



Adaptation Gap Report 2023 – Case Study

Adaptation finance: Mobilizing the private sector

This case study is part of the publication “Adaptation Gap Report 2023: Underfinanced. Underprepared. Inadequate investment and planning on climate adaptation leaves world exposed” (ISBN No: 978-92-807-4092-9). Suggested citation: United Nations Environment Programme (2023). Adaptation finance: Mobilizing the private sector. An online resource of *Adaptation Gap Report 2023: Underfinanced. Underprepared. Inadequate investment and planning on climate adaptation leaves world exposed*. Nairobi. <https://doi.org/10.59117/20.500.11822/43796>

The need for adaptation action is increasing as temperatures rise, and public finance alone will not be able to provide enough investment to achieve the impact required.

Unlocking private finance in support of climate action is one of the main challenges governments, international organizations and development banks have been grappling with since the Paris Agreement entered into force.

While the amount of private investments in adaptation is unclear, it remains a critical component of the global climate finance landscape. Most research to date has focused on public spending on adaptation rather than private adaptation, showing that overall progress in adaptation finance is insufficient.

Using small amounts of public funding to leverage large amounts of private-sector investment for clean energy and climate resilience projects in low- and middle-income countries, the Private Financing Advisory Network (PFAN) has been looking at tackling this challenge since 2006.

The overall process demonstrates that adaptation investments do not always require grant financing or compensation to be economically and financially viable. By providing expertise and mentorship, the PFAN initiative can help adaptation projects overcome barriers and facilitate private adaptation investments.

The Canadian International Development Research Centre worked with PFAN and the Frankfurt School of Finance & Management through two calls for proposals, which saw 477 business proposals seeking equity investment for climate adaptation projects. Thirty-nine well-developed adaptation projects emerged as bankable in various sectors, including agriculture, urban adaptation, water and sanitation, microfinance and microinsurance, energy access, tourism, forestry, ecosystem services and adaptation products and services.

The approach and methodology aimed at developing practical experience of identifying, developing and financing adaptation projects were proved successful as they tested impact investors’ appetites to fund adaptation projects and build the capacity of both developers and investors.

For example, the African Bamboo project, one of the 39 emerging projects, sought equity finance for its innovative business model of converting bamboo into wooden decking, including anticipatory adaptation components like identifying highland and lowland growing areas where bamboo would prosper. The business model was analysed, and potential grant funders were identified to support its initial development before seeking private-sector finance for scaling up. This helped the project overcome challenges arising from imperfect capital markets and asymmetric information, which impacted the return profile of the investment.

The Classic Foods project from Kenya was another project inducted into PFAN’s list of investor-ready projects. The company pioneered the collection and processing of milk from small-scale farmers by providing refrigeration for bulk milk and thus an opportunity to supply farmers with a range of inputs, including animal feeds and grains. The project aims to help farmers adopt sustainable farming methods that improve soil productivity and lead to better economic prospects. It also trains farmers in effective agricultural practices and reducing post-harvest losses.

The projects were showcased at two separate Investor Forums to attract potential investors and international funding agencies interested in supporting adaptation projects initiated by small and medium-sized enterprises. The Investor Forums provided an opportunity to share project development and management best practices, expose project developers to the thinking and expectations of investors and finance providers in a low-risk environment and provide a forum for investors and finance providers to interact with developers. It also provided a clearer understanding of the investment perspective of adaptation business models.

The PFAN pilot adaptation workstream raised a total of US\$2 million for four different adaptation projects.

Feedback from the Investor Forum highlighted that adaptation projects are attractive to investors, although they must be in line with financial, strategic, regulatory and risk management considerations; private finance providers will always be motivated by factors beyond just the goal of adaptation itself.

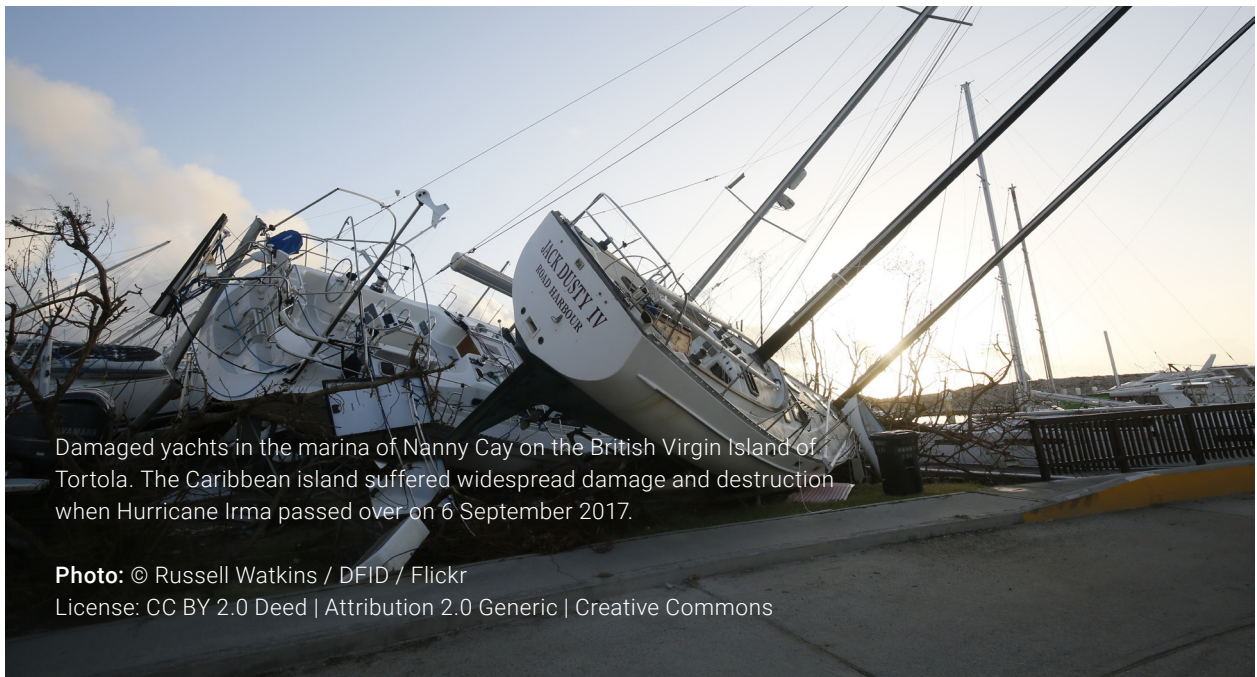
Designing and operationalizing mechanisms that may help address market imperfections and unlock private adaptation finance is a lengthy process, and efforts by initiatives such

as the PFAN are essential to facilitate private adaptation finance in the interim.

The PFAN model also demonstrates that private adaptation investments can be facilitated or realized by targeting market imperfection directly and without compensating private actors. The model has shown there is an enormous innovation potential with respect to reducing climate impacts and creating new sustainable business models in response to the climate crisis. It has also demonstrated the importance – but also the challenges – of providing a stage for this creativity to thrive.

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