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Providing International Adaptation Finance for Vulnerable Communities: A Study on Potentials and Limits of Social Investment Funds

Britta Horstmann
Günther Schulz-Heiss

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The German Development Institute / Deutsches Institut für Entwicklungspolitik (DIE) is a multidisciplinary research, policy advice and training institute for Germany's bilateral and multilateral development cooperation. On the basis of independent research, it acts as consultant to public institutions in Germany and abroad on current issues of cooperation between developed and developing countries. Through its nine-month training course, the German Development Institute prepares German and European university graduates for careers in the field of development policy.

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Bonn, July 2014 Britta Horstmann, Günther Schulz-Heiss

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Abbreviations

AAA	Accra Agenda of Action
AF	Adaptation Fund
AFB	Adaptation Fund Board
AFR	Africa
AFRICATIP	Association Africaine des Agences d'Exécution des Travaux d'Intérêt Public
CEO	Chief executive officer
CCT	Conditional cash transfer
CDD	Community-driven development
CDM	Clean Development Mechanism
COP	Conference of Parties
CSO	Civil society organisation
DRR	Disaster risk reduction
EAP	East Asia and Pacific
ECA	Europe and Central Asia
FHIS	Fondo Hondureño de Inversión Social (Honduras)
FIS	Fondo de Inversión Social (Social Investment Fund) (Guatemala)
FISE	Fondo de Inversión Social de Emergencia (Social Investment Emergency Fund) (Nicaragua)
FISDL	Fondo de Inversión Social para el Desarrollo Local (El Salvador)
FODESAF	Fondo de Desarrollo Social y Asignaciones Familiares (Costa Rica)
FONCODES	Fondo de Cooperación para el Desarrollo Social (Cooperation Fund for Social Development), formerly Fondo Nacional de Compensación y Desarrollo Social (Peru)
FONVIS	Fondo de Inversión Social de Venezuela (Venezuela)
FOPAR	Fondo Participativo de Inversión Social (Argentina)
FOSIS	Fondo de Solidaridad e Inversión Social (Chile)

FPS	Fondo (Nacional) de Inversión Productiva y Social (Social and Productive Investment Fund) (Bolivia)
FSE	Fondo Social de Emergencia (Emergency Social Fund) (Bolivia)
FY	Financial year
GCF	Green Climate Fund
GEF	Global Environment Facility
IDA	International Development Association
IDB	Inter-American Development Bank
IFI	International finance institution
ILO	International Labour Organization
KfW	Kreditanstalt für Wiederaufbau (KfW Development Bank)
KP	Kyoto Protocol
LAC	Latin America and Caribbean
LG	Local governments
LoCAL facility	Local Climate Adaptive Living facility (UNCDF)
MENA	Middle East and North Africa
NAMA	Nationally appropriate mitigation actions
NAP	National adaptation plan
NAPA	National adaptation programme of action
NGO	Non-governmental organisation
NIE	National Implementing Entity
O&M	Operation and maintenance
ODA	Official development assistance
PAMI Program/ RSS	Programa Alimentario Matemo Infantil/ Red de Solidaridad Social (Colombia)
PFM	Public financial management
PIU	Project implementation unit
PMP	Participatory municipal planning
PMU	Project management unit

PPCR	Pilot Program for Climate Resilience
PRONASOL	Programa Nacional de Solidaridad (Mexico)
PRS	Poverty reduction strategy
REDLAC	Social Network of Latin America and the Caribbean
SAP	Structural adjustment programme
SEDESOL	Secretaría de Desarrollo Social (Peru)
SIF	Social investment fund
UNCDF	United Nations Capital Development Fund
UNFCCC	United Nations Framework Convention on Climate Change
ZAMSIF	Zambian Social Investment Fund

Summary

Context

The provision of (international) finance for adaptation needs in vulnerable and local communities is a key element and declared political goal of the United Nations Framework Convention on Climate Change (UNFCCC) and national governments in addressing the adverse effects of climate change. Towards that respect, governments need to design effective and efficient institutional arrangements that allow the channelling of adaptation funds while meeting national and international funding requirements.

At the international level, governments are currently facing a dilemma between maximising the use of financing institutions under the climate regime on the one hand, and maximising the use of country institutions and systems on the other. While both the Adaptation Fund (AF) and Green Climate Fund (GFC) under the climate regime are pioneering the use of country institutions through their direct access modality, their possibilities of maximising the use of country systems are (so far) limited in comparison to financing modalities of official development assistance (ODA). This might be to the disadvantage of local adaptation needs as adaptation finance under the climate regime has been mainly distributed on a project-based approach which implies high transaction costs, thus disadvantaging small-scale adaptation needs at the local level. The targeted allocation of (international) adaptation finance to vulnerable communities, small-scale adaptation needs, and to actors at the local level is an area that calls for innovation.

Goal and methodology of study

In this context, this study looks at the potential of social investment funds (SIFs) in allocating adaptation finance. The potential of using SIFs in adaptation finance is discussed on the basis of climate and development finance criteria and a review of operational strengths and weaknesses. Towards that end, the study provides a brief overview of the international adaptation finance architecture, related financing requirements, and challenges. It furthermore delineates the evolution, geographical extension and financial magnitude of these types of funds along with their operational

characteristics and discusses related practical experience and evaluations. The analysis is based on a literature review and own work experience.

The potentials, limits, and challenges of using SIFs in adaptation finance

The analysis shows that SIFs can be a strong partner for the distribution of resources to communities vulnerable to climate change. Social investment funds are government-owned institutions which have been used by international financial cooperation for more than 20 years. They have been established in more than 60 countries and have been used to channel high volumes of public money to local level development activities (e.g. 60 % of the International Development Association (IDA)'s social protection portfolio between 2000 and 2007). In many countries, SIFs can, therefore, serve as a learning experience for institutional design or, where they still exist, as a potential facility through which to channel adaptation finance.

Experience with SIFs in the past indicates that the SIF model is generally in a good position to provide targeted investments for small-scale adaptation needs in a decentralised and community-driven way. They are known for their potential to bundle large numbers of small-scale projects at the local level into national programmes, thereby reducing transaction costs. Part of the SIF model's success builds on community participation in project selection, design, implementation and management. The involvement of local actors and institutions is also a prerequisite for successful adaptation processes. Under the SIF model, considerable parts of the project cycle are delegated to communities, local governments and/or the private sector. The actual engagement, related financial potential and possible roles of the private sector in adaptation processes and finance in distinction to the public sector are so far unclear. Here, SIFs offer one possible model for cooperation and engagement.

The SIF model offers a good opportunity for an integrated approach to adaptation finance at the policy and institutional level. SIFs could particularly play a role at the interface of adaptation to climate change, social protection and risk management due to the overlap in goals, concepts and approaches. From an institutional perspective, the SIF model allows different channels and sources of international and

domestic finance to be bundled, integrating them under a common institutional and operational roof. However, if seen in the wider context of public financial management, the links and degree of integration with government institutions and processes are less clear and can imply trade-offs. While one strength of SIFs was to pilot and establish new procurement models, for example, the lack of integration into public financial management systems and the use of country systems has been criticised in SIF operations. While the SIF model has been successfully adapted to changing government policies in various different national contexts over time, coordination with and integration into government processes is seen as a main challenge.

In an institutional arrangement of adaptation finance, SIFs can potentially take over several political and institutional functions. As shown by past practical experience, SIFs successfully took over four basic functions in institutional arrangements and in the delivery of resources that overlap with important requirements of (international) adaptation finance and/or play an important role in adaptation processes as such: i) SIFs have acted as engines of local development in supporting vulnerable regions; ii) SIFs have acted as laboratories for innovation in delivering investments to the ground, at times even inducing wider sector reforms; iii) SIFs have acted as promoters of social capital by working in a multi-sectorial way at the local level, aiming to support communities in designing and managing own project activities and processes; and iv) SIFs have acted as an interim solution in times of dysfunctional government institutions or crisis situations. SIFs could, therefore, be an interesting financing model for the adaptation needs in fragile governance contexts, after climate-related disasters or in cases of discrimination of minorities which are highly vulnerable to the impacts of climate change due to a lack of access to social services. The decision on the role and function of SIFs in adaptation finance is important because it can influence institutional design options and the perspectives on these regarding their strengths and weaknesses.

From an institutional point of view, the main challenge is to maximise the use of country systems by integrating an existing SIF into a national adaptation financing arrangement or applying key SIF principles to similar institutional entities dedicated to adaptation finance. From an operational point of view, the overall challenge is to factor in climate change-related risks and changes to SIF operations.

There are three main approaches and entry points to factor in climate change-related risks in the SIF model: i) mainstreaming (or climate-proofing) climate change adaptation-related risks into existing projects (e.g. currently being piloted in Peru); ii) the identification of project types and the design of project menus that specifically target adaptation needs, and iii) the design of targeting techniques that prioritise people and communities highly vulnerable to the effects of climate change. The design of project types and menus is particularly challenging, as the SIF model requires a certain degree of standardisation of project activities which presupposes a minimum quantity of similar adaptation needs across a country with sometimes extremely different climatic conditions from region to region. When designing targeting techniques, the lack of climate data might constrict the usefulness of an allocation formula that links vulnerability indicators with climate or weather data. If weather-related data, for example, are not comparable or available across regions, it might disadvantage regions and communities that are most in need. In such a case, an alternative approach could be to focus on indicators for adaptive capacity.

The SIF model allows context-specific information and requirements to be considered at the project level as it is based on a demand-driven approach in project selection and allows for modifications in project design. However, it is not the best choice for very small- or very large-scale investments in terms of financial volume or in terms of particular adaptation needs because these are highly context-dependent, not repeatable, or cannot be standardised to a certain extent. The suitability of the SIF model for adaptation finance presupposes that a certain minimum of communities share the same adaptation needs and therefore require the same, or similar, type of goods or services.

Outlook

Towards an application of the SIF model in adaptation finance in practice, country-specific analysis as well as an updated overview on its current use by international financing institutions and partners would be useful. Particularly an analysis of SIFs in the area of risk management merits further attention.

1 Introduction

The provision of international climate finance for adaptation needs in local and vulnerable communities currently faces a dilemma: while developing countries in particular stress that adaptation finance should serve the vulnerable, that it should be additional to official development assistance (ODA) and that it should thus not be distributed by the established institutions and modalities of ODA but rather by institutions under the governance of the climate regime and by country-based institutions, the dedicated and newly established funds that have been set up under the climate regime to address these claims are currently of a disadvantage to small-scale adaptation needs of vulnerable communities as regards access possibilities.

So far, adaptation finance under the climate regime has mainly been distributed on a project-based approach which implies relatively high transaction costs for small-scale adaptation needs. And many – not all – of the adaptation needs of vulnerable communities at the local level are small in terms of financial volume. While the direct access modality of the Adaptation Fund and Green Climate Fund allow the use of country institutions and systems, the Funds' possibilities to maximise the use of these are (so far) limited in comparison to official development assistance, which can even channel climate finance through general budget support. National governments are currently facing the challenge of merging different interests and requirements into effective and efficient institutional arrangements that allow adaptation funds to be channelled while meeting national and international financing requirements.

In this context, this study looks at the potential of social investment funds (SIFs) in allocating adaptation finance to vulnerable communities. Social investment funds are known for their potential to bundle a large number of small-scale projects at the local level into national programmes, thereby reducing transaction costs. They are government-owned institutions which have been used by the international financial cooperation for more than 20 years and have been designed to promote a decentralised and community-driven investment approach, often targeted at disadvantaged and vulnerable groups.[1] Awarding responsibilities in project planning and implementation

1 Throughout this study, we will use the term 'community' for a social group and the locality they live in, whereas we refer to 'local governments' as the lowest administrative or governing body of a country's public governance system.

to communities and the private sector is one of their key characteristics. Social investment funds have been established in more than 60 countries and in many still form part of the institutional landscape.

The potential use of SIFs: motivation and limits of study

To support the goal of delivering adaptation funds to vulnerable communities, this study first and foremost looks at SIFs as institutions that channel finance from various sources and not as institutions that directly access adaptation finance under the Adaptation Fund or respectively the Green Climate Fund (despite this being a possible scenario of how SIFs could be used).

The study is motivated by an interest in using existing institutions to the extent possible and in introducing innovations where necessary for devolving funds and responsibilities to local actors. We believe that the targeted allocation of adaptation finance to vulnerable communities, to small-scale adaptation needs, and to actors at the local level is still an area that needs innovation. Exploring the potential of SIFs in this context is a goal of this study. With regard to the dilemma outlined above, the delivery of international adaptation finance through the SIF model might provide a solution for certain types of adaptation activities. So far, little experience has been gathered on how national institutions with direct access to international climate funds can devolve funds (and responsibilities) to the sub-national level.

Furthermore, the authors would like to underline that this study does not intend to *recommend* social investment funds for the delivery of adaptation finance in general. The intention is to provide an overview of the subject and to spur on the debate concerning their potential use, strengths and weaknesses. The application of a SIF model to adaptation finance in a country context always requires a country-specific analysis. For this reason, the analysis also does not look at the institutional arrangements needed between national institutions with direct access and SIFs.

Overview of the study

The study evaluates the potential of SIFs on the basis of climate and development finance criteria and a review of their operational strengths and weaknesses, which is based on practical experience with these types of funds. To this end, Section 2 provides a brief overview of the international

adaptation finance architecture, and characterises the main challenges and criteria that an institutional arrangement should meet from an international climate-finance and development-effectiveness perspective. These two perspectives are then merged into a set of international minimum adaptation finance criteria and requirements.

Based on a literature review and own work experience with social investment funds (Schulz-Heiss 2011), Section 3 delineates the evolution of SIFs, as well as their geographical distribution and financial magnitude. An overview of the evolution and changing nature of SIFs over time provides a better understanding of their strengths and weaknesses as these also have to be understood in the context of changing policy needs and contexts. Based on evidence and analysis provided in the literature, Section 4 characterises general operational characteristics in country contexts and analyses-related strength and weaknesses. Against the background of the minimum requirements in international adaptation finance delineated in Section 2 as well as based on practical experience in channelling development finance through SIFs (Sections 3 and 4), Section 5 discusses the potential, limits and challenges of using SIFs for channelling adaptation finance to vulnerable communities.

2 Delivering adaptation finance: architecture, requirements and challenges

Past discussions on the strengths and weaknesses of SIFs over time have shown that their evaluation is always also a matter of political perspectives and requirements. An evaluation of the potential, limits and challenges of using SIFs for channelling adaptation finance in general and international adaptation finance in particular therefore requires a brief description of the current political context. Towards that end, this section aims to briefly illustrate the current requirements and challenges that decision-makers in the field of climate change finance are facing when considering setting up institutional structures for the delivery of finance for climate change adaptation purposes. With regard to the dilemma illustrated in the Introduction, finding an integrated approach between climate and development finance is certainly one of the main challenges.

Questions related to the institutional design and governance of delivering adaptation finance have come to the forefront in recent years in contrast to a

focus on the amount of available funding in the first decade of international climate negotiations. One reason for this is that many governments see the need to support climate change adaptation activities in a targeted way. A second reason is the prospect of additional international adaptation funds and the demand for an effective, fair and transparent distribution of these funds. Another major reason is the increased number of actors providing adaptation-related funding[2] and related problems caused by fragmentation.[3] The institutional landscape that relates to the delivery of adaptation finance has become increasingly complex over the past years.

Understanding the dynamics of this international institutional landscape and related financing requirements also helps to promote a better understanding of the kind of institutional structure needed in national contexts. Towards a transparent assessment of SIFs, the delineation of adaptation funding criteria and requirements at the same time serves to explain part of the ground on which our assessment in the final section is based.

2.1 Adaptation finance architecture: a brief overview

At the present time there are a multitude of institutions providing financial support for adaptation activities in developing countries (see Figure 1). For the implementation of financial commitments under the mandate of the UNFCCC, parties can use the financial mechanism of the Convention, the Adaptation Fund under the Kyoto Protocol or bilateral, regional, or other multilateral channels (UNFCCC, Article 11.5). The bilateral, regional, and multilateral channels used are often institutions that also channel official development assistance (ODA; see arrows (Figure 1) for possible channels). The operating entities of the financial mechanism of the UNFCCC are currently the Global Environmental Facility (GEF) and the Green Climate Fund (GCF). The GCF is still in the process of being set up while the Adaptation Fund works under the guidance of Kyoto Protocol parties and is operated by the Adaptation Fund Board which received its own legal capacity in 2011 in Germany. The fund is currently financed by the carbon market and

2 See e.g. UNFCCC's adaptation funding interface, http://unfccc.int/adaptation/implementing_adaptation/adaptation_funding_interface/items/4638.php; or http://www.climatefundsupdate.org).

3 For a brief explanation of challenges related to fragmentation see e.g. World Bank 2010, 263f.

channels a share of proceeds from Clean Development Mechanism (CDM) revenues and voluntary donations. In the second commitment period from January 2013 to 2020, the fund shall also receive a share of proceeds levied on transfers or issuance of certificates from the other Kyoto Protocol carbon market mechanisms (Decision 1/CMP. 8).

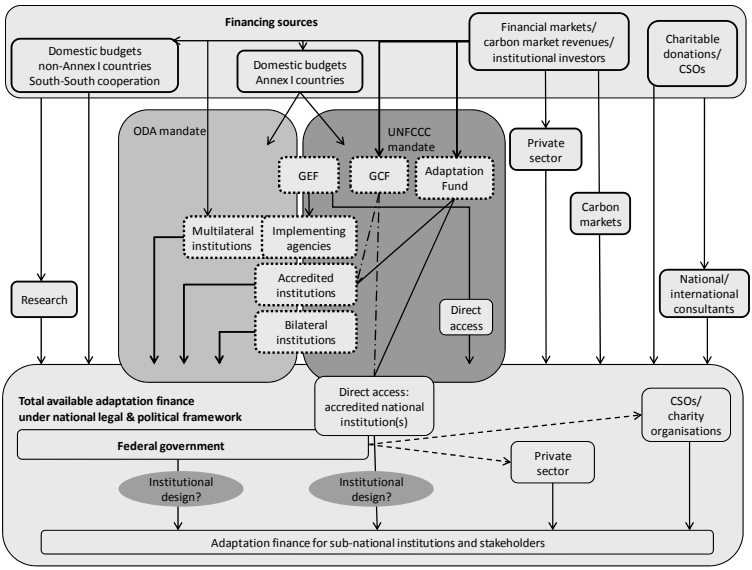
Under the UNFCCC, there are three basic modalities of accessing or delivering international adaptation finance:

- Direct access through an accredited national institution i) to the Adaptation Fund (National Implementing Entity); ii) to the GEF for reporting activities; and iii) to the Green Climate Fund once fully operationalised (see dotted arrow Figure 1).
- Indirect access through a multilateral institution which is accredited i) to the Adaptation Fund (Multilateral Implementing Entity), and/or b) to the GEF (Implementing Agency).
- Bilateral, regional, and multilateral channels.

Apart from institutions of the climate regime and ODA, adaptation finance in developing countries can also be provided through own domestic budgets or through other developing countries (non-Annex I countries; South-South cooperation), the private sector or international and national civil society organisations (CSOs) and foundations. These actors can at the same time administer or deliver adaptation funds from own or other sources (see Figure 1). The role of CSOs and the private sector for the delivery of adaptation funds varies, and depends on national practice and the question of to what extent laws and regulations allow or incentivise their engagement (see dotted arrow Figure 1).

Although the climate regime is perceived by many to be the only legitimate framework for the delivery of international adaptation finance, a large share of adaptation funding is being delivered by institutions in the context of official development assistance (ODA). In terms of volume, it can be assumed that the major share of adaptation finance in developing countries is public money in form of ODA, channelled by the public institutions of ODA. This has been shown via the estimates and calculations of available adaptation funds (e.g. Persson et al. 2009, 112) and becomes obvious when looking at the funding volume of initiatives like the Climate Investment Facility of the World Bank (e.g. www.climatefundsupdate.org; Schalatek et al. 2012).

Figure 1: International adaptation finance architecture: schematic overview of sources, main channels and stakeholders



Sources: Graph modified based on own research and Persson et al. 2009, 165; Glemarec et al. 2011, 63; www.climatefundsupdate.org; Buchner et al. 2011

The Green Climate Fund is expected to channel a *"significant share of new multilateral funding for adaptation"* (Decision 1/CP.16 Paragraph 100, in FCCC/CP/2010/7/Add.1). However, the extent to which the share of adaptation finance under the Climate Convention will significantly increase in the future is currently unclear, particularly given the collapse of the carbon market that is considered to be an important future funding source under the climate regime and currently finances the Adaptation Fund and Germany's International Climate Initiative. If donors cap their contribution to multilateral channels, bilateral financing institutions could even become the largest source of international public climate change finance in the coming years (Glemarec et al. 2011, 76). Currently, there is no comprehensive analysis of the volume of adaptation finance coming from, or being channelled through, the private sector, charity organisations or research, national and international consultants.

The multitude of different institutions and the importance of development assistance for adaptation finance illustrate that the creation of synergies between development and climate finance is a key challenge for establishing efficient and effective funding arrangements for the delivery of adaptation finance. This challenge has an international and national dimension. It also illustrates that the design of adaptation governance and institutions in developing countries is particularly decisive for the delivery of adaptation funds. Governments in developing countries face the difficult challenge of bundling and coordinating various funding flows and institutional modalities, and aligning them with national development plans.

A brief analysis of the adaptation finance architecture also shows that the question of how best to design national institutional structures for delivering international adaptation finance for local adaptation activities is embedded in international funding requirements under the climate regime as well as in a general development context, one which is to different degrees determined by requirements of official bi- and multilateral development cooperation. For this reason, the following sections highlight the main requirements in terms of goals and criteria that an institutional arrangement has to meet from a climate change perspective (Sub-section 2.2) and from a development perspective (Sub-section 2.3).

As it is not possible to consider the specific circumstances of public financial management in particular developing countries within the scope of this study, the description of the main challenges and funding requirements in the field of development finance is based on the international aid or development-effectiveness agenda. This agenda was reaffirmed by 160 countries and 52 international organisations in December 2011 as a result of the fourth High Level Forum on Aid Effectiveness ("Busan Partnership for Effective Development Cooperation"). It is the main global agenda which aims at improving the delivery and management of financial resources between donor and recipient countries, based on past and current experiences in development cooperation.

2.2 Climate change financing requirements

At the UNFCCC summit in Copenhagen in 2009, developed countries agreed to scale up funding for the implementation of adaptation actions in developing countries and to improve access to these financial resources (Copenhagen

Accord, Paragraphs 3 and 8). With the Copenhagen Accord and the Cancun Agreement in 2010, they committed to mobilising USD 100 billion annually by 2020, of which a share was to be used to support adaptation activities in developing countries. These funds *"may come from a variety of sources, public and private, bilateral and multilateral, including alternative sources"* (Decision 1/CP.16, Paragraph 99, in FCCC/CP/2010/7/Add.1)**.** The goal is to deliver these new funds for adaptation *"through effective and efficient fund arrangements"* (Copenhagen Accord, Paragraph 8).

Under the UNFCCC and the Kyoto Protocol, developed countries have committed to providing new and additional financial resources to assist developing country parties to adapt to climate change and meet related costs (UNFCCC, Art. 4.3, 4.4; Kyoto Protocol (KP), Art. 11.2, Art. 12.8). These costs may be incurred for example in connection with the formulation, implementation and publishing of national programmes and measures to facilitate adequate adaptation in a country (UNFCCC, Art. 4.1(b)). The arrangement indicates that funds provided for related tasks should be adequate and predictable in their flow (UNFCCC, Art. 4.3, KP, Art. 11.2; Decision 1/CP.16, Paragraph 97). In the case of the Green Climate Fund, developed countries have agreed to promote a balanced allocation of funds for mitigation and adaptation activities (Decision 3/CP.17, Paragraph 8).

Funding under the Convention should not only support the implementation of the Convention, but should also contribute to the achievement of the World Summit on Sustainable Development and the Millennium Development Goals, and contribute to the integration of climate change considerations into development activities (see e.g. Decisions 5/CP.9 and 6/CP.9).

When it comes to the distribution of these funds for particular adaptation activities, the climate regime highlights general criteria and requirements that should be met by an institutional arrangement under the mandate of the climate regime as listed in Box 1.[4] Beyond these general criteria, the GEF, the Adaptation Fund, and the Green Climate Fund have more specific requirements in place that can vary. These usually specify and detail the listed funding requirements and, where applicable and of importance for the institutional design in delivering funds, these requirements are briefly indicated in Box 1.

4 Past and future guidance given to the operating entity of the financial mechanism of the Convention shall apply *mutatis mutandis* to the Kyoto Protocol (KP, Art. 11.2).

If countries choose to access international adaptation finance directly through a national institution (see Figure 1), the institution has to meet international fiduciary standards. These international standards exist for the Adaptation Fund[5] so far and will most likely be set up in a similar form for the direct access modality of the Green Climate Fund. As this study only provides a general overview of SIFs, these standards are not relevant for this analysis. They can, however, be relevant in a country-specific analysis of SIFs.[6]

Parties reconfirmed the general requirements listed in Box 1 for the delivery of climate finance in decisions at the Conference of Parties (COP) in Cancun and Durban on the Green Climate Fund (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraphs 2 and 3). This includes the objective that climate finance in the light of sustainable development shall also *"promote environmental, social, economic and development co-benefits"* (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraph 3). The Green Climate Fund is still in the design stage, however its Governing Instrument, which includes the objectives and guiding principles of the Fund, has already been approved at COP 17 in Durban.

Beyond the adaptation requirements listed in Box 1, additional central goals and guiding principles of the Green Climate Fund will be to *"catalyse"* public and private finance at the national and international level, and to *"strengthen engagement at the country level through the effective involvement of relevant institutions and stakeholders",* taking a *"gender sensitive approach"*. The GCF shall strive to maximise impacts and a *"results-based approach"* will be an important criterion for allocating resources (for all previous quotations, see Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraphs 3 and 51. While the requirement of having

5 See accreditation process at www.adaptation-fund.org.

6 There are two scenarios: first, they are directly relevant if a national institution applies for direct access. In theory, this is a possible role for a social investment fund if the fund under discussion has the respective legal and institutional status in a country. Second, the fiduciary standards can be relevant in a detailed analysis (e.g. feasibility study) at the country level as to whether the respective institution or fund (here SIFs) qualifies for delivering adaptation funds as a subordinated institution to the institution with direct access. The rationale behind such an assessment would be that the national institution with direct access can more easily adhere to international fiduciary standards if the subordinated institutions in the delivery chain do so as well.

a results-oriented framework in place is not specified in the convention text or Kyoto Protocol, it is detailed in GEF documents for the Least Developed Countries Fund and Special Climate Change Fund, and was introduced by the Adaptation Fund Board at its 10th meeting.[7] The Green Climate Fund may even apply a results-based financing approach (Governing Instrument for the Green Climate Fund, Para 55).[8]

Box 1: General criteria and requirements for channelling adaptation finance under the climate regime

1. Target the vulnerable: The UNFCCC and the Kyoto Protocol both aim to support those countries that are particularly vulnerable to the adverse effects of climate change (UNFCCC, Preamble, Art. 3.2, Art. 4.4, Art. 4.9; KP, Art. 12.8, AF, Strategic Priorities and Guidelines, Art. 5(a)). Beyond the support of vulnerable countries, the Adaptation Fund has the strategic priority that countries shall give particular attention to the needs of the most vulnerable communities (AF, Strategic Priorities, Policies and Guidelines, Art. 8). In general, funding under the Adaptation Fund can be made available for national, regional and community-level activities (Decision 5/CMP.2, Paragraph 2). The Green Climate Fund intends to design its access modalities in a way that encourages the active involvement of relevant stakeholders, including vulnerable groups (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraph 31). As a shared vision for long-term cooperative action, parties at the conference in Cancun also recognised subnational and local governments as important stakeholders (Decision 1/16 (7)).

2. Cost-effectiveness and efficiency: The UNFCCC adopts a catalytic and synergetic role, including its financial mechanism. Policies and measures to deal with climate change should be cost-effective to achieve global benefits at the lowest possible costs (UNFCCC, Art. 3.3) and consistency between climate change-related activities should be sought

7 For the GEF, see for example GEF 2008, GEF 2010; for the Adaptation Fund see for example the "Results Framework and Baseline Guidance: Project-level" at https://www.adaptation-fund.org/sites/default/files/Results%20Framework%20and%20Baseline%20Guidance%20final%20compressed.pdf.

8 For an explanation of the difference between results-based management and results-based financing, see for instance Klingebiel 2012.

with those undertaken outside the framework of the financial mechanism (Decision 11/CP.1).

3. Country-drivenness: The UNFCCC reaffirms the principle of sovereignty (UNFCCC, Preamble). Climate change-related activities should be *"appropriate for the specific conditions"* of each country, respecting the need for economic development (UNFCCC, Art. 3.4). Impact assessments, for example, should be formulated and determined nationally (UNFCCC, Art. 4.1(f)).

The Adaptation Fund is more explicit on this criterion, saying in its Strategic Priorities, Policies and Guidelines that adaptation projects and programmes that will be financed need to be based on the needs, views and priorities of the respective country (Paragraph 5(b); see also Decision 28/CMP.1). The criterion of country-drivenness is also reflected in the institutional access modality of the Adaptation Fund and the Green Climate Fund that allow developing countries to access resources through accredited national institutions (Decision CMP 1/.3, Paragraph 29; Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, para 31).

A *"country-driven approach is also a core principle to build the business model"* of the Green Climate Fund (Decision B.01-13/06, Paragraph (c)(i)), including its private sector facility (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraph 42).

4. Promoting an integrated approach: In line with the principle of country-drivenness, measures undertaken under the Convention should be in line with sustainable development and be integrated with national development programmes (UNFCCC, Art. 3.4; see also Adaptation Fund, Strategic Priorities, Policies and Guidelines of the Adaptation Fund, Paragraph 6). In order to achieve complementarity and coherence between activities of other funds under the Convention and other funds and channels, the Green Climate Fund *"will promote coherence in programming at the national level through appropriate mechanisms"* (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraph 34).

The promotion of an integrated approach under the Convention is foremost a goal at the policy level. To what extent this goal is being

extended to the institutional level is not clear yet. In the Governing Instrument of the Green Climate Fund, parties state that the *"Fund shall operate in the context of appropriate arrangements between itself and other existing funds"* and that the *"Fund will also initiate discussions on coherence in climate finance delivery with other relevant multilateral entities"* (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraphs 33–34).

5. Context specific: Policies and measures should take into account different socio-economic contexts (UNFCCC Art. 3.3).

6. Full cost and co-financing: The financial mechanism provides financial resources on a grant or concessional basis (UNFCCC, Art. 11.1). Parties to the Convention commit to refund the *"agreed full costs"* for activities such as reporting and the *"agreed full incremental costs"* (or additional costs) for the implementation of adaptation activities. In the latter case, co-financing by the implementing country is necessary. The Adaptation Fund of the Kyoto Protocol pays the *"agreed full costs"* incurred by developing countries in implementing their commitments under the Convention (KP, Art. 11.2(a)). The Green Climate Fund supports adaptation activities on the basis of *"agreed full and agreed incremental costs"* and can also provide support for capacity building and preparatory activities that enable countries to access funding (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraphs 35, 38 and 40).

7. Transparency: *"The financial mechanism shall have an equitable and balanced representation of all Parties within a transparent system of governance"* (UNFCCC, Art. 11.2; see also Decision 1/CMP.3, Paragraph 17). While the Convention text is limited to the system of governance, parties to the Convention explicitly extended the transparency requirement for the Green Climate Fund to the entire funding operations or particular related aspects (Decision 3/CP.17/Annex Governing Instrument for the Green Climate Fund, Paragraph 3; Decision 2/CP.4, Paragraph 3(c); Decision 5/CMP.2, Paragraph 1(c)). The Adaptation Fund at its 21st meeting approved an open information policy (see AFB/EFC.12/.5/Rev.1).

2.3 Development financing requirements

The delivery and management of financial resources from developed to developing countries have received a lot of attention on the international aid agenda in the past years. A main reason for this was the criticism voiced by various actors that aid was ineffective, thereby undermining the legitimacy of development policy and development cooperation (see Ashoff 2010, 29–38). One of the main problems development cooperation is facing is the multitude of existing and the still increasing number of actors. Currently there are around 40 bilateral and 30 multilateral donors, each with various sub-organisations, often with their own goals, institutional interests and processes (Ashoff 2010, 48). This fragmentation of aid impairs aid effectiveness and efficiency as it leads to increased transaction costs and may weaken a country's ownership of development activities and may burden already limited institutional capacities (e.g. OECD 2008, 11; Acharya / De Lima / Moore 2006). With the goal of addressing these problems of aid delivery and management, developing and developed countries endorsed several main declarations and documents on aid effectiveness, milestones being the Paris Declaration on Aid Effectiveness in 2005 (OECD 2005), the Accra Agenda of Action in 2008, and the Busan declaration on effective development co-operation in 2011.

The basis of the aid effectiveness agenda is the Paris Declaration, in which developed and developing countries agreed to improve effectiveness particularly by:

- *"strengthening partner countries' national development strategies and operational frameworks",*
- *"increasing alignment with a countries' priorities, systems and procedures,"*
- 'increasing accountability of donors and partner countries to their citizens',
- 'eliminating duplication and operating as cost-effective as possible',
- *"reforming and simplifying donor policies and procedures"* and
- by *"[d]efining measures and standards of performance and accountability of partner country systems in public financial management, procurement, fiduciary safeguards and environmental assessments"* (Paris Declaration on Aid Effectiveness, Article 3).

Five key principles form the basis of the reform agenda: ownership; alignment; harmonisation; managing for results; and mutual accountability, which are detailed by respective indicators that allow for the monitoring and evaluation of progress (see Table 1).

With the Accra Agenda for Action (AAA), countries consolidated the principles of the Paris Declaration and specified or added aspects, for example, in the field of gender (AAA, Paragraphs 3, 13, 42); transparency (AAA, Paragraph 22, 24a); or the role of international funds that should support country ownership and align and harmonise their assistance proactively with national contexts (AAA, Paragraph 9, 16, 19c; compare World Bank 2011, vii, 2). *"As new global challenges emerge donors will ensure that existing channels for aid delivery are used and, if necessary, strengthened before creating separate new channels that risk further fragmentation and complicate co-ordination at country level"* (AAA, Paragraph 19c).

The outcome document at the High Level Forum on Aid Effectiveness in Busan basically reconfirms the commitments made in Paris and Accra and aims to broaden the scope of the agenda by including new actors (see Busan Declaration, Paragraph 14) such as emerging donors like China, India, Brazil, or Russia (see also Paragraph 30), civil society organisations or the private sector (Paragraph 32) and by putting *"aid effectiveness"* in the context of *"development effectiveness"* (Paragraphs 28-34) whereby aid is seen as only one way to catalyse development (Busan Declaration, Paragraph 28; *"from aid to development effectiveness"*).[9]

The Busan outcome document, called the "Busan Partnership for Effective Development Cooperation", also highlights the particular challenges that potential substantial climate change resource flows between countries might imply. Against this background, the signatories intend *"to support national climate change policies and planning as an integral part of developing countries' overall national development plans"* and want to *"ensure that where appropriate these measures are financed, delivered and monitored through developing countries' systems in a transparent manner"* (Busan Partnership for Effective Development Cooperation, Paragraph 34 (a)).

9 For further information on the Forum, see http://www.oecd.org/dac/effectiveness/fourthhighlevelforumonaideffectiveness.htm.

Although the Busan Document is not binding it is being endorsed by 160 countries and 52 international organisations. The aid-effectiveness process had been driven by the Working Party on Aid Effectiveness, a multi-stakeholder group consisting of developing and developed countries, South-South co-operation providers, and civil society organisations. Since mid-2012, the "Global Partnership for Effective Development Cooperation" has taken over and has the mandate to support the implementation of the Busan agreement.[10]

Table 1: Core principles of the aid effectiveness agenda

Principles	Indicators
1. Ownership Partner countries exercise effective leadership over their development policies and strategies, and coordinate development actions.	*1. Partners have operational development strategies*: Number of countries with national development strategies (including PRSs (Poverty Reduction Strategies)) that have clear strategic priorities linked to a medium-term expenditure framework and reflected in annual budgets.
2. Alignment Donors base their overall support on partner countries' national development strategies, institutions and procedures.	*2. Reliable country systems:* Number of partner countries that have procurement and public financial management systems that either a) adhere to broadly accepted good practices, or b) have a reform programme in place to achieve these.
	3. Aid flows are aligned on national priorities: Percent of aid flows to the government sector that is reported on partners' national budgets.
	4. Strengthen capacity by coordinated support: Percent of donor capacity-development support provided through coordinated programmes consistent with partners' national development strategies.

10 For details on the mandate and steering process of the "Global Partnership for Effective Development Cooperation" see http://www.undp.org/content/dam/uspc/docs/Mandate_of_the_Global_Partnership_for_Effective_Development_Co-operation.pdf.

Table 1 (cont.): Core principles of the aid effectiveness agenda	
Principles	**Indicators**
	5a. Use of country public financial management systems: Percent of donors and of aid flows that use public financial management systems in partner countries, which either a) adhere to broadly accepted good practices or b) have a reform programme in place to achieve these.
	5b. Use of country procurement systems: Percent of donors and of aid flows that use partner country procurement systems which either a) adhere to broadly accepted good practices or b) have a reform programme in place to achieve these.
	6. Strengthen capacity by avoiding parallel implementation structures: Number of parallel project implementation units (PIUs) per country.
	7. Aid is more predictable: Percent of aid disbursements released according to agreed schedules in annual or multi-year frameworks.
	8. Aid is untied: Percent of bilateral aid that is untied.
3. Harmonisation Donors' actions are more harmonised, transparent and collectively effective.	*9. Use of common arrangements or procedures:* Percent of aid provided as programme-based approaches.
	10. Encourage shared analysis: Percent of a) field missions and/or b) country analytic work, including diagnostic reviews that are joint.

Table 1 (cont.): Core principles of the aid effectiveness agenda	
Principles	**Indicators**
4. Managing for results Managing resources and improving decision-making for results.	*11. Results-oriented frameworks:* Number of countries with transparent and monitorable performance assessment frameworks to assess progress against a) the national development strategies and b) sector programmes.
5. Mutual accountability Donors and partners are accountable for development results.	*12. Mutual accountability:* Number of partner countries that undertake mutual assessments of progress in implementing agreed commitments on aid effectiveness including those in this Declaration.
Notes: Methodological annotations The term 'partner countries' in the list of indicators usually refers to those countries that receive aid, see e.g. indicators under the principle of 'alignment'. However, under Indicator 12, the term includes both signatories to the aid-effectiveness agenda, donor and recipient countries.	
Source: OECD, Paris Declaration on Aid Effectivenes	

2.4 Common challenges and assessment criteria

The agreed funding criteria under the climate change and development agenda show that these two agendas share common political objectives in finding an appropriate mode of delivering finance, a central one being a country-driven and integrated approach at the national level where countries have ownership over their development and adaptation policies. Box 2 provides a brief comparative overview between the financing requirements of the two agendas which illustrates commonalities as well as differences.

Box 2: Comparison and synthesis of climate and development financing requirements

Synthesis funding criteria*	**Climate Change Regime***	**Development Effectiveness Agenda (Paris Declaration)**
	Full cost and co-financing	
	New and additional finance	
	Adequate, predictable, sustainable finance	Indicator 7: Aid is more predictable (alignment)
Cost-effectiveness and efficiency	Cost-effectiveness and efficiency	Whole aid effectiveness agenda aims at improving cost-effectiveness and efficiency
Support particularly vulnerable countries, *communities, and groups*	Support particularly vulnerable countries, *communities and groups*	
Country-driven (excluding Indicator 1)	Country-driven	Ownership: Effective leadership by partner countries over development policies and strategies
Country-driven/ integrated approach Indicator 3 Indicator 4[2] Indicator 5a Indicator 5b	Integrated approach	Indicator 3: Percent of aid flows reported on partners national budgets

Synthesis funding criteria*	**Climate Change Regime***	**Development Effectiveness Agenda (Paris Declaration)**
		Indicator 4: Capacity development support (technical assistance) provided through coordinated programmes consistent with partners' national development strategies
		Indicator 5a: Use of partner country public financial management systems
		Indicator 5b: Use of partner country procurement systems
Coordinated approach[3] Pooling of funds Indicator 6 Indicator 4	Finance can come from a multitude of sources/ funding arrangement can channel funds from a multitude of sources	Common practice and challenge that the Aid Effectiveness Agenda aims to address: Indicator 4: Capacity development support (technical cooperation) provided through co-ordinated programmes [...] Indicator 6: Avoid parallel implementation structures
Programme-based approach	-	Indicator 9: Percentage of aid provided as programme-based approaches
Encourages shared analysis (Indicator 10)	-	Indicator 10: Encourage shared analysis (harmonisation)
Context specific	Context specific	
	Catalytic approach[1]	

Synthesis funding criteria*	**Climate Change Regime***	**Development Effectiveness Agenda (Paris Declaration)**
Gender sensitive[1]	Gender-sensitive[1]	AAA (Paragraphs 3, 13, 42)
Results-based approach[1]	Results-based approach[1]	Indicator 11: Results-oriented frameworks in place
Transparency Indicator 11	transparency	Indicator 2: Procurement and public financial management systems in place Indicator 11: Results-oriented/ transparent and monitorable performance assessment frameworks in place to assess progress against national development strategies and sector programmes
-	-	Indicator 12: Mutual accountability

Notes: Methodological annotations

* Text in italics: criteria are not listed in UNFCCC or KP text; see Sub-section 2.2 for references and explanations or see the column on aid effectiveness;

1 Explicit target/principle of the GCF

2 Indicator 4 is only partly covered by the Convention namely with regard to *"consistency with national development strategies"*; not covered is the goal by the development effectiveness agenda that "*50% of technical co-operation flows are implemented"* through *"co-ordinated programmes*".

3 The requirement that a funding arrangement needs to channel funds from a multitude of sources is subsumed under the criterion of coordination, as the pooling of funds from various sources can be one way of coordination.

The list of common adaptation financing criteria for this study does not include:

- Indicator 1 of the aid effectiveness agenda: while the principle of ownership is generally reflected in the principle of "country-drivenness" or "integrated approach", Indicator 1 is currently not an adaptation financing requirement under the climate regime.

- Indicator 2 of the aid effectiveness agenda: the commitment behind this indicator is to "Work together to establish mutually agreed frameworks that provide reliable assessments of performance, transparency and accountability of country systems". This commitment aims at the country-level and not at the mode of delivery at a fund level; therefore, similar indicators 5a and 5b are used in this analysis.
- Indicator 5b: is of relevance for the direct access modality only.
- The following criteria are not included as these primarily refer to the availability of finance for partner countries and not to the design of delivery: full cost and co-financing, additionality, adequate, predictable, sustainable finance (compare also Indicator 7 of the aid effectiveness agenda), and Indicator 8 (untied aid);
- Indicator 10 of the aid effectiveness agenda: this is not a relevant criterion for the quality of delivering finance
- Indicator 12 of the aid effectiveness agenda: the principle of mutual accountability refers to the assessment of progress in implementing the aid effectiveness agenda only
- Catalytic approach: the meaning of this criterion is not specified under the climate regime

Despite common goals, there are also tensions between the two agendas. Looking at the current task of designing an appropriate (national) institutional structure for delivering adaptation finance, two major challenges emerge, when comparing the political target course and discourse of these agendas with practical implementation. One is the maximisation of using country systems and institutions; the other is the design of institutional structures that are targeted at the support of vulnerable communities and allow funds to be channelled for small-scale adaptation needs and to the local level.

2.4.1 Maximising the use of country systems and institutions in adaptation finance

The use of country systems and institutions to the extent possible is a central goal of the development effectiveness agenda in order to increase effectiveness and efficiency in the use of funds and in order to decrease institutional fragmentation. So far, climate negotiations and decisions under the climate regime have led to a proliferation of climate-related funds and more institutional fragmentation. One political reason for the proliferation of climate funds is that developing countries have demanded that any adaptation funds must be new and additional to official

development assistance (ODA) to avoid undermining other important tasks of development cooperation and because of the historical responsibility of developed countries in causing climate change. Along with this, developing countries and other actors do not regard adaptation finance as aid, and therefore claim that adaptation finance should not be subject to conditions of ODA and modes of delivery.

This perspective on adaptation finance contributed to further fragmentation in the landscape of adaptation financing institutions, inside and outside the mandate of the climate regime. Under the climate regime it led to the creation of two additional funds, the Adaptation Fund and the Green Climate Fund. Paradoxically, these two additional funds at the same time are innovative and have the potential to support the implementation of the development-effectiveness agenda through their direct access modality that pursues the use of country institutions. The direct access modality allows countries to directly access international climate adaptation finance through accredited national institutions.[11] However, as illustrated in more detail in Box 3, the current possibilities of using country systems are much higher under the conditions and modalities of ODA than under the current financing modalities of the climate regime. From the perspective of implementing a country-driven and integrated approach, maximising the use of country systems and institutions in international adaptation finance is therefore still a challenge.

11 The Adaptation Fund is regarded as innovative for its independence of ODA sources: it has a majority of developing countries in its governing board and it allows developing countries to directly access international funds (Horstmann / Chandani-Abeysinghe 2011). The Green Climate Fund will also have a direct access modality for national institutions. Usually, countries rely on one of the multilateral institutions to access international funds. An example of direct access in the field of development finance is The Global Fund to Fight AIDS, Tuberculosis and Malaria.

Box 3: Different views on country-drivenness and ownership: using country systems and (enhanced) direct access

The objectives of the direct access modality of the Adaptation Fund and Green Climate Fund relate to the principle of country-drivenness and the implementation of an integrated funding approach under the climate regime. Under the aid effectiveness agenda, the direct access modality would fall under the requirement of ownership (except Indicator 1, compare Table 2 and Box 2) and particularly the goal of alignment, where donors commit to base their overall support of partner countries on national institutions and procedures (compare Box 2).

However, the extent to which country systems shall and can be used for the delivery of adaptation finance under the aid effectiveness agenda goes beyond the possibilities of the direct access modality. The use of country systems under the Adaptation Fund's direct access modality is limited to the use of a National Implementing Entity (NIE). An NIE's responsibility includes the *"overall management of the projects and programmes financed by the Adaptation Fund, [...] all financial, monitoring, and reporting responsibilities",* and the compliance with the fiduciary risk management standards (e.g. financial management, procurement, monitoring and evaluation, project development, appraisal and oversight).

Under the aid effectiveness agenda, only looking at the principles of the Paris Declaration as a reference point, the use of country systems also includes reporting on national budgets, partly through programme-based approaches (Indicator 3, Indicator 9 (see Table 2)) and the use of national results-oriented frameworks (Indicator 11).

Whether, and to what extent, the climate regime is going to strengthen the principle of country-drivenness and the role of countries in the delivery of adaptation finance in the future is left to negotiations. One concrete possibility is the design of direct access under the Green Climate Fund. The governing instrument (Paragraph 47) allows the Board to *"consider additional modalities that further enhance direct access, including through funding entities with a view to enhancing country ownership of projects and programmes"* (compare, for instance, Bird / Billett / Colón 2011; Müller 2011; Berliner et al. 2013). At its fourth meeting in June

2013, the GCF Board decided to consider additional modalities that further enhanced direct access at its first meeting in 2014.[12]

2.4.2 Support for vulnerable people: finance for small-scale adaptation needs and for the local level

Another gap between discourse and practice exists in the implementation of a vulnerability-oriented funding approach, a central goal of adaptation finance under the climate regime. Adaptation finance is supposed to support those countries that are particularly vulnerable to the effects of climate change. From a legal perspective, this goal applies to the country level only but can, through provisions in the Adaptation Fund and Green Climate Fund, be extended to the community-level (see Box 1).[13] The implementation of a vulnerability-oriented funding approach requires institutional structures that allow for the support of small-scale adaptation needs and for devolving funds to the local level as many – though not all – adaptation needs of vulnerable communities are small in terms of scale and financial volume and require the involvement of local institutions and stakeholders for successful implementation.

Empirical examples suggest that there is a need to make advances in practical implementation in order to meet this central goal of adaptation finance. The delivery of international adaptation finance has so far not been prioritised on the basis of a clearly defined vulnerability criterion (Horstmann 2011; Horstmann / Scholz 2011; Remling / Persson / Davis 2012). Experiences from the implementation of the Hyogo Framework for Action in Africa, for example, show that less than half of the countries which reported on

12 See Decision B.04/06 in Green Climate Fund 2013: *"The Board: […] (b) Noted that the Board will consider additional modalities that further enhance direct access, including through funding entities with a view to enhancing country ownership of projects and programmes; and that the Fund will provide for readiness and preparatory activities and technical assistance, such as the preparation or strengthening of low emission development strategies or plans, NAMAs, NAPs, NAPAs, and for in country institutional strengthening, including the strengthening of capacities for country coordination and to meet fiduciary principles and standards and environmental and social safeguards, in order to enable countries to directly access the Fund".*

13 Note that 'community' is not clearly defined in these funds and can also include local government; compare Footnote 1.

the status of the implementation of the framework have budget allocations dedicated for disaster risk reduction at the local level (UNISDR 2011a, 5). Although local capacities and the role of local governance are acknowledged to be central in disaster risk management, a field closely intertwined with adaptation, the Global Assessment Report on Disaster Risk Reduction 2011 points to a huge and widening gap between rhetoric and reality. While many countries have decentralised disaster risk management and reduction, existing financial and technical resources do not match local governments' new responsibilities. Dedicated budget allocations to local governments for disaster risk management *"remain the exception rather than the rule"* (UNISDR 2011b, Chapter 4.7.1).

An early analysis of national adaptation programmes of action (NAPA) documents indicates that the gap between rhetoric and action is probably similar in the field of adaptation to climate change. Only 20 of 173 adaptation projects identify local-level institutions as partners or agents in facilitating adaptation projects, even in areas where local institutions could be viewed as a basic component of an adaptation strategy, including agriculture, water, forest management or fisheries (Agrawal 2008, 42–43).

The delivery of adaptation finance to vulnerable communities involves various challenges (see e.g. Reid et al. 2009; Agrawal 2008) as will also become evident in the subsequent analysis of SIFs (see in particular sub-section 4.2.2 on the limits in reaching the poorest and in working with the community). With regard to the delivery of international adaptation funds, one of these challenges is the reduction of transaction costs. Given the relatively high transaction costs of small-scale adaptation needs, their chance to benefit from international adaptation finance is currently low. Under the climate regime, most funds have so far been disbursed on a project-based approach, including the Adaptation Fund that explicitly wants to move to programmatic funding approaches where appropriate (Operational Policies and Guidelines, Paragraph 15(h)). This situation is not ideal, given the need to scale up support both financially and geographically.

Box 4: General challenges in delivering adaptation finance

- Creating synergies between development and climate finance
- Reducing fragmentation/increasing coordination
- Implementing an integrated approach (policies, institutions, procedures)
- Reducing transaction costs
- Maximising the use of country systems
- Delivering (international) finance for small-scale adaptation needs and to the local level

To date, there is little experience in the design of national institutions that directly devolve international adaptation funds to the local level. South Africa is the first country under the Adaptation Fund that in 2013 handed in a proposal to design a Small Grants Facility for enabling local-level responses to climate change. The United Nations Capital Development Fund (UNCDF) has set up a pilot programme, the Local Climate Adaptive Living (LoCAL) facility that channels adaptation finance to local governments. Grants are disbursed as part of a local government's regular budget envelope on the basis of Performance Based Climate Resilience Grants (UNCDF, s.a.). Countries like Bangladesh, the Philippines or Ethiopia have set up dedicated national funds that aim to raise and bundle bilateral, multilateral and national finance for the support of local-level adaptation activities (see Marston 2013 for a brief overview on Bangladesh and Philippines; on Ethiopia see, for example, FDRE / MoFED 2012). While these national funds do not (yet) directly access international climate finance, they can offer examples and learning experience for other countries with regard to the design of national institutions for bundling and channelling funds to sub-national levels. Similarly, development finance has substantial experience with the devolution of bilateral funds.

To this effect, and in the context of the above described challenges of adaptation finance, this study will now analyse to what extent social investment funds (SIFs) could serve as an institutional structure for the delivery of adaptation funds. Past experience in the context of development finance indicates that social investment funds (SIFs) might offer a good

possibility for mainstreaming the delivery of adaptation finance into an existing institutional arrangement while meeting criteria and requirements of adaptation and development finance delivery as outlined above (see also Box 5).

For the final discussion of the potentials, limits and challenges of using SIFs for adaptation finance, these criteria and requirements have been merged into an integrated set of assessment criteria and equivalent questions. Box 2 allows for a brief overview and comparison of the climate and development agenda criteria and already synthesises those criteria that are being used as a baseline for further analysis. Box 5 gives an overview of these integrated criteria and requirements together with equivalent assessment questions, which will be addressed in Section 5. For further explanations on the deduction of the assessment criteria, see also the respective methodological annotations in Table 1 and Boxes 2 and 5.

Box 5: Delivering adaptation finance: minimum requirements, assessment criteria and questions

Requirements and assessment criteria for the delivery of adaptation finance		**Equivalent assessment question**
Cost-effectiveness and efficiency		• Can SIFs contribute to a cost-effective and efficient delivery of funds? • Can SIFs reduce transaction costs?
Support vulnerable	countries	• In which countries do SIFs operate?
	communities and groups	• Do SIFs allow for the operationalisation of a vulnerability-oriented funding approach? • Can SIFs finance activities at national, regional and community level? • Do SIFs allow for the effective involvement of relevant institutions and stakeholders?
	Indicator 9	• Can SIFs finance programme-based approaches?

Requirements and assessment criteria for the delivery of adaptation finance		**Equivalent assessment question**
Country-driven/ integrated approach		• Do SIFs strengthen country ownership?
	Alignment	• Do SIFs use country systems?
	Indicator 4	• Do SIFs promote consistency with national development strategies and programmes?
	Indicator 5a	• Do SIFs use national public financial management systems for distribution?
	Indicator 5b	• Do SIFs use public procurement systems?
Coordinated approach	Multitude of channels and sources	• Can SIFs be used to channel funds from a multitude of channels and sources?
	Indicator 4	• Do SIFs allow for the coordination of programmes? • Do SIFs promote coherence in programming and the delivery of adaptation finance?
	Indicator 6	• Do SIFs help to avoid parallel implementation structures?
Context specific		• Can SIFs consider context-specific information and requirements?
		• Can SIFs be adapted for financing policy implementation in different socio-economic contexts?
Gender specific		• Do SIFs allow for a gender-sensitive approach?

Requirements and assessment criteria for the delivery of adaptation finance		Equivalent assessment question
Transparency		• Are SIFs transparent in governance and allow for a balanced and equitable representation of stakeholders? • Are SIF operations transparent?
	Indicator 11	• Do SIFs have transparent and monitorable performance assessment frameworks to assess progress against national development strategies and sector programmes?

Notes: Methodological annotations

In order to simplify the representation of international minimum adaptation financing requirements:

- Indicator 9 (programme-based approaches) is being shifted to the criterion of 'supporting vulnerable communities and groups'.
- The criterion 'results-based approach' (Indicator 11) is assigned to the criterion of transparency as a results-based approach is one possible means to achieve transparency.
- Indicator 3 (report on national budgets) is merged with the criterion of 'programme-based-approach', as some programme-based approaches (e.g. budget support, sector budget support) can also be reported on budgets.
- The criteria 'country-driven' and 'country-driven/integrated approach' are merged.
- The criterion 'joint analysis' is left out as it is not directly related to the delivery of finance.

3 Social investment funds: evolution, geographical distribution and financial magnitude

In the context of official development assistance, (ODA), social investment funds (SIFs) have been operating for more than 20 years in numerous countries around the world. Their names have changed over time and from country to country. They are, *inter alia*, called social development funds, community or communal investment funds or simply social funds.

For the description of these funds, past studies have tried to establish typologies, distinguishing for example between 'transitory' and 'permanent' social funds (ILO 1994 quoted in Chacaltana 2002, 3), or differentiated funds according to their main policy objectives as emergency funds, infrastructure funds, employment funds, community development funds, or those that support social inclusion or decentralisation processes (see Cornia 1999 and Jorgensen / Van Domelen 1999; see also Serrano-Berthet 2007).

As most of these funds have multiple objectives and as their purpose and design have evolved over time, there is no simple, general typology or commonly accepted definition. Funds have developed 'vertically' as well as 'horizontally'. To give an overview, we therefore first describe the 'vertical' evolution from a historical perspective, classifying social investment funds according to generations that share certain policy objectives, and then analyse their 'horizontal' development in the form of geographical extension and financial magnitude. After that, Section 4 looks at the operational details of these funds, describing and analysing common characteristics, strengths and weaknesses.

3.1 A working definition

For this analysis, we have chosen to use the term 'social investment funds' (SIFs) in order to emphasise their common focus on investments and to differentiate them from funds that deal with recurrent expenditures or transfers, i.e. non-investments, such as entities dedicated to the operation and maintenance of national parks or social welfare funds managing transfer payments to households on a recurrent basis.

As there is no universally accepted definition of SIFs, we will use a 'commonly accepted' definition which describes them as facilities or

> *agencies that finance small projects in several sectors targeted to benefit poor and vulnerable groups based on demand generated in a participatory manner by local groups and screened against a set of eligibility criteria (Jorgensen and Van Domelen 2001). Social funds operate as intermediate agencies that appraise, finance, and supervise implementation of social investments identified and executed by a wide range of actors, including local governments, nongovernmental organizations (NGOs), local offices of line ministries, and community groups* (Bhatia 2005, 1).

International finance institutions (IFIs) also refer to SIFs as loan or grant 'operations' or 'projects'. While this properly reflects the view of a lending institution, this analysis looks at SIFs as facilities that form an institutional entity at the country-level, managing social investments in the form of projects.

3.2 The evolution of SIFs: the development context

The evolution of SIFs was driven by two important developments, first, a situation of economic and social crisis (Bhattamishra-Barrett 2008, 49), and second, the renaissance of community-based development approaches (Binswanger-Mkhize / De Regt / Spector 2009).

Economic, social, and institutional crisis

The first SIFs were developed by the World Bank and Inter-American Development Bank as short-term emergency funds in a context of economic and social crisis (De Silva / Sum 2008, 2). In the mid-1980, many developing countries had fallen into deep economic and fiscal crisis and, advised by the Bretton Woods Institutions, accepted 'structural adjustment programmes' (SAP), aimed at restoring industrial competitiveness and fiscal sustainability (e.g. World Bank 2010, 85). Among other measures, SAPs usually included massive lay-offs of public-sector employees, much of it by downsizing or outright closing unsustainable state-owned enterprises. The ensuing unrest of a well-organised labour force threatened to render SAPs socially and politically unviable. As a measure of rapid response, nationwide public works programmes were to be set up, to put the unemployed temporarily back to work (e.g. Marc et al. 1995). It was expected that this would boost domestic demand in the short run, until the expected structural impact of SAPs led to increased competitiveness, subsequent sustained growth and full employment. In this context, SIFs were also seen as a *"major World Bank initiative in response to the failure of structural adjustment to safeguard the needs of the poor"* (Abbot / Covey 1996, 2)

Part of the crisis was an institutional bottleneck for the delivery of investments. During the times of fiscal bonanza, central line ministries and other state-owned entities had grown a lot in terms of staff but little in terms of effectiveness, and even less as regards efficiency. This posed a serious impediment to the fast and cost-effective implementation of hundreds of

small, labour-intensive public works required across a country. A case study from Zambia, for example, states that *"government institutions proved that they were unable to provide a co-ordinated, targeted and multi-sectoral response to emergency situations that would assist poverty reduction"* (Crosbie 2009, 11 based on Marc et al. 1995).

To meet the challenges of the economic, social and institutional crisis, the Government of Bolivia as the first country decided to set up a small, publicly-owned entity called the "Emergency Social Fund" (FSE, *Fondo Social de Emergencia*). The fund featured a lean bureaucracy and simple operational rules and many private sector-like management approaches, including market-based recruitment and outsourcing. In 1987, the International Development Association (IDA) was ready to provide financing on conditional terms to the FSE. The FSE soon became famous for "*its demand-based approach, its efficiency and transparency, and its rapid results*" (Graham 1992) which spurred the set-up and massive development of social investment funds around the world.

The success of the first 'emergency-types' of SIFs in quickly generating employment and boosting demand led to a 'horizontal' spread across countries and continents. Partners of international development assistance (ODA) acted as catalysts and knowledge managers in that process. In parts, these roles have been assumed by regional associations of SIFs[14] later on, which started to emerge as the funds multiplied in different continents.

At the same time, many SIFs have also evolved 'vertically', which explains the persistence of many of these entities in the same country over time. Showing an amazing flexibility in adapting to changing policy environments and the needs of their national owners and ODA partners, most SIFs continued to be useful institutional set-ups far beyond the emergency situation they were created to respond to initially (De Silva / Sum 2008, 25).

A renaissance of community-driven development approaches

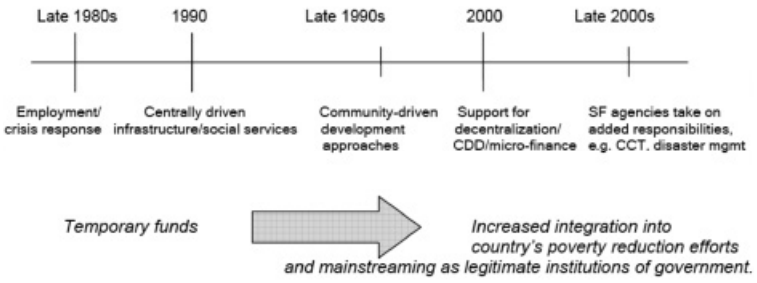
An important driver for the vertical development of SIFs was the renaissance of community-driven development (CDD) approaches in the 1990s (compare Figure 2). As sector bureaucracies of that time were often

14 Such as the Social Network of Latin America and the Caribbean (REDLAC, by its Spanish acronym) and the Association Africaine des Agences d'Exécution des Travaux d'Intérêt Public (AFRICATIP).

reluctant to encourage rural empowerment and many sector approaches were *"too slow to deal with the adverse employment and welfare consequences of economic reforms and adjustment programs of the 1980s"* (Binswanger-Mkhize / De Regt / Spector 2009, 27), actors in development cooperation, among them the World Bank, *"looked for better ways to reach communities directly"* (ibid.).

Social funds were *"multi-sectoral and gave communities the opportunity to specify their subproject priorities"* which provided an opportunity for *"several new experiments in community-based development [...]"* using community consultation and participation models (Binswanger-Mkhize / De Regt / Spector 2009, 28; compare also World Bank 2010, 6). While SIFs were developed *"to transfer resources to local levels and execute projects in a participatory manner"*, CDD *"programs emerged that went a step further and transferred resources directly to community management, while at the same time introducing coordination at the local government level"* (Binswanger-Mkhize / De Regt / Spector 2009, 8–9). The World Bank used the term CDD *"to denote this broad class of interventions that transferred control over resources and decision-making from central agencies to communities"* (De Silva / Sum 2008, 2, quoting Dongier et al. 2003).

Figure 2: Evolution of SIFs' objectives and activities



Source: De Silva / Sum 2008, 3

In the field of safety net programmes, social funds were seen as an innovative mode of delivering non-food assistance through non-governmental channels and became a primary means of delivering social assistance (Subbarao et al. 1997, 17, 137). Part of this innovative mode was that SIFs were most

commonly associated with the private model of delivering social assistance while not necessarily excluding the public sector and traditional public delivery models (Subbarao et al. 1997, 97). The *"private delivery model involves a range of service deliverers, notably, private contractors, NGOs, and community groups sometimes in addition to public agencies"* (Subbarao et al. 1997, 96). In this context, SIFs neither provide nor produce a service but facilitate service provision and production (Subbarao et al. 1997, 97). Largely influenced by the experience of Bolivia's FSE, the concept incorporates market principles into the programme design through the demands of beneficiaries (Subbarao et al. 1997, 137).

In order to describe the main trends in the vertical evolution of SIFs in more detail, we give a brief overview of SIFs based on a generation model (compare IDB 2002, quoted in Chacaltana 2002, 3).

3.2.1 Trends in vertical SIF evolution: generation models

Trends in the vertical evolution of SIFs can best be captured by a generation model. The generation model is similar to, but goes beyond, a classification according to main policy objectives (see above) by identifying the commonalities that funds had at a certain time period with regard to several characteristics (see Table 3). The generation model was first constructed as part of a study by the Inter-American Development Bank, classifying IDB funds on a time axis (IDB 2002).

While the focus and design of an SIF is first and foremost a reflection of national policies in a given country, the commonalities of SIF generations also reflect macro trends in the international development debate and within ODA agencies.

Although real funds form the basis for our depiction of SIF generations, they only describe general trends and are too a certain extent ideal-type descriptions. These facilitate the illustration and analysis of strength and weaknesses of certain models. In practice, there are considerable differences in the vertical evolution of SIFs between countries with regard to content, pace and timing. The extent to which current SIFs share characteristics of a generation can vary as well (compare also Sub-section 3.2.3).

First generation

The safety nets programmes '1st generation' are emergency-type SIFs focusing on short-term economic employment opportunities (Vermehren / Serrano-Berthet 2005, 95) in times of economic downturn through a boost in public investment – 'to hire people to dig a ditch and fill it up again', as a popular explanation of these Keynes-style measures goes. These funds specifically address the input aspects of public investment by emphasising the speed of implementation and labour intensity in project selection. The outputs and benefits arising from projects, such as, for instance, a new drainage system and corresponding improvements in land-use, are welcome and desired, but they are not the focus of the '1st generation'-type of SIFs.

With speed of spending being a major concern for the effectiveness of SIFs, projects had to be technically simple, fast to start and implement, and the project management cycle needed to be as lean and swift as possible. Accordingly, whoever showed the capacity to implement public works fast, be it a public or private entity, was a suitable project executing agent for a 1st generation SIF. This mostly excluded local governments and communities.

Another key concern for SIFs of the first generation was the precise targeting of investments towards the temporarily unemployed and those negatively affected by SAPs, also called 'the adjustment poor'. Resources were allocated based on *ex-ante* defined eligible investments, often in urban areas.

> *However, the distinction between 'chronic poor' and 'adjustment poor' was never clearly defined, or targeted. Consequently both the remit and scope of the Social Investment Funds began to evolve into wider programmes – with a shift of emphasis from 'income maintenance to community based provision of social services'* (Crosbie 2009, 6 quoting Cornia 1999).

Second generation

By shifting emphasis to a community-based provision of social services, second generation SIFs shifted their focus from being an emergency response mechanism to a longer-term approach aimed at fighting structural poverty and massively expanding access to basic social infrastructure (Vermehren / Serrano-Berthet 2005, 95). Policy objectives could include the provision of more and better schooling and health facilities or safe drinking water in remote locations.

Going along with the change of policy objectives, SIFs also changed their operational targets and techniques as well as rules and procedures. The target group of second generation SIFs shifted from the temporarily unemployed, frequently urban, to the structurally poor, mostly concentrated in rural areas. In several Latin American countries, *"SIFs also developed programs for special target groups like orphans, disabled youngsters, youth at risks, and the elderly"* (Vermehren / Serrano-Berthet 2005, 95). The targeting techniques of reaching these groups developed into state-of-the-art reference points in many countries, including multi-dimensional poverty mapping and participatory poverty assessment. SIF beneficiaries were identified through parameters such as income, access to basic services (e.g. health and education), or vulnerability of rain-fed agriculture to hazards.

SIFs turned their attention away from the speed and employment-intensity of investment to the benefits and impacts of public investment. Not only the investment itself, but also its quality and expected impact were of importance. Project selection criteria accordingly emphasised the development impact of projects. Towards that respect, empowerment of civil society structures at the local level and community participation in project selection and execution were regarded as key, and have become a hallmark of 2nd generation SIFs worldwide. The selection of project executing agencies for SIFs followed the logic of community-driven development. The identification, selection and implementation of projects were devolved to local community groups.

Rules and procedures governing the project cycle of SIFs became complex at the expense of speed. Calls for the incorporation of cross-cutting issues such as gender and environmental sustainability, aimed at further improving project quality, but also contributed to a loss of the simplicity that had characterised first generation-type SIFs.

In a bid to better handle increased complexities, some countries and their development partners opted to create additional SIFs emphasising a specific sector or issue, such as rural development, gender, or the environment. The ensuing proliferation of SIF-type funds within a single country has sometimes been considered a strategy of 'product diversification' by recipient countries to increase access to international resources on conditional ('soft') terms, which became available as new development issues rose on the international agenda.

Third generation

Third generation SIFs emphasise the promotion of decentralisation and good local governance which has been a principal goal of many development strategies (Vermehren / Serrano-Berthet 2005, 96). While the IDB study (2002) already identified this trend for the time period 1998/9 to 2002, an analysis of World Bank social funds for the fiscal years 2000 to 2007 comes to a similar result. Noting a general diversification of fund goals, the

> *most common trend has been to increase the role of social funds in governments' decentralization processes, by shifting more responsibility for managing local level investments and providing more direct training and capacity building for overseeing these investments to local governments* (De Silva / Sum 2008, 2).

The decentralisation process forced governments and donors to rethink the role of SIFs in the promotion of local development. While some countries ignored this task or transformed their SIFs into pure fiscal transfers (e.g. PRONASOL/Mexico), the majority of countries reformed their SIFs. These reforms included merging funds, absorption by line ministries, or the institutionalisation as permanent institutions. Vermehren and Serrano-Berthet (2005, 100) identify two main strategies emerging from these reform initiatives: one emphasises the role of SIFs for decentralisation and local development processes; the other stresses the institutional role of SIFs in reaching vulnerable and poor groups, for example as part of countries' social safety nets.[15]

For the implementation of these strategies, countries assigned two major roles for SIFs. One was to transform SIFs into conditional matching grant mechanisms, thereby rationalising fiscal transfers to municipalities with a pro-poor bias and aligning and leveraging municipal investments toward national priorities (Vermehren / Serrano-Berthet 2005, 102). Through this, SIFs were also used as compensatory fiscal transfers aiming to counterbalance existing inequalities between different government districts.[16]

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15 This analysis of strategies is based on Bolivia, Peru, El Salvador, Honduras and Nicaragua. For a more detailed outline of these strategic directions, see Vermehren / Serrano-Berthet 2005, 101 ff.

16 See e.g. the role of the Fondo Nacional de Inversión Productiva y Social (FPS) in implementing Bolivia's anti-poverty policy, National Compensation Policy (Vermehren / Serrano-Berthet 2005, 102). For a detailed analysis see also Isidoro Losada 2006.

Table 2: Examples of local government involvement in planning, financing, implementing SIF-financed activities						
	Planning		**Financing**		**Implementation**	
Country	**Do projects come from participatory municipal plans?**	**Statutory guidelines for participatory municipal planning (PMP)**	**Do local governments (LGs) manage the funds?**	**Allocation mechanism**	**Who has the main responsibility for implementation (contracting, supervising, etc.)?**	**Are LGs and communities involved in maintenance?**
Honduras FHIS	Yes	Yes Municipal development Strategic plans	Only accredited LGs Some LGs also transfer to community groups	Formula-based (poverty map)	Accredited LG, municipal associations Non-accredited SIFs	Yes Municipal maintenance plans, community maintenance organisations
Nicaragua FISE	Yes	Yes Municipal planning system	Only accredited LGs Some LGs also transfer to community groups	Formula-based (poverty map). Transitioning to matching grants reflecting sectoral priorities	Accredited LGs Non-accredited SIFs	Yes Preventive maintenance fund Community maintenance organisations

Table 2 (cont.): Examples of local government involvement in planning, financing, implementing SIF-financed activities						
	Planning		**Financing**		**Implementation**	
Peru FON-CODES	Yes	Yes Participatory budgeting law	Only accredited LGs	Formula-based (poverty map)	LG or joint community-LG teams	Yes
El Salvador FISDL	Yes	Yes Minimum criteria guidelines	All LGs that gain the contract	Competitive biddings	LGs	Yes
Bolivia FPS	Yes	Yes Popular participation law	LG approves payment and FPS pays contractors	Formula-based, indicative municipal allocation (poverty map). Matching grant reflecting sectoral priorities	LGs	Yes
Notes: Abbreviations: See list of abbreviations. Source: Vermehren / Serrano-Berthet 2005, 103 (with editorial changes)						

Table 3: Trends and characteristics of SIF generations

	SIF models		
	First generation (end 1980s–mid 1990s)	**Second generation** (mid 1990s–end 1990s)	**Third generation** (end 1990s–2007)
Overall policy objective	Promote short-term employment/social compensation;	Promote local development, provision of/access to social and economic infrastructure/ services	Promote decentralisation and good local governance
Principal concern of intervention	Project spending, (labour) inputs; speed of implementation	Development impacts, project outputs/ benefits,	Strengthen local governments; good governance training; matching grant mechanism (pro-poor, alignment with national priorities)
Main targeting techniques	Ex-ante defined eligible investments; registers of unemployed	Poverty maps, participatory poverty assessments	Poverty maps (incl. institutional capacity fiscal indicators)
Direct beneficiaries	Unemployed, mostly urban, public and private	Poor communities/community-based groups; mostly rural; public and private actors	Local governments (public sector only); often excluding major cities
Local government participation	Mostly excluded	Mostly excluded	Delegation of ownership and responsibility to local governments in planning, implementation, oversight, operation

Table 3 (cont.): Trends and characteristics of SIF generations			
	SIF models		
Community participation	Mostly excluded from project cycle management	Empowerment of local community groups through participation in/outsourcing of project cycle	Emphasis on participatory municipal planning and community participation in project cycle
Relation with line ministries	Inter-institutional agreements defining operations and maintenance (O&M) responsibilities	Often parallel to public structures, used to help trigger reforms in the social welfare sector	Many SIFs were transformed into permanent institutions or integrated into line ministries
		Facilities often lacked staffing for adequate operation	Intensive work coordination and alignment with line ministries
		Operation and maintenance (O&M) arrangements failed; projects financed under previous operations needed repair	
Complexity of SIFs	Low for the sake of speed	Increasingly high following complexity of objectives	Moderate to high, attempts to 'de-bureaucratise' procedures
Sources: Own additions and modifications based on Schulz-Heiss 2011 and IDB 2002, quoted in Chacaltana 2002; Crosbie 2009; Vermehren / Serrano-Berthet 2005			

The other role was to use SIFs to strengthen good local governance and build communities' capacities in (participatory) municipal planning, financing and managing local infrastructure services (Vermehren / Serrano-Berthet 2005, 102).

According to the new development objectives, SIFs adapted their targeting techniques. Poverty maps, for example, were produced for the identification and prioritisation at the district or regional level. These poverty maps could entail criteria of institutional capacities or 'fiscal poverty' such as the endowment of local governments with funds, staff and other resources.

According to the new development objectives, SIFs also changed the role local governments could take in the management of funds. The analysis of SIFs in five Latin American countries by Vermehren and Serrano-Berthet (2005; Serrano-Berthet 2005) provides an interesting overview of how SIFs devolved ownership and responsibility to local governments in the field of planning, financing and implementation (see Table 2 for an impression).

Many SIFs of the third generation only invested in activities that were developed as part of participatory municipal planning processes. This represents a major change to second generation SIFs that financed

> *isolated projects presented mostly by individual communities or politicians and approved centrally by SIFs. This [...] approach was criticized because of its potential to undermine local governments, and its lack of transparency and downward accountability* (Vermehren / Serrano-Berthet 2005, 104).

Third generation SIFs also transfer all or a substantial portion of resources directly to local governments (as the main 'client' of SIFs), whereby some municipalities transfer these resources further down to community groups (Vermehren / Serrano-Berthet 2005, 106). In earlier SIF models until the late 1990s, most SIF funding was managed centrally.

Beyond the influence of policy trends that affected the evolution of SIFs, an important cross-cutting function of SIFs throughout time included risk management. As risk management also plays an important role in adaptation processes, we will highlight the main approaches and functions of SIFs in this area in the following section.

3.2.2 SIFs and risk management

From the first generation onwards, SIFs have held an important place in risk management. The World Development Report 2000/1 (World Bank 2000) categorises SIFs *"as publicly provided, formal risk management mechanisms"* (De Silva / Sum 2008, 8). Jorgensen and Van Domelen (2001) write that SIFs are well *"positioned to enable community-based institutions to manage risk due to their close involvement with a range of community, public and market agents, and the rapidity and flexibility of their response"* (De Silva / Sum 2008, 7; see also Batthamishra-Barrett 2008, 52).

Two main perspectives and related political contexts of risk management played an important role in the evolution of SIFs: disaster risk management, and social protection. From the beginning onwards, SIFs have regularly been used to provide rapid assistance in the aftermath of natural disasters (e.g. IEG 2006; Chacaltana 2002; Siri s.a.; Vermehren / Serrano-Berthet 2005, 95; compare also Table 4). Evaluations or case studies have shown that SIFs had a leading role in reinstating basic services and promoting stability, for example in Honduras and Nicaragua after Hurricane Mitch (see World Bank 2010, 272; Vermehren / Serrano-Berthet 2005, 95), and have proven to be flexible and innovative instruments for both directly responding to natural disasters and contributing to risk reduction (IEG 2006).[17] In El Salvador, for example, SIFs provided resources for small construction projects like retrofitting or adaptation of structures for extreme weather conditions (Warner / Bouwer / Amman 2007).

Furthermore, SIFs were used for risk management in the field of social protection, for example supporting safety nets and community-driven risk arrangements (see above). The main reference point for SIF operations of the World Bank from 2001 onwards – as an example for a major SIF lender – was the bank's Social Protection strategy paper (De Silva / Sum 2008, 5; for the strategy, see World Bank 2001). The strategy entails a broader approach to risk management in social protection policies (see also Holzmann / Jorgensen 2000).

17 For an overview of characteristics that place social funds in a good position for risk reduction and risk response, see World Bank 2010, 7–8.

Table 4: Overview of risks addressed by social funds in Latin America

Categories of Risk	Risk reduction	Risk mitigation	Risk coping
Economic risks	Job training programmes: e.g. FOSIS (Chile); RSS (Colombia); FONVIS (Venezuela); SIF (Belize)	Some productive projects: e.g. Redes Rurales (Peru); Microcredit (Chile)	Workfare programmes: e.g. FONCODES (Peru)
Natural risks		Programme of reforestation: e.g. FISE (Nicaragua); FOPAR (Argentina); Programme of collection and use of ground: e.g. FHIS (Honduras); SEDESOL (Peru); FOPAR (Argentina)	Floods (El Nino): several countries; Mitch Hurricane: FIS (Nicaragua); FHIS (Honduras); FIS (Guatemala); Earthquakes: FONCODES (Peru)
Social risks		Helping programme for victims of human rights violations: e.g. FIS (Guatemala), Protection of poor women rights: e.g. FODESAF (Costa Rica); FONVIS (Venezuela)	Displacements programmes for victims of social violence: e.g. RSS (Columbia); Community homes for abandoned children: e.g. FODESAF (Costa Rica); FONVIS (Venezuela)
Health risks	Nutrition Programmes: e.g. FONCODES First Fund (Peru); FIS (Panama); FONVIS (Venezuela)		Helping programme for disabled people: e.g. FODESAF (Costa Rica); RSS (Columbia)

Table 4 (cont.): Overview of risks addressed by social funds in Latin America			
Categories of Risk	**Risk reduction**	**Risk mitigation**	**Risk coping**
Life-cycle risks	Programmes that give attention to mothers/children: e.g. PAMI Program/RSS (Columbia); FONCODES First Fund (Peru)		
Political risk		Protection of poor women's rights: e.g. FODESAF (Costa Rica); FONVIS (Venezuela); FIS (Guatemala); RSS (Colombia)	
Environmental risk	Investment programme in Environment Sanitation: e.g. FIS (Guatemala); SIF (Belize); FONVIS (Venezuela)	Financial market solutions for environmental problems: e.g. Ecomercados Program/ FODESAF (Costa Rica)	Programme of trash collection: e.g. FISE (Nicaragua); FOPAR (Argentina)
Notes: Abbreviations: See list of abbreviations. The risk categories used for the analysis are based on the Social Risk Management framework by Holzmann / Jorgensen (2000). The analysis is only based on SIFs in South American countries. Source: Adapted from Chacaltana 2002, 17			

With the general[18] broader conceptualisation of risks and their role for poverty reduction, the role of SIFs in risk management also broadened. While early SIF interventions focused on risks related to natural disasters or the economic crisis, later SIFs aimed to address a variety of social risks that might render communities vulnerable to external shocks. Categories of risks addressed by SIFs include for instance: economic risks, natural risks, social risks, health risks, life-cycle risks, political risks or environmental risks. Examples of the risks categories addressed in the past by SIFs are provided in Table 4. The risk management arrangements and the related responsible actors that SIFs support broadly fall into three categories: informal (e.g. informal saving groups at the community level); market-based (e.g. access to micro-finance); and public arrangements (e.g. community-based disaster risk reduction strategies).[19] Table 5 lists further examples of risk management-related activities in these three categories.

Over time, SIFs also expanded their support of risk management functions. While early SIF generations focused their support on risk coping (e.g. public works programmes, conditional cash-transfers, reconstruction), following generations increasingly addressed functions of risk mitigation (e.g. strengthening local institutions), or risk reduction (e.g. increase access to basic services, water supply and sanitation; De Silva / Sum 2008, 7; Chacaltana 2002, 20).[20]

As the risk categories listed in Table 4 and 5 are mainly based on a conceptual framework from the years 2000 and 2001 (by Holzmann / Jorgensen 2000) and not on an empirical analysis of running SIFs, the risk categories that SIFs currently address can be different in practice. There is no general updated review or analysis on the role of SIFs in the area of risk management.

18 See also discussions by other actors in other arenas, e.g. Watts / Bohle 1993, or Kasperson / Kasperson 2005.

19 See Batthamishra / Barrett 2008, 54ff on ideas of how SIFs could support community-based risk management arrangements and on potential problems that may arise due to SIF support.

20 For a trend analysis of social funds in disaster risk management in Honduras, Nicaragua, Madagascar and Armenia, see Siri (s.a.).

Table 5: Examples of risk management arrangements and strategies supported by SIFs			
Arrangements and strategies	**Informal**	**Market-based**	**Public**
Risk reduction	*Social fund interventions:* • Strengthening informal community-based institutions • Building linkages between community and public/private actors • Enhancing social capital by putting in place processes that promote trust and cooperation at community level		*Social fund interventions:* • Support for socially inclusive policies and legislation. • Increasing access to basic services, (e.g. preventive health care, water supply, primary education) • Promoting participatory local planning processes • Public awareness campaigns for positive behaviour change, e.g., health awareness raising, HIV/AIDS prevention, better nutrition. • Support to community-based disaster risk reduction strategies
Risk mitigation portfolio	*Social fund interventions*: • Support to informal community savings groups • Enhancing social capital by putting in place processes that promote trust and cooperation at community level	*Social fund interventions*: • Increasing access to micro-finance services. • Investments in income-generating activities	*Social fund interventions*: • Land titling training and related support • Increasing access to legal assistance and • Legal literacy programmes for women and marginalised groups • Training for community members (e.g., vocational training for unemployed youth, adult literacy classes)

Table 5 (cont.): Examples of risk management arrangements and strategies supported by SIFs

Arrangements and strategies	Informal	Market-based	Public
Risk mitigation insurance	*Social fund interventions*: • Supporting community risk management arrangements, e.g. providing matching grants to burial societies in Africa		
Risk coping	*Social fund interventions:* Enhancing social capital by putting in place processes that promote trust and cooperation at community level		*Social fund interventions:* Support to public works programmes Support to conditional cash transfers Temporary employment generation to cope with economic crisis Interventions to support relief and reconstruction after natural disasters (e.g., Pakistan earthquake, Malawi drought, Honduras – floods, etc.)

Source: De Silva / Sum 2008, 7

3.2.3 Coexistence and trade-offs between generations

The SIF generations are not mutually exclusive. Most funds support several objectives and activities (De Silva / Sum 2008, 2) and few SIF belong to one generation only. Instead, many SIFs rather preserve and use their 'generation heritage' to different degrees at different points of time.

Depending on the political circumstances and needs, governments also redesign, for example, second or third generation funds into first generation funds. A reason for such a redesign can be an economic downturn (see e.g. Peru, National Fund for Social Development/Fondo Nacional de Cooperación para el Desarrollo Social)[21], *"the response to short-term rehabilitation needs (e.g. Nicaragua, Honduras, Madagascar and Jamaica)"* (De Silva / Sum 2008, 2), like a natural disaster (see, for example, Haiti) or a general re-centralisation of social politics, as for example in Bolivia (World Bank 2004, quoted in Isidoro Losada 2006).

The redesign of SIFs throughout time illustrates that the attribution of a SIF to one generation should not be interpreted as a value judgement. Second or third generation SIFs are not inherently better than first generation funds. The quality of a specific SIF at a given moment depends on how far and well the fund has been able to adapt to the specific policy concern of the specific country at the specific point in time. Against this background, the SIF generation model simply helps to understand the genesis and primary goals as well as strengths and limitations of past SIFs as will be outlined in further detail in Section 4.

The evolution of SIFs shows that they can be designed in a flexible manner according to changing national and international policy environments and development currents. The development of SIFs in Bolivia illustrates this particularly well. Since the emergence of the FSE, Bolivian governments have changed and introduced different types of SIFs tailored to their respective policy needs (compare Isidoro Losada 2006), changing from dedicatedly pro-market to pronouncedly state-interventionist or mainstreaming new policy needs such as the Millennium Development Goals (see Treviño Paredes et al. 2005).

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21 Before 2005, the fund was called FONCODES, *Fondo* Nacional de *Compensación y Desarrollo Social.*

There are, however, also tensions and trade-offs between the three generations of funds. Direct interaction between a national SIF and grassroots communities and civil society organisations, as practiced by 2nd generation funds, for example, tends to weaken the position of local governments who are the principal clients of 3rd generation SIFs. A well-known example for deliberately weakening local governments through a strong national SIF was FONCODES under the Fujimori regime in the 1990s (see Schady 1999).

Similarly, a high degree of autonomy by local governments in choosing from a multi-sector 'menu' of projects eligible for SIF financing – typical for 3rd generation funds – may reduce the incentives to implement national sector policies, as the outcomes of participatory planning processes only occasionally coincide with national targets for local investment.

3.3 Geographical distribution and financial magnitude

To compile updated and precise figures on the total number and geographical breakdown of social investment funds today is not an easy affair, and it is even more difficult to arrive at definite numbers on the volume of funds and operations they have been handling. There are four main reasons for this:

1. The sheer magnitude and worldwide spread of SIFs make a country-by-country analysis a major endeavour. Such an analysis does not exist so far and is also beyond the scope of this study.
2. SIFs have evolved over more than 20 years, as have their names as illustrated above. Therefore, identifying them is very difficult. In some cases, the role and functions of SIFs have been taken over by and integrated into other institutions, which renders it even more difficult to identify SIFs.
3. The development banks that have been providing much of SIF funding mostly do not treat SIFs as a separate portfolio. As the funds have evolved into instruments of quite different policies over time, operations and resources executed through SIFs are earmarked according to portfolios as different as infrastructure, human development, governance and the various sectors which the instrument has been serving. An overview would require cross-cutting portfolio analyses.

4. While ODA agencies tend to report SIFs as closed once the corresponding ODA operation has terminated, most SIFs have outlived the initial external support and continue to thrive on national budget resources, or have diversified their funding structure to other domestic and external sources. According to a major review by De Silva and Sum from 2008, this is the case for most World Bank-supported SIFs. Another major review even finds *"many instructive cases of social funds financed wholly by governments"* (Bhatia 2005, 6).

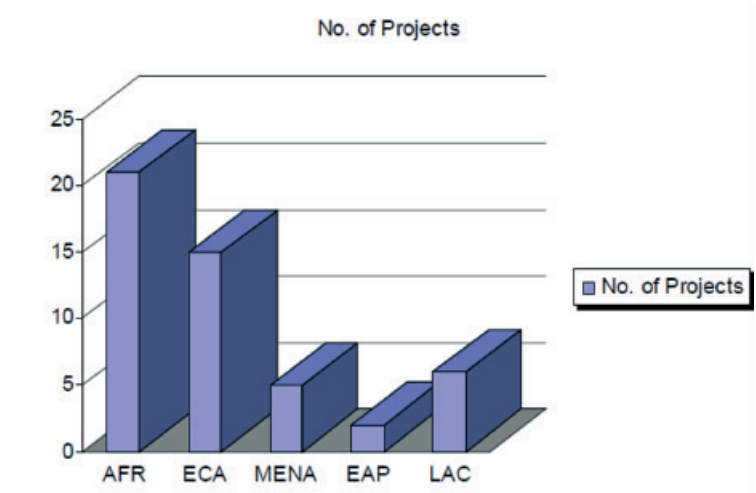
Nevertheless, reviews in literature and secondary data available on the subject provide enough references to get an idea of the order of magnitude of past SIFs. A stocktaking exercise in form of a workshop organised by the Kreditanstalt für Wiederaufbau (KfW Development Bank) and the World Bank in 2004 concluded that SIFs had received ODA support of more than USD 4 billion in more than 60 countries, earning them the attribute of *"one of the most successful financing instruments of multilateral and bilateral ODA in terms of financial volume"* (Juntermanns / Schickinger 2004, 2). In 2004, the KfW estimated that its financial support to SIFs amounted to EUR 400 million for 26 countries (Juntermanns / Schickinger 2004, 2).

A review published in 2005 (Bhatia, 1) concluded that the World Bank financed almost USD 4 billion in social-fund-type projects in some 60 countries and estimated that an additional USD 5 billion was leveraged from other multilateral, bilateral, and domestic resources. The IDB alone has invested USD 2.7 billion in 40 different SIFs.

The latest and most comprehensive review of SIFs financial volumes and regional distribution is a World Bank lending review of their social protection portfolio from 2008 for the fiscal year 2000 to 2007 (De Silva / Sum 2008). At the World Bank, social funds are – next to community-driven development operations – the main instrument by which the Bank engages with, and delivers assistance to, communities in developing countries (World Bank 2010, 6). The review calculates that the Bank's commitment to SIFs had reached USD 5.4 billion by 2007. On a time axis, the lending trend analysis illustrates the rapid horizontal growth of SIFs. Between the first SIF in 1987 and 1999, the bank committed USD 3.5 billion, covering 98 projects in 57 countries (De Silva / Sum 2008, 11; see also Rawlings / Sherburne-Benz / Van Domelen 2004). Another 42 programmes have been established between 2000 and 2006 (De Silva / Sum 2008; compare also Bhattamishra / Barrett 2008, 50).

SIFs have been established in all ODA-eligible regions as illustrated in Figure 3 and Table 6. African countries had the largest number of social fund projects between the fiscal year 2000 and 2007, accounting for 50 percent of the Bank's Social Protection portfolio (De Silva / Sum 2008, 17). Latin America and the Caribbean, initially regions with most SIF lending, have received less lending through these funds in recent years. According to UN Habitat (2009, 18) the average fund size in Latin America is USD 240 million compared to USD 18 million in Asia. In countries where the International Development Association (IDA)[22] operates, the SIF portfolio represents 61 percent of lending for social protection operations between the fiscal year 2000 and 2007 (De Silva / Sum 2008, 14).

Figure 3: Regional distribution of SIF projects in the social protection portfolio of the World Bank, FY 2000 to 2007



Source: De Silva / Sum 2008, 16

22 IDA is part of the World Bank and operates in the poorest countries, see http://www.worldbank.org/ida/what-is-ida.html for further information.

Table 6: Countries with SIFs from the World Bank's social protection portfolio between 1987 and 2007

AFRICA	EUROPE AND CENTRAL ASIA	LATIN AMERICA AND THE CARIBBEAN	MIDDLE EAST AND NORTHERN AFRICA	EAST ASIA PACIFIC and SOUTH ASIAN REGION
Angola Benin Burundi Comoros Congo, dem. Rep. Eritrea Ethiopia Ghana Guinea Lesotho Liberia Madagascar Malawi Mali Nigeria Sao Tome and Principe Senegal Tanzania Togo Uganda Zambia Zimbabwe	Albania Armenia Bosnia and Herzegovina Bulgaria Georgia Kosovo Macedonia Moldova Romania Tajikistan Turkey Ukraine Uzbekistan	Argentina Belize Bolivia Colombia Ecuador El Salvador Guatemala Guyana Haiti Honduras Jamaica Nicaragua Panama Peru Saint Lucia	Algeria Egypt Lebanon Morocco West Bank and Gaza Yemen	Cambodia Lao PDR Philippines Sri Lanka Thailand Timor-Leste

Source: Author's representation based on data by De Silva / Sum 2008

The extent to which the World Bank data is representative for SIF lending over time is unclear. There is no comprehensive overview on the status of SIFs; particularly data on the last seven years is lacking. What is important to note for the scope of this study are two points:

- There is experience with SIFs as a financing agency in at least 60 countries across the globe. As many governments opted to reform SIFs

(compare 'third generation' above), they are probably still part of the institutional landscape in a vast number of developing countries.

- The fact that SIFs have been established in many countries and the high financial volume that has been trusted to and channelled through SIFs underpin the importance of SIFs as a financing agency for local-level development activities.

From the perspective of international adaptation finance, SIFs therefore merit further discussion to the extent they can be used to channel international finance to the ground.

3.4 Preliminary conclusions

The brief analysis of the evolution of SIFs over time has shown that SIFs have been intensively used by international development banks, ODA agents and recipient governments for the delivery of international finance for investments at the local level. SIFs have been financed by different sources coming from development aid, multilateral banks or national budgets and have been used to channel resources to the regional, local and community level.

The primary goals of SIF interventions have changed over time. Despite these changes, SIFs have persisted and have been reformed. This demonstrates on the one hand that it is possible to adapt SIF operations to new policy goals and targets, and more importantly, that SIFs have been valued as a facility or agency for the delivery of investments at the local level and have therefore been maintained. One reason for the appreciation of SIFs is the possibility to involve local actors to varying degrees in the management and use of funds. Another is the development of techniques that allowed a targeted approach for fund allocations.

SIFs and adaptation finance share strategic perspectives

From an institutional perspective and in the context of countries' poverty reduction strategies, SIFs and adaptation finance share strategic perspectives. Vermehren and Serrano-Berthet in 2005 concluded that governments have assigned three main strategic roles to SIFs, which at the same time means that governments and the various responsible actors involved in reform processes have identified three roles for whose fulfilment they attribute a particular strength to SIFs. These three roles are:

1. *"**Engines of local development**: As decentralization processes deepen in Latin America, governments – at the central and local level – assign social funds a major role in financing local investments and building capacity at the municipal and community levels to ensure a transparent, inclusive and participatory development process*
2. ***Laboratories for innovation**: Many social funds have not only introduced innovative practices and procedures, but have also created innovative programmes and approaches to development, with particular focus on the poorest and most vulnerable*
3. ***Promoters of social capital**: Social funds are one of the few central government organizations that work in a multi-sectorial way at the local level, building community organizations and capacity of communities to design and manage their own development process"* (Vermehren / Serrano-Berthet 2005, 115, accentuation by author).

With regard to the international financing requirements and challenges, these strategic roles are particularly interesting as they overlap with important requirements of international adaptation finance (see Section 2) and/or adaptation processes as such:

- Adaptation finance should not only support vulnerable countries but also groups and communities (see Box 1), but so far the delivery mode to local levels is often unclear and/or contested. As this is a major role of SIFs, they can offer an example and should be looked at more closely.
- Innovation in the delivery of finance is also an overarching goal or need in adaptation finance. The Adaptation Fund allows for innovative approaches as the proposal of South Africa shows. Although many actors generally reject ODA channels from a negotiation perspective, they should not with regard to the technical and practical experience of delivery channels, particularly when strategic and/or practical goals overlap. In addition, as outlined above, many SIFs have been transformed into nationally owned institutions.
- Finally, the local level and local level institutions (should) play an important role in adaptation processes or related tasks like disaster risk reduction and management. Adaptation finance, furthermore, aims at an integrated, cross- or multi-sectorial, approach.

Beyond this strategic perspective on the roles of SIFs in development finance and possible roles in adaptation finance: To what extent is the experience of SIFs relevant for current challenges of adaptation finance delivery? Based on the previous analysis, four points are particularly important:

1. **Institutional experience**: SIFs provide context-specific experience in the institutional design of *delivering investments* to the local level. They are probably still part of the institutional landscape in a vast number of developing countries. They can, therefore either i) be used directly to deliver adaptation funds if they already finance activities relevant for adaptation strategies; ii) be adapted to also deliver adaptation funds; or iii) provide useful lessons for designing institutional structures for delivering adaptation finance. (On the extent of thematic overlap of the SIF portfolio and climate change adaptation finance, see the third point.)

2. **Experience in delegating ownership and responsibility**: Beyond delivering resources to the local level, SIFs can provide an example and lessons learnt of how ownership and certain responsibilities in the management of adaptation funds (such as project identification and selection, planning, implementation and maintenance; compare Table 2 and Section 4) *can be devolved* to local governments and communities. As described in Section 2 and Box 3, this is a current challenge of international adaptation finance.

3. **Thematic overlap**: This brief analysis shows that SIFs financed or still finance activities in a wide range of issue areas aiming to address one or several objectives and capacities that can also be relevant for adaptation processes. As outlined above, two of these relevant issue areas are disaster risk management and social protection.

   Several Global Assessment Reports on Disaster Risk Reduction highlight the role of effective social protection for disaster risk management of household resilience and underline the increasing recognition of social protection for increasing pre-disaster resilience (UNISDR 2011b, particularly Section 4.6.4; UNISDR 2009). Malawi's new Social Support policy, for example, explicitly links social protection to disaster risk reduction (UNISDR 2011b, Box 4.7). The possible linkages between these two areas and climate change adaptation have

been widely acknowledged and analysed (see, for example, Jones et al. 2010; Davies / Oswald / Mitchell 2009; Heltberg 2007; Bockel / Thoreux / Sayagh 2009; World Bank et al. 2011; World Bank 2012; Davies et al. 2009; Cipryk 2009; Stirbu 2010; IPCC 2012). In practice, however, these three areas are often *"silos"* (World Bank et al. 2011, 15ff) rather than being integrated in the form of policies, institutions or instruments.

SIFs could offer an opportunity for an integrated, cross-sectoral means of implementation, but of course there are practical challenges as the examples listed in Table 7 illustrate and, so far, insufficient attention has been paid to longer term reconstruction needs in disaster risk reduction (UNISDR 2011a, 4), and long-term risks posed by climate change (Davies et al. 2009, 3, 7–10).

Table 7: Challenges of implementing social protection measures for climate adaptation and disaster risk reduction (DRR)

Social protection measure	Benefits for adaptation and disastser risk reduction	Challenges
Weather-based crop insurance	• Rapid payouts possible • Guards against the adverse selection and moral hazard • Frees up assets for investment in adaptive capacity • Easily linked to trends and projections for climate change • Supports adaptive flexibility and risk taking	• Targeting marginal farmers • Tackling differentiated gender impacts • Affordable premiums for poor • Subsidising capital costs • Integrating climate change projections into financial risk assessment • Guarantee mechanisms for re-insurance

Table 7 (cont.): Challenges of implementing social protection measures for climate adaptation and disaster risk reduction (DRR)

Social protection measure	Benefits for adaptation and disastser risk reduction	Challenges
Seed transfer	• Boost agricultural production and household food security • Post disaster response tool • Seed varieties can be tailored to changing local environmental conditions • Cost effectiveness of seed voucher and fair projects • Fairs promote crop diversity and information sharing	• Ensuring locally appropriate seed and fertiliser varieties • Protection of crop diversity • Reduce distortion of local markets • Focus on access rather than only availability • Inclusive approach that draws in marginal farmers
Asset transfer	• Ability to target most vulnerable people • Easily integrated in livelihoods programmes	• Ensuring local appropriateness of assets • Integrating changing nature environmental stresses in asset selection
Cash transfers	• Targeting of most vulnerable to climate shocks • Smoothing consumption allowing adaptive risk-taking and investment • Flexibility enhanced to cope with climate shocks	• Ensuring adequate size and predictability of transfers • Long term focus to reduce risk over extended timeframes • Demonstrating economic case for cash transfers related to climate shocks • Use of socio-ecological vulnerability indices for targeting

Source: Davies et al. 2009, 25

Beyond disaster risk management and social protection, other issue areas can be relevant for adaptation processes as well, like supporting informal and/or local institutions. The extent to which SIF-supported activities and capacities link to adaptation processes needs to be analysed further in a respective country context. The important prerequisite for an integrated approach in the form of policies, institutions, and instruments is an integrated perspective and analysis of these topics.

4. **Risk management as an analytical entry point**: The perspective of risk and risk management has played an important role in past SIF interventions and offers a good conceptual entry point for an integrated approach, as it is a central element in all three areas: climate change adaptation, social protection, and disaster risk management.

   An updated review or analysis of the role of risk management in current SIF operations is lacking. As it is important to tailor SIFs to country contexts, such an analysis can also be directly conducted at the country level. At least three questions should be answered in such an analysis: i) Are there SIFs in the country? ii) To what extent do they have a role in risk management? iii) To what extent are the risks addressed by SIFs relevant for adaptation to climate change?

So far, SIFs seem to provide much potential for adaptation finance, at the strategic level in an institutional arrangement, as a facility for channelling adaptation funds, or as a learning experience for institutional design. To what extent SIFs have demonstrated the necessary operational quality in practice in the past will be looked at in the following section.

4 Social investment funds: operational characteristics, strengths and weaknesses

In an evaluation by the World Bank's Operations Evaluation Department (World Bank 2005)[23], the operational track record of SIFs looks promising. The World Bank's social fund portfolio in Africa has a 96 percent 'satisfactory' rating and is therewith one of the best performing portfolios in Africa (De Silva / Sum 2008, 17). However, the reforms undertaken between SIF generations also indicate that there were weaknesses and reform needs.

23 Renamed Independent Evaluation Group (IEG) in 2005.

For an assessment of the strength and weaknesses of the SIF model and its potential role in adaptation finance, it is important to understand and look at the 'design logic' and operational characteristics in more detail. With regard to the question of how best to design the institutional structure at the national level, we particularly look at criticism related to the institutional arrangement and experience with the delivery of resources to poor communities or to the local level.

4.1 Common operational structure and core features

As highlighted by the definition in Section 3, SIFs channel funds to small-scale projects, based on demand generated in a participatory manner by local groups or governments. The SIF model is seen as a pioneer in working with and subcontracting work to local actors through innovations in project management and organisational procedures which has *"led to the effective and speedy implementation of numerous small, localized subprojects"* (Bhatia 2005, viii, 1, 3; World Bank 2002). An overarching goal of SIF investment is that these should benefit the poor (World Bank 2002, 12; see Sub-section 4.1.5).

Small-scale investments in social infrastructure, including a demand-driven approach and stakeholder participation in these investments, are seen as key features of SIF models, along with a certain degree of institutional autonomy that allowed innovations in project management and organisational procedures. From a public-sector perspective, a key feature of SIFs is *"the existence of a separate, flexible, grant-making facility for local projects"* (Serrano-Berthet 2007, 1; compare also Abbot / Covey 1996, 3–4). The next section gives a brief overview of the general institutional structure and procedures of channelling funds. Some of the related core features are further detailed in the Sub-sections 4.1.1 to 4.1.5.

4.1.1 Legal status, institutional structure and procedures

SIFs are usually government-owned entities with a high degree of managerial and operational autonomy, supervised by a board or steering committee of key stakeholders while delegating responsibility in project implementation to subcontractors.

The fact that international development banks and other ODA partners have provided the bulk of finance for the start-up and continuity of most SIFs has contributed to the view that these funds are basically ODA projects. However, most SIFs are part of the overall public sector (Bhatia 2005, vii) owned by governments and are used as vehicles to implement national policies beyond the end of initial ODA support. A major review of World Bank operations comes to the conclusion that governments have managed to sustain SIFs as the vast majority still operate after bank operations have been terminated (De Silva / Sum 2008, 19). There are SIFs that are financially completely owned by national governments (Bhatia 2005, 6).[24]

Institutional autonomy

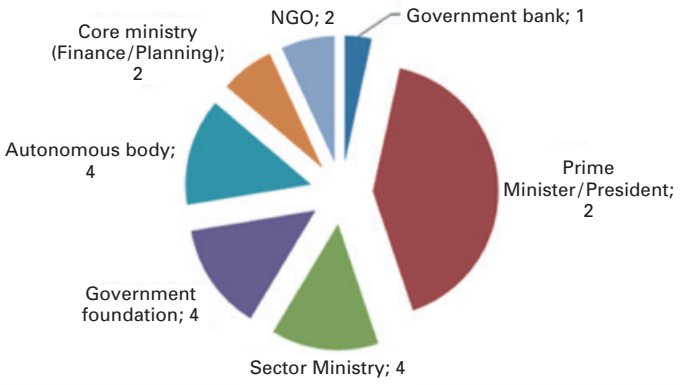
SIFs are usually managed by an autonomous or semi-autonomous agency, located within the government, but set up parallel to government structures (Abbot / Covey 1996, 4; UN Habitat 2009, 3; Crosbie 2009, 11; Bhatia 2005, 104–105). SIFs can be under ministerial units or programmes (UN Habitat 2009, 3; Bhatia 2005, 104), government banks or foundations, but they can also be set up as a non-profit company (Bhatia 2005, 18, 104), or they can be legally owned by non-profit foundations (De Silva / Sum 2008, 5) or NGOs (Bhatia 2005, 105). In a review of 15 World Bank SIFs, most SIFs were an independent agency under the president and prime minister and even more were accountable to them (Bhatia 2005, 105).

The autonomy of SIFs can comprise legal, managerial and operational, policy or financial autonomy and varies *"according to the political and administrative profile of a country"* (Bhatia 2005, 17). Autonomy is achieved by setting up the fund as a separate legal entity, often established by an executive decree or public law (De Silva / Sum 2008, 2; Bhatia 2005, 17–18), or by *"partial exemption from existing public sector laws and regulations, such as civil service salaries and procurement and disbursement regulations"* (Bhatia 2005, vii).

The degree of autonomy varies greatly from fund to fund (World Bank 2002, 2). In an evaluation of SIFs in the European and Central Asia Region, Serrano-Berthet (2007, 5) concludes that *"there is more autonomy in operational*

24 However *"[n]ational governments rarely support more than 20 percent of the Funds [sic.] finances, therefore leaving the fund's semi-permanent status to rely on the financial whims of donors"* (UN Habitat 2009, 19).

Figure 4: Examples of institutional agency of 29 SIFs



Source: Adapted from Bhatia 2005, 105

and managerial procedures than in budgetary and accountability issues". While many SIFs usually have a good degree of managerial and operational autonomy, they have less policy autonomy. Their policies are predetermined and overseen by either the government (mostly a ministry), or by a board of directors or steering committee (Bhatia 2005, vii, 18; Serrano-Berthet 2007, viii). Often, government officials hold a significant share of seats in the board or committee; however, these can also include NGOs, private sector representatives and, in some cases, donor agencies (Bhatia 2005, vii, 105). The board can also include sub-national government levels especially in the 3rd generation-type of SIFs.

Board participation of line ministries is one possibility used to support alignment with national policies and standards, such as master plans for irrigation or construction standards for classrooms, as well as overall development strategies.

Fund management and stakeholder engagement in the project cycle

While SIF policies and strategies are predetermined and supervised by a ministry, board, or steering committee, a chief executive officer (CEO) has responsibility for day-to-day operations. This officer is elected or appointed by the supervising entity or even higher levels of government (president or

even parliament) as some SIF CEOs have come to manage portfolios bigger than single line ministries. The degree of powers conferred on SIF CEOs is a measure for SIF autonomy itself. It may include the approval of individual projects, usually up to a certain amount, without prior vetting by the board.

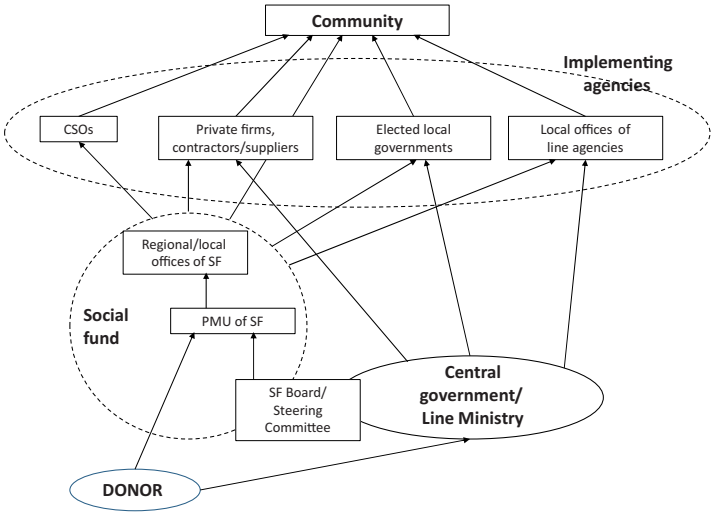
In some SIFs, funds are collected, disbursed, managed, and monitored by a central fund's in-house project management unit (PMU) (UN Habitat 2009, 19). The PMU acts as a kind of 'mini-bank', or 'holding agency of funds' and distributes these to sub-contractors such as NGOs or micro-credit-groups (Crosbie 2009, 8) or local governments. Many SIFs also have regional offices or officers. In well consolidated SIFs, however, donor funds are not handled by a specifically 'shielded' PMU, but rather by the already established structure of the respective fund, according to commonly agreed-upon procedures and guidelines (see e.g. FISE 2001 and FPS 2011). This increased use of country systems has, for example, become a standard practice in programmes carried out by SIFs in Nicaragua, Peru and Bolivia by the German Development Bank KfW.

Operational manuals

One defining feature of SIFs' management *"is their use of operational manuals for day-to-day functioning"* (Bhatia 2005, vii). Operational manuals are *"legitimized by the credit agreement between the host country and the donor"* (Bhatia 2005, 19) and describe how projects are to be carried out from identification to delivery. Operational manuals describe the guiding principles and modes of operation, including requirements on participatory approaches in project identification and selection, technical and economic minimum standards for different kind of projects to assure quality, and transparent outsourcing and contracting (as an example see e.g. FPS 2011 or FISE 2001).[25]

25 See also Weissman 2001 for an in-depth discussion of the importance and characteristics of operation manuals in SIFs.

Figure 5: Example of an institutional SIF structure



Notes:

SF: Social fund

PMU: Project management unit

Source: Adapted from Bhatia 2005, 95

Figure 5 gives an overview of a very simplified institutional structure of SIFs and the stakeholders involved. *"For simplicity neither all the institutions nor all the links are depicted. For example, regional governments are not shown, and in many cases the community receives the money directly from the social fund and therefore the community becomes both the implementing agency and the beneficiary. The elected local governments and the local offices of line agencies would be under the administrative control of the local governments and thus not shown separately. The political and administrative arm of a truly decentralized body would be the same"* (Bhatia 2005, 94).

Demand-driven project selection

Investment decisions by SIFs are driven by supply and demand (World Bank 2002, 17). A common feature of SIFs is their bottom-up, demand-driven approach in the selection and design of projects (UN Habitat 2009, 5; Abbot / Covey 1996, 4; Vermehren / Serrano-Berthet 2005, 110; De Silva / Sum

2008, 2). Instead of fund managers pre-designing projects, community or local government representatives can hand in project proposals (Abbot / Covey 1996, 3; Crosbie 2009, 11). In third generation funds, SIFs induce local governments to apply demand-driven approaches in their own planning process with local communities.

Supply-driven project selection

However, the range of choice is usually limited by supply factors. SIFs have more technical expertise in some sectors than others, often have a limited menu of project options, and use eligibility and appraisal criteria, and targeting mechanisms (World Bank 2002, 17; on targeting mechanisms see Sub-section 4.1.5).

The **menu of project options** defines a range of permissible projects (compare also Abbot / Covey 1996, 3; Crosbie 2009, 11), often limit the variety of projects that can be financed and provide standard blueprints for the type of projects mostly demanded. Communities or local governments choose from the menu according to their local priorities or local development (public investment) programmes. Usually, they are also given a certain degree of choice with regard to context-specific design features of the project. However, the design of the project menu depends on project design and goals. The menu can be an 'open menu of eligible investments' or restrict the scope of activities to infrastructure (compare project design options in Carvalho et al. 2004, 20). The social fund in Nicaragua, for example,

> *found that without giving communities a menu of social infrastructure, communities were able to articulate more freely their preferences and mention other things that were not part of the central government's policy for poverty alleviation* (Carvalho / Gillian / White 2004, 19; compare also Sub-section 4.1.4 on further aspects).

The menu of permissible projects is commonly part of the central agency's allocation scheme which is embedded in a national poverty reduction strategy and top-down targeting strategy (compare UN Habitat 2009, 19).

The central agency allocates funds based on the fund's objectives and pre-specified **eligibility criteria**, which can include the level of community participation and prevalence of poverty within the community (Bhattamishra / Barrett 2008, 50). At times, SIFs used full-fledged cost-benefit analysis to assess the quality of projects proposed for funding. Proposals put forward by local governments to the national SIF FONCODES in Peru, for example,

have to follow the elaborate procedures of *ex-ante* evaluation prescribed by the national system of public investment, overseen by the Ministry of Finance.

Project implementation

After project selection, the project is either implemented by the community itself or by selected contractors (UN Habitat 2009, 5). As SIF project cycles have a defined beginning and end, the engagement of the sub-contractor *"is only required to serve the purpose of delivering the project and no further"* (UN Habitat 2009, 24).

4.1.2 Outsourcing of work and co-financing

SIFs delegate the execution of considerable parts of the project cycle to the private sector, communities and/or local governments.

Depending on the SIF, local actors can take over responsibilities in the management of funds and projects, as outlined in Table 2 on the role of local governments in planning, financing, and implementing projects. One example area where SIFs delegate responsibility to communities or community groups is procurement (or contracting). SIFs usually have a private-sector approach in commissioning procurement opportunities to sub-contractors (UN Habitat 2009, 3) like communities. Among the SIFs analysed by Bhatia (2005, 27) *"[m]ost social funds allow community-based contracting for projects below a certain predetermined limit"*. SIFs pioneered such community-based contracting procedures, which allow an effective and speedy implementation of numerous, small, localised subprojects. *"[D]irect financing of communities basically promotes the delegation of contracting functions for small investments directly to community groups. This not only promotes transparency, it also results in significant cost savings over traditional, centralized procurement systems"* (Bhatia 2005, 27).

"Providing funding to local-level institutions, such as community-based groups, NGOs and local governments in a more flexible, transparent and rapid manner" was one central and common goal of SIFs (Abbot / Covey

1996, 4).[26] In the mid-1990s, the World Bank estimated that between 15 and 20% of social funds flowed through NGOs (Malena 1996, 17, quoted in Abbot / Covey 1996, 4).

The benefits of this division of labour and specialisation in terms of cost-effectiveness and speed of small-scale public investment made SIFs delegate a number of specialised tasks to specialised third parties, while keeping the overall control of the full project cycle. Outsourcing the financially most important part of the project cycle, like construction works in project execution, became part of the success story and the rule with SIFs, as ministries of education and other non-specialised public entities turned out not to be especially good in constructing buildings, for example. Furthermore, conflicts of interest between different parts of the project cycle – such as construction and supervision – were predetermined if fulfilled by the same actor. Much of public investment done this way was slow and expensive. Some SIFs went further and outsourced other parts of the project cycle such as project supervision to independent engineers. Scope, rules and procedures of outsourcing – usually by some form of competitive bidding – became part of the management approach described in operation manuals.

A recent ex-post evaluation of the social fund FISE (*Fondo de Inversión Social de Emergencia*) in Nicaragua by the German Development Bank KfW concluded that *"the introduction of so-called municipality-based projects ("Proeyectos Guiados por la Comunidad"/PGC) [...] was especially important"* (KfW 2013, 5) for strengthening human capital and for the overall impact of small-scale projects at the local level. The involvement of the population has meanwhile become standard practice and is compulsory by law (KfW 2013, 5).

As SIFs evolved into 2nd and 3rd generation funds, the number of stakeholders involved in the different parts of the project cycle became bigger, and the division of labour more complex. Line ministries, for example, got more closely involved in revising project proposals for their sector sustainability, such as the availability of teachers to run a school to be built with SIF funding, or the environmental impact of a road to be constructed. The increasing incorporation of 'soft' components in SIF standard projects, such as community

26 See Carvalho / Gillian / White (2004, Box 4) for an example from Zambia that describes the transition from a second generation fund directly involving communities only to a third generation fund also involving local government actors.

organisation and training in rural water supply, further added to the complexity of the project cycle and often demanded the incorporation of new partners and outsourcing modalities, such as contracting NGOs for 'soft' components of projects. Among the alternative and additional modalities of outsourcing tested, community execution to replace or complement outsourcing to private-sector companies received special attention in various countries.

Co-financing

As already indicated above, SIFs usually require a certain percentage of co-financing of the total project costs by communities and local governments. Contributions from communities are frequently made in kind comprising unskilled labour and locally available construction materials. Local governments participate with cash contributions from their fiscal revenues such as local taxes and block transfers from national government. In both cases, the contribution is not to exceed what beneficiaries can afford, but should go beyond a symbolic token to enhance ownership by beneficiaries.

Depending on the circumstances, the proportion of participation of the beneficiary or counterpart in total project costs is frequently in the range of 5 to 15 % for communities and 25 % or more in the case of local governments (Schulz-Heiss 2011). The rate of co-financing can vary and can be part of a targeting strategy in resource allocation (compare Sub-section 4.1.5). Details of terms and conditions for accessing funds are usually spelled out in SIF operational manuals, in order to ensure equal and transparent treatment for all SIF clients.[27] A World Bank evaluation from 2002 showed that one in four social fund projects (14 of 52) required no community contribution and in those projects where it was required was not always made (World Bank 2002, 18).

27 Mainly in the past, SIF funds have also been distributed in the form of loans instead of grants. Many 2nd generation SIFs have, at some point, dealt with poor, private-sector groups of civil society, such as farmer associations, on a loan rather than grant basis when financing 'productive' investments supposed to have an economic as well as financial return, such as the purchase of improved seed or irrigation facilities. Others SIFs have dedicated whole programmes to the set-up of microfinance schemes to benefit such groups and individuals (Gross / De Silva 2002). The microfinance sector has undergone a dramatic development since, and private-sector institutions and banks, rather than SIFs, now finance these programmes. 3rd generation SIFs in some countries, on the other hand, have served as banks to subnational governments. This specialised role, however, is nowadays assigned to specialised financial institutions, mostly state-owned banks, rather than SIFs.

From an economic and theoretical perspective, co-financing and the selection of projects on the basis of demand through community participation ensures high net benefits of SIF investments (World Bank 2002, 17).[28] In Yemen, for example, this has led to substantial cost savings in school construction (Bhatia 2005, 68, Box 4.4). In general, practical examples have shown that, through the collaboration between government agencies, community stakeholders and the private sector, SIFs have been able to mobilise community resources and stimulate private contracting capacity (World Bank 2002, xvii).

4.1.3 Scope and type of product

SIFs usually finance large volumes of small-scale projects in a variety of different sectors.

Cross-sectoral scope

The SIF model is not tied to a special sector or issue of government policies but has shown itself to be a suitable vehicle for a wide range of public policies. Since the beginning, SIFs have operated in a variety of sectors beyond the realm of a single line ministry (De Silva / Sum 2008, 2). While the success of the SIF model has spurred a 'product diversification' into single-sector or single-issue funds in some countries, mainstream SIFs maintain their character of multi-sector funds. While SIFs were initially often founded for a specific purpose, most social funds gradually address several objectives (e.g. delivery of basic services, capacity-building of local institutions, etc.; see De Silva / Sum 2008, 25; Weissmann 2001; World Bank 2002, 2).

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28 See also Batthamishra / Barrett 2008, 61: *"Relative to market-based arrangements, community-based arrangements have important informational advantages. Since rural communities typically have intimate knowledge regarding the circumstances and needs of member households, they are better able to identify the most needy and vulnerable among them, thereby improving targeting outcomes. In addition, due to their close physical proximity and frequent, repeated interactions between them, they can use relatively low-cost methods of contract enforcement, such as peer monitoring and the threat of social sanctions. These advantages enable the viable delivery of financial services, such as microinsurance, microcredit and microsavings, at prices that are accessible to poor households, which is often not the case for a typical commercial provider."*

Typical activities financed by SIFs were construction or rehabilitation of schools, piped water supply systems and health facilities and roads (World Bank 2002, 1; Carvalho / Gillian / White 2004, 18). As the sample of SIFs in Table 8 shows, several activities financed by SIFs like irrigation works, erosion or flood control could potentially be of importance for adaptation to climate change. The sample also illustrates that the SIF model was used for financing local activities that reduced green-house gases, e.g. by financing electrification through renewable energies or energy saving technologies.

Table 8: SIF investment by type of activity

Activity	Projects (%)	Activity	Projects (%)
School construction/ rehabilitation	94	Culverts	38
Construction and/or rehabilitation of piped water supply systems	91	Footpaths	38
Construction/rehabilitation of health facilities	85	Provision of teaching supplies and/or educational furniture	53
Road construction/ rehabilitation	83	Markets	34
Bridge construction/ rehabilitation	60	Erosion control	32
Drainage works	57	Forestry	30
Construction and/or rehabilitation of wells, handpumps	55	Flood control	28
Irrigation works	53	Microcredit	25
Training, capacity building, technical assistance	53	Housing/ dwellings for children, elderly	23
Solid waste disposal, sanitation works	45	Agroprocessing	21

Table 8 (cont.): SIF investment by type of activity			
Activity	**Projects (%)**	**Activity**	**Projects (%)**
Latrine construction/ rehabilitation	43	Infrastructure for street children, homeless	19
Provision of medicines/ equipment	42	Electrification	15
Sports complexes, community centers, day care centers	40		
Notes: N =53; several activities per fund possible. Source: World Bank 2002, 67			

Type of product

Products developed by SIFs have been diversified over time, in response to the new and changing needs of public policies. SIFs have run free-standing training programmes for capacity building, have set up microfinance schemes for small private enterprises and have piloted innovative forms of welfare systems, including 'conditional cash transfers' which have turned into recurrent government programmes in many countries (De la Brière / Rawlings 2006).

The main output and core business of SIFs, however, are projects. The only type of SIF output which has come to rival 'projects' to some degree at the beginning of this century has been microfinance schemes, which accounted for a third of physical outputs in a review of World Bank operations with SIFs between FY 2002 and 2006 (De Silva / Sum 2008, 23). Development thinking and practice, however, has turned to other, more specialised institutional arrangements to deliver microfinance.

Volume of projects

Although governments have at times turned to SIFs for the management of large-size public investments (e.g. beyond the million-dollar barrier), SIFs have mainly financed small-scale projects (Crosbie 2009, 11), typically in

the range of USD 10,000 to 100,000. Micro-projects of a few or less than USD 1,000 are usually unattractive for SIFs. Here, grass-roots based NGOs and local governments are better positioned for project implementation (Schulz-Heiss 2011).

The number of projects SIFs can finance annually is high. Between the Fiscal Years 2002 and 2006, for example, the World Bank supported 20 SIFs delivering over 90,000 projects (De Silva / Sum 2008, 23), which on average equals 900 projects annually per SIF (for the quantity, access, and utilisation of physical infrastructure supported by SIFs, see also World Bank 2002, 11, Box 2.1.) .

4.1.4 Specialisation, standardisation, bundling of projects

Specialised institutional skills, standardisation and bundling of projects into programmes have helped SIFs reduce transaction costs and mainstream national policies and quality standards.

SIFs around the world have specialised in particular skills and targets required in delivering public investments. As projects in each sector require at least some amount of sector-specific expertise, the menu of projects available through SIFs has usually been limited to those most demanded, allowing them to maintain the comparative advantages of specialisation and a lean institution.

Through the standardisation and bundling of small projects into packages, SIFs can achieve a high volume of operations and relatively reduce transaction costs. Standardisation of operations is achieved by operation manuals, as well as the design and cost blueprints that describe the way projects are to be carried out from identification to delivery. For example, once a similar kind of school room has to be constructed in dozens or hundreds of places, project preparation and supervision activities can be bundled into packets that reduce staff time and travel costs. The same construction design can be used many times with little adaptation, spreading its fixed costs between large numbers of projects. A standardisation of proven procedures for project identification and follow-up can dramatically cut down the cost of trial and error involved in one-of-a-kind projects, and even reduce the time and cost of staff training needed per project.

Box 6: Alignment with national policies through standardisation: hexagonal classrooms in Bolivia

An example of how SIFs standards have been used as a 'transmission belt' between national and local investment decisions is the national educational reform programme of Bolivia in the late 1990s. The national Ministry of Education had come to consider hexagonal classrooms the most appropriate environment for teachers and students to implement the pedagogical reform curricula. But local mayors did not like the design for the increased complexity and cost of construction and maintenance, and kept on building pre-reform, rectangular-shaped classrooms. At that time, local governments were in charge of the provision of schooling infrastructure and had fiscal autonomy.

Hexagonal classrooms finally started to appear all over the country once the national government provided additional funding for local school construction through the Social Investment Fund FIS (Fondo de Inversión Social, later renamed FPS Fondo Nacional de Inversión Productiva y Social), which had adopted the requirements of the Ministry of Education as a project standard. As the design became more familiar and appreciated, mayors started to adopt the reform classroom even if their projects were financed from non-SIF resources (Schulz-Heiss 2011).

Standardisation is also used as a tool for policy coherence between different governance scales and to mainstream national policies, quality standards and norms in decentralised projects.

Project standards can be applied to the mainstream sector as well as cross-cutting concerns like the consideration of gender aspects in project identification and implementation (Kuehnast 2003) or mainstreaming participatory approaches in local investment decisions as is the case in 3rd generation SIFs in Africa today assisted by German financial cooperation (interview KfW/Governance Policy Division, Frankfurt, 10 Aug. 2010). SIF standards can also become national benchmarks for local investments, for example by establishing maximum unit costs for construction (compare Bhatia 2005, 27; as an example see FISE 2001).

Not all small-scale, local projects are suitable for standardisation and mass production, and the pros and cons in designing project menus needs to be considered carefully:

> *The more open the menu of possible investments, the greater the room for choice at the community level, and the more likely that the social fund is financing investments that are the top priority for the community. However, an open menu reduces the potential for efficiency through standardization and specialization, and makes it more difficult for the social fund agency to meet all the sector-specific technical and institutional requirements for sustainability* (Carvalho / Gillian / White 2004, 23).

4.1.5 Poverty targeting mechanisms

Poverty targeting plays a central role in fund disbursement because an overarching self-defined goal of SIFs is to the benefit of the poor. 'The poor' are usually the main target group of SIF investments:

> *The poor, poorer, poorest, or poverty are mentioned in the objectives of more than three quarters of social fund projects. Furthermore, the poor, or some category of poor people, are an explicit target group in the majority of cases ('poor' in 80 percent of projects, 'poorest' in 46 percent of projects, 'vulnerable' in 44 percent of projects, and 'low-income" in 10 percent of projects). [...] Other target groups are 'unemployed' (in 20 percent of projects), 'indigenous' (in 10 percent of projects), and 'women' (in 61 percent of projects)* (World Bank 2002, 12).

Targeting takes place through a number of approaches and mechanisms, including the design of menus and targeting criteria as well as the design of rules and procedures of community participation regarding the identification of project priorities, the formation of project committees or implementation (Jorgensen / Van Domelen 1999, 7; Van Domelen 2007, vi).[29]

Four basic approaches are being used by SIFs: implicit and explicit targeting mechanisms and proactive and reactive approaches (World Bank 2002, 15; Carvalho / Gillian / White 2004, 21). Through the design of the project menus and the definition of activities being financed, SIFs can implicitly

29 For an overview of elements of a social fund targeting mechanism, see Van Domelen 2007, iv. The toolkit aims to provide *"concepts, empirical evidence, noteworthy case studies of different approaches and the operational elements necessary to develop more comprehensive poverty and vulnerability targeting mechanisms*" (Van Domelen 2007, i).

favour activities of interest to the poor and/or of a public nature. Explicit targeting techniques include poverty maps or allocation formula, often based on data on the geographic distribution of poverty combined with population data. Usually they are geared to the district level for reasons of data availability (see World Bank 2002, 84). The kind of data being used usually depends on the fund's purpose where indicators in an education project (should) differ from health projects for example.

*"*Proactive targeting *allocates funds in a pro-poor manner either by excluding the better-off (a cut-off) or using a progressive allocation rule"* (World Bank 2002, 15) For example, the Zambian Social Investment Fund (ZAMSIF) has a formula for district allocations that *"gives much more weight to the poorest districts than to those that are less poor: the poorest of all receive $30 a head and the least poor only $1.30"* (Carvalho / Gillian / White 2004, 21).

Reactive targeting instead waits for requests from communities and favours those from poor districts by applying eligibility criteria like poverty data, *"and/or by reducing the required level of community contribution"* (World Bank 2002, 15, 168), or the rate of co-financing.

Prioritisation through the rate of co-financing can serve two purposes, or a balanced blend of both. 'Discounts' in beneficiaries' contribution may be introduced to reflect differences in the 'ability to pay' of communities, similar to price reductions for the unemployed, students or the elderly. In SIF programmes, they are typically based on local poverty indicators available and published country-wide, in order to make the intended pro-poor bias transparent and non-discretional.

Differences in the rate of co-financing have been also introduced to reflect priorities of national policies. For example, the required co-financing by local governments may be higher for the extension of electricity grids than for the provision of drinking water, thereby reflecting national priorities for sanitation in a given country at a given moment. Local governments are expected to react to this market-like signal.

4.2 Strengths and weaknesses of the operational model

4.2.1 Strengths

The above analysis has shown that the SIF model can be adapted to a wide range of policy goals and that products have been diversified over time in response to new and changing needs of public policies. SIFs have *"been successful in channeling substantial external resources toward local development, disbursing rapidly and achieving their physical output targets"* (World Bank 2002, 48). Accordingly, SIFs have been valued for their *"organizational effectiveness and innovation in project management"* (Bhatia 2005, 3 based on World Bank 2002), cost-effective outputs (Bhatia 2005, 69),[30] as a *"quick and efficient investment mechanism that allows communities to take the lead"* (Bhatia 2005, 1), or as an efficient institutional model that promotes concrete results at the local level (De Silva / Sum 2008, 25).

The key operational characteristics that particularly contribute to effectiveness and efficiency are the degree of autonomy required to achieve project objectives, community-involvement in decision-making, institutional specialisation, standardisation of procedures, and the bundling of projects as well as outsourcing or sub-contracting parts of the project cycle to local government and non-government actors. SIFs have fostered partnerships between government agencies, the private sector, NGOs and community-based organisations and have been able to mobilise capacity and community resources and *"in some cases have strengthened the private sector capacity"*, e.g. capacities in contracting (World Bank 2002, xxix).

SIFs have many operational features and procedures that contribute to transparency in fund management. Bhatia even puts forward as a key hypothesis of the review *"that social funds are cost-effective primarily because they reduce corruption"*, however, has to admit that there is *"insufficient evidence to come to a definite conclusion"* (Bhatia 2005, x). Nevertheless, the author emphasised the *"high degree of transparency in social fund operations"* (Bhatia 2005, 66). Means that promote transparency include computerised management information systems, widely distributed operation manuals,

30 *"Social funds do not always have lower unit costs than other kind of agencies, but there is notable variation across countries and sectors"* (Bhatia 2005, 1 based on Rawlings / Sherburne-Benz / Van Domelen 2004).

sustained information education and communication campaigns, simple and transparent procurement practices, including databases on unit costs, and, last but not least, frequent audits (Bhatia 2005, viii, x, 27, 69).

In a survey of 29 funds, the majority of funds were audited by national auditors supplemented by international firms. Most SIFs are included in the government budget and are covered in the auditor general's report to parliament. Again, the majority of funds *"had an accounting officer responsible for answering to parliament on the proper use of funds"* and *"there was a high likelihood of scrutiny by the Public Accounts Committee"* (Bhatia 2005, 37, 107).[31]

The strength of SIFs is their specialisation on the delivery *"of small-scale infrastructure […] where the community-level requirements for technical, institutional, and financial sustainability are usually less complex"* (World Bank 2002, 49). Accordingly, channelling funds through SIFs should be considered *"when deficiencies in small-scale infrastructure are a significant constraint in development"* (Carvalho / Gillian / White 2004, 13). Some case studies conclude that the *"quality of social infrastructure and level of service is better in areas served by social funds than in ones served by other agencies"* (Bhatia 2005, 1, based on Rawlings / Sherburne-Benz / Van Domelen 2004).

Critics maintain that *"SIFs appeared more interested in bricks and cement than in development outcomes"* (Vermehren / Serrano-Berthet 2005, 96). As the shift to the third generation model shows, SIFs can also finance longer-term development goals, however this requires

> *significant changes in the social fund agency's performance incentives, staffing, and skills mix. […]. For example, building capacity and social capital at the community level are time- and human resource-intensive processes, making disbursements potentially slower and less predictable* (World Bank 2002, 48).

Evidence on outcomes and welfare impacts (e.g. school enrolment, incidence of diarrhoea, infant mortality) shows that communities supported

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31 However, *"the World Bank and donors often establish parallel auditing systems for their projects that undermine developing countries supreme audit institutions, on whose work they cannot always rely. That demonstrates that this issue is not specific to social funds, but that it is part of the wider impact that donor funding has on recipient countries"* (Bhatia 2005, 37).

by SIFs do not necessarily perform better than non-SIF communities. One reason given for a limited impact on key development indicators is that SIFs face challenges in ensuring complementary inputs for the operation and maintenance of a project investment (see also below; World Bank 2002, xvii; compare also Carvalho / Gillian / White 2004, 7).

While the impacts on development and effects for the poor are not always clear, there is sufficient evidence that allows for the conclusion that SIFs were able to implement a pro-poor funding approach. Funds reach the poor and poorest people both at the geographic and household levels (Van Domelen 2007, 22; World Bank 2002, 12ff; Bhatia 2005, 1 based on Rawlings / Sherburne-Benz / Van Domelen 2004; Schady 1999)[32], however, there is little systematic data on targeting outcomes at the household level[33], particularly for decentralised allocation schemes (see Faust 2012).[34] A World Bank evaluation from 2002 concludes:

> *At the geographic level, poorer areas received more social fund resources per capita than better-off areas. This result attests to the strong demand for support expressed from poor areas, as well as improved outreach and targeting efforts by the social funds. At the household level, the majority of beneficiaries were poor, and the poorest of the poor showed reasonable access to benefits – the poorest ten percent of the people represented between 8 and 15 percent of social fund beneficiaries, depending on the country studied. As community infrastructure cannot exclude any community member from access, better-off households also benefited [in a range of 29 to 45 percent of social fund investment]. In all cases analyzed, social funds were at least as well targeted and usually better targeted than other social programs, and typically much better targeted than general public social and municipal spending* (World Bank 2002, 153).

Particularly Peru has succeeded in allocating *"a significant share of its resources to the poorest districts with continual fine-tuning of the targeting mechanism and a focus on rural areas that led to improved performance over time"* (World Bank 2002, 13). In 2007 Van Domelen concludes that

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32 The study by Schady (1999) *"shows that FONCODES funds flowed disproportionately to poor provinces"* (Bhatia 2005, 65).

33 See Van Domelen 2007, ii; and World Bank 2002, 12–13. The analyses refer to the same data set in 6 countries: Armenia, Bolivia, Honduras, Nicaragua, Peru, and Zambia published in Rawlings / Sherburne-Benz / Van Domelen 2004.

34 Faust (2012) looks at the allocation patterns of Bolivia's decentralised FPS and related diffusion and neighbourhood effects.

> *common to all country findings, the poorest districts provinces received at least their population share based on poverty ranking. This refutes the assertion that within demand driven programs the poorest districts lack the capacity to participate* (van Domelen 2007, ii).

At the general district level, however, *"allocations are still best described as mildly progressive"* (World Bank 2002, 13).[35]

Evidence shows that community-level investments reflect expressed local priorities (Bhatia 2005, 1 based on Rawlings / Sherburne-Benz / Van Domelen 2004; World Bank 2002, 17) and the levels of household satisfaction with the chosen project (Van Domelen 2007, ii). Whether the top-ranking priority was chosen is difficult to determine as results vary. Project choice can be influenced by elite capture or the strategic behaviour of the community in choosing a lower priority if deemed more likely to be approved (Van Domelen 2007, ii–iii).

Finally, the experience has shown that SIFs are strong in contexts of ineffective institutions. As SIFs are usually set-up as autonomous or semi-autonomous agencies parallel to a government, they "*have a clear and significant role when existing institutions are ineffective and the need for flexibility and speed is paramount"* (Carvalho / Gillian / White 2004, 13), for example, after natural disasters, in post-conflict situations or in fragile contexts. In this context, the SIF model has been frequently implemented, for example, in South Asia and Africa in response to disasters or conflict combined with goals of political and social stabilisation (IEG 2011, 18). In channelling support directly to communities, SIFs are also able to support informal risk management mechanisms (De Silva / Sum 2008, 25, compare Sub-section 3.2.2).

4.2.2 Weaknesses and trade-offs

The particular operational design features of SIFs can be seen as a strength, but depending on the policy and project objectives, they also have their trade-offs and negative aspects. Some points of criticism such as corruption or political interference in investment decisions are more generic in nature (Bhatia 2005, 71) and not specific to SIFs, but might, however, have received more attention in the context of SIFs due to the large volumes that some funds managed to attract.

35 For further information on targeting outcomes and performance of SIFs, see also World Bank 2002, 12–13, 89ff, and 153.

Some points of criticism also relate to trends in development thinking and reflect trade-offs inherent in policy targets. For example, reaching the most vulnerable communities directly, claimed to be a 'success' by 2nd generation funds, may cause collateral damage to local governments that get by-passed on the way. *Vice versa*, 3rd generation funds exclusively focussing on (local) governments may suffer 'leakages' when trying to reach the communities most in need.

Among the particular design features and objectives of SIFs, there are two areas that repeatedly elicited criticism and debates: One area centres on limitations in reaching the poorest and the challenges involved in working with local communities. The other, more substantial area, centres on the institutional feature of autonomy and the wider implications and impacts on national institutions and public financial management.

Limits in reaching the poorest and working with the community

While the demand-driven approach in project selection and the role of the community-based arrangement is generally acknowledged, there are also voices of caution highlighting the limits in reaching the poorest and working with the community:

- **Limits in reaching the poorest**: *"Eliciting local demand can allow local participation in subproject decision making and management, but it may make it difficult to reach the poorest communities which are often least competitive in preparing and presenting proposals"* (Carvalho / Gillian / White 2004, 5; IDB 1998, 5). The poorest groups tend to be poorly organised and least equipped to solicit benefits from demand-based programmes (Subbarao et al. 1997, 137). *"Often communities compete at the municipal level for financial support; one of the lessons from this approach is that the priorities expressed by a community are likely to reflect the needs of the majority, while the needs of more vulnerable members such as orphans, female-headed households, disabled, and elderly, may not be heard"* (Gibbons 2004, quoted in Vermehren / Serrano-Berthet 2005, 110).[36]

36 This was one of the reasons why SIFs introduced programmes with special target groups as part of a country's social safety nets (see examples in Vermehren / Serrano-Berthet 2005).

- **Dependency and influence of local leaders**: Access of the poorest to SIF funds depends on the capacities of local leaders or 'prime movers' (e.g. a local chief or headmaster; see e.g. Carvalho / Gillian / White 2004; UN Habitat 2009, 19; World Bank 2002, 17, 48). While the vast majority of beneficiaries were satisfied with the chosen subproject, the demand-driven approach is not necessarily synonymous with responding to the highest priority problem of the community (World Bank 2002, 48, 17). The community-driven mechanism allows a bias for certain sectors *"because of the important role of prime movers in […] project formulation, submission, and implementation"* (World Bank 2002, 48). While there is consistent evidence that community leadership plays a critical role, *"it is less clear whether it is for good or ill"* (Van Domelen 2007, iii); on the problem of *"capture or manipulation by local elites"*, see also Bhattamishra / Barrett 2008, 59, 62–63).
- **Limits in technical decision-making and management**: *"Although community-based arrangements may have superior local knowledge and achieve better targeting and contract enforcement outcomes, they may face limitations in technical decision-making and management"* (Bhattamishra / Barrett 2008, 61).
- **Limits in dealing with externalities or economies of scales**: *"[…], local decision-making may help to overcome information asymmetries by bringing to bear local knowledge, but does not lend itself to projects that require decisions to be made above the local level in order to deal effectively with externalities or to tap economies of scale"* (Carvalho / Gillian / White 2004, 5).
- **Crowding out**: Supporting informal risk management arrangements, SIFs need to be designed carefully to avoid i) displacing these and/or the role of related initiatives by NGOs or the private sector and ii) to avoid moral hazard by inducing risky behaviour (Carvalho / Gillian / White 2004, 9; on crowding out effects see Bhattamishra / Barrett 2008, 58).

Impacts on national institutions and public financial management

Bypassing public sector bureaucratic procedures, the SIFs' autonomy allowed funds to be channelled to communities rapidly, in a transparent manner and at low administrative costs during times of crisis. While such SIF interventions are of less concern when designed as temporary, short-

term measures, their impact on overall public sector management became a key concern in many countries when SIFs pursue longer-term policies complementing social sector policies (Subbarao 1997, 156) and when SIFs provide similar investments as existing government agencies (Vermehren / Serrano-Berthet 2005, 96).

A key question is whether SIFs help build institutional capacity or whether they displace, weaken or even undermine existing government institutions and reforms (Bhatia 2005, vii). Some analysts claim that innovations in fund operations altogether *"inspired rather than undermined"* reforms in public sector management (De Silva / Sum 2008, 4). Critics question that the innovations are transferable to permanent public-sector agencies or even provide a threat or moral hazard to improvements in public sector management at large (De Silva / Sum 2008, 4; World Bank 2002, xxvi). SIF support can, for instance, discourage local governments to improve the efficiency of their own local tax system. This can be the case if project selection criteria favour those with low amounts of tax revenues and block transfers from national government budgets. Such 'compensatory fiscal transfers' are a well-known moral hazard from past SIF experiences, for which a careful balancing of the incentive structure became a concern in SIFs of the 3rd generation. Here, measures designed to this end included the allocation of additional SIF funding as a reward for an above-average record in the operation and maintenance of public works or other indicators of good local governance.

Another major concern is the lack of integration into and coordination with government processes (Vermehren / Serrano-Berthet 2005, 96; Bhatia 2005, 4; Juntermann / Schickinger 2004). Social funds are even accused of undermining sectoral coordination (Bhatia 2005, ix). Coordination with government agencies is seen as one of the biggest challenges to avoid the negative implications for the management of public expenditure (Bhatia 2005, 38; World Bank 2002, xxvi; Tendler 2000 in Bhatia 2005). Past SIFs *"did not sufficiently follow line ministries' policies and guidelines"* Vermehren / Serrano-Berthet 2005, 96) and *"have ability to divert attention away from existing, accountable, governmental structures"* (UN Habitat 2009, 24).

If not designed well, SIFs can have adverse effects on the public sector[37] as shown by experience (Carvalho / Gillian / White 2004, 9) and a World Bank evaluation. SIFs had

> *negative institutional effects for public planning processes and budget accountability when they have been inadequately integrated in […] processes at central or local levels and when social fund disbursements have accounted for a significant share of public expenditure* (World Bank 2002, xxix).

Coordination needs are particularly apparent with regard to recurrent sectoral budgets and maintenance costs and technical standards (Bhatia 2005, 38).[38] Past SIFs were accused of not ensuring the technical and financial sustainability of investments and nobody seemed to be responsible for maintaining the infrastructure (Vermehren / Serrano-Berthet 2005, 96). As SIF projects are usually limited in time, it needs other government entities and partners to assure recurrent expenditure needs are met (UN Habitat 2009, 24; Carvalho / Gillian / White 2004). The lack of infrastructure maintenance can also be related to the lack of civic ownership and motivation as the community engagement of SIF interventions ends with the delivery of the project (UN Habitat 2009, 24).

Finally, creating a specialised fund involves the danger of duplication between funding activities while parallel structures can create *"shadow governments"* (Bhatia 2005, 17 based on Goodman et al. 1997). SIFs have been accused of being funded off-budget, thus escaping financial oversight and parliamentary control (Bhatia 2005, 20, 29). An internal survey of the institutional structure of 29 social funds by the World Bank concluded that 86 % of them were included in government budgets. However, as highlighted by Bhatia (2005, 29 and Annex 5), a detailed study on financial management arrangements and the integration of SIFs in national budgetary processes is missing.

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37 For example: negative competition effects, negative resource mobilisation and allocation effects/undermining inter-governmental fiscal frameworks; negative systematic planning and accountability.

38 *"Mechanisms to coordinate social fund activities with recurrent sectoral budgets and technical standards typically depend on (i) line ministry representation on social fund steering committees, (ii) framework agreements between social funds and line ministries that define cooperative agreements at various stages of the project cycle, and (iii) line ministry approval for subprojects"* (Bhatia 2005, 38 based on World Bank 2002).

Whether the SIF model can have a role in adaptation finance finally needs be considered in a country-context. Strength and trade-offs of the model depend on *"project objectives, the nature of services to be delivered, and the country context"* (Carvalho / Gillian / White 2004, 5). Five factors in particular should be looked at in a given context (see World Bank 2002, Box 5.1 for further details):

1. The strength of existing institutions and public sector reforms in a country;
2. The national budgeting process, structure of public expenditures, and sectoral planning;
3. The extent of political, administrative, and fiscal decentralisation;
4. The social structure and capacity of a community context (World Bank 2002, 49–50; Carvalho / Gillian / White 2004, 13); and
5. The nature of required goods and services (Carvalho / Gillian / White 2004, 13).

As outlined in Sub-section 3.4, SIFs took three principal strategic roles in institutional contexts: they were used as engines of local development, as laboratories for innovation and as promoters of social capital. Because the SIF model works particularly well in situations of dysfunctional institutions, SIFs had and can have two additional roles in two situations where institutional autonomy is an asset:

1. *"*Stop-gap*: Government structures and systems are dysfunctional and the Fund provides a temporary means of channeling resources to the local level.*
2. Compensatory*: There are exceptional problems that the regular transfer systems or sectoral programming are not well designed to address, such as natural disasters, discrimination of minorities, or deep pockets of poverty"* (Serrano-Berthet 2007, 2).

5 Potentials, limits and challenges of using social investment funds for adaptation finance

SIFs have played an important role as an agency for the delivery of public investments to the local level. For this purpose, SIFs can be and have been designed in a flexible manner according to changing national and international policy environments and development currents. SIFs have been established in all regions in more than 60 countries and have been used to channel high financial volumes for local-level development activities. It is likely that SIFs are still part of the institutional landscape in a vast number of developing countries. Between 2000 and 2007, the SIF portfolio still represented more than 60 percent of IDA lending for social protection operations, for example. The quantitative extension, the existence of the SIF model over time in many countries, combined with a thematic closeness to the needs of adaptation to climate change turn them into a potential financing model for local adaptation activities for many countries.

As the analysis on strengths and trade-offs of the SIF model has shown, its rationale and appropriateness for adaptation finance should explicitly be considered in a country context. Whether some of the SIF characteristics, such as institutional autonomy, develop into a strength or weakness depends on the role of SIFs in an institutional arrangement in a country context and on the objectives of the activities to be financed. In this regard, whether the SIF model is appropriate for adaptation finance and for which kind of adaptation activities finally needs to be determined from the perspective of a country's adaptation policy and institutional context. Balancing the related trade-offs of the SIF model, also means considering whose adaptation needs and goals within a country should be supported through the SIF model. As the analysis of SIF generations shows, the financing model can be beneficial for one target group, e.g. a local community, while at the same time having adverse effects at another scale, weakening e.g. local government administrations.

The analysis shows that SIFs and adaptation finance share common concerns which provide potential entry points for the use of SIFs in adaptation finance. In general, these common concerns comprise the goal of targeting financial support towards poor and vulnerable people in particular and implementing an integrated funding approach. In the context of these shared concerns, SIFs are generally in a good position to (help) meet current adaptation funding

requirements and challenges and can potentially take over several political and institutional functions in adaptation finance. There are, however, also adaptation-specific challenges as detailed below.

5.1 Meeting adaptation funding requirements?

The current political agendas in the field of climate change and development effectiveness led to the formulation of financing requirements which were synthesised in integrated assessment criteria and questions as outlined in Box 5 in Section 2. Looking at the operational characteristics of and experience with SIFs, as detailed in Section 4 in summary, to what extent are they in a position to meet these funding requirements?

Support the vulnerable, gender specific

While SIFs can be an institutional option for the distribution of international climate finance in many vulnerable countries, they have not been established in all, as available analysis on the geographical distribution indicates. However, to date there is no comprehensive overview on where the SIF model has been used.

At the country level, SIFs have gained substantial experience and performed well in targeting resources to poor or vulnerable districts, local governments or community groups. To consider the needs of particularly vulnerable groups within poor communities, many SIFs introduced programmes for special target groups, women playing an important role as beneficiaries of these programmes. This experience generally places the SIF model in a good position to implement a targeted funding approach, despite the limits and challenges (see Sub-section 4.2) that exist in practice in reaching the poorest and most vulnerable groups. Part of the SIF model's success builds on community participation in project selection, design, implementation and management (for stakeholder involvement, see also text on transparency below). Considerable parts of the project cycle are delegated to communities, local governments and/or the private sector (see also below on SIFs as a learning experience for institutional design). This implementation structure, specific operational characteristics of SIFs, as well as the approach to bundle funds from a multitude of sources under one operational programme and institutional roof helped to reduce transaction costs and have allowed

past SIFs to support many small-scale projects (see also the text on cost-effectiveness/efficiency below).

Cost-effectiveness and efficiency

SIFs are known for their cost-effective and efficient way of channelling resources. The SIF model is seen as a pioneer in working with and subcontracting work to local actors through innovations in project management and organisational procedures which has led to the effective and speedy implementation of numerous small-scale projects at the local level. However, effectiveness and efficiency are particularly due to the specialisation on small-scale investments in social infrastructure that have a limited technical, institutional and financial complexity that both allow standardisation and specialisation on the side of the SIF agency and are manageable for a community. Specialisation and standardisation have been important factors in reducing transaction costs. The comparative advantages in cost-effectiveness and efficiency of the SIF model are less clear in the context of the increasing complexity of a project and/or considering potential additional costs necessary to ensure complementary investments to maintain a SIF investment and welfare impacts over time.

The country-driven and integrated approach

The SIF model offers a good opportunity for an integrated approach to adaptation finance at the policy level. SIFs could especially play a role at the interface of adaptation to climate change, social protection and risk management due to the overlap in goals, concepts and approaches (compare Sub-section 3.4). From an institutional perspective, the same holds true if SIFs are considered as an isolated institution. They offer an integrated institutional approach by bundling different channels and sources of international and domestic finance and integrating them under a common institutional and operational roof. However, if seen in the wider context of public financial management, the links and degree of coordination with government institutions is less clear and can imply many trade-offs (see text on coordination below). While one asset of SIFs was to pilot and establish, for example, new procurement models, the lack of integration into public financial management systems and use of country systems has been criticised in many SIF operations. While audits, for example, were frequently undertaken by national auditors, parallel systems had also been

used (compare Sub-section 4.2). Depending on the purpose of the fund, this lack of integration can also be a calculated move and can be seen as strength, as in the case of emergency-type SIFs.

Coordination

The track-record with regard to coordination is mixed. To what extent SIFs help avoiding parallel implementation structures highly depends on the degree of autonomy granted. If seen as an isolated institution, SIFs allow for a coordinated funding approach by bundling funds from a multitude of sources (compare above). However, as SIFs often operate in parallel to other existing government entities (such as line ministries), coordination with national policies, guidelines and standards and the integration into government processes is seen as one of the main challenges (compare also related criticism in Sub-section 4.2). The degree of integration of SIF programmes into national processes of budget management, however, has not been well studied.

Context specific

The evolution of SIFs over time has shown that the model can be adapted to different socio-economic contexts. The SIF model also allows one to consider context-specific information and requirements at the project level as it is based on a demand-driven approach in project selection and allows for modifications in project design. However, it is not the best choice for very small- or very large-scale investments in terms of financial volume or in terms of particular adaptation needs, being those that are highly context dependent, not repeatable or that cannot be standardised to a certain extent.

Transparency

From a theoretical perspective, SIFs adopted many operational practices that can promote transparency in fund operations. The board or steering committee can be a tool for integrating main stakeholders in the general design of the fund's procedures, operations and political decisions. Operational practices that can promote transparency include community-based contracting, accessible operation manuals and databases on procurement costs, information campaigns, or audits. However, the degree of transparency finally depends on the quality of implementation.

5.2 Potential political and institutional functions of SIFs in adaptation finance

Experience with the application of the SIF model has shown that SIFs can be a strategic partner in adaptation finance. In a context of national institutional arrangements, SIFs can take over several functions which are potentially relevant for the implementation of adaptation policies. Beyond that, past SIF interventions can provide 'lessons learned' with respect to the design of institutional structures or they can be used directly or after modifications for distributing adaptation funds.

SIFs as a 'strategic partner' in adaptation finance

In the past, SIFs successfully took over functions in institutional arrangements and in the delivery of resources that overlap with the important requirements of (international) adaptation finance and/or play an important role in adaptation processes as such. Four basic functions can be identified from the literature (compare Sub-sections 3.4, 4.2; Vermehren / Serrano 2005; Serrano-Berthet 2007):

1. **SIFs acted as engines of local development** in (directly) supporting vulnerable regions, districts or communities. Adaptation finance should also support vulnerable groups and communities, but so far the delivery mode to local levels is often unclear and/or contested.
2. **SIFs acted as laboratories for innovation** in delivering investments to the ground, at times even inducing wider sector reforms. Innovation in the delivery of finance is also an overarching goal or need in adaptation finance. Adaptation finance currently offers a window of opportunity for innovations as the proposal of South Africa to the Adaptation Fund shows.
3. **SIFs acted as promoters of social capital** by working in a multi-sectorial way at the local level, aiming to support communities in designing and managing own project activities and processes. The support of local level activities and institutions (should) play an important role in adaptation processes or related tasks, such as disaster risk reduction and management and therefore also in adaptation finance.
4. **SIFs acted as an interim solution** in times of dysfunctional government institutions or crisis situations. As the SIF model has proven to work

particularly well in these situations due to its autonomy, this could be an interesting financing model for adaptation needs in fragile governance contexts, after climate related disasters or in cases of discrimination of minorities who, due to a lack of access to social services, are highly vulnerable to the impacts of climate change.

As shown by the analysis, the decision on the role and function of SIFs in institutional adaptation financing arrangements is important as it can influence institutional design options and perspectives on these regarding their strength and weaknesses. For example, while a high degree of institutional autonomy of a SIF can be an asset in contexts of political fragility or after disasters, it can be judged negatively from the perspective of development effectiveness.

SIFs as a learning experience for institutional design

SIFs provide specific experiences in the institutional design of delivering funds for small-scale projects at the local level. With regard to the lack of experience in devolving international adaptation funds to the local level (compare Sub-section 2.4), the SIF model is particularly interesting with regard to its experience in resource targeting, devolving fund management to the local level, and promoting collaboration between public and private stakeholders. Past SIFs provide examples and 'lessons learnt' on community participation in project selection, design, implementation and management. They have elaborated models of stakeholder engagement in disbursing funds and procuring equipment and have been able to mobilise community resources and private contracting capacity. The involvement of local actors and institutions is a prerequisite for successful adaptation processes. Also, the need for private-sector engagement in adaptation action and finance has been repeatedly stipulated by political actors. So far, however, the actual engagement, related financial potential and possible roles of the private sector in adaptation processes and finance in distinction to the public sector are unclear. Here, SIFs offer one possible model for cooperation and engagement.

As a facility for channelling adaptation funds

Due to the relevant experience of SIFs and as SIFs still exist in many countries, they might also be directly used as an agency for channelling adaptation

funds or be adapted to also deliver funds for adaptation related activities and services, provided there is a benefit for adaptive capacities. The brief analysis shows that SIFs financed or still finance activities in a wide range of issue areas aimed at addressing one or several objectives and capacities that can also be relevant for adaptation processes, particularly in the area of risk management and social protection, whose links to adaptation have been widely acknowledged and analysed, but whose integrated implementation in practice is lacking behind (see Sub-section 3.4). For the last seven years, however, there has been no comprehensive overview on the status of SIFs in general and on the role of SIFs in the area of risk management in particular.

In general, the SIF model can be a strong partner at least for the distribution of parts of resources to communities vulnerable to climate change. However, there is one major drawback or condition: The suitability of the SIF model for adaptation finance presupposes that a certain minimum of communities share the same adaptation needs and therefore require the same or similar type of goods or services. If this is not given, the SIF model is probably not the best choice.

5.3 Adaptation-specific challenges for practical implementation

Based on these findings, what are the related adaptation-specific challenges for using the SIF model in adaptation finance in practice? From an institutional point of view, the main challenge is maximising the use of country systems by integrating an existing SIF into a national adaptation financing arrangement or applying key SIF principles to similar institutional entities dedicated to adaptation finance. From an operational point of view, the overall challenge is to factor in climate change-related risks and changes in SIF operations.

There are three main approaches and entry points to factor in climate change-related risks in the SIF model: i) mainstreaming (or climate proofing) climate change adaptation related risks into existing projects; ii) the identification of project types and the design of the project menus that specifically target adaptation needs; and iii) the design of targeting techniques that prioritise people and communities highly vulnerable to the effects of climate change.

The first approach is currently, for example, being piloted in Peru in a joint approach between the HELVETAS Swiss Intercooperation and the Peruvian social fund FONCODES, the National Cooperation Fund for Social Development. The main idea is to integrate climate change adaptation criteria and activities in the national FONCODES programme *Mi Chakra Emprendedora – Haku Wiñay*, in English: 'my entrepreneurial farm'. This government-run programme for rural productive development focuses on populations in extreme poverty and aims at expanding and diversifying income-generating activities as well as production to guarantee food security. The pilot activity intends to integrate climate change adaptation requirements into rural, agriculture-related technologies and instruments for planning, managing and evaluating projects as well as in the training and technical assistance of technical staff and farm experts (*yachachiq* in the native language).

The second approach, the identification of project types and the design of a project menu are particularly challenging. Researchers generally stress the context-specific nature of adaptation activities. There are only a few studies that try to establish adaptation-related typologies.[39] However, the SIF model requires a certain degree of standardisation of project activities which presupposes a minimum quantity of similar adaptation needs across a country with sometimes extremely different climatic conditions. In addition, the SIF experience shows that the project activity should ideally also be for the benefit of the whole community as a public good and avoid elite capture. Finally, there is the challenge of ensuring a high level of attribution in a project menu between one project type and its effects on vulnerability or adaptive capacity. While this project type might lead to reduced vulnerability in one place, it might somehow be beneficial in another place but not lead to reduced vulnerabilities against climate change risks. For constructing useful adaptation menus, a major challenge will also be the scale of analysis required. The analysis needs to look at the context-

39 See, for example, Maru / Langridge / Lin 2011: *"We found a limited number of climate vulnerability and adaptation studies that directly and indirectly developed typologies to help understand climate risk, and the example applications of typologies that have been developed have limitations in rigour, validity and even practical utility at times"* (Maru / Langridge / Lin 2011, 1). For other typology related studies see, for example, Agrawal 2008 on local types of institutions and adaptation practices; Sietz / Lüdeke / Walther 2011 on the categorisation of vulnerability patterns, or Zorom et al. 2013 on farm typologies for the Sahel.

specific details of social structures and the capacities of a community as well as the nature of required goods and services, and at the same time needs to be carried out on scale across the country.

The scale of analysis required and the requirements of related data can also be a challenge for the development of an adaptation-specific targeting strategy, the third entry point for factoring in climate change-related risks. Lack of climate data might constrict the usefulness of an allocation formula that links vulnerability indicators with climate or weather data. If weather-related data, for example, is not comparable or available across regions, it might disadvantage regions and communities that are most in need. In this case, an alternative approach can be to focus on indicators for adaptive capacity. Here, similar to the identification of project types as outlined above, the challenge is one of attribution between the indicator and its relation to vulnerability or adaptive capacities in a climate change-context.

Outlook

The body of literature available after 25 years of operation of social investment funds worldwide has been sufficient to identify defining features, strength and weaknesses and to arrive at a number of conclusions with respect to the challenges of channelling the benefits of international adaptation finance to vulnerable communities. Towards an application of the SIF model in adaptation finance in practice, country-specific analysis, as well as an updated overview of its current use by international financing institutions and partners, would be useful. In particular, an analysis of SIFs in the area of risk management merits further attention.

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