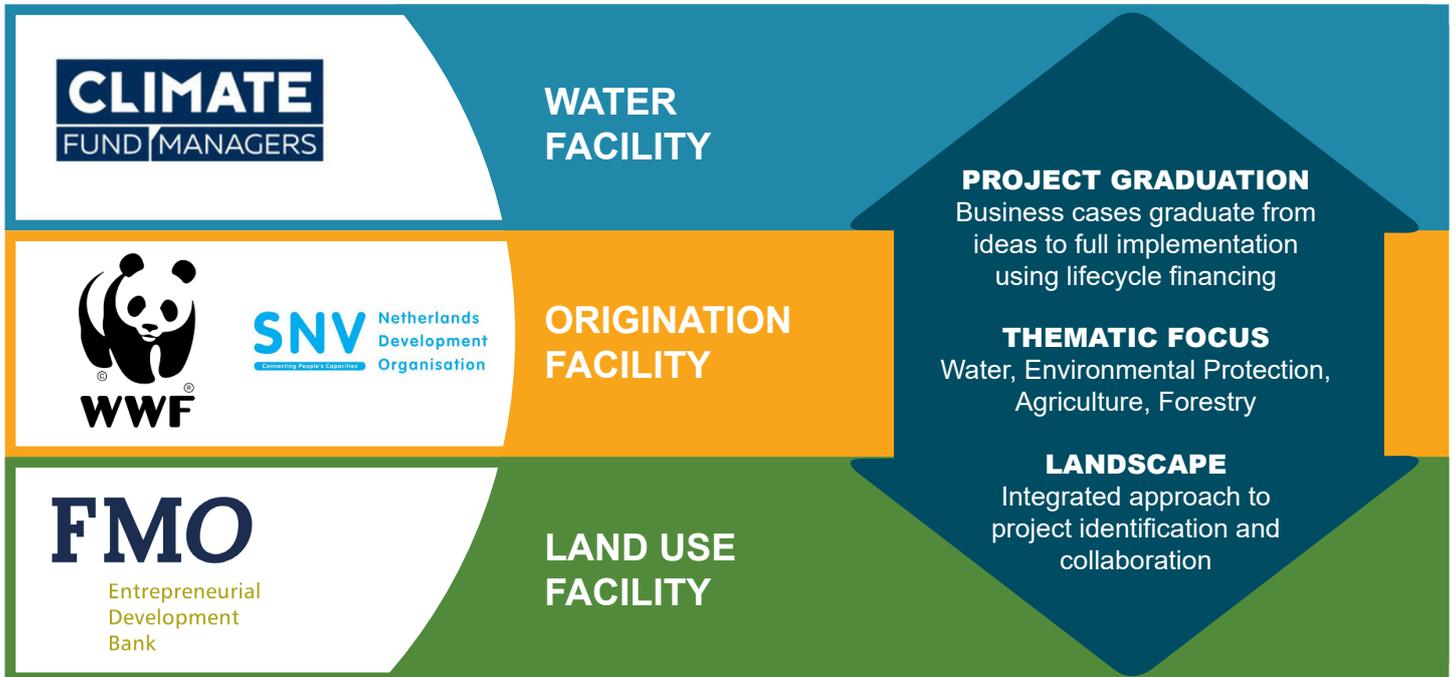
February 2019



Executive Summary

Climate change poses an unprecedented threat to humanity in the 21st century. With notable shortfalls in funding and a dominant focus on climate mitigation by global financing parties to date, Dutch development bank Nederlandse Financierings-Maatschappij voor

Ontwikkelingslanden N.V. (“FMO”) has partnered with Climate Fund Managers (“CFM”), World Wildlife Fund Netherlands (“WWF”) and SNV Netherlands Development Organisation (“SNV”) to manage the Dutch Fund for Climate and Development (DFCD).



The Netherlands based consortium will be led by FMO and (i) provide finance and Technical Assistance (TA) to projects with a focus on climate change adaptation; (ii) mobilize external private sector funding at scale; and (iii) align directly with DFCD Theory of Change (ToC). A substantial allocation of investments will be reserved for OECD DAC Least Developed Countries (LDCs) and other Netherlands development cooperation priority countries (collectively, ‘the focus countries’). Investments made by the consortium parties will seek to improve the wellbeing, economic prospects and livelihoods of vulnerable groups – particularly women and children – and, enhance the health of critical ecosystems – from water basins to rivers, tropical rainforests, marshland and mangroves. The consortium’s activities will also help protect communities and cities from the increasing frequency of extreme weather events and benefit depleting biodiversity in areas that provide people with water, food, medicine and economic opportunity.

In addition, the consortium has been established to overcome **two prohibitive market barriers** for financing climate adaptation, and to a lesser extent, climate mitigation projects in the focus countries:

Available Funding: Recognizing an estimated \$3.5 trillion is required for developing countries to implement climate pledges to prevent potentially catastrophic and irreversible effects of climate change, the

consortium will utilize the full €160 million of DFCD funding to directly **mobilize between €500 million – €1 billion** in institutional and other commercial capital during the lifetime of the DFCD.

Originating Bankable Projects: The consortium will also demonstrate that as a collective it can achieve greater environmental and developmental impact than the sum of its parts. Notably, the consortium will adopt an innovative **‘landscape’ strategy for deal origination and execution**, with consortium parties actively sourcing and developing investment opportunities for other consortium parties in-and-around, as well as downstream, the vicinity of their own investment activities. This will be achieved through transparent, collective knowledge sharing at consortium level; demonstrating that four complementary institutions – a DFI, a private sector investment manager, an environmental NGO and a social development NGO – can operate harmoniously to achieve *climate resilient economic growth* in DFCD target countries.



To achieve the DFCD mandate the consortium will be structured with three separate but operationally linked **'Facilities'** each with a unique role across the project lifecycle; each with a unique thematic sub-sector focus:

Origination Facility ("OF")	
<p>Managed by WWF-NL and SNV collectively, the OF is positioned exclusively for project identification and (pre-)feasibility development activities with a cross DFCD thematic subsector focus. This window will seek to leverage the landscape strategy for activity sourcing and develop opportunities into viable business cases for the two investment windows (as below). The OF will provide grant funding and TA for its activities.</p> <p>€30 million will be allocated to this window to be deployed in ~ 70 projects.</p>	<p>DFCD Theory of Change (ToC) Outcomes:</p> <p>All through its early-stage project graduation strategy.</p>

Land Use Facility	
<p>Managed by FMO, the Land Use Facility targets investments that have graduated from the OF in sectors relating to agroforestry, sustainable land use and climate resilient food production. The Land Use Facility has at its disposal the full range of financial instruments offered by FMO to provide growth finance to companies, including grants, equity and debt. It will also source opportunities from FMO's external networks and will provide post-construction phase community development and TA financing.</p> <p>€55 million will be allocated to this window to be deployed in ~ 25 companies.</p>	<p>DFCD Theory of Change (ToC) Outcomes:</p> <ul style="list-style-type: none"> • Climate-resilient land use and ecosystems; • Climate-resilient food security; • Lower GHG emissions; • Climate-resilient water supply and sanitation; and • Improved wellbeing, economic prospects, livelihoods, inclusion

Water Facility ("Climate Investor Two" or "CI2")	
<p>Managed by CFM, the Water Facility will also target investments that have graduated from the OF in sectors related to water, sanitation and environmental protection. The Water Facility will contribute to the development, construction and operational phases of investments. To achieve this the Water Facility will provide development grants, equity for construction and operational debt to projects. It will utilize the proven fund structure of Climate Investor One and will target a €50 million Development Fund, a €500 million Construction Equity Fund and a €500 million Refinancing Fund. The Water Facility will also source opportunities from CFM's external networks and will provide post-construction phase community development and TA.</p> <p>€75 million will be allocated to this window to be deployed in ~ 30 projects.</p>	<p>DFCD Theory of Change (ToC) Outcomes:</p> <ul style="list-style-type: none"> • Climate-resilient water supply and sanitation; • Climate-resilient land use and ecosystems; • Improved wellbeing, economic prospects, livelihoods, inclusion; and • Lower GHG emissions.

The consortium partners were sought for their long-standing collective track record in both climate finance, development finance, a proven ability to mobilize private sector capital at scale, as well as institutional knowledge and advocacy work. The consortium parties have collectively provided over €2.2 billion in climate finance in the period 2015-17, and collectively have access to an investment **pipeline of €1.2+ billion** across the thematic sub-sectors and focus countries. This pipeline enables the consortium to already hit the ground running within the current budget year of the Netherlands government.

Fund Governance

With FMO as the Lead Partner and MoFA's direct counterpart for the DFCD, the consortium parties will collaborate through the Origination Facility for deal origination. Subsequently each Facility will make its investment decisions in an independent Investment Committee (IC) in accordance with the DFCD Assessment Framework. FMO and CFM will be granted a seat on the IC of the OF to increase the likelihood of projects receiving follow on finance after the OF has completed its activities on a project. The consortium will be governed through a **DFCD Advisory Board**, which role is primarily to (i) monitor/report/evaluate the implementation & progress and financial & impact results of the three Facilities; (ii) act as a general forum for communication; and (iii) monitor significant trends in global climate policy & finance and assess its ramifications for the DFCD.

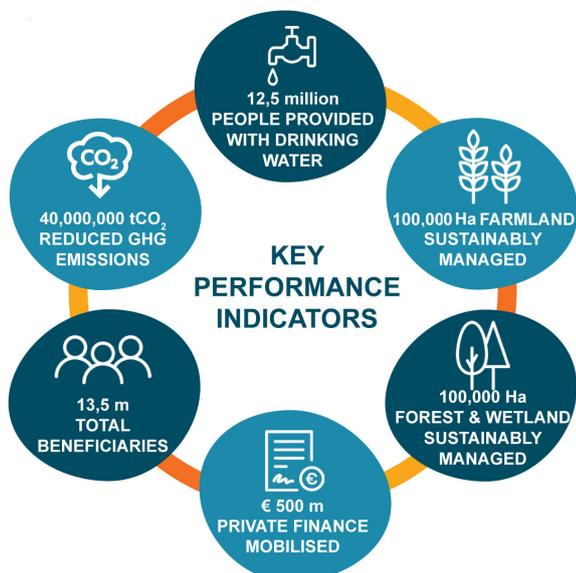


Consortium Impact

The DFCD will focus on a set of high impact investment themes within four key Rio Marker 2 sectors all of which are critical to tackling climate change and achieving the SDGs:

- Climate resilient **water systems and freshwater ecosystems**: drinking water & sanitation supplies, restoration & sustainable management of wetlands, headwaters & floodplains
- **Forestry** for the future: promoting afforestation and reforestation
- Boost food security with **climate smart agriculture**: funding more sustainable, efficient and productive approaches from smallholder farmers to agri-business
- **Protecting the environment**, protecting people: restoration of ecosystems, such as wetlands and mangroves, which are nature's best defences against extreme floods, droughts and storm surges.

The following estimated impact will be delivered by virtue of DFCD fundir



Strategic Rationale for the Netherlands

The incorporation and domiciliation of the consortium in the Netherlands may provide real economy and strategic benefits to Dutch business, exporters, citizens and government.

DFCD funding will provide ample opportunity for Dutch knowledge centres and companies to expand their activities in the DFCD focus countries and sectors, notable the water and food security industries, backed by a reputable and experienced Dutch consortium. Jobs will be created and knowledge will transcend to developing economies, positioning the Netherlands as a leading centre for climate adaptation. Dutch institutional investors will also be approached to invest in the Water Facility (CI2) and co-financing opportunities will be encouraged for other Dutch institutions across both investment windows. In the course of 2019, the future NL Business entity will come into force, which is a new €800 million equity funded collaborative vehicle between FMO and the Dutch state. FMO will ensure maximum synergy between the DFCD and this entity.

The consortium thereby provides the Dutch government with a prominent vehicle that can deliver climate impact and contribute to diplomatic efforts to strengthen the international response to the climate challenge.

Bidding Application (Public Version)

Dutch Fund for Climate and Development

Disclaimer: The DFCD Bid Application (Public Version) is an edited version of the public tender proposal the Consortium of FMO, WWF-NL, SNV and CFM (hereinafter "the Consortium") responded to in February 2019. This document is published at the request of the Dutch Ministry of Foreign Affairs as to promote transparency, after the tender was awarded to the Consortium in May 2019.

This public Bid Application version is shortened and edited version of the submitted tender document as to improve readability and remove sensitive information. Since the DFCD was awarded the tender, the DFCD's mandate, governance structure, strategy and procedures have been further defined in collaboration with the Ministry of Foreign Affairs, meaning that information included in this public tender document can be incomplete and outdated.

This document is solely intended for reference, transparency, and discussion purposes, and is not provided as the basis for any professional advice. Except when stated otherwise, the Consortium Partners are the exclusive owners of all intellectual property rights of the information contained in this document.

If you have any questions about this document, we welcome you to contact info@thedfcd.com.

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I. Introducing the Consortium

1. The Consortium as the best vehicle to executive on the DFCD mandate

FMO has formed a Consortium with SNV, WWF-NL and CFM, bringing together four organisations uniquely positioned to overcome two of the largest barriers to realising climate and development outcomes in developing countries: originating bankable projects and crowding-in private finance to achieve scale. These organisations are bundling their outstanding expertise in social development, environmental management and development finance to scale up public and private development finance to deliver high quality projects for climate adaptation and mitigation. To do this, FMO and its partners propose to set up three facilities: (i) an Origination Facility managed by SNV and WWF-NL; (ii) a Water Facility managed by CFM; and (iii) a Land Use Facility managed by FMO.

As at least 50%, but preferably 65%, of the fund's resources need to go towards climate adaptation projects. Overcoming the barriers to bring projects to scale needs to be in the core design of projects financed by the DFCD's grants. Without the right expertise, convening capacity and financial means to overcome these, projects will struggle to reach the bankable stage, where private financiers can come in and communities can benefit from transformative interventions at scale. The remaining 35-50% spent on mitigation is anticipated to come either through projects with cross-cutting mitigation and adaptation impacts, or from projects in similar themes but with a primary mitigation component such as non-adaptation linked forestry and energy access and efficiency in the agricultural sector.

The Consortium has a strong track record in climate change, finance knowledge and advocacy. Collectively the Consortium Parties have provided over €2.2Bn in climate finance, with a large majority provided for climate change mitigation finance. This demonstrates the extent to which climate adaptation finance is less developed than climate mitigation finance and the corresponding need for climate funds with dedicated climate change adaptation objectives and targets.

The Consortium defines Climate Change Mitigation as the act of reducing GHG emissions into the atmosphere or sequestering GHG emissions from the atmosphere. Climate Change Adaptation is defined as the process of adjustments in human and natural systems, in response to actual or expected climate stimuli or their effects, that moderate harm or exploit beneficial opportunities.

These definitions are in line with how each of the Consortium members determine the contribution of their existing projects to climate adaptation and mitigation. Both definitions and the related projects are fully in alignment with the proposed DFCD Theory of Change.

Core to the Consortium's DFCD proposition is the allocation of €30m to the Origination Facility to support the creation of viable new projects to help address the climate adaptation needs of local communities in developing countries. Such projects involve local governments, civil society and businesses to turn embryonic ideas into bankable business cases. Bankable projects will be developed using landscape approaches that provide unique opportunities to build the resilience of entire ecosystems to climate change and benefit the communities and businesses that depend on them.

Under the management of WWF-NL and SNV, with extensive experience development and environmental projects and presence in more than 100 countries, the Origination Facility will aim to successfully develop 35 projects to a bankable stage. Once such projects are considered bankable, the two other partners in the Consortium, CFM and FMO, will guide these through their investment facilities, the Water Facility and the Land Use Facility. By providing debt and equity capital, the FMO and CFM managed facilities can bring such projects to sufficient levels of financial and development return, subsequently attracting other providers of capital.

With the synergetic cooperation of these three facilities, the Consortium can generate a multiplier effect, catalysing at least €500m in private finance. This structure allows the DFCD to (i) finance ca. 25 agriculture and forestry projects through FMO; (ii) to cover ca. 30 water infrastructure investments through CFM; and (iii) originate climate smart business action with strong developmental benefits through SNV and WWF's presence and partnerships in vulnerable regions and their understanding of local needs and potential solutions. Together, as shown in the Figure below, the Consortium Parties can close the funding-and-support

gap that stops private sector projects with desirable impacts graduating from early-stage idea to financing and through to completion.

Collectively, this offering allows the DFCD to provide support at all project scales, maturity stages and in many of the most vulnerable regions of the world (see Figure below). This enables the Consortium to cover the most critical investment sectors for climate resilient development while also supporting emission reductions. SNV and WWF-NL's expertise in working with the world's most vulnerable communities ensures full recognition of the deep interconnectedness between climate and development. Through integrated sets of interventions at landscape level, the Consortium will be able to draw from expertise across a wide range of high impact investment themes covering the water and sanitation, agriculture, forestry and environmental protection sectors.

Figure: Through DFCD the Consortium Parties bridge the funding gap and bring projects to financial close

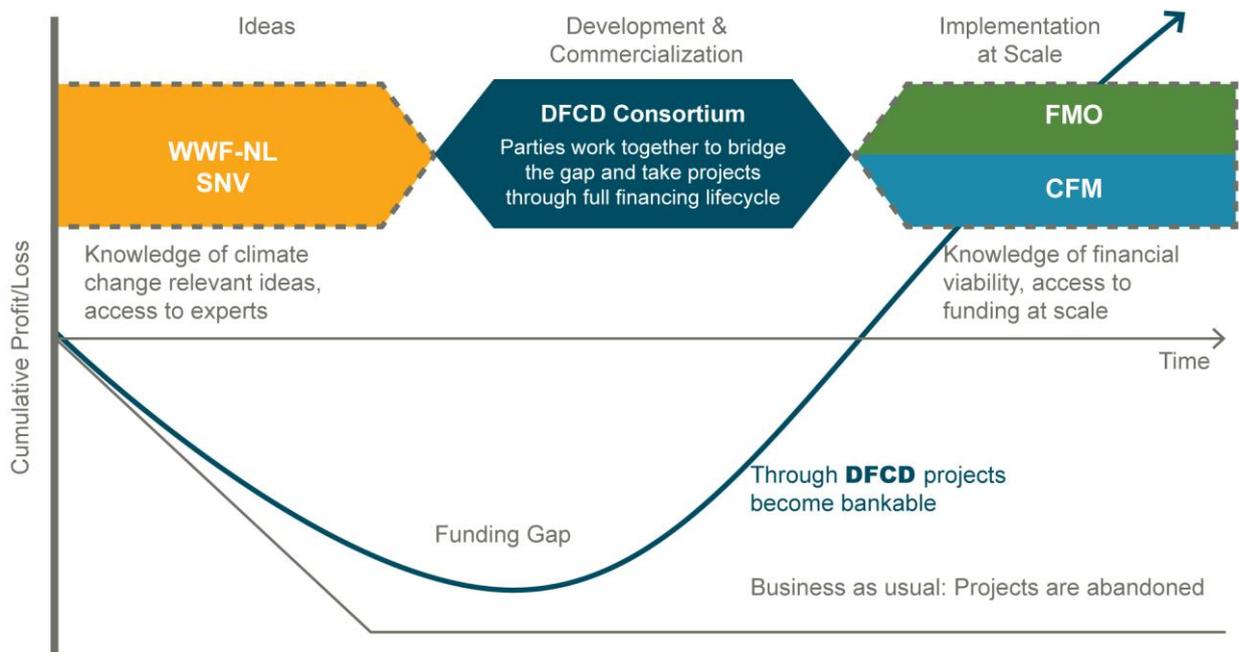
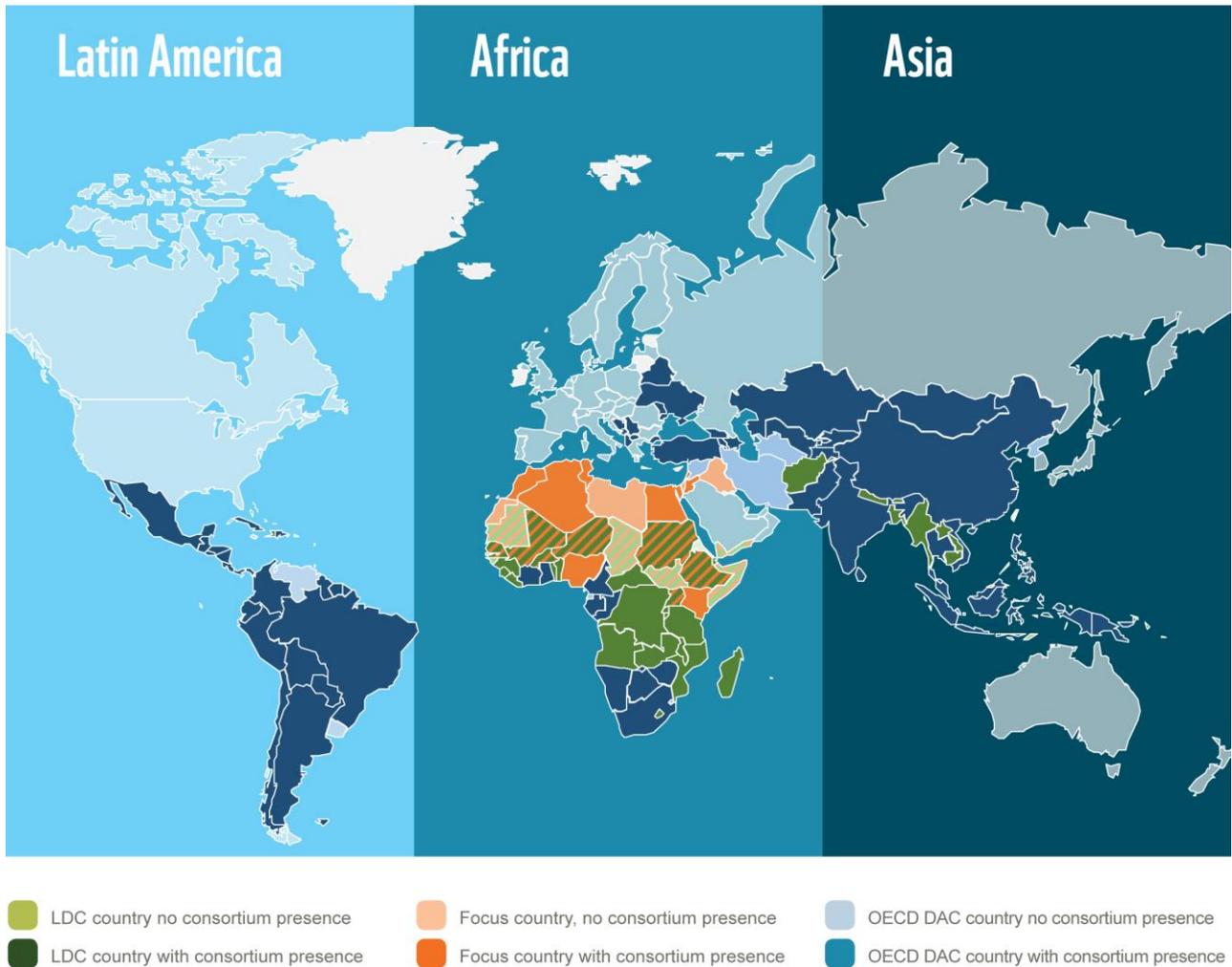


Figure: Consortium Parties' geographical presence



In addition, the proposed DFCD aligns with, and fortifies, the Dutch government's climate diplomacy.

The proposed Consortium structure for the DFCD assembles four organisations with strong international networks at global, regional and local level. At the same time, these organisations are solidly anchored in Dutch society, including in its business and investment community. This constellation provides an opportunity for the Dutch government to use the DFCD as a platform to connect global consensus forming on climate change policy to sustained local climate change action. FMO aims to strengthen that connection by (i) mutually leveraging each partner's international network, reputation, experience and expertise; (ii) designing a fund that provides support to local communities and businesses in the crucial pre-investment and project development phase; and (iii) putting scalability core and central to the design of the fund, using the power of finance to scale up what works well and meet the even higher ambition in mitigation and adaptation actions that future generations are demanding. As such, the Consortium activities will also strengthen the implementation of the nationally determined contributions of countries.

The networks of each of the Consortium Parties are robust, nationally and internationally. Relevant partnerships are visualised in the Figure below and include; (i) SNV's membership of the NDC Partnership, co-chaired by the Dutch Minister for Foreign Trade and Development Cooperation, which supports countries in achieving their commitments to the Paris Agreement. SNV also has an extensive network of private and public sector organisations in its countries of operation; (ii) FMO, is by virtue of being at the centre of the European Development Finance Institutions network, well connected to sister organisations e.g. in Germany, the UK, France and the Nordic countries as well as multi-lateral development banks like IFC, IADB, ADB and AfDB and a suite of international commercial banks. In addition, FMO is the only Dutch organisation to be an accredited entity of the Green Climate Fund and is pillar-assessed at the European Commission, greatly

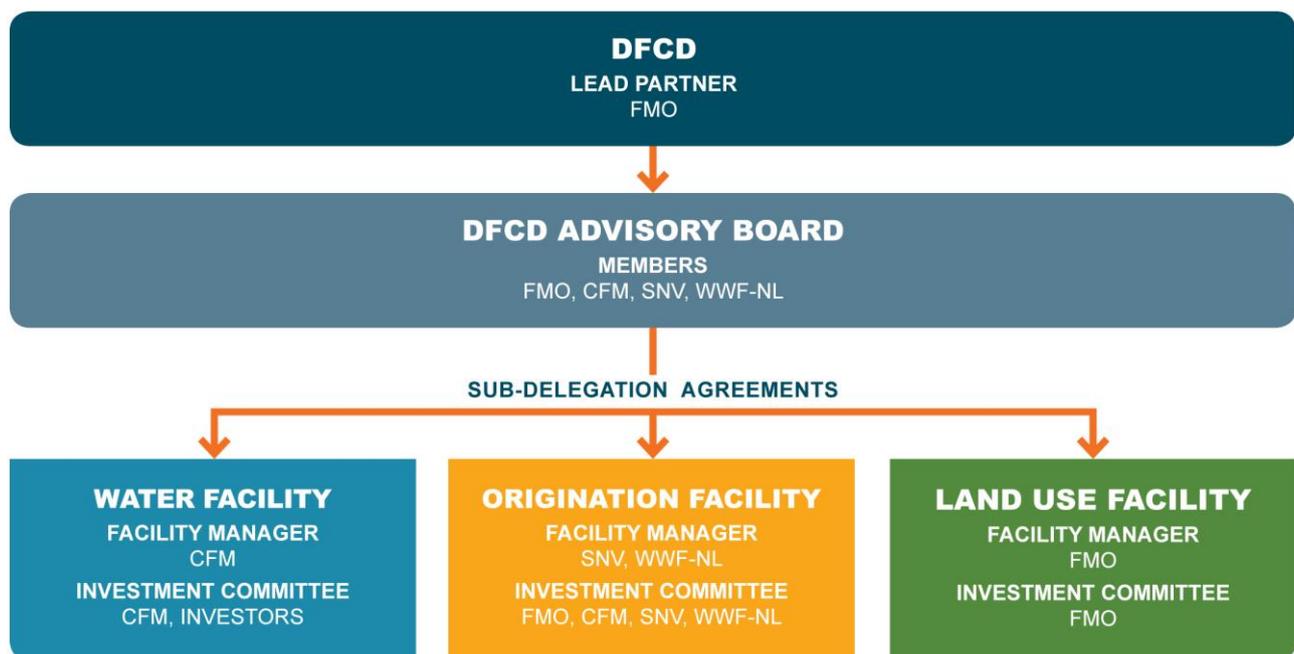
expanding the possibilities to find synergies with these large players in the climate finance arena; (iii) CFM, by virtue of the investors in Climate Investor One, has existing relationships with donors and commercial investors including the EC, GCF, USAID, and pension funds & banks; (iv) WWF is the world's largest conservation organisation, with offices in more than 80 countries and "boots-on-the-ground" projects in all of these. In addition, WWF-NL has created strong linkages with Dutch and international businesses in the field of climate and water. Its cooperation with large corporate enterprises illustrates the ability to mobilize businesses to identify climate risks and opportunities for adaptation in the communities in which these businesses are active.

The Consortium is committed to building on these networks to further increase the effectiveness of its activities. They will allow the Consortium Parties (i) to find additional public and private partners to create leverage; and (ii) to learn and share experiences and knowledge gained with others. In carrying out their work under the DFCD, the organisations will seek to ensure that all learning is widely disseminated. The Consortium Parties will actively seek to engage other Netherlands-based organisations to support the growing Dutch ecosystem of bodies supporting international climate action.

2. The DFCD fund structure: three interlinked facilities

A fund structure with three separate, but linked, fund facilities will allow each Consortium partner to build on its own expertise, while maximising synergies with the others. All Consortium Parties have strong capabilities in their respective areas of expertise and will seek to contribute to the overall DFCD objectives through separate, but linked, DFCD facilities, as presented in Figure below.

Figure: The Consortium is governed by an Advisory Council and three Investment Committees that oversee three separate but linked DFCD facilities



The proposed fund management and governance arrangements aim to maximise effectiveness and efficiency by creating only the necessary processes beyond what the four Parties already have in place. Each organisation will be responsible for an action plan for its facility, with program and investment management delegated to the facility level and an Investment Committee for each facility approving all investments. Beyond this, the governance mechanisms which ensure that the DFCD deliver on its mandate and theory of change are:

- The DFCD Advisory Board, with representatives from all four Consortium Parties, will be responsible for overall governance and tracking of results. It will be responsible for ensuring that activities are consistent with the DFCD fund mandate, strategy and theory of change. It will oversee the collaboration of the three facilities. It will also be responsible for ensuring that results are monitored and evaluated and the DFCD learns from its activities and results over time, a key feature of the Consortium.

- To ensure projects graduate from the Origination Facility, its investment committee includes representatives from the finance facilities.
- FMO, as the Consortium Lead Partner, bears final responsibility for the proper functioning of the DFCD (see below).
- All projects entering the three facilities are screened with a DFCD-wide universal Assessment Framework.

The setup with three facilities adds value through a DFCD-level *programmatic approach*². In sum, the programmatic approach has three pillars:

- *Project graduation pillar:* the Origination Facility supports business cases that can be taken forward with reduced transaction costs in the Water Facility and the Land Use Facility. The Origination Facility is expected to generate a significant part, but not all, of the pipeline of the finance facilities addressing the issue experienced by many international climate funds that there is a lack of bankable projects.³
- *Thematic focus pillar:* the four Consortium Parties will specialise in a set of water, agriculture, forestry, and environmental protection related investment sectors that link clearly to the DFCD ToC outputs, outcomes and impacts. This allows specialisation and learning within, and between, the facilities, as well as outside of the DFCD, over time.
- *Landscape pillar:* the facilities will create an integrated response at the landscape level, that adequately addresses climate impacts through synergies and de-risking between projects, and which is informed by landscape-specific climate risk studies. The target landscapes will largely be those where SNV and WWF-NL are already active, but also landscapes where CFM and FMO source projects themselves.

3. FMO as the DFCD's Lead Partner and Fund Manager

The lead party, FMO, will have ultimate responsibility for, and decision making power over, the Consortium's fund management activities through the mechanisms set out in the Consortium Agreement. This decision-making power is effected through sub-delegation agreements with CFM, SNV and WWF-NL as executing entities. The sub-delegation agreements safeguard the sub-delegated tasks to be performed in accordance with this bid document and FMO's own regulations, rules, policies, instructions and the mandate that it is managing on behalf of the public fund. Each of the FMO's Consortium Parties has extensive experience as partners in fund management consortia, in some cases with FMO, and has the necessary organisational systems and processes in place to do so effectively.

FMO has a long track record as a fund manager for Dutch government funds. With 50 years of experience in emerging markets, a balance sheet of over €8Bn, an additional €1Bn of assets under management in high impact investments in energy, infrastructure, and financial inclusion for the Dutch government, FMO is well positioned to oversee the DFCD. The existing State funds under FMO's management have demonstrated a strong mobilising effect. FMO has a strong track record on graduation of clients from government funds, such as MASSIF, to FMO's own balance sheet, as well as to other DFIs and private sector financiers.

FMO is experienced in acting as fund manager for other public entities such as the European Commission and the Green Climate Fund. As a 'pillar-assessed' entity, FMO manages the European Commission investments in Climate Investor One (€30m), AgriFI (€35m) and Electrify (€150m). FMO also manages the European Commission's stake in FMO's new risk sharing facility NASIRA. As an accredited entity of the Green Climate Fund, FMO has received board approval for a \$100m investment in Climate Investor One, Climate Fund Manager's first fund mandate.

² The Climate Investment Funds and its four programs were the first to use a programmatic national investment planning approach as their primary delivery modality. It is seen as integral to the CIF's ambition to achieve transformational change and has recently been positively evaluated (see https://www.climateinvestmentfunds.org/sites/cif_enc/files/knowledge-documents/evaluation_of_the_cif_programmatic_approach_final_report_and_management_response.pdf). The programmatic approach of the DFCD will have a thematic and geographic focus like the CIFs', but expands beyond the CIFs approach by introducing a project graduation mechanism that addresses the lack of bankable project pipeline. Like the CIFs, the DFCD will be committed to learning and sharing results, including on its programmatic approach.

³ Climate Investment Funds (2016), Climate Adaptation in Developing Countries, available at <http://www.vivideconomics.com/publications/climate-adaptation-in-developing-countries>

FMO will appoint a dedicated team for the management of DFCD that can build on the expertise of other teams within the organisation. The team will be part of FMO's Partnerships for Impact department, which manages and mobilizes third party funding from donors, Development Finance Institutions and commercial parties. The team can draw on a wide range of relevant in-house expertise across a range of departments with relevant sector expertise: Agribusiness, Food and Water, Energy, Financial Institutions, NL Business, and a Private Equity Department. It also has a strong back- and mid-office department, including a Risk Management department, a Credit department, and a Strategy department. In addition, FMO has Competence Centres for structuring more complex financing structures, such as mezzanine deals or local currency facilities, that are fully integrated in the investment process.

II. Content of the Proposal

1. Introduction to the value proposition

Managed by this Consortium of organisations with extensive and complementary expertise in environment, development and finance, the DFCD can become a fund that catalyses change in the approach to financing climate change projects, in particular adaptation projects. It will provide the Dutch government with a unique vehicle that can showcase a new way of delivering climate finance, positively contributing to global ambitions and efforts to strengthen the international response to the climate challenge. The Consortium's value proposition offers an innovative approach to the management of the DFCD, including:

- **Targeted response to barriers** impeding private sector action on climate and development throughout all stages of the project lifecycle, through a fund structure with three separate but linked fund facilities that build on different yet complementary skillsets of the Consortium Parties
- Optimal synergies between the three fund facilities through a **programmatic approach** that allows the fund to generate its own project pipeline, combine activities at the landscape level, and focus on the most critical climate investment sectors where the gaps in climate finance are greatest
- Enhancing **climate resilience of the most vulnerable groups** by applying an Assessment Framework that will identify projects that most clearly enhance the resilience of these groups to climate shocks, promote their access to natural resources, and improve their income and wellbeing
- Existing **bankable pipeline** and project leads ensuring a **rapid start to delivery of results** and **multiplication of results** over the fund lifetime as facilities are replenished with revolving funds
- A **commitment to share learning and results** to aid the international community in effective and efficient deployment of international climate finance
- **Clear Key Performance Indicators** linked to the Theory of Change to focus the fund's activities, with results of an indicative portfolio of i) 40m tons CO₂e reduced; ii) 100,000 Ha of farmland and 100,000 Ha of forest and wetland under sustainable management; iii) 12.5m people with improved access to climate resilient drinking water and sanitation; iv) 13.5m people benefitting from improved wellbeing, economic prospects and livelihoods; v); €500m of private finance mobilised (across the Fund and project levels).

This section outlines how the fund will align with the DFCD Theory of Change set out in the DFCD Grant Policy Framework. This section is structured as follows. Section below first introduces the global challenge to mobilise private finance for private sector action on climate and development and summarises the proposed DFCD response. The proposed Theory of Change is introduced in the following section and how this aligns with the outputs, outcomes and impacts of the DFCD Grant Policy Framework ToC. It then describes the programmatic approach shaping its activities, covering the precise ways in which the fund will ensure that its overall impact is maximised through a combination of the different fund facilities.

2. Addressing the challenge of climate finance mobilization

Climate finance has gained traction in recent years. The best estimates suggest that total global flows of climate-related investment in 2015/16 were 27% higher than in 2013/14.⁴ Flows are projected to increase further in the future. These financial flows have translated into real changes on the ground. After rapid investment in recent years, and hence rapid cost declines, renewable power is now the preferred technology for new electricity generation globally.⁵ The IEA reports that electric vehicles and other sustainable transport solutions are 'on track' for what is required for a Paris Agreement-aligned world.⁶ Climate finance and

⁴ CPI (2018), Global climate finance: an updated view, available at: <https://climatepolicyinitiative.org/publication/global-climate-finance-an-updated-view-2018/>

⁵ Frankfurt School-UNEP Centre/BNEF (2018), Global Trends in Renewable Energy Investment 2018, available at: <http://www.fs-unep-centre.org> and BNEF (2018), Emerging Markets Outlook, 2018, available at <http://global-climatescope.org/assets/data/reports/climatescope-2018-report-en.pdf>

⁶ IEA (2018), Electric Vehicles: Tracking Clean Energy Progress, available at <https://www.iea.org/tcep/transport/evs/>

international carbon markets have undoubtedly played a role in supporting the swift diffusion of technologies⁷ and in helping to bring down technology costs.⁸

But while some sectors and technologies demonstrate exciting progress, others are at risk of being left behind. Most notably, annual adaptation flows in developing countries are estimated to be just over \$20Bn, compared to estimates of need by 2030 of \$140-\$300Bn.⁹ Numerous reports and experiences highlight the particular challenges associated with engaging the private sector in adaptation – yet, mobilising private finance flows is critical to close the funding gap as public budgets alone are insufficient.^{10 11 12} The gap includes large investment needs in water infrastructure for which, in many developing countries, increasing water stresses from climate change necessitate large investments. In addition, forestry, land-use and climate smart agriculture investments that offer both adaptation and mitigation benefits risk being neglected by the current climate finance architecture: in 2015/16 just 2% of the climate finance spend of public bodies and DFIs was in the land-use sector.¹³

This neglect is despite evidence that climate finance in these sectors can advance the Sustainable Development Goals, including on alleviating poverty and supporting the most vulnerable groups.¹⁴ Indeed, the preamble to the Paris Agreement calls for actors that address climate change to “*respect, promote and consider their respective obligations on human rights, the right to health, the rights of indigenous peoples, local communities, migrants, children, persons with disabilities and people in vulnerable situations and the right to development, as well as gender equality, empowerment of women and intergenerational equity*”. Addressing these sectoral imbalances and maximising impact on all Sustainable Development Goals represents a key challenge for the international community, especially addressing the needs of vulnerable groups, while continuing to ensure that overall flows of climate finance increase towards the \$100bn target (and higher for the period beyond 2025). As Lord Nicholas Stern, author of the landmark Stern Review on the Economics of Climate Change (2006), has said ‘*Poverty and climate change are the two great challenges of the 21st century ... if we fail on one, we will fail on the other*’.

There is an increasing realisation that focusing on the quantity of climate finance flowing to different sectors is only part of the story. There is an increasing need to focus on developing high quality climate projects, as, for instance, emphasised during the climate negotiations at COP 24 in Katowice, Poland.¹⁵ This captures the idea that ultimately financial flows are only an input, and what matters are the outputs these flows generate, and the outcomes and impacts they facilitate. Commentators identify a number of characteristics that can indicate high quality climate finance.¹⁶ First, they may exploit innovative risk-sharing mechanisms and instruments to mitigate risk and mobilise public and private flows of finance at scale, recognising that the changes in private sector investment flows are indispensable to achieving enduring, ‘transformational’ change and that public finance on concessional terms risks distorting markets. Second, they may focus less on intervention types at the low-cost end of the marginal abatement and adaptation cost curves, but rather focus on the deployment of more difficult intervention types that are new in a certain geography or leverage new

⁷ Murphy et al. (2015), Technology transfer in the CDM: an updated analysis, Climate Policy, Volume 15, pages 127-145.

⁸ GIH (2018), Showcase Project: Noor Ouarzazate I Concentrated Solar Power Plant, Morocco, available at <https://www.gihub.org/resources/showcase-projects/noor-ouarzazate-i-concentrated-solar-power-plant/>

⁹ CPI (2018), Understanding and Increasing Finance for Climate Adaptation in Developing Countries, available at <https://climatepolicyinitiative.org/publication/understanding-and-increasing-finance-for-climate-adaptation-in-developing-countries/> Although data challenges mean that, at present, private sector flows into adaptation in developing countries are not tracked.

¹⁰ Ibid.

¹¹ Climate Investment Funds (2016), Climate Adaptation in Developing Countries, available at <http://www.vivideconomics.com/publications/climate-adaptation-in-developing-countries>

¹² WWF (2018), Banking on private finance to tackle the world’s water crisis, available at <http://wwf.panda.org/index2.cfm?336791/Banking-on-private-finance-to-tackle-the-worlds-water-crisis>

¹³ Ibid.

¹⁴ IPCC (2018), Indicative linkages between mitigation options and sustainable development using SDGs, available at https://www.ipcc.ch/site/assets/uploads/sites/2/2018/10/SPM4_19102018-724x1024.png

¹⁵ HBS (2018), Rising Public Climate Finance Flows Only Tell Part of the Story, available at <https://us.boell.org/2018/11/30/rising-public-climate-finance-flows-only-tell-part-story>

¹⁶ See, for instance, Sierra et al (2013) <https://www.brookings.edu/research/first-steps-toward-a-quality-of-climate-finance-scorecard-quoda-cf-creating-a-comparative-index-to-assess-international-climate-finance-contributions/> and E3G (2015) https://www.e3g.org/docs/E3G_Towards_an_effective_international_financial_ecosystem_for_climate_finance_010615.pdf

technology, to allow rapid learning and demonstration of viability. Third, they may demonstrate clear country ownership and alignment with stated national priorities.¹⁷ Fourth, they may have low transaction costs.

The proposed DFCD incorporates responses to these challenges in an innovative structure, tailored to provide high quality climate finance in alignment with the Grant Policy Framework's ToC. As summarised in the remainder of this section, it will do so through a programmatic approach that combines the partners' capabilities in a way that allows origination of the fund's own pipeline in a set of high-impact focus investment themes and enhance resilience in some of the most vulnerable landscapes in the world. The elements of the programmatic approach are embedded in the design of the fund's activity flow, governance, and Assessment Framework. In this way, the DFCD will provide the Dutch government with a unique vehicle that can showcase a new way of delivering climate finance and positively contribute to its global ambitions and efforts to strengthen the international response to the climate challenge.

In the first instance, the fund will focus on investment themes where there is the strongest need to demonstrate the opportunities for investment with low-carbon, climate-resilient development impact, and the role that international climate finance can play in supporting this. These focus investment themes fall within four sectors: (i) water and sanitation, (ii) climate smart agriculture, (iii) forestry, and (iv) general environmental protection.¹⁸ These investment themes have been selected because they have a direct climate impact, as highlighted by their inclusion in the *IPCC (2018) Special Report on Global Warming of 1.5 °C*. These investment themes can also effectively address the needs of vulnerable groups if contextual factors are properly accounted for. Projects that implement the investment themes will produce one or multiple outputs of the DFCD Grant Policy Framework. In water and sanitation, the themes include climate resilient drinking water and sanitation systems and industrial water management. In agriculture, they include conservation agriculture, irrigation efficiency, livestock management, agroforestry, and agricultural intensification. In forestry, they include afforestation and reforestation. In general environmental protection, it includes projects which provide adaptation responses through the restoration of natural ecosystems including wetlands and coastal mangrove forests that can enhance coastal defence and hardening.

The selection of these investment themes means that the Consortium will focus on delivering a large number of DFCD outputs, except for grid-tied renewables, transport, or energy efficiency. The Consortium has opted to prioritize the other DFCD outputs as it views their funding needs as greater, with grid-tied renewables in particular receiving substantial investment flows. These areas of focus are also consistent with the priorities of developing countries as stated in their Nationally Determined Contributions under the Paris Agreement.¹⁹

The focus on these – undoubtedly more challenging – investment themes demands a carefully crafted response that both addresses the common barriers to mobilising private sector action seen in these thematic areas, but also recognises their differentiating characteristics. The proposed DFCD structure, consisting of three separate but interlinked facilities, and harnessing the skills and international network of four organisations, delivers this. It consists of:

- An *Origination Facility (OF)*, managed by WWF-NL and SNV collectively, that will work with companies and entrepreneurs to turn embryonic ideas into bankable business cases. A lack of early stage project preparation has been repeatedly recognised²⁰ as a critical barrier to increasing investment flows. For private sector adaptation the challenges are often particular acute, as understanding of climate risks is limited and there is a need for working closely with potential project developers.²¹ The facility will develop

¹⁷ In turn, at a macro level, this relates to the earlier point regarding sectoral distribution as many developing countries perceive that their priorities are adaptation which, as described above, is currently not an area of focus for the international climate finance architecture.

¹⁸ Using the sector definition of the OECD DAC Rio Markers for Climate Handbook: https://www.oecd.org/dac/environment-development/Revised%20climate%20marker%20handbook_FINAL.pdf

¹⁹ For example, virtually all African NDCs and three quarters of South Asian NDCs mention investment needs in agriculture. More than 80% of African NDCs and 60% of South Asian NDCs recognise investment needs in water. In Africa, 60% of the \$115bn cumulative adaptation investment needs by 2030 as reported in NDCs is in water projects, and 20% in agriculture. Of the \$223bn mitigation investment needs in Africa 30% is in LULUCF/Forestry, and more than 20% in agriculture. Sourced from: <http://spappssecext.worldbank.org/sites/indc/Pages/INDCHome.aspx>

²⁰ ODI (2018), Private infrastructure financing in developing countries, available here <https://www.odi.org/sites/odi.org.uk/files/resource-documents/12366.pdf>

²¹ Climate Investment Funds (2016), Climate Adaptation in Developing Countries, available at <http://www.vivideconomics.com/publications/climate-adaptation-in-developing-countries>

projects to the stage where they can then be picked up at low transaction cost by either of the water or land use finance facilities, or undertaken by others. The OF will be managed by WWF-NL and SNV and will leverage their on-the-ground networks, especially in low-income countries. In this work the OF is also open to work with other local and international NGO's. The facility will provide grant funding and TA and will be allocated €30m of DFCD funding.

- A *Water Facility* which will focus on supporting project development and providing construction equity into water sector projects. The high capital intensity of many water infrastructure projects means that private sector capital is often unavailable for such projects. By providing risk-bearing equity capital, this facility will be able to crowd-in further investors to help ensure projects secure financing at affordable cost. It will also provide returnable grants for early to mid-stage project development support (including engineering design, contract negotiations, and full ES impact assessment), continuing early stage development activities undertaken by the OF. The construction equity fund will attract further private sector investors to leverage DFCD's investment at the fund level. It will be managed by Climate Fund Managers which has already successfully demonstrated the effectiveness of such a fund to support renewable energy infrastructure in developing countries through its Climate Investor One fund. The Water Facility will be allocated €75m of DFCD funding as seed capital for a €550m fund.
- A *Land Use Facility* which will provide a range of financial instruments to provide growth finance primarily for climate-smart agriculture and forestry projects. In these sectors, the biggest barriers to private sector investment often relate to being able to identify and structure the value proposition of the climate-related investment. The response often necessitates both technical understanding and the ability to flexibly deploy a range of financial instruments. This facility will be allocated €55m of DFCD funding and will be managed by FMO that will leverage its extensive experience in these areas.

The three facilities are collectively referred to as the Financing Facilities throughout, with the Water Facility and the Land Use Facility collectively referred to as the Investment Facilities.

This structure to deliver on DFCD's outputs and outcomes, and the wider needs of the international community for climate finance, requires close collaboration across the different parties. This will be facilitated by a common vision and set of working practices for the fund and its facilities, that collectively form its **programmatic approach**. This approach will help further bolster the ability of the fund to deliver the envisioned outputs and outcomes. It consists of three pillars as summarised in the Figure below and further elaborated in the next section. This will collectively ensure that the activities of the fund, and the projects it supports, can have a greater impact than the sum of their individual impacts.

- **Firstly, a project graduation mechanism** will reduce the transaction costs of moving projects from early stage discovery, structuring and development through to financing, construction and operationalisation. It allows the fund to efficiently generate part of its own pipeline of projects with significant climate and development outcomes.
- **Secondly, the fund will have a thematic focus** guiding its investment priorities. This will ensure that learnings from one project can be easily shared across Consortium projects, partners and more widely. It will also make it more likely that the fund's activities will attract interest from both public and private sector stakeholders seeking to understand how the projects, and the benefits they deliver, can be replicated.
- **Thirdly, the work will operate with a landscape lens.** The Consortium will focus its work in a set of landscapes in which vulnerable ecosystems and populations face an elevated risk of climate change impacts. The landscape focus provides opportunities to identify projects that amplify the impacts of others or to offset the negative impacts that a standalone project might have. For example, upstream conservation agriculture and solar irrigation efficiency projects may enhance the efficiency of downstream water treatment and drinking water supply installations. Further, by focusing on particular geographic areas, the fund complements the effect of the thematic focus in generating and disseminating lessons and gaining attention for the DFCD's work, ensuring efficiencies in sourcing project leads.

Figure: Programmatic approach across the three facilities



3. DFCD Theory of Change (ToC)

A. Impact, outputs and outcomes; secondary benefits; and Key Performance Indicators

The next figure presents the Theory of Change for the proposed Dutch Fund for Climate and Development (DFCD ToC) and how it aligns with the DFCD Grant Policy Framework Theory of Change (GPF ToC). It presents a theory of how the DFCD's inputs and activities will support outputs, outcomes and impact, as well as the key assumptions that need to be made for this theory to work in practice. The proposed DFCD ToC aims to achieve climate resilient economic growth in developing countries by addressing critical barriers to origination, financing and operation of private sector projects in the most vulnerable regions in the world. It directly advances a range of SDGs on climate, poverty, hunger and others related to human wellbeing and the environment. It will do so through the three separate, but linked, facilities that focus on critical investment themes in the water and sanitation, agriculture, forestry, and general environmental protection sectors where there are the greatest opportunities for a direct climate impact and improving development outcomes.

The core elements of the impact, outcome and output levels of the DFCD ToC match those of the GPF ToC;²² adding elements where the Consortium deems this relevant to the fund's design:²³

- At the **outcomes level**, the Consortium proposes to add an economic and human development outcome that comprises improved wellbeing, economic prospects, livelihoods and inclusion, particularly for vulnerable groups, women and children. Addressing climate change is critically linked to economic and human development, and poverty alleviation, through the effects that climate change has on the agriculture and ecosystems that poor people rely on; through the increase in probability and severity of natural hazards that disproportionately affect vulnerable people; and through its damaging impacts on

²² The DFCD Theory of Change presents the logic underpinning how fund management activities will support results with the available grant funding. Due to the wide range of activities, project types, and geographies that DFCD will support, the structure of the ToC deviates from a conventional ToC that sets out in detail the causal links between the exact activities that its proponent plans to undertake. The DFCD ToC as presented here matches the level of granularity of leading international climate funds with a similar nature to the envisioned DFCD, such as the UK-German NAMA Facility and the World Bank managed BioCarbon Fund Initiative for Sustainable Forest Landscapes.

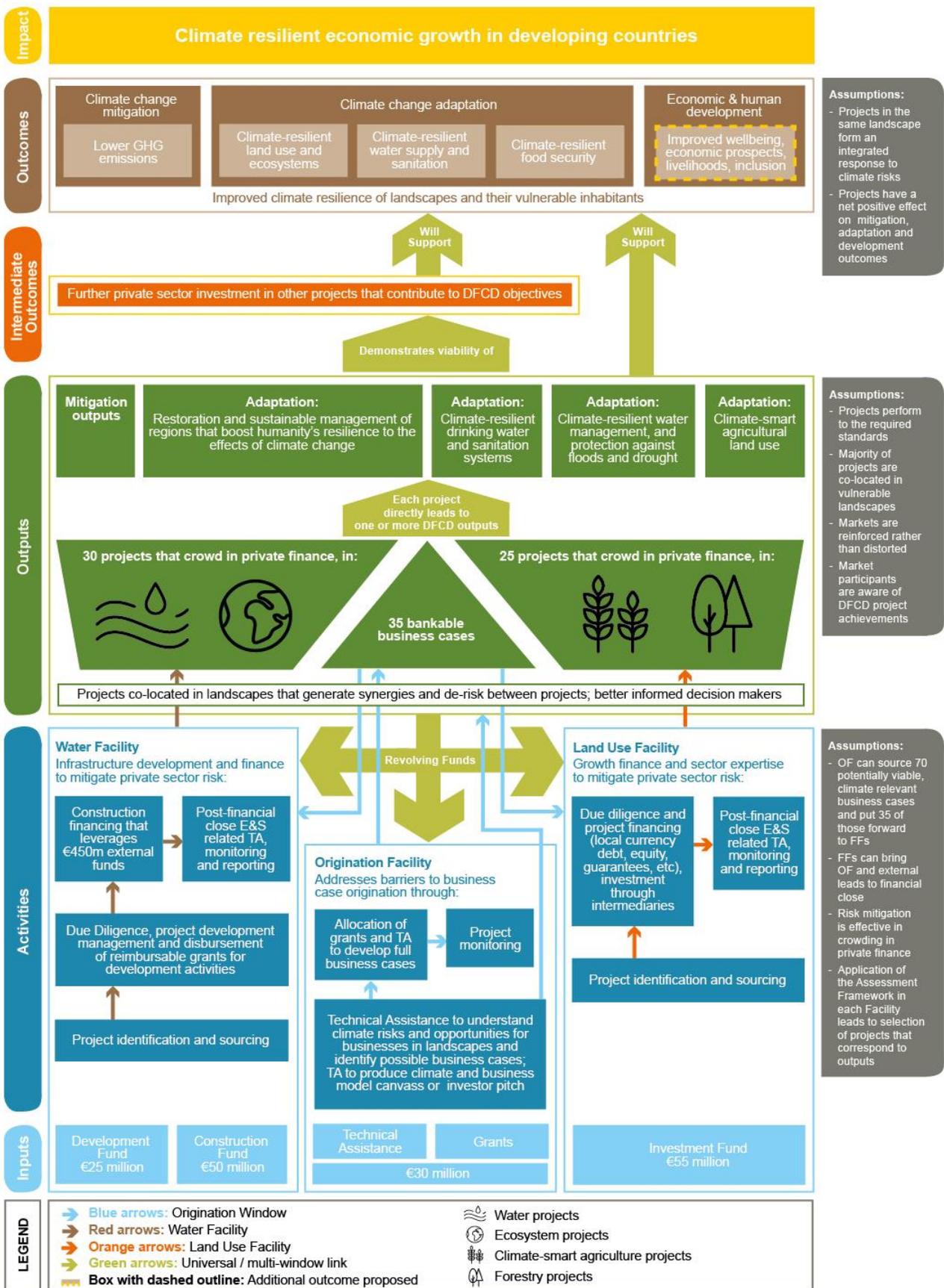
²³ The GPF ToC already describes many of the key causal relationships between the outputs, outcomes and impact layers. To avoid duplication, here the Consortium focuses primarily on the description of the causal relationships between those elements of outputs, outcomes and impact that are not covered in the GPF ToC.

human health. Building resilience to climate change is therefore essential to securing livelihoods.²⁴ The DFCD ToC also includes improvements of climate resilience at the landscape level, achieved through an integrated response across multiple DFCD projects. The key assumptions that need to hold for these outcomes to be achieved are that the DFCD outputs have a net positive contribution to mitigation, adaptation and/or development outcomes; and that projects in the same landscape interact to form an integrated response to climate risks and maximise synergies.

- An **intermediate outcome level** is added to capture a key aim of the DFCD: to demonstrate the viability of private sector action on climate and development. This demonstration effect allows the DFCD to achieve impacts beyond that which it supports directly with its projects and mobilise private finance at scale in projects with strong climate and development outcomes. The intermediate outcome requires DFCD interventions to reinforce rather than distort markets, and that market participants are aware of DFCD project achievements.
- At the **output level**, a key output from the Origination Facility is a set of 35 business cases that will be put forward for financing through the two Investment Facilities and/or can attract financing from other sources. Another key output, from the Water and Land Use Facilities, is the approximately 55 projects which the DFCD will provide financial support to in the period to 2037. The Consortium has identified focus investment themes within four Rio Markers sectors that either match or disaggregate the DFCD ToC's outputs into more specific investment options. DFCD projects are tailored to their context through taking a landscape approach including through landscape-level climate risk and opportunity assessments to inform private sector action. These studies will also involve engagement with local and national level decision makers, ensuring national ownership of the fund's work and delivering an output in the form of better informed decision makers. The delivery of these outputs assumes that projects perform to the required standards and that the majority of projects are co-located in vulnerable landscapes.

²⁴ World Bank (2016), *Shock Waves: Managing the Impacts of Climate Change on Poverty*, Washington DC, available at <https://openknowledge.worldbank.org/handle/10986/22787>

Figure: Theory of Change for the Dutch Fund for Climate and Development



The Consortium will build on a healthy, continuously expanding, pipeline that allows a rapid start, while impacts will be maximised through revolving funds that allow the initial capital to go further. The Consortium Parties have a significant pipeline of projects across all stages of the project lifecycle that can be taken forward under the DFCD upon commencement. This pipeline is continuously expanding through the parties strong existing networks and activities in some of the most vulnerable landscapes in the world and will be further strengthened by the activities of the Origination Facility. The revolvability of many of the Facilities through reimbursable grants, debt, equity and guarantees allows new activities to continue to be financed. The Consortium anticipates that Investment Facilities revolve 2-3x over the lifetime of the DFCD.

Results of an indicative DFCD portfolio against a set of Key Performance Indicators that capture some of the key elements of the ToC are presented in the Table below.

Table: Projected DFCD portfolio against Key Performance Indicators

Key Performance Indicator	Indicative Portfolio Result
Reduced or avoided GHG emissions in tonnes	40m tons CO _{2e}
Hectares of farmland under sustainable management improving resilience to climate change and shocks	100,000 Ha
Number of people (sex disaggregated) with improved access to climate resilient services for drinking water and sanitation	12.5m people
Hectares of forest and wetland under sustainable management or other improved practices, contributing to increased adaptive capacity of ecosystems and livelihoods against climate change and shocks	100,000 Ha
Value of direct private finance mobilised	€500,000,000
Total number of people (sex and vulnerable group disaggregated) benefitting from improved wellbeing, economic prospects, livelihoods	13.5m people

In addition to the outcomes and impact of the DFCD depicted in the ToC diagram, the fund will generate a range of other benefits, most notably including:

- **Contributions to all SDGs.** The SDGs are deeply interconnected; business action on one SDG can impact a range of other SDGs, both through synergies and potential negative impacts (trade-offs).²⁵ The assessment framework for project selection together with the DFCD support throughout the project lifecycle, ensures that DFCD projects will maximise synergies with all SDGs, including those that are not the primary target of the interventions. The landscape approach also allows any potentially negative trade-offs from individual projects, such as water pollution from agricultural projects and increased local food prices from land use change, to be mitigated through complementary projects in the same landscape and the technical assistance that all fund facilities provide.
- **Business cases reaching financial close without Water or Land Use Facility support.** Business case development supported through the Origination Facility or the Water Facility may not always reach financial close with DFCD investment. However, the support provided by DFCD will still bring companies a step further to receiving other financing. This, and the associated outcomes of these projects, are not accounted for in the DFCD ToC but constitute a significant secondary benefit of the fund's activities.
- **Increased export competitiveness of Dutch business.** The DFCD will invest primarily in themes that have a clear link to two core strengths of the Dutch economy: water management and agriculture. The Netherlands-based Consortium Parties will seek to leverage the capabilities of the Dutch water and agricultural sectors in their efforts where possible, which they have already done successfully in previous work.²⁶

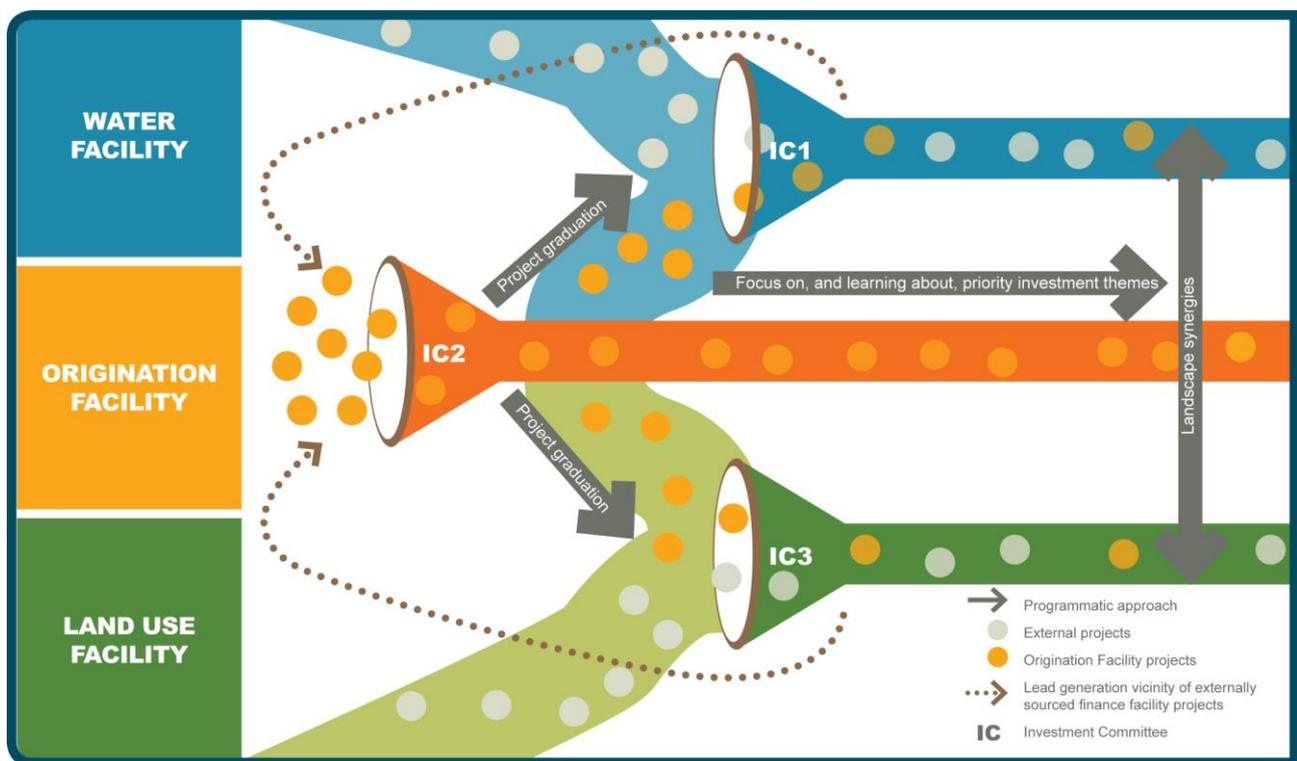
²⁵ UN Global Compact (2017), Blueprint for Business Leadership on the SDGs, available at <https://www.unglobalcompact.org/library/5461>

²⁶ For example, FMO has a dedicated NL business department and a strong track record in engaging Dutch companies in its development financing activities. CFM expect to partner with new financing partners, particularly large Dutch construction companies, Dutch pension funds, Dutch family offices and Dutch institutional investors. SNV has engaged Dutch knowledge providers such as Wageningen University in some of its flagship adaptation-related programs in climate smart agriculture. WWF is active in key Dutch initiatives profiling the water sector abroad, such as the Valuing Water Initiative. Some of the landscapes that the fund will operate in,

4. A programmatic approach

The fund will adopt a **programmatic approach** to its activities to provide a targeted response to barriers and integrating the three fund facilities to achieve greater results. The programmatic approach ensures that the combination of the facilities provides high quality climate finance, generating an impact that is greater than the sum of its parts, by promoting cost effective project graduation, specialisation and learning on high impact investment themes. As explained above, the programmatic approach has three pillars. This section describes how the programmatic approach guides the DFCD's activities through each of the three pillars. Figure 9 illustrates the flow of OF-sourced projects and externally sourced projects by the finance facilities over time and how the programmatic approach underpins the effectiveness of the fund's activities.

Figure 9 The project flow in the Fund



Note: IC = Investment Committee. Explanation: Each facility operates with a DFCD universal assessment framework for a pass/fail screen at intake and their own assessment frameworks for full assessment, as represented by the three funnels, to be overseen by investment committees IC1, IC2, and IC3 respectively. Blue dots represent projects sourced through the Origination Facility. Origination Facility business cases might be forwarded to the finance facilities (expected to be around half of 70 supported business cases) or be developed without finance facility support as stand-alone projects with complementarities to other fund projects in the same landscapes. At the same time, the finance facilities will also source projects externally as represented by the orange dots. Over time, the share of total live projects sourced from the fund's Origination Facility is expected to increase. At the same time, some of the externally sourced projects in the finance facilities might help generate new leads for the Origination Facility in these projects' vicinities, as indicated by the dotted arrows.

This section elaborates each of the three pillars further below.

such as the Mekong Delta, are already export destinations for Dutch companies, including for the water technology sector in which the DFCD will be active. The secondary benefits for Dutch export competitiveness resulting from DFCD efforts are a notable expected outcome.

A. Project graduation pillar

The Figure below shows the overarching principles of how the three facilities and the project graduation pillar collectively respond to the key barriers to origination and financing throughout the project lifecycle. The Consortium has identified five key steps in a project's lifecycle. The responses to the barriers presented in Figure 10 will be tailored to reflect the needs of the recipient and build on the decades of collective experience of the Consortium Parties, as well as international evidence and learning, on what makes high quality climate finance that delivers climate and development outcomes²⁷.

²⁷ IPCC (2018), Special Report: Global Warming of 1.5 °C, Chapter 4, available at <https://www.ipcc.ch/sr15/>

OECD (2018), Making Blended Finance Work for the Sustainable Development Goals, available at <https://dx.doi.org/10.1787/9789264288768-en>

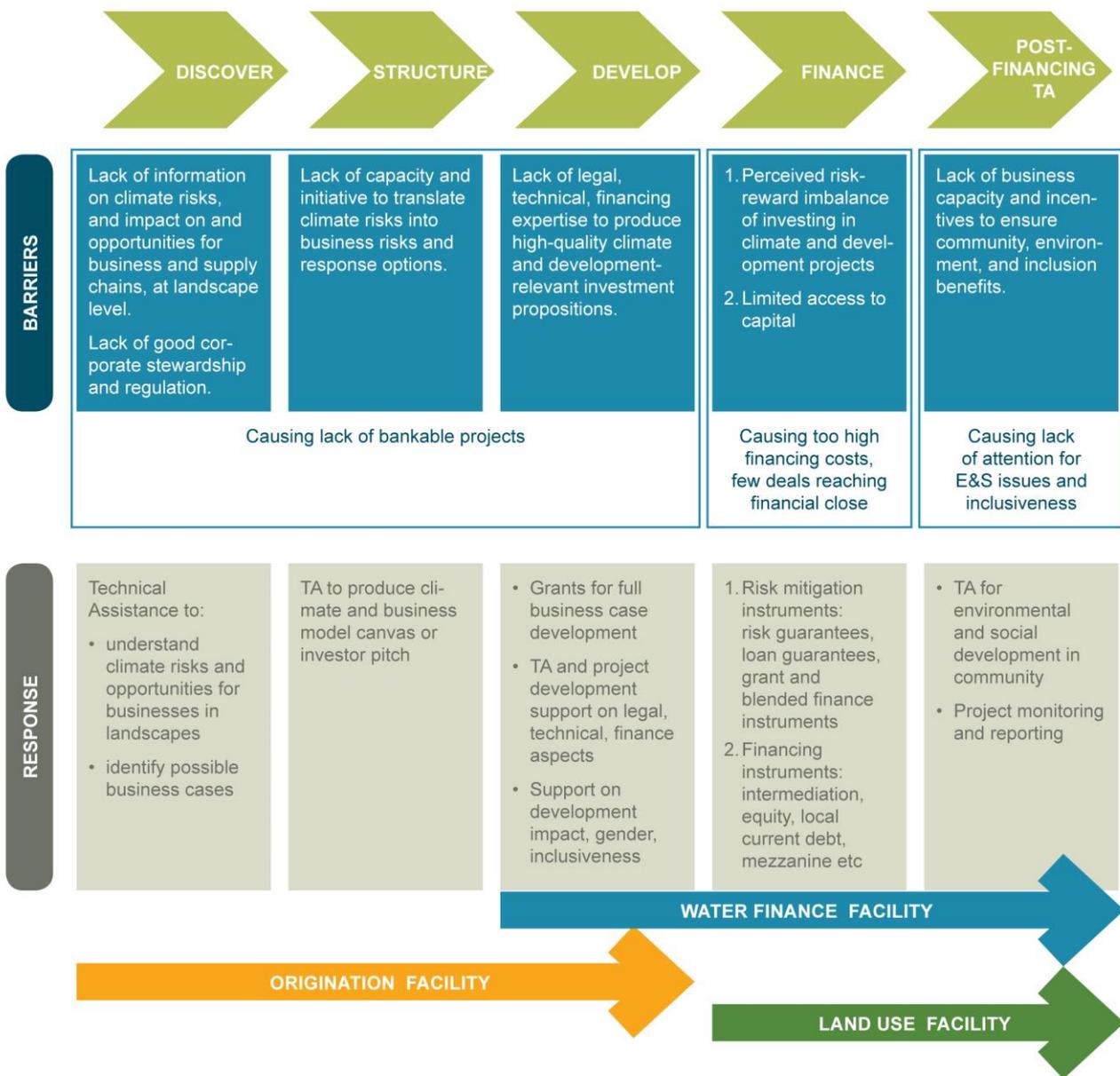
Climate Investment Funds (2016), Climate Adaptation in Developing Countries, available at <http://www.vivideconomics.com/publications/climate-adaptation-in-developing-countries>

CCFLA (2018), Summary of Good Practice of Successful Project Preparation Facilities, available at <https://worldcongress2018.iclei.org/wp-content/uploads/Summary-of-good-practice-of-successful-project-preparation-facilities.pdf>

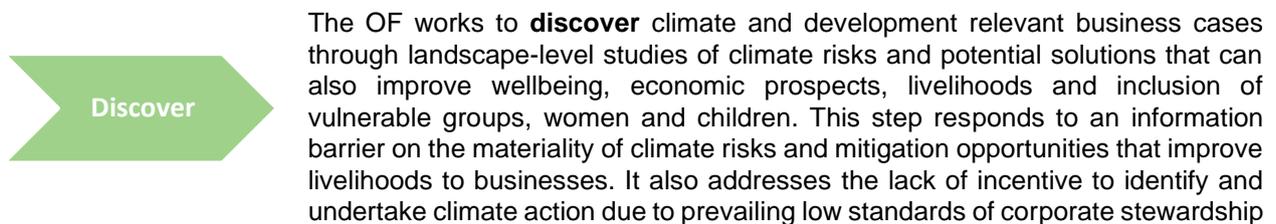
ODI (2018), Clean energy project preparation facilities: Mapping the global landscape, available at <https://www.odi.org/sites/odi.org.uk/files/resource-documents/12504.pdf>

The Nature Conservancy (2012), Climate Finance Readiness Lessons Learned in Developing Countries, available at <https://www.nature.org/media/climatechange/climate-finance-readiness.pdf>

Figure: The DFCD project graduation pillar ensures a targeted response to project origination and financing barriers²⁸



The barriers along the stages of the project lifecycle and the response provided by each facility is further elaborated below:



²⁸ This approach allows the DFCD to be “a key enabler of innovative projects, for instance by means of providing technical assistance or mitigating (perceived) investment risks, while private financiers can ensure economic sustainability and economies of scale” and ensure “mobilising private finance and cofinancing” while, by limiting the response to effectively targeting the binding constraints to private sector action, making sure that “the finance is additional to the market and does not distort (local) markets” (quotes from DFCD Grant Policy Framework).

and lenient or absent government regulation. The OF will be sector-neutral and operate across all investment themes, with WWF-NL mostly focusing on projects that address water and sanitation and ecosystem related challenges, and SNV on projects that address some of the critical challenges around social and environmental development in agriculture and forestry.

Structure

The OF helps businesses **structure** bankable business cases with a range of business planning and management tools. This addresses a barrier of low capacity and limited incentives in organisations to assess options to mitigate climate risks and harness climate-related opportunities in a gender-inclusive way. The support is offered to businesses and, on condition that they can ultimately demonstrate financial sustainability. The OF is also open to projects proposed by local and international CSOs and NGOs that contribute to this objective. Alongside their role in the investment committee of the OF, CFM and FMO will co-ordinate with the OF to provide advice on structuring bankable business cases, in order to maximize the probability that a project will graduate to the next stage.

Develop

The OF supports **development** of full business cases that are assessed and selected for their potential to deliver the DFCD outcomes and impact. This involves an in-depth assessment of a specific (set of) response option(s), that can be put forward to a Finance Facility. Development support may also be supported by grants that are capped at a maximum of 49% of the costs of business case development.

The Water Facility carries out project development activities in parallel with the OF, as water infrastructure projects often require a specific set of skills and expertise that CFM has in-house and can deliver effectively alongside, or subsequently, to the OF managers' support. The Facility will extend returnable grants for technical, legal, E&S risk assessment, and financial structuring support for development of more mature projects for which a lack of capacity in these areas is a barrier to reaching financial close.

Finance

At the **finance** step, the Water Facility takes equity positions in graduating or externally sourced projects, and provides an all-equity financing solution for the entire project's costs. It focused on water infrastructure companies' projects at the construction stage to address a barrier in the form of limited access to capital, to ensure adoption of best available technologies for achieving climate outcomes and maximising environmental and social co-benefits. A full equity offering reduces transaction costs that are typically associated with financing structures, including debt instruments and multiple financiers. Its activities will leverage private finance at the project level through mitigating (1) technical risks through its dedicated team of engineers; (2) legal risks through legal experts; and (3) financial risks by taking equity positions in projects at the construction stage, which private investors perceive to be risky. The construction equity fund will also crowd in private sector finance at the Fund level through CFM's ability to blend donor finance with private investments to create a tiered finance pool several times larger than the DFCD fund. CFM targets a €550m total fund.

The Land Use Facility will deploy a range of instruments at the finance stage to support the growth ambitions of projects that are being put forward by the Origination Facility or sourced externally. The Facility will focus on projects in the agriculture and forestry sectors but may also invest in other projects, such as in conservation and ecosystem restoration, if these contribute to an integrated response to climate risks in a landscape where a Consortium partner is already active. The Facility's instruments will include debt, equity, mezzanine financing, currency facilities, and guarantees. To support projects that are too small (below EUR 1 million) for direct financial support under FMO management, FMO will use its brokerage role to connect to an aggregator or other financial intermediary. FMO will address technical risk by accompanying its financial offering with

technical support from its in-house teams of sector specialists. As these resources will target a greater number of projects than can be financed through the DFCD, FMO will also deliver outcomes through applying its own funds to scale up promising projects, both directly and through financial intermediation.



Provision of **post-financing Technical Assistance (TA)** by both finance facilities will ensure that supported projects continue to deliver benefits. Often, project proponents lack the capacity and/or capabilities to ensure that environmental and social benefits extend in the project surroundings. FMO and CFM can support businesses to ensure these benefits materialise through technical assistance programs. Technical Assistance to address this barrier will be delivered by one, or a combination, of the finance facility managers, OF managers (which may generate efficiencies due to their prior engagement with these businesses), and external contractors.

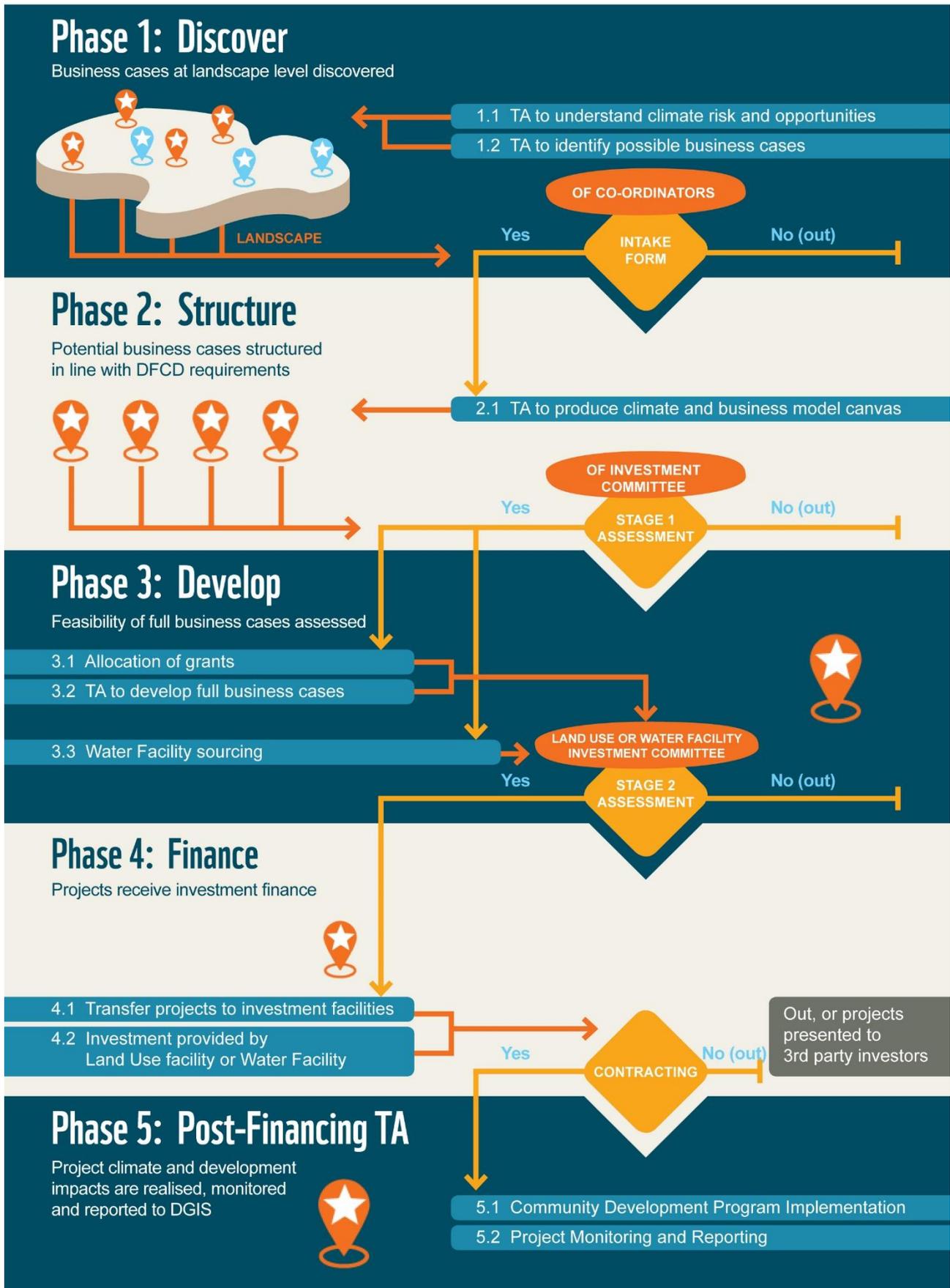
A key feature of the project graduation pillar is that it reduces transaction costs between the 5 steps of the project lifecycle by committing to standardised processes and modes of collaboration. This pillar thus addresses one of the key challenges to deploying capital that has been identified by other climate finance funds, which is that good projects often do not reach commercial viability.³⁰ This achieved in two key ways:

- **Streamlined processes:** The next Figure presents the process that a typical DFCD project follows through the 5 steps of the project lifecycle. The process chart indicates the 5 steps of the lifecycle with the process flow, types of support offered along the way, decision moments, Investment Committee oversight, and key outputs in standardised formats. The exact approach that different facility managers take to operationalising their support in the different steps can vary, to allow each manager to tailor support to the exact needs of recipients and leverage their existing proven tools and approaches. But the agreement on the project graduation flow with key decision points, allocation of decision making responsibilities to facility management and Investment Committees, and the application of a universal Assessment Framework will ensure that barriers hampering graduation are addressed from the earliest stages of the project lifecycle and do not require resource intensive additional efforts.
- **Embedded cross-facility collaboration:** the three facilities will, informally and formally, collaborate in their respective activities to ensure that projects in the earlier stages are likely to meet expectations in later stages. The main formal arrangement is that the Investment Committee of the Origination Facility includes a representative from each of the finance facilities, to support decision making that maximises the probability of a complete project graduation cycle. The Consortium Parties will also bring each other into activities for which they are well placed to assist. For example, CFM and FMO staff will advise WWF-NL and SNV on their project and financial structuring support to increase the likelihood that the finance facilities can take these projects on. Further cross-Consortium learning and collaboration may include WWF-NL and SNV helping CFM and FMO to maximise the development impact of their finance activities and through their post-financing TA, for example through support for smallholder farmers to help them transition to climate-smart agricultural practices. These modes of collaboration all further reduce transaction costs between the 5 stages.

The graduation pillar will also help efficiently move more mature project leads to completion. Each facility includes an option to fast-track or externally source promising project leads to ensure that the DFCD will have sufficient pipeline and funds to be disbursed within the required time period. The OF has explicitly designed a 'short track' that takes in existing, and more mature, business cases that address climate and development challenges in focus landscapes, to fast track them through the process and put them forward to the finance facilities. The finance facilities are also open to external projects that do not come through the OF. These externally identified projects will be assessed using the DFCD's universal first stage assessment framework. These projects may also benefit from support from the OF managers. For example, an external water project lead that receives project development support from CFM may also benefit from WWF-NL's technical assistance.

³⁰ Climate Investment Funds (2016), *Climate Adaptation in Developing Countries*, available at <http://www.vivideconomics.com/publications/climate-adaptation-in-developing-countries>

Figure: DFCD processes through the 5 steps in the project lifecycle



B. Thematic focus pillar

The Consortium will support projects in four sectors that align with a set of high-impact, evidence based investment themes in which climate mitigation or adaptation is a principal objective and that deliver the DFCD ToC outputs. A broad range of investment activities can help to achieve climate adaptation and mitigation objectives. To maximise the Consortium’s impact, an analysis of critical investment sectors has been undertaken to inform its investment strategy. Considering that the bulk of global climate investments has been directed to mitigation – mostly grid-connected, renewable power – a focus has been placed on themes in which DFCD investments could provide strong additionality, especially on adaptation. These fall within the Rio Marker sectors Water and Sanitation, Agriculture, Forestry, and General Environmental Protection, as depicted in the Figure below. Within each of these sectors, the Consortium will focus on a set of high impact investment themes, identified by the *IPCC (2018) Special Report on Global Warming of 1.5 °C* as constituting effective climate adaptation and mitigation action across vulnerable regions if contextual factors are properly accounted for. These investment themes will deliver DFCD outputs, as shown in the matrix of the Figure “DFCD priority investment themes within relevant Rio Marker sectors can deliver the DFCD outputs”. This set of investment themes is indicative of where the Consortium anticipates the bulk of DFCD funds to be invested and comprise those for which there is a strong evidence base that projects within the theme can constitute effective context-specific climate action with development impact; and in which there are critical needs in some of the most vulnerable regions of the world.

Figure: Consortium coverage of key OECD Rio Marker sectors for climate adaptation



Figure: DFCD priority investment themes within relevant Rio Marker sectors can deliver the DFCD outputs

DFCD OUTCOMES	DFCD OUTPUTS	OECD RIO MARKER SECTORS			
		WATER & SANITATION	ENVIRONMENTAL PROTECTION	FORESTRY	AGRICULTURE
LOWER GREENHOUSE GAS EMISSIONS	Investment in use of and access to renewable energy	<ul style="list-style-type: none"> Water & sanitation systems (including waste-to-energy) 	<ul style="list-style-type: none"> Water & sanitation (ecosystem restoration & head-water protection) 		<ul style="list-style-type: none"> Irrigation efficiency (including solar mini-grids)
	Sustainable carbon storage in and restoration of carbon sinks such as forests, peatlands & tropical rainforests		<ul style="list-style-type: none"> Coastal defence and hardening (including wetland restoration and other ecosystem based adaptation activities) Biosphere protection 	<ul style="list-style-type: none"> Afforestation & reforestation 	<ul style="list-style-type: none"> Agroforestry Sustainable intensification
CLIMATE-RESILIENT LAND USE & ECOSYSTEMS	Restoration & sustainable management of regions that boost humanity's resilience to the effects of climate change		<ul style="list-style-type: none"> Coastal defence & hardening (including wetland restoration and other ecosystem based adaptation activities) Flood prevention & control Biosphere protection 	<ul style="list-style-type: none"> Afforestation & reforestation 	<ul style="list-style-type: none"> Agroforestry
CLIMATE-RESILIENT WATER SUPPLY & SANITATION	Climate-resilient drinking water & sanitation systems	<ul style="list-style-type: none"> Water & sanitation systems (industrial & municipal) 			
	Climate-resilient water management, & protection against floods and drought	<ul style="list-style-type: none"> Climate resilient water management (industrial & municipal; and including headwater and floodplain management) 	<ul style="list-style-type: none"> Coastal defence & hardening (including wetland restoration and other ecosystem based adaptation activities) Climate resilient water management (including head water and floodplain management) Flood prevention and control Biosphere protection 		<ul style="list-style-type: none"> Irrigation efficiency
CLIMATE-RESILIENT FOOD SECURITY	Climate-smart agricultural land use		<ul style="list-style-type: none"> Biosphere protection 		<ul style="list-style-type: none"> Agroforestry Irrigation efficiency Sustainable intensification Livestock management Conservation agriculture

A summary of the investment themes that will guide the Consortium's project selection follows below:

Water and Sanitation

Expected number of projects in indicative portfolio: 20 (€75m total investment)

Water and sanitation span the broad range of measures that contribute to improved water management, supply, and access. Activities in this area look to address the increasing frequency and severity of droughts imposed by climate change that effect water systems under stress. This is a critical issue given that today more than half the world's population, roughly 4.3Bn people, live in areas where demand for water resources outstrips sustainable supply for at least part of the year³¹. Investment in this theme includes wastewater treatment and recycling which encompasses a range of processes used to reuse wastewater (including for energy use through biogas extraction and waste-to-energy) or allow it to be safely returned to the environment. It also includes

³¹ New Climate Economy (2018), *Unlocking the Inclusive Growth Story of the 21st Century: Accelerating Climate Action in Urgent Times*, available at <https://newclimateeconomy.report/2018/>

measures to improve efficiency and wastewater discharge in an industrial context and conservation that promotes natural ecosystem services. These investments can help to strengthen climate resilience through improving water security and its flow on effects for food production and economic wellbeing. It can also contribute to climate change mitigation where investments support new sources of electricity generation. Investments in restoration of wetlands and forests will significantly enhance the climate resilience of water supply systems. As such, ecosystem investments can bolster the financial viability of water supply systems in their vicinity – a co-benefit that the Consortium will seek to exploit through its landscape approach so as to make water projects more bankable.

The World Bank estimates that the annual adaptation costs for industrial and municipal raw water supply³² in developing countries will be around \$19Bn per year in the period 2010-2050, varying slightly according to different scenarios of how climate change affects the hydrological system³³. The highest costs are in Sub-Saharan Africa where they range from \$6.2 to 7.6Bn annually depending on the climate scenario. Latin America and the Caribbean region also require high investment in all scenarios (\$2.9 – 5.3Bn per year), while South Asia requires high investment in a dry scenario (\$5.9Bn).

The Consortium has a depth of experience in water and sanitation projects that includes water basin management - for instance in Zambia's Kafue Flats and the Lower Zambezi in Mozambique, and investments in drinking water supply, sanitation systems, and Integrated Water Resources Management (IWRM) such as SNV's OmiDelta involvement in Benin.

Other examples of investments in this space include the public-private partnership (PPP) that was formed to address wastewater treatment and reuse in Cairo, Egypt. Drinking water shortages are a pressing issue in Egypt, and climate change will exacerbate this, particularly in very densely populated areas. The existing wastewater treatment infrastructure in Cairo did not produce water with adequate levels of quality to enable the water to be used to irrigate agricultural and urban green areas, forcing the city's limited freshwater supply to be used instead. To address this, the government joined forces with the private sector to build new infrastructure to reuse urban wastewater for the purposes mentioned, thereby reducing freshwater use. The result was the construction of the New Cairo wastewater treatment plant with capacity to treat 250,000m³ of water daily and serve some 1m Cairo residents. In addition, the project reduced the water pollutants entering the River Nile so also had a considerable environmental impact on the surrounding environs.

Agriculture

Expected number of projects in indicative portfolio: 15 (€60m total investment)

Investments in agriculture present a broad range of opportunities for both climate adaptation and mitigation that contribute to more resilient economic growth. It is therefore a key sector, as outlined under the Rio Marker 2 categories, and can be divided into several more specific areas of activity. The Consortium proposes to work across a subset of these where the opportunities and need are deemed to be greatest. This includes the following key investment themes:

- **Conservation agriculture (CA):** CA spans a broad range of measures (e.g. crop rotation, cover crops, reduced tillage) that help to prevent losses of arable land threatened by reduced precipitation and water overuse. It also enhances biodiversity and natural biological processes above and below the ground surface, which contribute to increased water and nutrient use efficiency. CA can therefore not only support improved efficiency, sustainability and crop yields, but also labour savings and reduced production costs. Through the reduction of fuel use, CA can also contribute to climate change mitigation. Adoption of CA in developing countries is currently limited but has significant potential, especially in Eastern/Southern Africa and Asia where: (1) the cost of energy for farming operations is increasing; (2) the area affected by erosion is expanding; and (3) climate change is making water availability more critical³⁴. An example of the Consortium's work in this area includes SNV's climate smart agriculture projects across Kenya, Tanzania, and Uganda
- **Sustainable intensification of agriculture:** Sustainable intensification looks to increase the productivity of land and water resources in the production of food. It covers a broad range of measures including use of improved crop varieties and breeds, more efficient use of labor, and better farm management. It primarily supports climate resilience by responding to the effects of climate change on water availability. It also contributes to mitigation through limiting deforestation for agricultural purposes, particularly when combined

³² Costs of adaptation are defined as the cost of providing enough raw water to restore future industrial and municipal water demand to the levels that would have existed without climate change.

³³ World Bank (2010), *The Cost to Developing Countries of Adapting to Climate Change*, available at <http://siteresources.worldbank.org/EXTCC/Resources/EACC-june2010.pdf>

³⁴ Baudron et al. (2015), *Where to Target Conservation Agriculture for African Smallholders? How to Overcome Challenges Associated with its Implementation? Experience from Eastern and Southern Africa*, *Environments*, Volume 2, Issue 3, available at <https://www.mdpi.com/2076-3298/2/3/338>

with REDD initiatives. Investment needs here are particularly acute in Africa where food production per person fell from the 1970s and only recovered to the 1960 level in 2005.

- **Improved livestock management:** Livestock management looks to address the challenges posed by scarcer water resources, land degradation and increasing agricultural GHG emissions. Interventions include the promotion of better-quality feed and feed balancing to increase productivity and lower manure emissions, improved breeding and animal health, and improved manure management practices. Besides contributions to emission reductions, investments in this area are critical to improving food security and building resilience to climate change for family farms. An estimated 1Bn poor depend on livestock for food and income, thus animals' ability to adapt to marginal conditions and withstand climate shocks is critical.³⁵ South Asia, sub-Saharan Africa, Latin America, and Southeast Asia are areas of particular need in this regard.
- **Irrigation efficiency:** Investments in irrigation efficiency look to address the challenges of scarcer water resources caused by reduced precipitation and overuse. Improving efficiency in this area can lift gross crop yields and boost food security. It can also enhance crop quality, conserve nitrate groundwater concentration, save energy, and reduce greenhouse gas emissions. At a global level there are extensive needs and opportunities for irrigation efficiency. This particularly includes central, south, and Southeast Asia where efficiency values average less than 30%, driven by their high shares of surface irrigation used for rice cultivation. The World Bank estimates that between 2010-2050 \$2.4Bn annually needs to be focused on irrigation efficiency, mostly in South Asia (\$1.1Bn), East Asia and the Pacific (\$0.8Bn).
- **Agroforestry:** Agroforestry is one of a wide range of approaches for restoring degraded forests and agricultural lands, thereby contributing to landscape restoration. Broadly, agroforestry has been defined as systems where trees interact with agriculture. Agroforestry systems can involve a number of land management practices, including crop diversification, long rotation systems for soil conservation, boundary plantings, perennial crops, hedgerow intercropping, live fences, and improved fallows. Examples of such projects and the Consortium's experience in this area include FMO's involvement in the Miro Forestry project (see below section for further details) in Ghana and Sierra Leone. According to an estimate by the IPCC, 630 m ha of unproductive crop lands and grasslands could be converted into agroforestry worldwide. While more than 80% of agricultural areas of Central and South America and South East Asia can already be classified as agroforestry, there is still large potential in regions such as Eastern/ Southern Africa (around 40% of adoption) and North/ West Africa (between 20 and 30% of adoption).

Forestry

Expected number of projects in indicative portfolio: 10 (€70m total investment)

Forestry related projects cover a broad range of activities that primarily focus on afforestation and reforestation. Afforestation implies planting trees on land not forested for a long time (e.g. over the last 50 years in the context of the Kyoto Protocol), while reforestation implies re-establishment of forest formations after a temporary condition with reduced canopy cover due to human induced or natural perturbations. Projects focussed on afforestation and reforestation can serve to mitigate and manage the effects of climate change. Most notably, forestry projects can contribute to climate change mitigation by capturing ('biosequestering') atmospheric carbon and locking it into the living and dead biomass in the ecosystem (e.g. tree biomass, soil organic carbon). They can also however contribute to watershed services (e.g. soil erosion control, soil fertility improvement, flood control, ground water recharge, water quality) and land resource productivity by combatting desertification and controlling salinity. These benefits can help to improve climate change resilience and support development outcomes through increased availability of forestry-related resources (e.g. timber, fuel wood, fibre, fodder, fruits, flowers, gum, resin, honey, wax) and new or secured business opportunities such as ecotourism and carbon revenue.

The bulk of these opportunities in developing countries are concentrated in Sub-Saharan Africa, South America and South/ Southeast Asia. In Africa, the United Nations is spearheading the Great Green Wall project – an ambitious plan to plant a wall of forest stretching across the width of the continent just south of the Sahara Desert. Additionally, 56 countries, many from central and South America and central Africa, have pledged to restore 350m hectares of forest by 2030, under the Bonn Challenge. The Bonn Challenge was launched in 2011 by the German government and International Union for the Conservation of Nature (IUCN) and anticipates that countries will follow a forest landscape restoration approach. This involves turning agricultural or pastoral land into forests by planting new trees. Significant investment is required if countries are to meet their targets against these initiatives.

³⁵ FAO (2019), *Climate Change and the Global Dairy Cattle Sector: The Role of the Dairy Sector in A Low-Carbon Future*, available at <http://www.fao.org/3/CA2929EN/ca2929en.pdf>

The Miro Forestry project provides a good example of the investment opportunities in this area. Miro is one of the largest forestry plantation companies in West Africa, with currently 10,000 ha planted (5,966 ha in Ghana / 4,115 ha in Sierra Leone). Through investments from FMO, it has grown its total land bank to ~32.000 ha (including about 10% high conservation land). This has supported Miro to develop and manage high quality, cost competitive, FSC certified, fast growing industrial timber species (mainly eucalyptus/acacia) and to begin establishing the respective downstream production facilities and market entries needed to capture the maximum value of the wood grown. Miro's plantations sequester carbon and reduce demand for unsustainable natural forest harvesting, thereby contributing to climate change mitigation. The project also continues to generate positive social impact by creating local jobs, training and personal development opportunities, protecting rural communities and improving livelihoods. The 1,400 new jobs generated by Miro are an important source of income for the rural communities, as it is the first formal employer in those areas. It has also contributed to positive environmental impact through development of plantations on degraded scrublands and by protecting wetlands and other environmentally sensitive areas. .

General environmental protection

Expected number of projects in indicative portfolio: 10 (€25m total investment)

General environmental protections capture the broad range of adaptation and mitigation activities that stem from environmental interventions, but the Consortium's focus will be on coastal protection and water management to protect against floods and drought. Water-related disasters account for 70% of all deaths related to natural disasters, while floods affect 81 to 109m people annually and result in losses of between \$29 – 104Bn per year.^{36,37} Investments in this area therefore look to support climate adaption through addressing the effects of increasingly frequent and severe extreme weather events and sea level rise. This includes activity such as structural measures to protect against flooding (e.g. restoration of floodplains, forests and wetlands) as well as coastal defences to prevent damage from the sea (e.g. mangroves, sea-walls, dykes and embankments). Ecosystem based solutions are becoming increasingly recognised as very good investments, with large and sustained benefits for local people, and include approaches that utilise the natural capacity of, for instance, wetlands (particularly in urban settings), tidal marshes, mangroves, dunes, and coral reefs to effectively manage water and reduce storm waves and storm surges (see for instance WWF's Lower Zambezi project in Mozambique and Coral Triangle project in Indonesia). Complimentary non-structural measures including early-warning systems and awareness building are also important activities.

Investments in this area are critical according to the World Bank's Economics of Adaptation to Climate Change³⁸ study which provides an assessment of future flood defense investment needs. In the medium sea-level scenario, the report estimates that annual coastal adaptation investments of \$24.6Bn are needed for sea dikes, \$3.3Bn for beach nourishment and \$0.8Bn for river dikes and port upgrades (all in 2005 USD). These costs are particularly focussed in deltaic countries and small island states that are especially at risk from sea-level rise. Latin America, the Caribbean, East Asia and the Pacific together account for some two-thirds of the total cost of adaptation in this regard. With respect to riverine flood protection in developing countries, the World Bank estimates investment needs to be between \$5.3Bn and \$7.0Bn annually, depending on how climate change influences hydrological conditions. Regionally, these investment opportunities are distributed evenly across Latin America, South Asia, East Asia, the Pacific and Central Asia.

Nature based solutions in most cases contribute to climate resilient river basins and have multiple social and environmental benefits when compared to grey infrastructure. In addition, nature based solutions (NBS) may prolong the life of existing infrastructure (dams, water treatment works) and may prove a cheaper and more sustainable option (e.g. constructed wetland for wastewater treatment) than conventional infrastructure. NBS can help build climate change resilience in water management³⁹. In the developed world successful market-based approaches for NBS have been tested and invested in by the private sector⁴⁰. In the current fund the Consortium will look for opportunities to deploy similar investments in a developing context.

WWF's Coral Triangle project in Indonesia provides a good case study of the needs and opportunities in this area. The ongoing project works alongside local fisherman and businesses to improve fish stocks, support

³⁶ Alfieri (2016), *Global projections of river flood risk in a warmer world*, *Earth's Future*, Volume 5, Issue 2, <https://doi.org/10.1002/2016EF000485>

³⁷ New Climate Economy (2018), *Unlocking the Inclusive Growth Story of the 21st Century: Accelerating Climate Action in Urgent Times*, available at <https://newclimateeconomy.report/2018/>

³⁸ World Bank (2010), *The Cost to Developing Countries of Adapting to Climate Change*, available at <http://siteresources.worldbank.org/EXTCC/Resources/EACC-june2010.pdf>

³⁹ *Nature Based Solutions for Water Management*, 2018, DHI, IUCN & UNEP

⁴⁰ <http://www.quantifiedventures.com/environmental-impact-bonds/>

local livelihoods and protect marine ecosystems, with one of the key outcomes being improved coastal defences. One part of the project focuses on a model of sustainable mangrove utilization where rehabilitation and protection also play a critical role in managing erosion that results from sea level rise and severe weather. The dense root systems of mangrove forests trap sediments flowing down from rivers and off the land, helping to stabilize the coastline. This, in-turn, goes hand in hand with food security and economic livelihood improvements, as healthy mangroves provide nursery grounds for fish, shrimp and shellfish. In this way the project not only supports coastal protection and adaptation but a broader range of factors contributing to wellbeing. The project also has an impact on climate mitigation due to the carbon storage (biosequestration) of healthy mangroves.

C. Landscape approach pillar

The landscape approach pillar helps the DFCD originate projects with impact, use these projects to source interrelated projects, and catalyse a response to climate risks at the right governance level. As described above, the landscape is the geographic unit of analysis that the OF uses to create its climate risk assessments and investment plans. As such, the landscape approach helps the Consortium create a pipeline of projects with impact. But it also links the activities of the three facilities together in two ways. First, involvement in projects supported by the OF and sourced outside of the DFCD by the investment facilities may generate ideas for interrelated bankable projects in their surroundings, for example through field visits and stakeholder engagement. Second, for investment facility projects in vulnerable landscapes that are not yet covered by a landscape study on climate risks and business response options, OF managers can perform rapid landscape studies that can generate new project leads for the facilities in the surroundings of the project.

Through its landscape approach, the DFCD's co-located projects can catalyse further change in landscape governance to enhance climate resilience and mitigation action. The approach has the potential to respond to coordination barriers between key actors that can hamper action. For example, it can bring the beneficiaries and providers of ecosystem services together with regulators, local communities, companies and other stakeholders to understand how business action can contribute to an integrated response to climate risks and development challenges with strong local and national ownership. This is likely to inform a local policy agenda and have demonstration effects beyond the immediate clients of the DFCD facilities. As projects are planned in the local context while taking other current and future investments into consideration, the landscape lens allows maximisation of the impact of investments, while mitigating negative impacts. To illustrate the approach, Box 2 presents a case study of a landscape, Kafue, that has already been partly developed. Box 1 presents a case study of another landscape, the Mekong Delta, where multiple Consortium members are already actively looking for opportunities to co-locate projects and collaborate on ensuring an integrated response to climate risk.

Box 1. Existing activities and opportunities for further Consortium involvement in the Mekong Delta landscape

The Mekong Delta is one of Vietnam's most important agricultural and ecological regions. Spanning 13 provinces and being home to some 17m people, a mostly unskilled workforce primarily engage in agriculture. The delta faces a range of interconnected challenges and opportunities: although there is significant potential to grow the delta's economic significance and improve local livelihoods, this is constrained by large changes in the Mekong River basin and development trajectories within the delta itself. This translates into reduced availability of resources (notably fresh water, sand and access to transport and electricity infrastructure) and is aggravated by the increasing effects of climate change, including sea level rise and associated salination and changes in precipitation. The situation has reached a critical point that requires urgent action, a point acknowledged by Vietnam's Prime Minister with the signing of Resolution 120 in 2018. At this stage, development in the Mekong Delta must respect the large scale natural processes that created and maintain the delta's ecological function (which in turn support socio-economic growth), notably a recognition of the role that wetlands and rivers play in supporting the economy and intangible assets like biodiversity. For these reasons, investments are needed in the region to simultaneously:

- improve freshwater management;
- drive ecosystem management to sustain a healthy river and prevent further sinking and shrinking of the delta;
- ensure the sustainability and resilience of existing industries (particularly in agriculture, aquaculture, wild fisheries/brackish water economy sand mining/construction), and;
- diversify the region's industrial mix to build greater resilience.

These requirements are inherently interlinked, with progress in one impacting on the others. For this reason, there are important complementarities to be achieved through addressing them in a coordinated

fashion. For instance, investing in ecosystem management can mitigate the subsidence and rampant river bank and coastal erosion that will reduce salt water intrusions and help to improve fresh water availability while simultaneously supporting local communities and opening new and more resilient business opportunities. Enhancing wetlands & mangrove productivity will support more sustainable aquatic production while improving resilience to floods, typhoons, erosion and salt intrusion into rice fields. Similarly, investments to diversify the economy and reduce its water usage and pollution can support fresh water availability and ecosystem management.

Capturing these synergies and addressing the region's challenges in a holistic fashion requires coordination of a diverse range of stakeholders across civil society, government, industry, and finance. The Consortium's 'landscape approach' could leverage the group's existing footprint and complementary strengths. These activities include economic diversification through adaption of freshwater rice systems, forestry and growth of the mangrove-shrimp polyculture value chain. It also includes investments to improve climate resilience such as coastal protection and restoration.

By bringing these activities together through a coordinated action plan, the Consortium agencies will achieve a collective impact that is greater than the sum of their individual activities. For instance, the impact of SNV's longstanding 'Mangroves and Markets' projects could be enhanced through coordinating with one of the investment facilities in a way that provides additional coastal protection for mangrove restoration. Projects could also benefit from the different types of support that can be provided across the different facilities, notably WWF's work to promote more sustainable aquaculture and the efforts from WWF and HSBC to improve the textile industry's impact on water, energy and climate. As an example, the 'Mangroves and Markets' project could benefit from being passed onto the Water Facility for further development and support in reaching financial close. The investment facilities could also benefit from bringing in the Origination Facility to provide post-investment technical assistance for local communities and enhance the developmental impact of their projects. All the above would benefit from being planned in a way that does not affect the large scale natural processes that shaped the delta and make it naturally rich and resilient, like movement of water, nutrients and sediments.

To achieve the above at scale, the Consortium would look to develop a pipe of truly sustainable bankable project in the specific context of the Mekong Delta, fostering collective action and implementation, formalised by an inclusive basin management plan.

Box 2: Illustration of the landscape approach deployed in the Kafue Flats, Zambia

The Kafue Flats in Zambia provides a good example of the landscape approach in action. As an area of major ecological, industrial, and socio-economic significance for Zambia, the Kafue is the largest tributary of the Zambezi River. It is instrumental in providing electricity to half of the Zambian population and drinking water to half of the capital Lusaka. This has led the region to face a range of pressures creating trade-offs between expanded economic activity, resource management, climate adaptation and conservation.

One area where trade-offs are particularly apparent is in the drive for economic expansion and improved livelihoods which are critically constrained by effective water management. The Kafue Flats harbours one of the highest degrees of multi-sectoral water-users in Zambia which has critically constrained supply and created coordination challenges that limit effective management. As the last four years have very painfully demonstrated, the basin and its inhabitants are strongly affected by climate change, especially drought.

In order to overcome this, WWF-NL has taken a 'landscape' approach to planning and investment in the basin. This has involved the commissioning of a detailed study of the key risks and investment needs within the Kafue Flats. WWF-NL then used this to bring together key stakeholders across civil society, industry and government to discuss the study's findings and form the Kafue Flats Joint Action Group (KFJAG). With all parties involved, the KFJAG was able to develop a joint action plan to ensure that conflicting water use requirements are managed cooperatively. The KFJAG was also able to identify the key projects needed to secure the group's common interests in having an effective and climate resilient water supply.

As many of the commercial projects identified through this process are dependent on complimentary actions elsewhere (e.g. to secure demand or limit negative externalities), the landscape approach has been able coordinate projects in a way that de-risks investment opportunities. This has supported the crowding-in of private finance that is unlikely to have otherwise been available. In this way the landscape approach has not only provided the Kafue Flats with more effective planning coordination, but has also supported bankable investments and provided funding for complimentary development projects.

Table: Consortium minimum criteria for portfolio spread

Thematic distribution

In line with the Fund’s requirements, the Consortium will ensure that a minimum of 50% of DFCD funding, with a target of 65%, goes towards climate adaptation projects. This will be ensured through two mechanisms: (i) at an individual project level, through the screening phase of the Assessment Framework and (ii) at an aggregate portfolio level for each Facility through the mandate of the Facility’s investment committee, as described above. A portfolio that meets these requirements will be achieved through focussing activities in the investment sectors that are discussed further in the previous section “Thematic focus pillar”.

The balance of the Consortium’s selected investment sectors is weighted towards technologies and activities that support climate adaptation and reflect areas in which the Consortium has existing expertise. As such, the DFCD will be inherently structured to ensure that the mandated 50% DFCD requirement and 65% Consortium target are met. The remaining 35-50% spent on mitigation is anticipated to come either through projects with cross-cutting mitigation and adaptation impacts, or from projects in similar themes but with a primary mitigation component such as non-adaptation linked forestry and energy access and efficiency in the agricultural sector.

5. Risk Management

Introduction to the Risk matrix

The innovative nature of the proposed DFCD setup implies that there are risks to delivering the envisioned impact. These risks need to be carefully managed. To that end, the Consortium has put a set of mitigation measures and contingency plans in place.

The risk management framework of the DFCD is based on two pillars: (i) preventing business integrity, compliance and reputational risks; and (ii) prudent financial risk management. For FMO, acting in its role as Lead Partner, to be able to carry out the Fund’s strategy, it is essential to have an adequate risk management system in place to address both pillars of risks across all three Fund facilities. As there is a range of financial products provided across the three facilities, from grant finance in the Origination Facility to equity finance in the CFM Facility, the specialized and delegated financial risk assessment approach of the DFCD provides for an appropriate, project-specific assessment of financial risk. FMO, in its role as Fund Manager will receive reporting on the specific integrity, reputational and financial risks and mitigations assessed for each project financed by each of the Finance Facilities.

2. Preventing business integrity, compliance, ESG and reputational risks

For the DFCD risk management of compliance and integrity starts with the implementation of policies and processes ensuring adherence to relevant integrity laws and regulations, institutional standards, policies and good business practices and acting with integrity. The management of each of FMO, CFM, WWF-NL and SNV are committed to their employees, clients and counterparties adhering to the highest ethical standards and each of the Consortium institutions have already fully implemented and operationalized compliance frameworks and relevant policies on topics such as know your customer and sanctions, anti-bribery and corruption, conflicts of interest, internal fraud, private investments, privacy and speaking up.

The financing provided through all Facilities comply with strict anti-money laundering and Know Your Customer (KYC) practices embedded in FMO and CFM. To underpin this approach, quality counterparts are screened through a strict AML/KYC process which identifies at from an early-stage any known instances of malpractice of counterparts using open source internet searching, sanctions list screening using World-Check, trade registry verification, as well as the identification of Ultimate Beneficial Owners (UBOs) and Politically Exposed Persons (PEPs).

The DFCD will actively manage environmental and social risks in its emerging market projects. These risks stem from the intrinsic nature of the projects, which in some cases could carry negative environmental and/or social impacts. The risk appetite for deviations from the exclusion list and human rights violations by projects financed by the Fund is zero. The Fund furthermore expects the highest standards in professional conduct. Each of the Fund's investments will conform to international standards for managing environmental and social impacts and risks including the IFC Performance Standards (IFC PS), the International Labour Organisation (ILO) Core Conventions, and the UN Guiding Principles on Human Rights, among others. If at the time of making an investment decision, a project poses a potential reputation risk due to unacceptable Environmental and Social management practices, it will be rejected. By taking an active role in the project development, financial structuring and the Environmental, Social & Governance (ESG) of its investment activities, DFCD supervises, monitors and reviews project companies on an ongoing basis, positioning itself to become aware of, and to mitigate potential integrity and reputational risks from the onset. In the event of an incident occurring, DFCD will conduct a full investigation and a corrective action plan will be prepared to prevent any future recurrence.

In addition to project and counterpart-specific ESG risks, the Fund recognises that broader reputational risks can arise from the activities it undertakes by virtue of its focus investment sectors, focusing on water and land-use specific interventions in developing countries. For example, water cannot merely be regarded as a commodity given the 2010 recognition of The Human Right to Water and Sanitation (HRWS) by the United Nations General Assembly (UNGA).⁴¹ In this respect, the embedding of policies and procedures at FMO and CFM to assess human rights impacts during project screening in line with the UN Guiding Principles on Business and Human Rights provides a proactive approach. Through this, the Fund will seek to make investments that do not have a negative or unsustainable impact on water tables or adversely affect the abilities of communities from accessing existing Water Sanitation & Hygiene (WASH) systems. Such potential impact on existing access to water will be determined by feasibility studies and impact assessments conducted either by E&S professionals of FMO, CFM, WWF-NL or SNV, or as needed, by specialist third party consultants. Environmental and social risks cannot be completely avoided due to the nature of the Fund but they will be mitigated as much as possible through strict policies, upfront assessment and, when necessary, through agreements with the Fund's clients.

B. Prudent Financial Risk Management

Financial risk management for the Fund will be delegated to each of the facility managers, with risk reporting on individual projects and financials as well as aggregated across the exposure of the facility provided to FMO in its role as Fund Manager on a quarterly basis. As the Origination Facility is providing grant finance, rather than loans or investments, the core focus of the financial risk approach is ensuring financial alignment with counterparts. Financial risk will be minimized by assessing the financial figures of an organization entering into the Origination Facility, ruling out unviable businesses. Financing provided in the Origination Facility will be in the form of (revolvable) grants, for which the recipient of the grants will be required to co-fund, typically for 50%. WWF-NL and SNV apply their internal financial monitoring and risk management systems and procedures. For FMO and CFM, in their role of providing loans and equity finance the assessment of financial risk is embedded in the project assessment and approval process.

FMO reviews each transaction for the land use facility and provides consent to eligible proposals. The Investment Committee, comprising of senior representatives of several departments, reviews financing proposals for new transactions. Each financing proposal is assessed in terms of specific counterparty, product risk as well as country risk. All financing proposals are accompanied by the advice of the Credit department. This department is responsible for credit risk assessment of both new transactions and the existing portfolio. In addition, financial exposures in emerging markets are subject to a periodic review, which are in general executed annually. Exposures that require specific attention are reviewed by the Investment Review Committee. The larger and higher risk exposures are accompanied by the advice of the Credit department. If the Investment Review Committee concludes that a client has difficulty in meeting its payment obligations, the client is transferred to the Special Operations department – responsible for the management of distressed assets – where it is intensely monitored.

6. DFCD assessment framework

The two-stage Assessment Framework will be used for all activities financed through the DFCD fund. The full Assessment Framework is included in the Annexes (*Assessment Framework*). The first stage of the Assessment Framework (AF Stage 1) is used by all Consortium mem

⁴¹ UN (2010), Sixty-fourth session of the General Assembly: Agenda item 48, available here http://www.un.org/ga/search/view_doc.asp?symbol=A/RES/64/292

bers to screen project or business proposals against the core DFCD pre-conditions and functions as a knock-out criteria, projects must satisfy all pre-conditions to be eligible to receive DFCD funding. The second stage of the Assessment Framework (AF Stage 2) is used by FMO and CFM through their respective investment committees to assess projects prior to providing finance and is focused on a detailed assessment of: (i) climate and development impact in accordance with the Consortium's Theory of Change (and impact indicators); (ii) compliance with environmental and social safeguards; and (iii) financial viability (in accordance with the investment criteria of FMO and/or CFM and (iv): financial additionality and avoidance of market distortion. Projects and businesses which receive grant funding from the Origination Facility will be supported by WWF-NL or SNV to complete their climate and development impact assessments (based on the Consortium impact indicators) prior to their second stage assessment.

The Consortium's focus on leveraging private finance comes with a responsibility to ensure that it supports projects that would not have been implemented in absence of its support and that it does not distort markets. To guide the effective and efficient use of public resources in private sector projects, a cross-DFI working group that includes FMO has translated a set of principles on blended finance into guidelines for operations in 2018, which have been captured in the AF Stage 2. These align closely with the *OECD DAC Blended Finance Principles for Unlocking Commercial Finance for the Sustainable Development Goals*; and with the thinking in the recent World Bank working paper *Strategic Use of Climate Finance to Maximize Climate Action: A Guiding Framework*. FMO operationalises the DFI blended finance guidelines via the additionality test in its Stage 2 Assessment Framework for the Land Use Facility. CFM will deploy a similarly rigorous test in its Stage 2 Assessment Framework for the Water Facility. The Origination Facility managers will also use the Assessment Framework to avoid market distortion, with the guiding principle that the grants provided offer the minimum concessionality required for de-risking the development phase of private sector climate and development projects, and do not exceed 50% of the total costs of the project development phase. In setting these standards for ensuring avoidance of market distortion and sharing learning about the effectiveness of their operationalisation, the Consortium ensures that international leading practice on leveraging private finance for climate and development remains at the core of the DFCD.

The Assessment Framework implementation process will be based upon the following principles:

- **Clear instructions and guidelines to project promoters/ applicants on the information format required to apply for DFCD Funding.** This will be either an early stage Concept Note which contains all of the information necessary to determine eligibility (AF Stage 1) or, a more detailed application containing all of the information necessary to receive investment finance (AF Stage 2). Projects and businesses which receive grant funding from the Origination Facility will be supported by WWF-NL or SNV (or other partner if that is more effective) to complete their climate and development impact assessments (based on the Consortium impact indicators) prior to their second stage assessment.
- **Embedding the use of the Assessment Framework in the investment approval process of all DFCD members.** The completed Assessment Framework will be included in the financing proposals considered by the Investment Committee of each of the Consortium members when providing DFCD funding. The Investment Committee will only approve financing to projects or businesses when it confirms that the project is eligible based on the completed Assessment Frameworks.

Separation of impact assessment from project promotion functions within DFCD Consortium members.

Each of the Consortium members will use an independent, specialized team of subject matter experts to assess and confirm the climate and development and other impact of the proposed financing of the AF Stage 2. This assessment will be reported to the Investment Committees prior to any decision to provide financing, with final decision to be taken by the Investment Committee.

7. Mobilizing private capital

A primary objective of DFCD is to mobilise private sector investment in climate action through mitigating development and financing risks, as explicitly recognised in the Theory of Change (ToC). The DFCD ToC presented includes three modalities through which the fund will seek to mobilise private finance:

- At the **inputs and activities level**, the Water Facility will mobilise private finance from (largely OECD-country based) investors in its construction equity fund. CFM have successfully applied this model in its Climate Investor One mandate.
- At the **outputs level**, all projects developed and financed through the three facilities are expected to crowd in further private finance, as the DFCD investment is targeted at specifically addressing project risks that can unlock further investment.

- A dedicated **intermediate outcome** of the ToC recognises the significant further potential for mobilising private finance through a demonstration effect of the projects that it finances. As the DFCD will focus on the types of climate action that are more difficult to do, this demonstration effect can be powerful in achieving a sustainable effect of the DFCD through changing market perceptions. In addition, some of the project development work that affects the way in which landscapes are governed can change market conditions in order to crowd in more private finance.
- Finally, any projects supported by the OF without being eventually financed by the Investment Facilities may attract **other funding sources**.

Mobilisation is therefore achieved through the individual activities of the facilities at both Facility and project level and is amplified by the collective efforts under the programmatic approach that connects the three DFCD facilities.

The following sections provide more detail on the specific approaches and instruments that will be used across the three facilities to maximise private finance mobilisation by the DFCD.

A. Origination Facility

The Origination Facility has an important role in preparing projects for the Investment Facilities and, in the process of doing so, crowds in private finance in each business case, and facilitates landscape development that further catalyses private sector investment. These activities will seek to leverage external financing at both the project and fund level. At the project level, this will be achieved through co-financing requirements up to a value of 50%. The below Box presents an example of how this arrangement works in SNV's Innovations Against Poverty project. At a fund level this will be achieved through approaching relevant companies and investors for assistance in co-funding the resources for technical assistance and grants for business cases. This would draw on the incentives such actors have to de-risk their global supply chains and mitigate uncertainties connected to other investments. It is expected that, as funded projects cumulatively develop, the business case for investment in surrounding landscapes and through the development of business cases, there will be an additional impact on the business environment through engagement of stakeholders. This could mean that further external investments that are not connected to the Origination Facility will also be developed. This effect will be strengthened through support for business ecosystems such as the facilitation of stakeholder platforms and data sharing, strengthening business-to-business relationships, developing quality assurance and (self) regulation, strengthening business-development-service providers, and building training capacity.

The Origination Facility anticipates three sources of income that will further crowd in private sector finance and can help sustain the financial resources available for its activities. It will:

- ask the investee to pay back the grants provided for developing a business case. The investee can include these costs in the overall budget covered by the investors (CFM, FMO or others);
- fundraise grants from large companies that aim to climate-proof and 'green' their global supply chains. Large companies with a global footprint are increasingly aware of the risks of climate change to their supply chains and are seeking strategies to de-risk their operations; and
- fundraise from other DFIs and philanthropies, aiming to leverage their grant money with private sector investments. The OF will hereby provide a solution that reduces the investment gap for the SDGs and the Paris Agreement.

B. Water Facility

The Water Development & Finance Facility principally sets out to mitigate private sector technical and financial risks to mobilise private finance for water related infrastructure at both the facility and project levels.

Facility level

Climate Fund Managers will deploy €75m of DFCD funding to launch a Water Facility, also called *Climate Investor 2 (CI2)*, which will use a blended finance model to mobilize private sector capital at scale for adaptation & mitigation activities. CFM will achieve this by building from, and to some extent reproducing, the

already proven and acclaimed financing structure of the Climate Investor One (CIO) renewable energy facility,⁴⁴ also under its management. CFM has chosen a blended finance approach at the facility level as water related infrastructure sectors within the target countries of DFCD are predominantly financed by the public sector, placing strain on (local) government budgets – blended finance represents a more sustainable strategy in the long-term given the recent decline in ODA commitments to these sectors. In addition, CFM views the blended finance approach as an effective tool to demonstrate the business case for large-scale private sector mobilisation within these infrastructure classes.

The blended finance model at facility level reduces construction risk and enables private sector participation. The Water Facility will comprise of two separate but interlinked funds: a CI2 Development Fund (CI2 DF) and a CI2 Construction Equity Fund (CI2 CEF). The CI2 Development Fund will provide returnable grants (in the form of development loans) to projects that have proven to be feasible at a very early stage and now need more substantial development in order to prove up the bankability. This process, which can often take up to two years, comprises financial analysis, environmental & social assessments, permitting, detailed technical design, off take contracts. The Water Facility plays an important role in the continuation of projects and businesses generated by the Origination Facility. The OF focusses on initial pre-feasibility and feasibility of projects before passing on, whereby the Water Facility continues thereafter with a detailed development process. Projects successfully developed by the CI2 DF, will be transferred to the CI2 CEF for further financing to establish the project. CFM aims for at least 100% revolvability of funds.

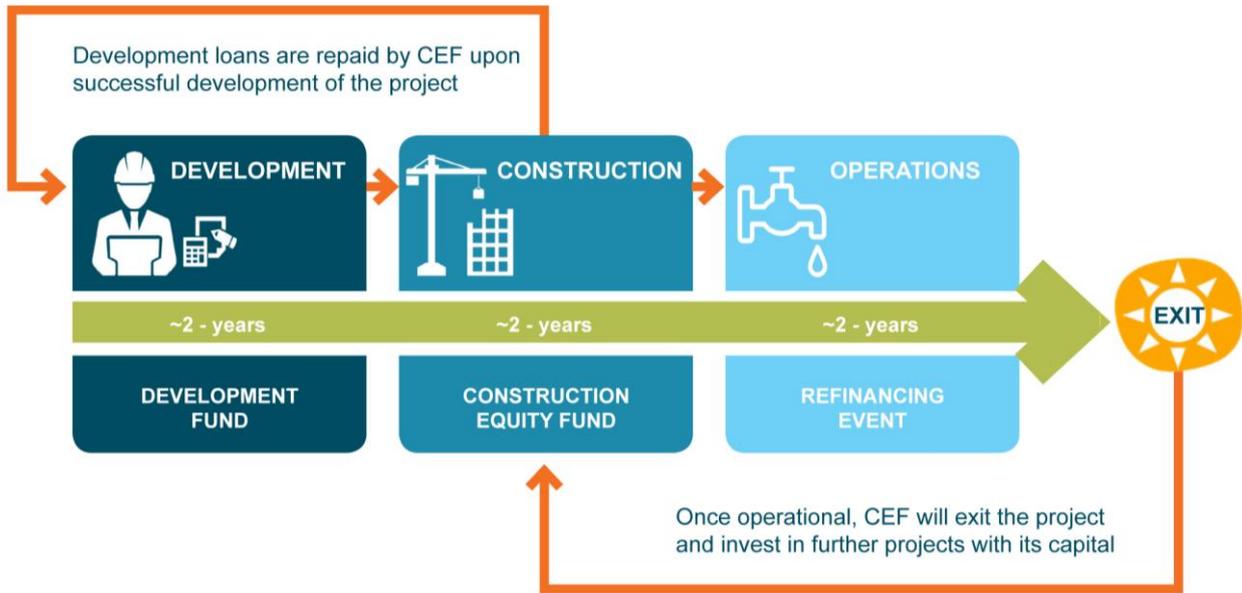
Project level

With DFCD funding, CFM will directly address project development and financing risks through its unique technical and financial offering to projects. In particular, the Water Facility:

- *Finances early to mid-stage project development activities:* DFCD will provide €25m to CI2's Development Fund, which will provide development loans in the development stage, the riskiest phase of a projects lifetime, due to the highest levels of uncertainty. CFM will raise a complementary €25m in donor funding for a total Development Fund size of €50m. The Development Fund will provide up to 50% of development costs with the remaining funding provided by private sector project developers. Capital mobilised in successful projects would amount to approximately €50m, of which €25m is attributable to DFCD capital. DFCD participation in CI2's Development Fund also offers positive enablement in respect of creating a proprietary, investment ready project pipeline for the commercial investors participating in the Construction Equity Fund.
- *Sets rules to ensure project proponents have a significant stake in the financing structure:* With the CEF mandated to not completely fund project costs in order to separate project & construction risk, DFCD funding will also enable private sector co-financing at project level.
- *Deploys a range of instruments and leverages its network to mitigate risk of co-financiers at the financial structuring phase:* CFM expect to partner with new financing partners, particularly large Dutch construction companies, Dutch pension funds, Dutch family offices and Dutch institutional investors, bringing patient capital into its Facility and projects. In addition, CFM will mobilise local or international debt during the operational phase of the project lifecycle (post construction).

⁴⁷ For instance, the IFC has found that demonstration effects are more likely when investors made money; the supported projects were first movers; a new technology, process, or "rules of the game" were introduced; other players were "on the brink" of action; and credible communicators were involved. See IFC Demonstration Effects Study, Report to the International Finance Corporation, Castalia Strategic Advisors.

Figure: Revolvability of the Water Facility



2. Land Use Facility

Project level

The DFCD funding into the Land Use Facility will be deployed to maximize mobilization of private capital on project level. In developing countries, investors are not always willing to invest in climate-resilient projects due to a lack of market knowledge, experience or a perception of high contextual risk⁴⁵. The Land Use Facility will operate as a blended finance facility, whereby FMO aims to optimize the use of the DFCD's public funding to reach highest development impact. Through this blended finance approach, the Consortium will use DFCD funding to:

- Support investments that are just at the threshold of commercial viability;
- Support first-of-its-kind projects that may create a demonstration effect;
- Pull in commercial investors to finance climate projects that they would otherwise have deemed too risky.

To contribute to the latter, the Land Use Facility aims to mobilize the highest possible amount from the commercial sectors with the lowest possible level of blended (public) finance financed by the DFCD. FMO aims to be instrumental in encouraging the participation of commercial banks and investors, but also multi- and bilateral development banks. FMO will provide risk capital solutions, thereby mobilizing other financiers and investors. This is likely to happen on two different levels: (1) parallel and (2) sequential.

Parallel financing implies that the projects are financed by FMO and other (market) parties at the same point in time, whereby the Land Use Facility generally accept a higher risk profile than other parties in the same project. FMO will assess opportunities for mobilizing DFI and commercial finance on a project-by-project basis. Following the existing OECD DAC methodology, FMO projects a total amount of private finance mobilized of €186m over the lifetime of the DFCD (2019-2037).

In addition, the finance of the Land Use Facility is expected to create significant catalysing benefits in the period after financial close of a project. Sequential co-financing refers to the Fund's capability of financing early, high-risk start-up phase, which will at a more developed phase be followed by DFI's and commercial banks on similar or more advantageous terms. Projects are assessed on an annual basis on their readiness to graduate to the portfolios of DFIs and/or commercial investors.

Revolvability of funds

To optimally drive market development and impact, FMO aims for a revolvability level of the Land Use Facility of approximately 75%. This will ensure sufficient levels of sustainability of the fund to continue investing the revolving cash flows, while at the same time allowing us to finance high-risk projects. The markets that the Land Use Facility will be active are high risk (e.g. politically or economically unstable environments; low-income countries; new market entries), as will be many of the investees (e.g. start-up nature), investees' projects (e.g. first-of-its-kind projects) and (end-) beneficiaries (e.g. smallholder farmers with limited agronomic and/or financial skills). The Land Use Facility will be additional to commercial investors and to DFIs. FMO estimates 2 to 3 investment cycles throughout the lifetime of the DFCD, which will result in DFCD capital being invested over two times.

8. DFCD Sustainability Impacts

The main target groups on which the Consortium aims to have a lasting, sustainable effect are the climate vulnerable populations of developing countries, especially fragile livelihoods and groups where development constraints are increased, for instance women and children. An additional target group are the investors, companies and entrepreneurs that the DFCD will work with and invest alongside, and their peers. The Consortium will deliver lasting effects for these target groups in six ways, as shown in the figure below.

⁴⁷ For instance, the IFC has found that demonstration effects are more likely when investors made money; the supported projects were first movers; a new technology, process, or "rules of the game" were introduced; other players were "on the brink" of action; and credible communicators were involved. See IFC Demonstration Effects Study, Report to the International Finance Corporation, Castalia Strategic Advisors.

Figure: The DFCD will deliver a sustainable effect for its target groups in six ways



Long-lived assets: The financing deals supported through the Investment Facilities of the DFCD will typically focus on assets with inherently long-lived technology and characteristics, in the range of 20-25 years. Moreover, the assessment framework will ensure that DFCD only selects projects where there is a clear expectation that, throughout this lifetime, the effects of the project will be sustained; for example, where there is confidence over the future demand for the goods and services that will be supplied, where costs can be predicted with confidence, and where the quality of inputs and raw materials, and the reliability of the supply chain providing them, is understood. The close working relationship that will be developed with project partners through the Origination Facility will both improve the quality of all business cases in this regard, and facilitate the assessment of which projects have the greatest potential for sustaining their effects.

Commercial focus: this complements the long-lived nature of the assets by ensuring a long-term interest by owners and investors in the projects. In contrast to grant financed projects, satisfactory financial returns will only be realised if the projects continue to provide strong operational performance and goods and services that are valued by their users. By contrast failure to ensure this – for example through poor maintenance – could have contractual or legal ramifications.

Focus on replication potential: the Consortium will focus on securing ‘demonstration effects’ from DFCD’s investment. This might be secured by changing either the perception or the actual risk reward balance of similar projects, or by encouraging action by governments or IFIs seeking to secure the same outputs and outcomes as DFCD. The Fund’s **programmatic approach** will be a substantial advantage in securing these effects: compared to a situation where there are diffuse individual projects spread across the world, the Fund’s concentration of activity in certain landscapes, and within certain investment sectors, makes it much more likely that a critical mass is reached such that others (both within and outside the landscape) will learn about the Fund’s activities and its outcomes. In addition, the Consortium will learn from the insights of others who have sought demonstration effects, and embed this learning.⁴⁷

Technical assistance: a key innovation of the proposed approach is the extensive resources allocated to the Origination Facility. The technical assistance activities this Facility provides will, in the first instance, deliver a

⁴⁷ For instance, the IFC has found that demonstration effects are more likely when investors made money; the supported projects were first movers; a new technology, process, or “rules of the game” were introduced; other players were “on the brink” of action; and credible communicators were involved. See IFC Demonstration Effects Study, Report to the International Finance Corporation, Castalia Strategic Advisors.

robust pipeline of strong project concepts to the Investment Facilities, with contextualized solutions in vulnerable landscapes. By investing in the broader context different stakeholders are engaged, contributing to de-risk the projects. But the capacity building activities of local businesses and entrepreneurs, and especially the market systems building activities, once built, will continue to endure, allowing those supported to develop future projects and also share knowledge across the wider community that others can emulate.

Engagement of stakeholders and decision makers. As part of the broader technical assistance activities of the origination facility, there will be a focus on stakeholder engagement, key for de-risking and creating a positive investment climate and opportunities to effect policy change. While policy engagement will only be pursued when it directly relates to helping support a particular business case, successful policy reforms could then have a powerful spill over effect, improving the business case for other businesses and entrepreneurs considering similar activities.

Learning culture: In recognition of the complexity of the climate and development challenge. The Consortium deliberately comprises organisations with varying perspectives and skills. In the first instance, this provides versatility and an ability to respond to a wide range of challenges, But, just as importantly, it provide a 'working laboratory' in which the Consortium can learn from differing perspectives and approaches. This internal learning culture will also have an external expression: the Consortium will both be open and transparent in sharing its lessons, allowing the international climate finance community to emulate its successes and understand its challenges, thereby encouraging a sustainable effect through the actions of others.

Büyük Menderes river basin – sustainable effect through stakeholder engagement

The Büyük Menderes river basin in southwestern Turkey is a vital source of water for the region and an area of rich biodiversity. It ends in a delta that hosts three wetland protected areas and five national parks. But the native flora and fauna and the quality of life of local people is under growing threat from water pollution. A key source of this pollution comes from textile manufacturers situated upstream around the industrial city of Denizli, which rely on water from the river and supply products to global apparel companies. WWF found that many small and medium-sized enterprises (SMEs) in the textile dyeing industry could cut their costs and reduce their environmental footprint – saving water, chemicals, and energy – through a variety of interventions, ranging from changing chemicals and improving water management, to investing in new equipment and infrastructure. All provided significant savings, with payback periods ranging from six months to two years. By working with industry associations, identify potential candidates, design effective interventions and group SME under a larger finance mechanism WWF is transforming the textile dyeing industry to become more sustainable and climate resilient; 40 SMEs were part of the pilot, the next tranche is with 300 companies. It is also taking a blended finance approach: development agencies provide a grant to cover the costs of a project's design, which is then used to raise commercial funding (US\$10-20m credit line for SMEs from a commercial bank). The benefits are not limited to the Turkish textile industry: the model can serve as a blueprint to improve water management by textile manufacturers worldwide as well as in other industries.

9. DFCD Impact Indicators

The Consortium will measure and report on impact indicators for all activities financed with DFCD funding across the three Facilities. As set out in the Theory of Change, the Consortium has selected key performance indicators (KPIs) for each of the four DFCD Outcomes as well as for the volume of private finance mobilized and number of individuals benefitting from the activities. The use of KPIs link and substantiate the activities of the three Financing Facilities with the DFCD theory of change. To this end they identify how the Consortium's activities will deliver the outcomes and impacts set out by DGIS. Through the use of KPIs the Consortium will be better able to report on aggregate impacts from the financing activities of each member.

Since the Consortium was awarded the DFCD tender, the Consortium has developed a separate DFCD Impact Indicator Guide for overall fund reporting in partnership with DGIS/Ministry of Foreign Affairs. For this reason the impact indicators originally included in the proposal have been removed. Parties interested in this impact guide can obtain the latest version by contacting info@thedfcd.com.

10. Planning, monitoring and evaluation

2. Planning, monitoring and evaluations of the DFCD: an overview

The basis for the DFCD's planning, monitoring and evaluations (PME) approach will be a common framework applied across all Facilities and overseen by FMO, covering all stages of the DFCD life cycle, from implementation through conclusion. As Lead Partner, FMO will delegate the implementation of a common assessment, monitoring and reporting framework to the managers of each of the Facilities, with each manager adapting the common elements to the specific characteristics of the Facility level activities. At fund level FMO will aggregate the monitoring and reporting of each of the Facilities and report to DGIS. This will ensure a consistent approach across Facilities and ease of aggregation of results, without creating large overhead costs.

The key components of the common framework include:

- **A fund level TOC** which illustrates how the different facilities contribute. The TOC demonstrates how activities undertaken through a programmatic approach across the three Facilities will support a pipeline of bankable and implemented projects which systematically contribute towards the identified climate objectives. The programmatic approach, anchored in landscapes and investment themes, and mobilising the range of specialisms embodied across the Consortium Parties, ensures that promising projects can be graduated from early stage concepts to financial close, that contextual constraints are systematically addressed, and that clusters of mutually reinforcing projects are developed such that the impacts realised add up to more than the sum of their parts.
- **A common assessment framework**, adapted to the specific needs of projects identified under each Facility. This will include common screening criteria and a requirement for projects to demonstrate their potential contribution towards fund KPIs before receiving approval from investment committees. Each Facility will then adapt this framework to the specific characteristics of their own pipeline, for example, the Origination Facility is unlikely to implement projects and so may have limited direct contribution to climate indicators, but the potential for projects to crowd in private sector investment downstream (e.g. through another facility) should be assessed, as should the potential for climate benefits at a later stage (e.g. with a qualitative assessment). Finance Facilities are likely to require more detailed project documents before (larger) investments are made, for example FMO already captures data on climate impacts of projects at contracting stage.
- **Fund-level evaluations** to assess relevance, additionality, catalysation, effectiveness, efficiency and impact from each of the facilities. In addition, there will be project-level evaluations by the Finance Facilities to assess impact on project level. These evaluations will be commissioned to an external consultant to ensure objective and high-quality reports.
- **A common approach and indicators for project level reporting and monitoring.** Individual projects will be expected to report contribution to KPIs following the same pattern. Each Facility will tailor the approach to the specific characteristics of their projects, so that no undue burden is placed on small or early stage projects. However, projects will be expected to report results on an annual basis. A common set of guidelines has been developed for reporting against indicators.

As Lead Party, FMO will ensure aggregation of the reports and evaluations, building on the strong PME processes that each of the individual organisation has in place on Facility level. FMO has significant experience in reporting and evaluating on its donor activities. FMO manages three large funds for the Ministry of Foreign Affairs for which provides regular financial and impact reports. FMO is also experienced in reporting the activities of other entities, for instance through the provision reporting on Climate Investor One. In addition, FMO has long-standing experience in commissioning external consultants and research institutes. It has in place an Evaluation Advisory Panel, that advises on topics to be evaluated, research methods to be employed, and consultants to be engaged.

B. Evaluation approach

Periodic evaluations at Fund level will be commissioned to assess Fund results. DFCD will be evaluated every five years by external consultants to provide an independent and objective assessment of the results of the Fund, in terms of relevance, additionality, catalysation, effectiveness, efficiency and impact from each of the facilities, as set out in Table below. The first evaluation will start after year 4 of implementation (2023) to assess the roll-out of the fund, its governance and its management. At the moment of the first midterm evaluation, it is not

expected that significant development results will have been achieved, since the portfolio will not have reached full maturity at this point. The first evaluation shall therefore provide insights and lessons learned to provide strategic guidance to DFCD management rather than establishing impact achieved in the first 3 years. Subsequent midterm evaluations thereafter will focus on the extent to which the DFCD Consortium is achieving its goals with regards to number of projects developed & implemented, along with key impact indicators. For the final evaluation, it is expected that development effects will have been fully realized.

able: Five criteria for evaluation of fund performance

Criteria	Elaboration
Relevance	the extent to which the investments are suited to the priorities and policies
Effectiveness	the extent to which the objectives were achieved
Efficiency	the extent to which activities were cost-efficient and timely
Impact	determining the positive and negative changes produced, directly or indirectly, intended or unintended. The focus will be on local social, economic, environmental and other development indicators as identified in the Indicators. It will be evaluated to the extent that these results can be attributed. There will be other factors which influence the results which need to be mapped. If applicable, investments might be benchmarked against other similar investments in the region.
Sustainability	the extent to which the investment activities are likely to continue operating after the fund has exited its investments.

Evaluation programs for Finance Facilities will be developed to assess project-level and theme-based impact. Each Finance Facility will manage an evaluation program which will: (i) measure and provide evidence of the impact achieved through the investments of the respective Finance Facility and (ii) provide recommendations and lessons learned to support management of the fund and inform policies for both investors and the Dutch Government with regards to climate adaptation.

The evaluations will provide an answer as to whether or not a project has been successful in achieving its objectives at impact and/or outcome level in an efficient and effective manner. It is a systematic assessment, not a one-off, but uses information from several time points inclusive of baseline, midline, routine monitoring, and end line information as part of the evaluation process. The better these stages they build on one another, the better the quality of the evaluation and the better the Consortium will be able to say at the end of the project what its achievements have been at impact, outcome and/or output levels.

Evaluations could follow different methodologies, to be determined depending on information requirements. Ex-post studies to measure effectiveness of the investment and impact generated at investment/project level. Thematic studies to advance knowledge on strategic topics of interest for the fund. Impact evaluations to establish, in a rigorous manner, evidence of the causal relationship between the financing of the project and the impact at household or end-user level. Prioritized will be those investments or themes where there is little scientific evidence and where some of the impacts reflected in ToC cannot be measured solely by impact reporting. If sufficient evidence already exists to make impact plausible, the focus will be on ex-post studies and thematic evaluations in line with DFCD's impact objectives.

2. Reporting approach

As Lead Partner of the DFCD, FMO will consolidate all reporting from the different facilities to integrated fund-level reporting. As part of this, FMO will provide several reports to the Ministry of Foreign Affairs:

- Annual report and accounts (annual);
- Activity plan (annual); and
- IATI updates (quarterly).

As Lead Partner, FMO will annually provide an Annual Report to the Ministry of Foreign Affairs, which will include (at least) an annual financial report with an audit statement, including at least a balance sheet, an income statement, a cash flow statement, explanatory notes, portfolio information and performance on environmental and social impact (indicators). The audit opinion will be drawn up in accordance with an audit protocol laid down by MoFA.

On a yearly basis, the Consortium will also submit an Activity Plan and accompanying budget, including liquidity forecast, for the forthcoming year. This report will cover an outline of the activities that are forecasted for the year ahead.

DFCD financing activities will be reported on according to the International Aid Transparency Initiative (IATI). FMO will publish and update IATI-compliant data on the DFCD activities on a quarterly basis. While FMO is not fully IATI-compliant at time of submitting this bid, FMO will ensure implementation of the IATI reporting standard based on the guidelines that have been prepared by the Netherlands Ministry of Foreign Affairs on how to use the IATI standard for publishing results and other information regarding the activities financed by the DFCD.

11. Operational activities

The Consortium has set up a structure that delivers cost-efficient management of the DFCD. To keep costs to a minimum, all four Consortium Parties are using as much as possible existing internal structures and systems to efficiently deliver on the task at hand. **Both over the initial 4-year period and the period until 2037, the Consortium will a highly efficient cost management structure and is fully in line with international best practice.**

Funding

Over the period 2019-2022, the Consortium projects to draw €160m from MoFA to fund its commitments to projects and to cover related operational costs. Through its three Facilities, the DFCD provides financing (loans; equity investments; mezzanine financing), guarantees, technical assistance and grants to projects.

The Investment Facilities are revolving and will provide over €335m in financing, technical assistance and grants during the lifetime of the DFCD (2019-2037). All returning cash flows resulting from equity exits, loan repayments and interest will be reinvested by the DFCD. The €75m and €55m committed to the Water and Land Use Facilities will thus revolve 2-3 times until 2037. The Water Facility has a projected revolving ability of at least 100%; the Land Use Facility aims to be at least 75% revolving. This will allow the DFCD to continue to deliver lasting sustainable effects on climate vulnerable populations in developing countries.

The Origination Facility will provide €26m in grants and technical assistance in the first four years of the DFCD⁴⁹. Due to the non-revolving nature of the funding products provided from the Origination Facility (grants and technical assistance), the funding of the Origination Facility will run out after 2022. The executing entities of the Origination Facility however, WWF-NL and SNV, will seek to replenish the facility by raising additional capital from the private sector, DFIs, donors and philanthropists during this initial four-year period to catalyse other donors and investors and to ensure continuation of the Origination Facility. In addition to recapitalization and catalysation through further fund raising, the Consortium is exploring the possibility to include another element of revolving ability into the Origination Facility, whereby the Water and Land Use Facilities will (partially) repay the grant or TA provided if a project graduates to be financed by either Facility. The total amount of grants and technical assistance provided by the Origination Facility over the lifetime of the DFCD can thus be significantly higher than €26m.

Both over the initial 4-year period and the period until 2037, the Consortium will a highly efficient cost management structure and is fully in line with international best practice.

12. Communication

This section sets out the communications strategy for the DFCD.

2. Strategy and objectives

The objectives of the communications strategy include:

- Position the DFCD Fund as a trusted, thorough and responsible partner, successful at investing in projects with climate and development impacts in developing markets, supporting ambitions to catalyse funds, forging partnerships with like-minded others and protecting its reputation through issue and stakeholder management.
- Showcase live examples from 'on the ground' to grow understanding and appreciation of the achieved impact: share milestones and successes, explain how challenges are turned into actionable opportunities.
- Where relevant, explain how the combined expertise of the Consortium enhance impact:

⁴⁹ Note that €4.1 million of technical assistance and grants will also be provided by the Investment Facilities.

- Networks and expertise on the ground for SNV and WWF-NL, realizing sustainable investment projects and a focused pipeline
- Network and expertise of CFM: transforming water & ocean pipeline into bankable, sustainable investments
- Network and expertise of FMO: due to 50 years of experience in investing in developing and emerging markets, DFCD can rely on robust processes and deep expertise in quality assurance, measuring impact through its green and reduced inequality labels, transformative projects with long-term impact on climate action and sound fund management practices

2. Organization of communication

The FMO Consortium will form a communication working group. This working group comprises of communications representatives of FMO, CFM, WWF-NL and SNV, and the MoFA will be invited to join. The working group will define expectations, ambitions, roles and responsibilities, informing a more detailed communications strategy and work plan that will meet both the corporate communication and marketing needs.

2. Disclosure

Trusted relationships and open communication are key to the Consortium's approach to implementing DFCD. Being transparent and providing opportunities to voice considerations at an early stage about the investments the Consortium proposes to approve, are important elements in open communications. To that end, all transactions (being each separate guarantee, loan, participation or donation) from the DFCD to a project will be disclosed to the public, prior to contracting, on the consortium member's website within a minimum of 30 days prior to contracting, stating as a minimum:

- the name of the project;
- the country/region;
- the amount and financial instrument provided;
- the potential social, environmental, and human rights risks and how these have been analysed;
- a contact address and process for stakeholders to ask questions or provide input.

Comments and considerations shared with respect to the proposed investments are carefully considered. After thirty days disclosure, the proposed investment can be confirmed, provided that no grave considerations have been presented. All confirmed and approved projects are subsequently disclosed 'ex-post' on the website for the duration of their tenure.

III. DFCD Assessment Framework

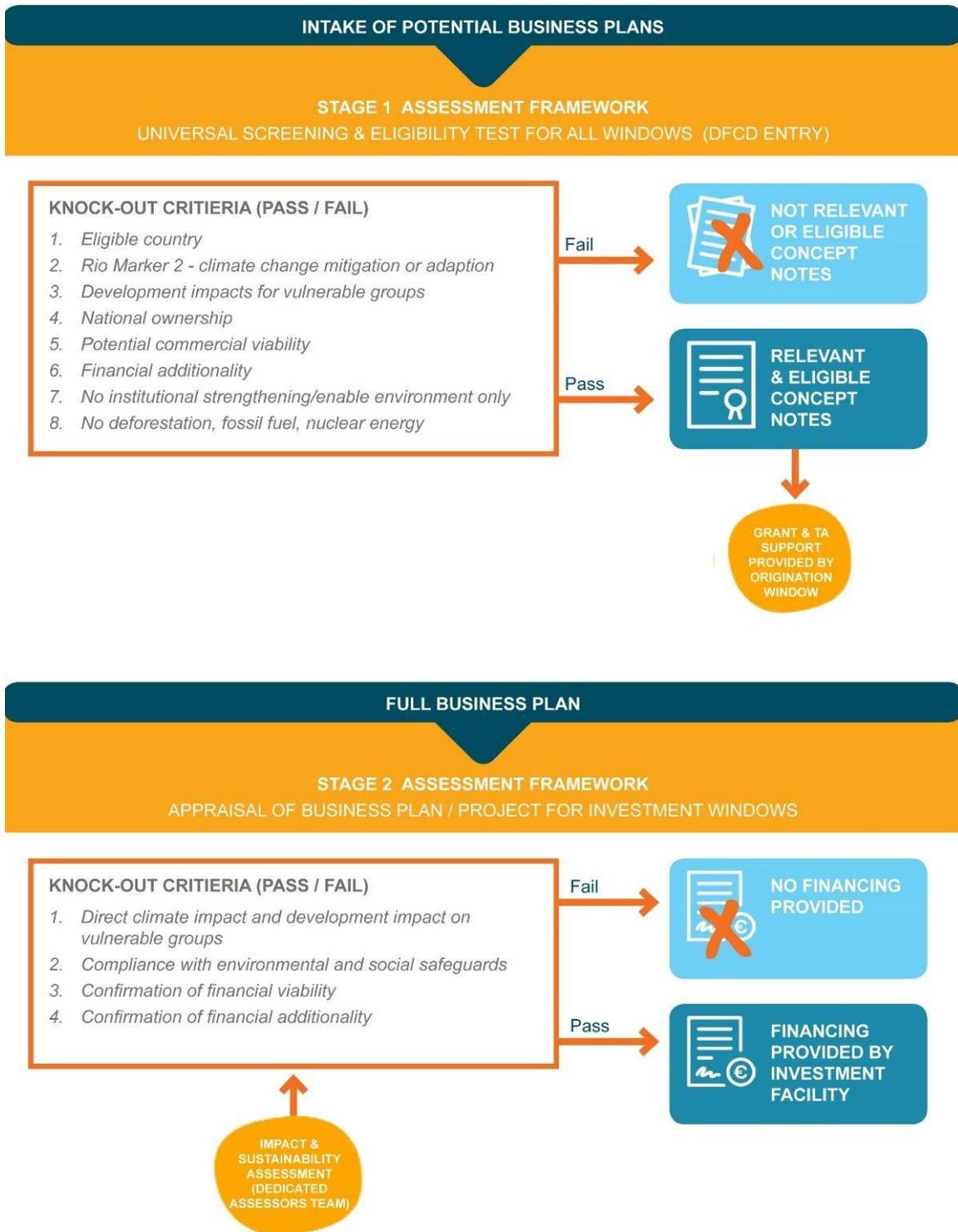
Table: Assessment Framework reference guide

Minimum conditions of investment	Assessment Framework reference
Financing is fully climate relevant according to Rio Marker 2	<ul style="list-style-type: none"> • Yes
The projects have a direct effect on climate change indicators ('direct climate return')	<ul style="list-style-type: none"> • Yes
The projects are relevant to development and actively strive to benefit the poorest populations and have a positive impact on women	<ul style="list-style-type: none"> • Yes
Projects to be financed must provide assurance of national ownership	<ul style="list-style-type: none"> • Yes
Projects to be financed must prevent or mitigate any undesirable effects for the environment, society, human rights and gender	<ul style="list-style-type: none"> • Yes
The finance is additional to the market and does not distort local markets	<ul style="list-style-type: none"> • Yes
Financing is not provided to projects involving fossil fuels, nuclear energy or deforestation, nor to projects aimed solely at an enabling environment and institutional strengthening	<ul style="list-style-type: none"> • Yes

Introduction Consortium DFCD Assessment Framework

The DFCD consortium will use a two-stage project Assessment Framework for all activities financed through the DFCD fund. **The first stage of the Assessment Framework ("AF Stage 1")** is used by all consortium members to screen project or business proposals against the core DFCD pre-conditions and functions as a knock-out criteria, projects must satisfy all pre-conditions to be eligible to receive DFCD funding. **The second stage of the Assessment Framework ("AF Stage 2")** is used by FMO and CFM to assess projects prior to providing finance and is focused on a detailed assessment of: (i) climate and development impact in accordance with the consortium's Theory of Change (and impact indicators) (ii) compliance with environmental and social safeguards, and (iii) financial viability (in accordance with the investment criteria of FMO and/or CFM. Projects and businesses which receive grant funding from the Origination Facility will be supported by WWF or SNV to complete their climate and development impact assessments (based on the consortium impact indicators) prior to their second stage assessment.

Figure: Overall Assessment Framework



Assessment Framework Implementation Process

The assessment process will be based upon the following principles:

- i. **Clear instructions and guidelines to project promoters/ applicants on the information format required to apply for DFCD Funding.** This will be either an early stage Concept Note which contains all of the information necessary to determine eligibility (AF Stage 1) or, a more detailed application containing all of the information necessary to receive investment finance (AF Stage 2). Projects and businesses which receive grant funding from the Origination Facility will be supported by WWF or SNV to complete their climate and development impact assessments (based on the consortium impact indicators) prior to their second stage assessment.
- ii. **Embedding the use of the Assessment Framework in the investment approval process of all DFCD members.** The completed Assessment Framework will be included in the financing proposals considered by the Investment Committee of each of the three Facilities when providing DFCD funding. The Investment Committee will only approve financing to projects or businesses when it confirms that the project is eligible based on the completed Assessment Frameworks.
- iii. **Separation of impact assessment from project promotion functions within DFCD consortium members.** Each of the consortium members will use an independent, specialized team of subject matter experts to assess and confirm the climate and development impact of the proposed financing, including expected impacts on the impact indicators of the AF Stage 2. This assessment will be provided to the Investment Committees prior to any decision to provide financing, with final decision to be taken by the Investment Committee.

1. First Stage Assessment Framework (AF Stage 1)

The AF Stage 1 consists of 8 pass/fail criteria to determine whether a project or business is eligible to receive DFCD funding. All projects must pass all 8 criteria to be eligible to receive funding. An explanation of the project or businesses' compliance with the AF Stage 1 will be set out in the Concept Note and assessed by the consortium member providing finance.

Criteria #1 – Financing is in a country that is eligible under the DFCD country list.

Pass/Fail

Based upon the OECD-DAC¹ country list and the Netherlands Ministry of Foreign Affairs Letter to Parliament: "Focusregio's en andere Nota-onderwerpen" (13 November 2018)² the fund will establish a country list of eligible countries for DFCD support. Only applications which aim to undertake activities in these selected countries will be eligible for support.

Criteria #2 – The project is fully climate change relevant according to Rio Marker 2

Pass/Fail

Project (ideas and objectives) will be assessed against the OECD definition of Rio Marker 2. Projects will need to receive a score of 2 under the Rio Marker 2 system for either climate change mitigation or adaptation. For *climate mitigation* the OECD handbook defines this that the project "contributes to the objective of stabilisation of greenhouse gas (GHG) concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system by promoting efforts to reduce or limit GHG emissions or to enhance GHG sequestration. For *climate adaptation* the OECD handbook defines this as follows: "It intends to reduce the vulnerability of human or natural systems to the current and expected impacts of climate change, including climate variability, by maintaining or increasing resilience, through increased ability to adapt to, or absorb, climate change stresses, shocks and variability and/or by helping reduce exposure to them." Projects will qualify provided their core objectives are to reduce emissions of greenhouse gases, including projects aiming to reduce the vulnerability and risks for people, agriculture or nature for climate variability and climate change. The Concept Note will include an explanation of the type of project, under which Rio Marker it qualifies and whether it scores a 2 under the definitions classified by OECD. The assessor's team will verify this information and whether it indeed scores a 2. By this assessment the project should fall under one of the categories with qualifying activities of the Indicative table to guide Rio Marking by sector/subsector (see tables pages 60-83 of the DCD-DAC (2016) report. See also:

OECD DAC Rio Markers Handbook for Climate & Rio Markers explanation DCD-DAC (2016), in particular pages 61-83

Criteria #3 – The project includes objectives or activities aimed at vulnerable groups (poor, disabled, children, other) and/or generating positive impact for women.

Pass/Fail

This criterion assesses whether the project has any activities or objectives (described in a project Concept Note) aiming at women and / or vulnerable groups (poor, children, disabled, ethnic communities, other). The Concept Note of the project needs to contain information on whether any of these groups will potentially benefit from the project. If there are no activities or objectives in the Concept Note referring to one of these groups the project will fail to meet this criterium and will not be eligible for DCFD financing.

¹ http://www.oecd.org/dac/financing-sustainable-development/development-finance-standards/DAC_List_ODA_Recipients2018to2020_flows_En.pdf

² <https://www.rijksoverheid.nl/binaries/rijksoverheid/documenten/kamerstukken/2018/11/13/kamerbrief-focusregios-en-andere-nota-onderwerpen/kamerbrief-focusregios-en-andere-nota-onderwerpen.pdf>

Criteria #4 -The project must provide assurance of national ownershipPass/Fail

The Concept Note of the project will contain a qualitative explanation of how the project fits with national development plans and priorities of the host country, including national climate change strategies and INDCs. The consistency of the project objectives and activities with the overall objectives, specific objectives or intended types of measures in the relevant national strategies should be explained in the Concept Note of the project promotor. If there is no alignment stated in the project document the project will fail to meet this criterium and will not be eligible for support.

Criteria #5: The project concept is potentially commercially viable & financial sustainablePass/Fail

The Concept Note for the project will contain a qualitative and quantitative explanation of the potential commercial viability for the project or business, including aspects such as (i) clearly identified clients / target groups with affordability to pay for goods or services, (ii) specific cost savings, (iii) potential for revenue generation and collection after implementation, and (iv) profitability.

Criteria #6 – The finance is additional to the market and does not distort local marketsPass/Fail

All activities that are financed from the DFCD are required to demonstrate their financial additionality. Additionality is interpreted in two ways. Relating to the *Origination Facility*, the development of the project concept (into a full proposal or business plan) should not be possible without the DFCD grant. This will be guaranteed by assessing whether the promotor does not have sufficient own means to develop the project concept and no subsidies (from host country or other institutions, such as IFI's) are in place for the development phase.

Regarding the *Investment Windows* the additionality check prevents the crowding out of private finance by DFCD financial support. Further, it relates to proposed terms and conditions by the Facility are not available from private (commercial) investors, at adequate scale, duration or on reasonable terms. Additionality can be proven through, for instance, the provision of local currency financing when not available, the provision of financing with longer tenors than provided by market parties, and the provision of mezzanine or growth equity.

Criteria #7 –The project should not be solely aiming at services such as institutional strengthening or enabling environmentPass/Fail

The objectives and activities in the project concept note will be assessed on the basis of this criterion. The core activities of the project consist of investment type of activities (works: new infrastructures and assets, renovations, land use change and improvements, direct aid to people etc.). When the project concept note contains core activities aiming at institutional strengthening (HR development & trainings, policy advise and development etc) or enabling environment (legislation change, policy support etc.) the project will fail this this criterion and will not be eligible for DFCD support.

Criteria #8 The project does not include any activities aimed at fossil fuels, nuclear energy or deforestationPass/Fail

Any projects with nuclear, fossil fuel or deforestation activities will also be ruled out under this criterion.

2. Second Stage Assessment Framework (AF Stage 2)

Projects and businesses which have passed the AF Stage 1 are eligible to receive funding from the investment windows managed by FMO and CFM. The AF Stage 2 is based on a more detailed project assessment and is designed to ensure that projects which receive investment finance have: (i) direct climate and development impact in line with the consortium's Theory of Change, (ii) fully comply with environmental and social requirements, and (iii) have sufficient financial viability as required by the investment criteria of FMO or CFM. Projects and businesses which receive grant funding from the Origination Facility will be supported by WWF or SNV to complete their climate and development impact assessments (based on the consortium impact indicators) prior to their second stage assessment.

The AF Stage 2 is based on four pass/fail criteria. Projects must pass all four criteria to receive investment financing from FMO or CFM.

Criteria #1: Direct climate and development impact on vulnerable groups, based on Theory of Change and Impact Indicators

Pass/Fail

Projects are assessed on both their direct climate change impact and their development impact on vulnerable groups.

Climate change impact: Under this overall criterion the direct climate change impact of the proposed projects are assessed. Projects should have either significant direct climate mitigation or adaptation impact in order to qualify for funding.

Development impact on poor and vulnerable groups: Under this overall criterion the direct developmental impacts of the proposed projects for vulnerable groups, in particular women and the poorest population are assessed.

Criteria #2: Compliance with environmental and social safeguards

Pass/Fail

The projects will comply with best practice Environmental and Social (E&S) safeguards. FMO and CFM will assess projects against the following international standards for E&S risk management: IFC Performance Standards, the World Bank Group Environmental, Health and Safety Guidelines or other internationally recognized sources, which include the International Labour Organization ("ILO") Core Labour Standards and ILO Basic Terms and Conditions of Work I and the International Bill of Human Rights in line with the UN Guiding Principles on Business and Human Rights.

Criteria #3: Financial viability

Pass/Fail

The financial viability of the project is an important criterion as funding business proposals with insufficient long-term market demand or insufficient revenues to cover long term operating costs need to be avoided. FMO and CFM will apply their investment criteria for this assessment. For CFM the key criteria are the ability of the investee companies to enter into contracts for revenues which provide sustainable and relatively predictable cash flows, limited exposure to demand and pricing risk and the ability of the investee companies to provide an appropriate risk adjusted return; and the ability of CFM to take a shareholding of significant influence in the investee companies. Entities that FMO invests in should be commercially viable with (expected) profitability complying with FMO's investment criteria for government funds.

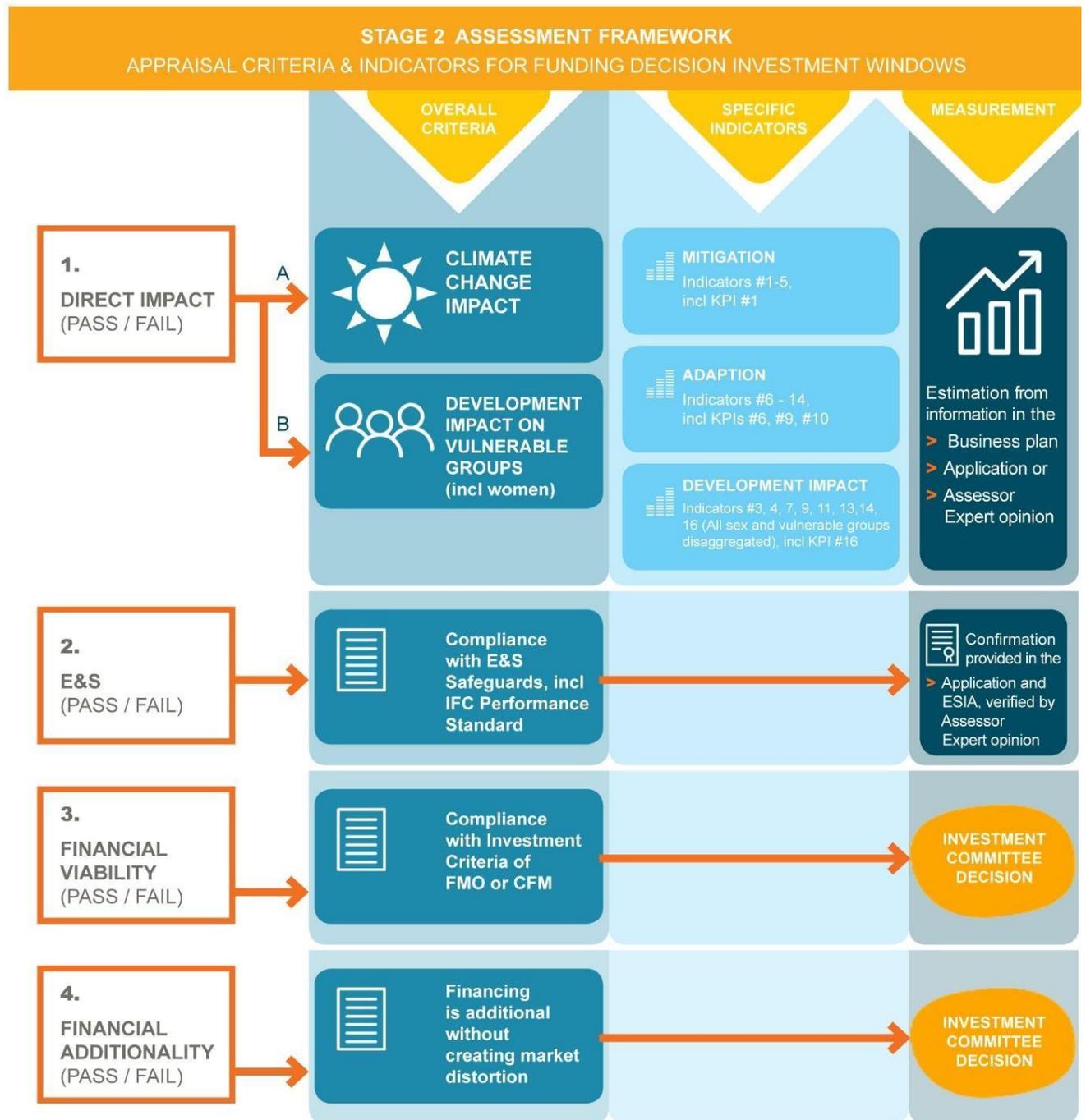
Criteria #4: Finance is additional and does not distort markets

Pass/Fail

To guide the effective and efficient use of public resources in private sector projects, a cross-DFI working group that includes FMO has translated a set of principles on blended finance into guidelines for operations in 2018. These align closely with the *OECD DAC Blended Finance Principles for Unlocking Commercial Finance for the Sustainable Development Goals*. FMO is currently in the process of operationalising the DFI blended finance guidelines and will use this to inform the additionality test, per the key principles set out below. CFM will work with FMO to ensure that it can deploy a similarly rigorous test in its Stage 2 Assessment Framework for the Water Facility. In setting these standards for ensuring avoidance of market distortion and sharing learning about the effectiveness of their operationalisation, the consortium ensures that international leading practice on leveraging private finance for climate and development remains at the core of the DFCD. Key principles for financial additionality:

- **Rationale for Using Blended Concessional Finance:** Support for the private sector should make a contribution that is beyond what is available, or that is otherwise absent from the market, and should not crowd out the private sector.
- **Crowding-in and Minimum Concessionality:** Support for the private sector should, to the extent possible, contribute to catalysing market development and the mobilization of private sector resources and minimize the use of concessional resources. Note: in general, as a basic rule the private capital in a transaction will be larger than the public funding coming in, to safeguard minimum concessionality.
- **Commercial Sustainability:** Support for the private sector and the impact achieved by each operation should aim to be sustainable. Support must contribute towards the commercial viability of their clients.
- **Reinforcing Markets:** support for the private sector should be structured to effectively and efficiently address market failures and minimize the risk of disrupting or unduly distorting markets or crowding out private finance, including new entrants.
- **Promoting High Standards:** private sector operations should seek to promote adherence to high standards of conduct in their clients, including in the areas of corporate governance, environmental impact, social inclusion, transparency, integrity, and disclosure.

Figure 2. Overall criteria and specific appraisal indicators for the second stage



IV. Glossary

Term	Definition
€	Euro
\$	United States Dollar
AEF	Access to Energy Fund (NL), managed by FMO
AF	Assessment Framework
AML	Anti – Money Laundering
Attribution	The ascription of a causal link between observed (or expected to be observed) changes and a specific intervention
Bn	Billion
CEF	Construction Equity Fund
CIF	Climate Investor Fund
CIO	Climate Investor One, a grid tied renewable energy fund managed by Climate Fund Managers
Climate-smart agriculture	An approach that helps to guide actions needed to transform and reorient agricultural systems to effectively support development and ensure food security in a changing climate
CO2e	CO2 equivalent – the amount of carbon dioxide (CO2) emission that would cause the same integrated radiative forcing or temperature change, over a given time horizon, as an emitted amount of a greenhouse gas (GHG) or a mixture of GHG
Co-benefits	The positive effects that a policy or measure aimed at one objective might have on other objectives, thereby increasing the total benefits for society or the environment
Conservation agriculture (CA)	A coherent group of agronomic and soil management practices that reduce the disruption of soil structure and biota*
Consortium	The DFCD Consortium, consisting of FMO, CFM, WWF-NL and SNV
Consortium Parties	FMO, CFM, WWF-NL and SNV
CSOs	Civil Society Organizations
DAC	The OECD Development Assistance Committee became part of the OECD by Ministerial Resolution on 23 July 1961. (OECD,2019)
DGIS	Directorate-General for International Cooperation part of the Ministry of Foreign Affairs, responsible for development cooperation policy and for its coordination, implementation and funding.
E&S	Environmental and Social
EC	European Commission
ESG	Environmental, Social and Governance
EU	European Union
Facility Managers	FMO, CFM, WWF-NL and SNV
Financial Close	The stage at which the conditions of a financial agreement have been satisfied, documents executed, and disbursements of funding becomes possible
Financing Facilities	The Origination Facility (managed jointly by WWF-NL and SNV), Water Facility (managed by CFM) and Land Use Facility (managed by FMO)
GCF	Green Climate Fund
GPF	Global Policy Framework
GHG	Greenhouse gas
IAP	Innovations Against Poverty
IATI	International Aid Transparency Initiative
IEA	International Energy Agency
IFC PS	IFC Environmental and Social Performance Standards: IFC's Environmental and Social Performance Standards define IFC clients' responsibilities for managing their environmental and social risks. (International Finance Corporation, 2019)
ILO	International Labour Organisation.
Investment Facilities	The Water Facility and the Land Use Facility

IWRM	Integrated Water Resources Management: a process which promotes the coordinated development and management of water, land and related resources in order to maximize economic and social welfare*
IPCC	The Intergovernmental Panel on Climate Change
IUCN	International Union for the Conservation of Nature
KPIs	Key Performance Indicators
KYC	Know Your Customer
LDCs	Least Developed Countries
Land Use Facility	Managed by FMO, this will provide a range of financial instruments to provide growth finance primarily for climate-smart agriculture and forestry projects
Lead Partner	FMO in its role as lead applicant for the Consortium
MASSIF	Managed by FMO, MASSIF is a Dutch government fund which focuses on small businesses and micro-entrepreneurs, women and youth entrepreneurs, as well as supporting innovations in inclusive business.
MoFA	Ministry of Foreign Affairs
NAMA Facility	The NAMA Facility provides tailor-made support for the implementation of highly ambitious and transformational NAMAs in developing countries. The Facility conducts competitive calls and selects the most ambitious and promising NAMA Support Projects for funding. (Nama Facility, 2019)
NDCs	Nationally Determined Contributions: a term used under the United Nations Framework Convention on Climate Change (UNFCCC) whereby a country that has joined the Paris Agreement outlines its plans for reducing its emissions
NGOs	A non-governmental organization
OECD	Organization for Economic Cooperation and Development
Origination Facility	Managed by WWF-NL and SNV collectively, this facility will provide grant funding and TA to work with companies and entrepreneurs to turn embryonic ideas into bankable business cases.
Paris Agreement:	An international agreement under the United Nations Framework Convention on Climate Change (UNFCCC) that commits signatories to 'Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C above pre-industrial levels'
PEPs	A politically exposed person (PEP) is an individual who is or has been entrusted with a prominent public function. (Comply Advantage, 2019)
PPPs	Public-Private Partnerships (PPPs) are arrangements whereby the private sector provides infrastructure assets and services that traditionally have been provided by government, such as hospitals, schools, prisons, roads, bridges, tunnels, railways, and water and sanitation plants ±
REDD+	Reducing Emissions from Deforestation and Forest Degradation: an international agreement with the objective of mitigating climate change through reducing net emissions of greenhouse gases through enhanced forest management in developing countries
Reforestation	Planting of forests on lands that have previously contained forests but that have been converted to some other use
Rio Marker 2 system	An OECD scoring system to determine and track ODA and investment flows with development aims.
SNV	Stichting SNV Nederlandse Ontwikkelingsorganisatie
SDGs	Sustainable Development Goals: the set of 17 global goals for development established by the United Nations
TA	Technical Assistance
ToC	Theory of Change
UBOs	Ultimate Beneficial owner refers to the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. (ComplyAdvantage, 2019)
UNGP	The UN Guiding Principles on Business and Human Rights are a set of guidelines for States and companies to prevent, address and remedy human rights abuses committed in business operations.(Business&HumanRights, 2019)
USAID	US Agency for International Development (US)
WASH	Water, Sanitation and Hygiene

Water Facility

Managed by CFM, this will focus on supporting project development and providing construction equity into water sector projects. This facility will raise additional private capital at fund level and is also referred to as Climate Investor Two (CI2)