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Private Finance for Climate-Change Adaptation: Challenges and Opportunities for Kenya

Summary

Private investments in climate-change adaptation are important. First, because the costs of adaptation are too high to be met by the public sector alone. And second, developed countries pledged to mobilise USD 100 billion annually by 2020 to support developing countries' climate change mitigation and adaptation; the private sector is described as a source of finance. Yet how realistic is it to rely on the mobilisation of private investments in adaptation, in particular for less developed countries? This Policy Brief aims to answer this question in relation to Kenya. It is based on interviews and an analytical framework that spells out enabling environments; mobilisation and delivery of private investments (see Figure 1).

As a first step, developing and developed countries, and the private sector can create enabling environments to mobilise private investments in adaptation. Adaptation is a priority to both the Kenyan government and its development partners. However, private adaptation has not been mainstreamed in key government policies. The Kenyan private sector appears unfamiliar with the concept of adaptation. Where it acts on adaptation, its purpose is generally resource efficiency or to address land degradation.

This makes it hard to track mobilised private investments. For example, rural communities might contribute to adaptation though improved water management. However, related expenditure remains unknown, as is the extent to which it is financed by banks. Neither actor tracks or reports investments in adaptation.

It is even harder to assess if private investments, once mobilised, actually deliver on adaptation. Regardless of the underlying motivations, many investments that reduce poverty or stimulate sustainable resource use contribute to adaptation. However, a private actor can also adapt at the expense of communities, for example by securing or fencing off its own water intake. There are no explicit checks and balances on private-sector impacts on adaptation. Safeguards such as environmental impact assessments (EIAs) do not explicitly address adaptation.

All of the above make it extremely difficult to assess private investments in adaptation in Kenya, in particular in the context of the above-mentioned USD 100 billion target. Kenya's private sector has taken little interest in the UN climate negotiations. It is currently not able to tap into international funds such as the Green Climate Fund. If it could, private actors might take more interest in adaptation and the UN negotiations. This in turn might also provide incentives for quantifying investments in adaptation.

The Kenyan government could encourage more private-sector investments in adaptation. By stimulating a shared public-private awareness and understanding of adaptation, the government could improve enabling environments for private adaptation; mobilise more private investments; and improve the tracking of private investments in adaptation. Moreover, the government and development partners could include adaptation criteria in project selection and EIAs in order to reduce private maladaptation and increase private adaptation.

Introduction

In the Paris Agreement, developed countries reaffirmed their commitment from the 2009 Copenhagen Accord to mobilise USD 100 billion annually by 2020 to support climate-change mitigation and adaptation in developing countries. A substantial share of this money will come from private sources. A second reason for mobilising private investments in adaptation is that the costs of adaptation are too high to be met by the public sector alone. UNEP's 2016 Adaptation Finance Gap report estimates the annual adaptation costs at up to USD 300 billion by 2030.

Yet how realistic is it to assume that the private sector can finance adaptation, in particular in less developed countries? This Briefing Paper aims to answer this question for Kenya. It is based on an analytical framework (see Figure 1), as well as 20 interviews with policy-makers, representatives of the private sector and civil society, and researchers in Kenya in 2016.

Researchers, policy-makers and others have been trying to identify the potential of private climate finance. Hundreds of billions of dollars are invested in climate-change mitigation annually, but very little of this goes to Africa. It is not clear exactly how much private finance is invested in adaptation. The small amount of research that has been done on adaptation has generally focused on positive contributions, neglecting negative private-sector impacts on climate resilience.

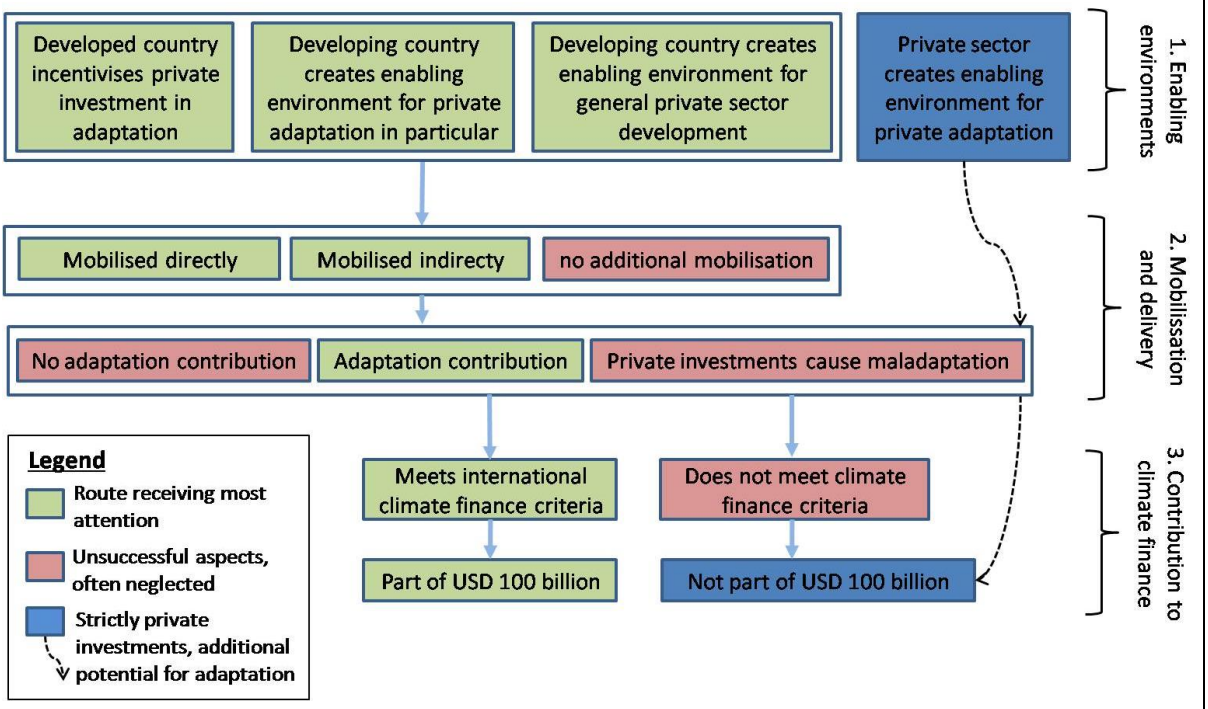
This Briefing Paper builds on the analytical framework for understanding private adaptation finance (see Dzebo & Pauw, 2015, and Figure 1). The framework focuses on the interaction between enabling environments, mobilisation and delivery mechanisms. It examines not only how investments can be made, but also the various reasons why adaptation objectives might not be met. For example, "enabling environments" might not actually mobilise additional finance, or consequent investments might increase vulnerability by causing maladaptation. The following pages look into these factors in the context of the study findings in Kenya.

Kenya

Kenya was studied because it prioritised adaptation and private-sector adaptation in its Intended Nationally Determined Contribution (INDC) in 2015. This national climate action plan was formulated in the context of the UN climate negotiations. Kenya's economy has grown by more than five per cent per annum during the past ten years, and its rapidly growing population has now reached 46 million. Kenya's economy is largely rural and is heavily dependent on its natural resource base. Water in particular is important, for instance for domestic use, energy generation, agricultural development, industrial growth and for livestock and tourism development. Kenya's natural resource base makes the country highly vulnerable to climate change.

Kenya's INDC stresses the need to build capacity among private-sector actors and to create resilience in value chains of tourism, agriculture, fisheries and livestock. It also stresses the importance of adaptation in the housing and the extractives sectors. Although the respondents in this study acknowledged this emphasis on private-sector adaptation, they also said that this was relatively new in Kenya and that the private sector's awareness of adaptation.

Figure 1: An integrated approach to private adaptation finance



Source: adapted from Dzebo & Pauw, 2015.

Enabling environments

How is Kenya creating an "enabling environment"? In other words, how is Kenya creating institutional and regulatory frameworks that create incentives for private investments in climate-related activities?

Kenya has a comparatively good **general enabling environment** for private investments. It is ranked ninth out of the African countries in the World Bank's "ease of doing business" ranking. However, the respondents mentioned only a few adaptation benefits, such as a rule prohibiting commercial loggers to cut trees under 20 years old (potentially preventing land degradation); and the adoption of policies on irrigation and drought-resistant seeds.

The Kenyan government is also working on an **enabling environment for private adaptation**. For example, Kenya's INDC refers to an enabling environment to foster the resilience of private investments in trade and manufacturing, and the demonstration of business cases. Several respondents referred to the climate change bill (later enacted as the Climate Change Act 2016), which was drafted with private-sector participation. It raises the legal status of addressing climate change and the mobilisation and transparent management of climate finance. Kenya also set up new institutions: a National Climate Change Council chaired by Kenya's president, and a Climate Change Directorate under the Ministry of Environment and Natural Resources. "Climate desks" are established at the National Treasury, the Ministry of Energy and Petroleum, and the Ministry of Agriculture, Livestock and Fisheries.

Many respondents expect these measures to improve the enabling environment for adaptation, address coordination problems and enhance ministries' capacities. For example, one respondent stated that the link between value chain management and adaptation has been weak because adaptation has not been an important issue for ministries of trade and agriculture.

Enabling environments are also created from abroad. The Paris Agreement encouraged the government to table a climate change bill and influenced its architecture and the focus on climate finance. The formulation of a Climate Change Action Plan was financed by DFID. Finally, development agencies such as DANIDA and GIZ actively promote private-sector participation in climate projects. A number of respondents were critical of the latter: for example, the focus on private actors was said to be at the expense of NGOs, which have many years of experience in adaptation and capacity-building. Indeed, a respondent from the private sector said that his company had very little experience in working with development agencies.

Finally, an **enabling environment is created by the private sector**. One respondent stated that Kenya, unlike some Western countries, does not have "100 big companies that demand more climate ambition from the government". The private sector does however enable other private actors' adaptation, for example through value chain management. For example, the Kenya Tea Development Authority, the Coffee Board of Kenya and the Kenya Flower Council enforce policies on their farmers as suppliers and members. For high-value export crops such as tea and flowers, the industry sets quality standards; employs extension officers; and tracks back bad harvests. This is not the case with crops such as maize and beans, and with subsistence farming.

Modern technology can also contribute to adaptation. For example, millions of Kenyans have gained access to finance through the mobile money transfer technology of M-Pesa, which boosted their resilience to harvest losses, for instance.

A number of respondents noted that the financial sector is investing more and more in mitigation activities such as clean cooking stoves and solar energy, but not in adaptation-related products such as biofertilisers and irrigation equipment.

Overall, we identified a variety of ways in which private adaptation is stimulated, most often indirectly. However, a comprehensive enabling environment for adaptation financing is still lacking. Raising awareness of adaptation is an important step, both at ministries and among private actors, who often deal with adaptation without being aware of it. The creation of an enabling environment that is more effective in mainstreaming adaptation is a task for public and private actors alike.

Mobilisation and delivery

All respondents mentioned the lack of quantitative data on mobilised private investments in adaptation. It is therefore unclear how effective enabling environments are. Apart from the low private-sector awareness (see above), the respondents ascribed this to the absence of a definition of "private adaptation finance". For example, it is not known how much communities spend on adaptation, and to what extent such expenditure is financed by financial institutions. None of these actors keeps track of adaptation. This is similar for companies: respondents said that they invest in sustainable water catchment management and sustainable tourism, but that this is neither labelled nor quantified as adaptation.

Direct mobilisation of private investments means that a public agency provides seed funding or co-finances projects together with private actors. Respondents mentioned just one example of this: Kenya Biologics' development of organic fertilisers started with seed funding from the donor-supported Climate Innovation Centre, and later received an investment in the form of private equity from a Dutch firm. Several respondents from both the private sector and development organisations complained that climate finance is currently too close to central government for the private sector to benefit and for donors to retain ownership over the finance they provide.

The causal links of **indirect mobilisation** are not always clear. Although it may involve financial instruments, it usually entails non-financial interventions, such as policy and regulatory conditions or public investments (e.g. in infra-

structure) that enable or influence private investments. One respondent stated that indirect mobilisation could be encouraged by making private actors aware that adaptation requires targeted investments. Respondents cited various examples of private investments contributing to adaptation, including (loans for) climate-smart agriculture; social entrepreneurship; ecotourism; and improved water management. However, the extent to which such contributions are indeed "indirectly mobilised" remains unclear. Representatives of donor agencies said that they do not track indirectly mobilised private investments.

Finally, it is also possible that **no private finance is mobilised**, despite the presence of an enabling environment. Very little is known about this. However, several respondents referred to the non-enforcement of policies to stimulate adaptation in the agricultural sector. For example, farmers still grow crops close to rivers and on slopes. Despite extension services, farmers also still do monocropping. Finally, much climate-smart agriculture depends on in-kind contributions from smallholders, meaning that no finance is mobilised.

It is hard to assess whether private adaptation is mobilised, and even harder to assess whether private investments really **deliver on adaptation.** In general terms, many of the actions described above that reduce poverty or make natural resource use (in particular water) more sustainable, also contribute to adaptation. This is regardless of whether they are motivated by the need to address climate change impacts.

However, as some respondents pointed out, private adaptation can also increase vulnerability elsewhere. For example, if a company protects its water supply, it might either benefit communities (if increased water efficiency increases water availability to communities) or harm them (if the company secures its water intake at the cost of others' access to water). This is why transparency and safeguards are important. According to a number of respondents, businesses have not adopted explicit checks and balances with regard to their impact on adaptation. Respondents also stated that current safeguards used by both the government and development agencies, such as EIAs, have very little effect on adaptation. The inclusion of specific adaptation criteria in EIAs, for example on water and land use, would reduce private maladaptation and increase private adaptation.

Contributing to climate finance

One of the conditions for private adaptation investments to form part of the USD 100 billion of climate finance, is that they need to be mobilised by developed countries. Although Kenya's Climate Change Action Plan focuses on private mitigation finance, it also seeks to mobilise private adaptation finance. Regardless of who mobilised it, there is currently little direct, explicit private investment in adaptation. Several respondents said that Kenyan private actors are users and implementers of adaptation interventions, not financiers – and that the global political debate on the USD 100 billion hardly sparked the private sector's interest to date.

This situation might change if Kenyan private actors could tap into the Green Climate Fund or other funding opportunities. At the same time, this might also provide an incentive to monitor and quantify private investments in adaptation.

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