GREEN CLIMATE FUND

REFORM OF THE INTERNATIONAL FINANCIAL ARCHITECTURE TO TACKLE GLOBAL CHALLENGES

Summary

The global finance landscape remains fragmented and not fit-for-purpose, with limited access for developing countries in direst need. Urgent reforms are required to simplify access, scale up concessional finance, and mobilize private sector capital through blended finance mechanisms. Strengthening country ownership and improving transparency across financial flows are key priorities. The Fourth Conference on Financing for Development (FFD4) should advocate for these reforms to close the sustainable development finance gap and accelerate progress toward global goals, especially for vulnerable and low-income countries. FFD4 must be the running point that transforms global financing landscape into a truly inclusive, scalable, impactable, fit-for-purpose and sustainable engine for achieving the SDGs, Post-2015 development Agenda, and Paris Agreement goals by 2030.

Key messages

As highlighted in the Independent High-Level Expert Group on Climate Finance, **the current international financial architecture is failing to tackle the unprecedented climate and development crises** we are facing, both in terms of scale and speed. The report stresses the need to realign financial systems with the Paris Agreement and sustainable development goals (SDG).

An urgent and comprehensive reform of the current financial ecosystem is imperative, through redefining the roles and responsibilities of every stakeholder involved - from multilateral development banks (MDB) and multilateral climate funds (MCF) to bilateral agencies, private sector players, philanthropies, and civil society organizations. Each of these entities holds a piece of the puzzle, and only through coordinated and inclusive approach and action, where all of them should be part of the debate and discussion, can we hope to mobilize the necessary resources and expertise to meet the existential development and climate challenges. The renewed finance framework will require an **integrated approach** that boosts all sources of finance, public and private, domestic and international, to mobilize the scale and quality of finance required and deliver on the global development and climate goals. To address these challenges, we must ensure that the global finance architecture is fit for purpose.

RELEVANT ACTION AREAS

- Addressing Systemic Issues
- International Development Cooperation
- Domestic and International Private Business and Finance

ABOUT THIS SERIES

The Financing Policy Brief Series has been prepared by the Inter-agency Task Force on Financing for Development to inform the substantive preparations for the Fourth International Conference on Financing for Development (FfD4), to be held in Sevilla, Spain, from 30 June to 3 July 2025.

The Inter-agency Task Force on Financing for Development is comprised of more than 60 United Nations Agencies and international organizations. The policy briefs in this series were not subject to review by Task Force Members, and represent the views of the authoring organizations.

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MDBs are key to both unlocking investment opportunities and mobilizing additional resources, through own lending and catalyzing private finance. They have long been central players in financing development projects, from infrastructure to social programs. But in the face of the climate emergency, their mandates should be revised to tackle both the development and climate challenges, and their operations must expand accordingly. These institutions are uniquely positioned to catalyze large-scale climate investments, yet their governance models and risk frameworks have not kept pace with the growing urgency of the climate crisis. Reforming MDBs means moving beyond traditional, cautious lending approaches that limit their impact. They must be empowered to take on more risk, crowd in private capital, and leverage new resources such as hybrid capital and Special Drawing Rights (SDR), in order to direct significantly additional financing toward climate resilience and green infrastructure. As underlined in the Capital Adequacy Framework report, this requires significant changes to their capital structures, risk appetite, mandates, governance and operating models. It also means further aligning their activities with the goals of the multilateral climate funds like the GCF, creating a coordinated pipeline of financing, capacity building and policy support at country level that addresses both immediate adaptation needs and long-term decarbonization.

Concessional finance is the scarcest and most vital source of finance for meeting urgent and high priority needs. A fivefold in concessional finance is needed by 2030[1]. Despite significant pledges, persistent barriers remain, including the fragmented nature of climate finance, complex access requirements, and limited concessional finance, that are slowing the flow of funds to where they are most needed. And as stressed in the Bridgetown initiative 3.0, further significant sources of funding such as liquidity mechanisms, additional SDR allocations and new global solidarity levies are required to bridge the rapidly widening financing gap.

The GCF plays a pivotal and catalytic role in providing concessional finance by offering funding at more favorable terms than market rates to support climate action in developing countries. The GCF's concessional finance help scale up climate actions by lowering financial barriers, mobilizing private and public sector funding, and driving investment in areas where market-based finance is insufficient. The GCF is thus uniquely positioned to support high-risk and high-impact projects, to derisk private investments, to provide blending finance from multiple sources, and to facilitate long-term investment in Middle-Income, Low-Income and Vulnerable Countries. Through its Readiness program, the GCF can also support capacity building in developing countries to access fundings and implement projects. The broad network of GCF implementing partners, both local and international, ensures global coverage, yet with a tailored approach that remains country led. The on-going GCF reforms will lead to simplified access, increased scale and impact on the ground. Public finance alone cannot close the vast funding gap needed to address climate change.

Private capital must step up, not just as a financial source but also as an engine of innovation. The private sector has the resources and creativity to scale new technologies and business models that can drive the green transition. Yet, too often, private investment is volatile and constrained by short-term profit motives or a lack of regulatory certainty. Policymakers must create the conditions for the private sector to invest more heavily in climate solutions, especially in the adaptation area. This means providing transparency in the level of risk, offering the right incentives, such as tax credits for green investments, and ensuring that regulatory frameworks reward sustainable practices. Beyond the financial incentives, businesses must also be held accountable for incorporating climate risk into their operations and investments. Climate change is not just an external risk; it is a fundamental business risk, and private companies must treat it as such.

Domestic resource mobilization will be central, given its dominant role and importance in anchoring the macroeconomic sustainability of all finance. Many developing countries face unsustainable debt burdens, partly due to over-reliance on external borrowing.

1. Second Report of the Independent High-Level Expert Group on Climate Finance, November 2023

Strengthening domestic resource mobilization can reduce the need for further external debt and improve a country's creditworthiness. This makes countries less vulnerable to external shocks and more capable of managing their public finances independently, contributing to more stable international financial systems.

To achieve the desired impact, the reform of the whole international finance landscape, and not just pieces of it, is needed in an integrated and coherent manner. More efforts are needed to drive understanding of the need for system wide efforts.

Problem statement

Institutions built on 20th-century frameworks are failing to adequately respond to 21st-century challenges. The international financial architecture is highly fragmented, structurally unfit to respond to the compounding crisis countries are faced with and inequitable, leaving developing countries without the affordable finance required to meet global climate and development goals. Addressing these issues requires that the finance landscape works with all its components as one system, scaling up finance, accelerating its mobilization, and reforming governance to provide balanced representation for developing countries.

1. Scale and Quality of Finance Needed

Current finance commitments, including climate finance, fall significantly short of the amounts needed to address global challenges. The Grantham Research Institute and Brookings Institution's report (May 2022) highlights that achieving the Sustainable Development Goals (SDGs) requires a total of $6.9 trillion annually, with $2.4 trillion earmarked for climate action in emerging markets and developing economies.[2] Despite this, actual financial flows remain far below these targets.

Current finance models remain dominated by loans rather than tailored instruments, increasing borrowing costs for developing nations. This hampers the effectiveness of development efforts, particularly in regions already experiencing severe fiscal stress and climate impacts.

Investment by the private sector also remains limited, as the financial architecture is not maximizing use of the relevant instruments and incentives to reduce the costs of capital. In the Climate finance space, private sector investment has strongly favored mitigation over adaptation. International public finance commitments for adaptation fell in 2021, and only 66% of bilateral adaptation finance between 2017 and 2021 was effectively disbursed.[3] On the adaptation side, climate-resilient infrastructure is critical for protecting communities from worsening climate impacts with the Global Commission on Adaptation estimated that $1.8 trillion invested in climate-resilient infrastructure by 2030 could generate $7.1 trillion in total net benefits.

To improve the quality of finance, we need to focus on the following areas:

- Simplification of access to finance: It is essential to streamline access to financial resources to align with the narrowing window of opportunity for climate action. This requires all institutions to undertake comprehensive reforms and disseminate best practices across the system. By ensuring a 21st-century balance between risk and impact, institutions can more effectively support transformative projects and scale up climate investments.
- Enhanced transparency: Transparency is key for enabling accurate assessment of funding gaps, as well as comprehensive risk assessments. A more transparent system allows stakeholders to identify

2. Bhattacharya A et al. (2022) Financing a big investment push in emerging markets and developing economies for sustainable, resilient and inclusive recovery and growth. London: Grantham Research Institute on Climate Change and the Environment, London School of Economics and Political Science, and Washington, DC: Brookings Institution. [https://www.lse.ac.uk/granthaminstitute/publication/financing-a-big-investment-push-in-emerging-markets-and-developing-economies]
3. Songwe V, Stern N, Bhattacharya A (2022) Finance for climate action: Scaling up investment for climate and development. London: Grantham Research Institute on Climate Change and the Environment, London School of Economics and Political Science.[https://www.lse.ac.uk/granthaminstitute/publication/finance-for-climate-action-scaling-up-investment-for-climate-and-development/#:~:text=This%20report%20was%20prepared%20by%20the%20Independent%20High-Level]

where resources are most needed and helps ensure accountability, building trust and facilitating better decision-making.

- Supporting country ownership and ambition: Strong country ownership must be at the heart of climate finance strategies. Country programs and platforms should be designed to empower national governments and stakeholders, leveraging the comparative advantages of multiple financiers. By aligning diverse financial flows with national priorities and ambitions, we can ensure more effective and sustainable climate outcomes.

2. Speed of Finance Mobilization

The fragmented landscape of climate finance has created inefficiencies in mobilizing funds quickly. With multiple financing mechanisms operating under different mandates, eligibility criteria, and access modalities, it drains developing countries' limited capacities as they face significant barriers in navigating this landscape. This delay in accessing funding, particularly for the most vulnerable nations, undermines their ability to act swiftly in response to the climate crisis.

3. Reforming Governance for Balanced Representation and addressing Systemic Issues

The governance structures of international financial institutions remain imbalanced, with insufficient representation from climate-vulnerable developing countries. This imbalance means that financial decisions often fail to align with the priorities and fiscal realities of these nations. Additionally, systemic issues in global financial systems, such as the role of credit rating agencies, exacerbate inequalities. Developing countries avoid or limit adopting ambitious climate policies due to the risk of credit downgrades, which would increase borrowing costs. Additionally, prudential regulatory policies designed to safeguard financial stability have unintentionally limited capital flows to developing nations, further hindering their access to global capital markets. Lastly, inadequate transparency and inconsistent monitoring of climate finance flows make it difficult for investors to accurately assess project risks, raising the cost of finance and slowing investment flows.

Policy solutions

To address the global challenges identified above, every part of the international financial architecture must work together as a coherent system. The following policy reforms and solutions are critical:

1. At the **global level**, sources of international finance must adopt more **inclusive coordinated approach to the international finance landscape** to mobilize the necessary resources and expertise and to level up to meet the sustainable development and climate challenges. Institutions in the current architecture must modernize their approach to collaborating and coordinating among the fragmented landscape of actors, including leveraging and increasing investments from the private sector and philanthropic sources through blended finance mechanisms and public-private partnerships, which can help de-risk investments and attract more private capital.

   The total scale of investment allocated to achieving the impact aligned with the global goals must also be increased. This could include:

   - Reallocating special drawing rights (SDRs) so they may be more easily used,
   - Advancing options for mobilizing investments from alternative sources, including international levies being explored by the Global Solidarity Levies Task Force.

2. **At the country level Promoting coherence and complementarity within the finance architecture** to reduce risks arising from fragmentation of climate finance sources with different and complex requirements, eligibility criteria and application processes. Countries can establish a country platform to help translate development and climate ambitions into pipelines of investable projects and programs. Individual and collective efforts are needed to significantly reduce access barriers for countries with low capacity, enabling them to secure funding quickly and at the necessary scale. The GCF Readiness Program plays a crucial role in enabling and enhancing ambition at the country level by providing technical, institutional, and financial support to developing countries. This program helps countries

strengthen their capacity to access climate finance and implement ambitious climate actions

3. **Improve access and availability of concessional finance.** As recommended by the UN Secretary-General's Roadmap for Financing the 2030 Agenda, to increase impact, key players need to shift from traditional lending models to a catalytic role, whereby more concessional financing and tailored (non-debt) instruments —such as guarantees, debt-swaps and additional innovative de-risking tools. By way of example, the Green Climate Fund's policies allow flexibility in financial instruments, including a risk appetite that supports a willingness to assume first-loss and junior positions which enables it to address clear investment barriers tailored to each investment to catalyze additional investment and deliver impact.

4. **A revised country ownership model,** with improved representation of developing countries in governance and decision-making of climate and development finance institutions would contribute to prioritizing and allocating resources effectively. **The GCF is already well-positioned to support this approach, given its operational focus on country ownership and its balanced governance model that includes 50% of board members from developing countries with same voting and decision-making rights as developed countries.** The **GCF Readiness Program**, combined with its **vast network of partners**, plays a transformative role in empowering countries to achieve ambitious climate goals. This powerful combination of readiness support and global partnerships enables countries to effectively scale climate action by leveraging expertise, resources, and on-the-ground implementation.

5. **Scaling up of development and climate finance for resilience and adaptation.** Development and climate finance institutions must increase their allocation towards adaptation and resilience to fulfill the commitments of the Paris Agreement. The GCF has already demonstrated leadership in this area by allocating 50% of its resources to adaptation, setting a model for other institutions.

6. **Leveraging Climate and Development Data and Monitoring.** Improving data collection and transparency around climate and development finance flows is essential for ensuring accountability and measuring progress. A robust reporting system should be established to track the effectiveness of climate finance, using a set of standardized metrics to measure outcomes. Climate funds and MDBs can play a key role in fostering greater transparency by supporting the development of these metrics and facilitating independent monitoring efforts.

Specific recommendations for FFD4

The Fourth Conference on Financing for Development (FFD4) provides an opportunity for member states to call for needed reforms to the global finance architecture. The following recommendations should be considered to enhance climate finance effectiveness and accessibility:

1. **Supporting and improving complementarity:** Member states should call for enhancing complementarity and coherence among key players in the highly-fragmented financing system; for a comprehensive rewiring of the multilateral development finance institutions to make more use of concessional and debt-free instruments, to better align with the current needs of developing countries; and a new country engagement model, with greater participation and decision-making power for these countries. An inclusive, coordinated approach to the reform, including all relevant actors (MDBs, MCFs, private sector, philanthropies), is urgently needed.

2. **Scaling Blended Finance and adaptation financing:** FFD4 should highlight the importance of blended finance mechanisms, public-private partnerships and de-risking instruments as essential tools for closing the climate finance gap. Governments must commit to strengthening regulatory frameworks and addressing systemic constraints to scale blended finance and ensure that public funds are used strategically to de-risk private investments.

3. **Simplifying Access to Climate Finance:** The outcome document should emphasize the need for ongoing efforts to harmonize and simplify access to climate finance, including simplification of access within each institution and making best practices across the broad international finance architecture the default

ones. Building on the GCF's initiative to enhance complementarity and coherence, FFD4 should promote concrete steps to harmonize application processes across climate funds, reduce bureaucratic barriers, and ensure faster disbursement of funds.

4. **Promoting Accountability and Impact:** FFD4 should advocate for improved mechanisms for tracking climate finance flows and assessing their impact. Better monitoring systems, supported by multilateral organizations, can ensure that climate finance is targeted effectively and used to address the most pressing needs of developing countries.

By incorporating these recommendations, FFD4 can help close the climate finance gap and unlock the resources needed to accelerate global climate action, particularly for vulnerable countries.