

# Design Considerations for the Green Climate Fund Micro-, Small- and Medium-Sized Enterprise Programme

ActionAid USA, Friends of the Earth US, Institute for Policy Studies

We welcome the creation of a Pilot Programme to support micro-, small-, and medium- sized enterprises (MSMEs) with an allocation of up to US\$200 million over the course of the GCF Initial Resource Mobilization period. MSMEs account for the vast majority of private companies in developing countries, with the informal sector composing the largest share. A robust and effective Pilot Programme thus holds the potential for deep penetration of climate-friendly, sustainable economic activity in developing countries. Multilateral development banks have a poor track record in effectively reaching and cultivating MSMEs in environmentally and socially sound ways. There is much to be learned from an effective MSME pilot at the GCF.<sup>1</sup>

The MSME Programme could play a significant role in meeting several of the GCF's objectives. The Fund's governing instrument stresses the importance of country ownership, including channeling private finance to SMEs and local actors, as well as stressing the importance of support for private sector activities in SIDS and LDCs.

The disproportionately high share of MSMEs and micro-enterprises in developing countries operated by women entrepreneurs means that it also has the potential to contribute significantly to operationalizing the GCF's gender-sensitive approach.

## Scope

- **Demand-driven.** As a first step for establishing the MSME Programme, it will be critical to start with a comprehensive overview of what MSMEs themselves say they need, with the MSME Programme designed to reflect MSME-determined needs. For example, energy access practitioners have themselves communicated clearly about the financial barriers that need to be addressed in order for them to substantially expand their reach.<sup>2</sup>

- **Strengthening “local actors”.** The MSME Programme should look to support local financial institutions. Given the design of the GCF, any serious attempt to reach MSMEs will by necessity have to go through financial intermediaries. The intermediaries chosen to administer the MSME programme should be required to show strong local knowledge, including a track record of working with credit unions, cooperatives, and local banks. To ensure country ownership the MSME Programme should, to the greatest extent possible, prioritize direct access financing rather than working through international intermediaries. In support of this objective, capacity building for local financial institutions should be a priority area to be addressed in the chosen pilot projects.

---

<sup>1</sup> For more background on this topic, see Friends of the Earth U.S. and Pan African Climate Justice Alliance (2013) Pro-poor Climate Finance: Is There a Role for Private Finance in the Green Climate Fund, <http://www.foe.org/news/archives/2013-04-pro-poor-climate-finance-is-there-a-role-for-private>

<sup>2</sup> See, for example, Ashden and Christian Aid, Lessons on Supporting Energy Access Enterprises, <http://www.christianaid.org.uk/images/Ashden-Christian-Aid-Energy-Access-Enterprises-Report.pdf>

Areas which should be covered include capacity building to ensure that local financial intermediaries are able to provide the requisite due diligence to ensure sub-project compliance with the GCF's environmental and social safeguards, fiduciary standards, and co-benefit outcomes (i.e. including development outcomes).<sup>3</sup>

The MSME Programme should also target the local supply chain, including technical support and capacity building for local manufacturers, suppliers, distributors and technicians responsible for operation and maintenance – helping to create a strong national value chain that provides broader economic benefits.

- **Distributed renewable energy.** Without anticipating the full sectoral scope of the MSME Programme, initial priority should be given to the distributed renewables sector, which holds significant potential for matching its objectives, including growing local economies, an anchor for sustainability. A key characteristic of distributed renewables is that they produce energy close to where it will be used. A second fundamental is that the ownership model for this type of energy generation is also distributed: small companies, co-ops and communities can be the producers of their own energy.

Distributed renewables can offer the opportunity to rapidly scale-up renewables capacity, precisely because they do not have the development times of large-scale infrastructure. MSME programmes to roll out solar home systems, for example, could help millions of people to access energy rapidly (they are far quicker to deploy than grids) in a climate-friendly manner while supporting the local economy. As industry sources such as the Global Off-Grid Lighting Association point out, distributed renewable energy is a market that is restricted on the supply rather than the demand side – with a lack of access to various classes of capital.

As the GCF's Private Sector Advisory Group has pointed out, support for distributed renewables could include provision for “flagships or lighthouse projects, such as the elimination of kerosene or charcoal cooking, support (off-grid) LED lighting, distributed renewables, or off-grid solar.”<sup>4</sup> There already exist real-world examples of how to target MSMEs in the renewables sector. UNEP's Rural Energy Enterprise Development (REED), for example, targets seed capital to renewable energy entrepreneurs in developing countries, with a focus on small-scale projects that have “significant potential for scalability” but are unlikely to attract commercial funding.<sup>5</sup> A number of national development banks also provide specific MSME financing facilities, including the provision of soft loans and technical assistance.<sup>6</sup>

- **Reaching micro- and small-scale enterprises.** In operationalizing the MSME Programme, it is important that the Programme engages micro- and small-scale enterprises as well as medium-sized ones. The MSME Programme should target a floor of two-thirds of its funding towards micro- and

---

<sup>3</sup> This will be a considerable challenge. The IFC's record of working through financial intermediaries is poor as far as positive social and environmental impacts. For example, see CAO (2012) CAO Audit of a Sample of IFC Investments in Third-Party Financial Intermediaries. Office of the Compliance Advisor-Ombudsman, World Bank Group. [http://www.cao-ombudsman.org/newsroom/archive/documents/Audit\\_Report\\_C-I-R9-Y10-135.pdf](http://www.cao-ombudsman.org/newsroom/archive/documents/Audit_Report_C-I-R9-Y10-135.pdf).

<sup>4</sup> Recommendations from the Private Sector Advisory Group to the Green Climate Fund, [http://www.gcfund.org/fileadmin/00\\_customer/documents/MOB201507-10th/16\\_-\\_Recommendations\\_from\\_the\\_PSAG\\_20150618\\_fin.pdf](http://www.gcfund.org/fileadmin/00_customer/documents/MOB201507-10th/16_-_Recommendations_from_the_PSAG_20150618_fin.pdf)

<sup>5</sup> Griffith-Jones, S. et al. (2011), p.27

<sup>6</sup> Dalberg. (2015). Increasing MSME access to climate finance. Retrieved from [http://cdkn.org/wp-content/uploads/2015/10/CDKN-Dalberg-Access-to-Finance-for-MSMEs\\_-final-1.pdf](http://cdkn.org/wp-content/uploads/2015/10/CDKN-Dalberg-Access-to-Finance-for-MSMEs_-final-1.pdf), p.44

small-scale enterprises.

The classification of what counts as an MSME, including the defining size and total revenue of a particular company, should reflect developing country realities, rather than those of developed countries – and, in the absence of a GCF-wide definition, should adapt to local norms. For example, the Indian government defines micro-enterprises as those whose investments in equipment do not exceed Rs.25 lakh (around US\$40,000), and small enterprises as those whose investments in equipment range from Rs.25 lakh to Rs.10 crore (around US\$750,000).

- **Informal sector.** The MSME Programme should explicitly reach out to the informal sector, which accounts for the vast majority of MSMEs in developing countries. Technical assistance and capacity building, as well as a small grants scheme (see below) can be particularly important in this regard.

## Financial Instruments

In order to reach small-scale actors that otherwise have limited access to finance, it is important that the MSME Programme is able to cover (or substantially reduce) the costs of initial investment risks and capital, as well as provide technical support and capacity building. Options include:

- **Technical assistance and capacity building.** Grant financing for technical assistance and capacity building should form a core part of the activities of the MSME Programme.

The Technical Assistance Facility of the KawiSafi Ventures Fund provides a good example of the potential scope, with support for “business development services” (advice for entrepreneurs on accounting, marketing, after-sales support, etc.), management and employee training; support to develop companies’ capacity to monitor and evaluate projects, including fulfilling environmental and social safeguard requirements; and support to improve corporate governance.<sup>7</sup> Notably, it also dedicates a significant proportion to “gender specific interventions”, including training women as solar technicians, education to support the effective uptake of solar systems in place of kerosene cook stoves, and work with women-focussed micro-finance and savings groups. This gender dimension is welcome, though could be enhanced by a firmer commitment to ensuring that fund investments go to women entrepreneurs and women-led companies.

- **Payment guarantees.** In the case of distributed renewable energy, payment guarantee schemes could prove particularly useful. Such schemes could help to ensure that renewable energy providers receive both up-front investment to cover capital costs as well as long-term tariff guarantees to ensure cost competitiveness with older, dirtier forms of energy. This is likely to involve a grant element provided by the GCF to cover the full incremental costs of increasing the proportion of renewables in the electricity mix. The institutional arrangements are likely to vary, but could include a coordinating role for national renewable energy access agencies.<sup>8</sup> A more detailed account on how this could be implemented has been elaborated by What Next Forum and Centre for Science

---

7 GCF/B.11/04/Add.05/Rev.01. Funding proposal package for FP005. Retrieved from: [http://www.gcfund.org/fileadmin/00\\_customer/documents/MOB201511-11th/04\\_Add\\_05\\_-\\_FP005\\_and\\_NOL.pdf](http://www.gcfund.org/fileadmin/00_customer/documents/MOB201511-11th/04_Add_05_-_FP005_and_NOL.pdf), p.3

8 Hallstrom, N. (2014), Hallstrom, N. (2014). Global renewable energy support programme. Retrieved from: <http://www.whatnext.org/resources/Publications/Energy/White-Back-Page.pdf> p.25

and Environment.<sup>9</sup>

- **Loans and guarantees.** If the MSME Programme is to provide loans and guarantees across the full spectrum of MSMEs, including the informal sector and early stage companies, it needs to be able to provide non-collateralized capital, and at the same time avoid an over-reliance on “track record” and credit history. This necessarily entails an element of risk, although this should be considered appropriate in the case of the MSME Programme.

The MSME Programme of the ICICI Bank in India provides a good example of how to evaluate credit risks in the absence of a long, formal track record – using a “360 degree” approach that incorporates credit scorecards (based on industries and market segments), value analyses, site visits and personal references.<sup>10</sup>

- **End-user finance.** In the case of finance for renewable energy access, end user financing remains a key gap (hence, the insistence on capacity support for local financial intermediaries). There are several models for how this might be addressed. For example, the MSME Programme could provide grants to project developers/local financial institutions so that they can reduce or waive up-front payments (“margin money”), or so that they can restructure consumer loans to increase concessionality, reduce interest rates, increase grace periods or lengthen repayment periods.<sup>11</sup> End-user financing of this sort can contribute significantly to energy access, and to the growth of a potential market (e.g. for solar home systems) for MSMEs to operate in.

- **Risk guarantees.** Risk guarantees and related facilities could play an important role, but the focus should fall on how to reduce risk for MSMEs themselves and domestic financial institutions, rather than looking at how to reduce risks for large institutional investors. This could be achieved by various means, including providing (partial) risk guarantee facilities to domestic intermediaries, and capacity building/advice, where needed, on evaluation of project risks and business models for renewables, energy efficiency and other forms of climate change financing.

- **Consumer protection.** As previously discussed, the MSME Programme should include informal sector, micro-scale and start-up companies that often have little financial track record. Invariably, some of these companies will fail, but the burden of this should not fall on consumers (such as households or other MSMEs). The KawiSafi Technical Assistance Facility also offers a good example here, in offering consumer protection grants that could provide:

1. Capital to service installed solar home systems in the event that a solar company goes bankrupt, most likely through partnership with an existing service provider;
2. Capital to facilitate an acquisition of / partnership with a defunct company by a viable company so that consumers will still receive after-sales support;
3. A mechanism to provide some level of monetary value to consumers for their purchased

---

9 CSE and What Next? (2015) Programme for Global Renewable Energy and Energy Access Transformation, [http://www.cseindia.org/userfiles/GREEAT\\_Final.pdf](http://www.cseindia.org/userfiles/GREEAT_Final.pdf)

10 Dahlberg (2015) Increasing MSME Access to Climate Finance, p.32

11 See, for example, the case studies in Selco (2009). Access to Sustainable Energy Services via Innovative Financing. Retrieved from: [http://www.selco-india.com/pdfs/selco\\_booklet\\_web.pdf](http://www.selco-india.com/pdfs/selco_booklet_web.pdf) and Arc Finance Ltd (2009) End-user finance. A guide for sustainable energy enterprises and NGOs. Retrieved from: [https://www.ashden.org/files/pdfs/reports/Enduser\\_finance\\_guide.pdf](https://www.ashden.org/files/pdfs/reports/Enduser_finance_guide.pdf)

products in the event of a company bankruptcy where products can no longer be serviced.<sup>12</sup>

- **Small Grants Facility.** A small grants facility could be a useful component of the MSME Programme. A small grants facility recently approved by the Adaptation Fund offers a good, replicable example of how this might be structured – via a mix of local capacity building for local institutions, alongside direct grant support of up to US\$100,000 for community-based organizations and local NGOs.<sup>13</sup>

## Multi-stakeholder consultation

Multi-stakeholder engagement should be understood as a lasting partnership with the full range of climate and development stakeholders, especially affected communities.<sup>14</sup> Consultations should be structured such that stakeholders can contribute to planning consultation meetings, prepare and participate fully (including in local languages), and meaningfully influence the outcomes. Efforts should be made to include women's organizations and representatives of marginalized groups. Affected communities should be empowered to exercise their right of free, prior and informed consent. The MSME Programme should, where appropriate, support training and skills-building for (local) government and civil society actors, to help them participate in meaningful consultations and assume effective roles.

## Adaptation

The MSME Programme is not supposed to be limited to mitigation and energy access. Adaptation is largely a public, non-profit-producing endeavour. There have so far been few profitable adaptation opportunities that benefit those most in need. Careful thought will need to be put into the Programme's approach to MSMEs and adaptation, especially with regard to whom the Programme is supposed to benefit. The GCF Adaptation Window more broadly should focus on adaptation of vulnerable communities, not on supply-chain resilience for multinational companies. Because of the specific focus of the MSME Programme on local enterprises, it is possible that the programme *could* support resilience efforts for these private sector actors, so long as the beneficiaries of these enterprises are local and thus the ultimate goal of increasing resilience of communities is still achieved.

## Transparency, monitoring and evaluation, and learning

The MSME Programme should implement the highest degree of transparency possible in policy, operations, and implementation. Clear rationales should be provided for why certain pilot projects were chosen and others rejected. Rigorous monitoring and evaluation are foundational and determinant of the ability to learn from the Pilot Programme.

---

12 GCF/B.11/04/Add.05/Rev.01, p.3

13 Adaptation Fund. (2015). Taking Adaptation to the Ground: A Small Grants Facility for Enabling Local Level Responses to Climate Change, <https://www.adaptation-fund.org/project/taking-adaptation-to-the-ground-a-small-grants-facility-for-enabling-local-level-responses-to-climate-change/>

14 For a good example offering more detailed guidance on multi-stakeholder guidance, see <https://www.interaction.org/document/creating-strong-stakeholder-engagement-feed-future>