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Working with Local Financial Institutions to Integrate Climate Lending

How-to Guide

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1. What are the main challenges to accessing affordable capital in SSA?

Smallholder farmers and agricultural businesses in sub-Saharan Africa (SSA) often have limited access to affordable short- and long-term finance. This includes limited access to early-stage finance necessary to start a business, working capital to maintain and scale operations over time, and long-term refinancing to inject new capital at later stages. These challenges are rooted in the limited maturity and depth of local capital and financial markets.

USAID Missions can work closely with financial institutions (particularly local banks and microfinance institutions) to overcome these challenges and unlock climate finance through potential interventions outlined below:

Challenge	Description	USAID Mission intervention options
Limited early-stage capital	Due to their high risk and long return on investment timelines, agriculture investments need early-stage, concessional financing to cover initial start-up costs. This type of capital is not always available for agricultural businesses, especially smallholders.	• **Provide grants and concessional finance through blended finance structures**, including catalytic first-loss capital, to help businesses reach "tipping points" that can mobilize private investment with attractive risk-adjusted returns. • **Provide technical assistance, capacity building, and advisory support** to help agriculture businesses and projects develop robust business plans, conduct feasibility studies, and improve their financial management capabilities. This will help de-risk projects, making them more attractive to investors and lenders. • Provide support to local financial institutions to **develop suitable financial products** for sustainable agriculture projects. This will help to deepen pool of long-term debt financing for projects. • Foster **partnerships between local financial institutions and international climate finance organizations** (e.g., Green Climate Fund, GCF) to unlock additional capital sources for climate projects.
Limited long-term (patient) capital	Agricultural businesses can find it hard to access patient capital in the commercial market, i.e., capital with extended tenors and favorable terms to match prolonged return on investment timelines. This limits growth opportunities and the sustainability of agribusinesses.	• Collaborate with financial institutions, impact investors, and other donor agencies to establish a **dedicated fund for financing sustainable agricultural initiatives.** The fund could prioritize flexibility in terms, extended tenors, and favorable repayment conditions; it should also prioritize projects that benefit marginalized groups, promoting gender equality, and ensuring underrepresented agribusinesses have equal access to funding. The fund could also provide technical assistance and capacity-building support to early-stage agribusinesses, including project development guidance, financial management training, and access to networks of experts. • Promote the issuance and uptake of **green bonds and impact investing** in the agricultural sector by providing technical assistance and training to agribusinesses for preparing detailed project proposals, conducting environmental and social

Challenge	Description	USAID Mission intervention options
		impact assessments, and aligning projects to the Sustainable Development Goals (SDGs) ● Facilitate **public-private partnerships (PPPs)** to mobilize patient capital by sharing risks and rewards between public and private sector actors. Governments could provide policy support and incentives, while private investors and financial institutions offer the necessary funding. This collaborative approach increases the pool of available capital and reduces the risk for individual investors.
Inadequate development and deployment of climate finance instruments	Sustainable agriculture projects in sub-Saharan Africa are predominantly reliant on concessional finance (i.e., grants and low-rate project debt) provided by the public sector. Innovative climate finance instruments such as green bonds and carbon finance have only recently started to emerge. In fact, Africa's green bond market represents less than 1% of the global green bonds market, with the vast majority of green bonds issued in the region concentrated in South Africa. African carbon market activity, also falls well below of its estimated potential.	● Work with local financial institutions and donors to **develop pilot transactions** to demonstrate the successful use of innovative climate finance instruments, such as green bonds and carbon finance. ● Provide **technical assistance, capacity building, and financial support** to local financial institutions to develop carbon markets. ● In countries with more advanced bond markets, work closely with governments and local institutions to further **develop markets for a variety of** capital market instruments including green bond and sukuks, social bonds, and sustainability bonds that can provide access to long-term, large capital pools. ● Provide **targeted support** to financial institutions and strengthen capital markets to enhance the effectiveness and scalability of financial instruments, improve market liquidity, and catalyze investments in sustainable agriculture.
High risk profile for agriculture businesses	Agricultural businesses in sub-Saharan Africa are perceived as high-risk-low-return investments. Currency risk, political and market volatility in the region, and the inherent climate risk of agriculture due to its dependence on weather patterns all amplify the perceived investment risks for agribusinesses. This perception is further heightened when businesses focus on smallholders.	● Support the development and deployment of targeted **risk-mitigating instruments to address a variety of investment risks.** These can include, for example, credit guarantee schemes and risk-sharing mechanisms. ● Provide **technical assistance to bolster governance** and financial management capacities of agribusinesses and improve their risk assessment and mitigation capabilities. ● Work closely with local financial institutions and donors to **develop** structured finance mechanisms to de-risk investments in early-stage agribusinesses, particularly those catering to small-scale farmers, making them more appealing to risk-averse private sector investors.

2. What can be done to address these challenges?

Existing solutions to the barriers in agribusiness have largely centered on the provision of grants and concessional finance to support businesses through technical assistance and the provision of early-stage capital. Risk mitigation instruments (such as currency hedging instruments and guarantees) have also been used to reduce specific investment risks and improve the attractiveness of agriculture investments in the region.

Innovative solution	Description	Examples
Blended finance structures	These structures involve the use of both concessional and non-concessional finance to lower inventors' risk perception and, in turn the overall cost of capital for smallholders and agribusinesses.	• Aceli Africa (Aceli) is a market incentive facility that provides capital to small- and medium-sized (SMEs) agribusinesses in Africa. It provides concessional financing and reduces the perceived risk of its borrowers for private investors. Aceli also provides various financial incentives for agribusiness to engage in areas that promote sustainable development goals. • FEFISOL Microfinance Fund II is a fund dedicated to financing microfinance institutions and small agricultural entities in Africa. It offers diversified financial products, in 12 to 15 local currencies, therefore mitigating the risk of FX losses. In addition, the fund provides technical assistance, and supports the implementation of assessment and monitoring tools for agricultural performance. Set for implementation in over 28 African countries, FEFISOL II aims to benefit 110 microfinance institutions, agricultural entities, and cooperatives.
Capital market instruments	These include green bonds, social bonds and sustainability bonds and can help to attract long-term, large investors who are seeking stable and predictable returns on their investments. By pooling together several different projects, their instruments offer larger ticket sizes and diversified investment opportunities, reducing the overall risk for investors.	• The Nigeria Green Bond Programme was established in 2018 by FSD Africa, FMDQ Group, and Climate Bonds Initiative. The program integrates technical support and capacity building training for issuers and directly engages with regulators to encourage the creation of an enabling environment for green bond issuance. Since its inception, $76 million in corporate and sovereign green bonds have been issued to 928 beneficiaries. • The Kijani Bond, issued in August 2023 by the Cooperative and Rural Development Bank (CRDB) in Tanzania, is anticipated raise TZS 40 billion ($300 million) during its first phase.
Carbon finance	Under carbon finance, mitigation projects generate tradable credits for each unit (i.e., metric ton) of carbon emissions avoided or removed. These credits can then be sold on voluntary (or compliance) carbon markets to counterparties looking to offset their own carbon emissions and meet net-zero emissions targets. Proceeds from carbon	• The Northern Rangelands Trust (NRT) in Kenya focuses on soil carbon projects that advance carbon sequestration and mitigation through sustainable rangeland management, agroforestry, and community conservancies. • Boomitra is a tech-driven platform that focuses on soil monitoring, carbon sequestration, and climate finance to support farmers and ranchers in adopting sustainable agricultural practices. It facilitates the adoption of carbon-sequestering agricultural practices, quantifies the resultant additional carbon captured, and collaborates

Innovative solution	Description	Examples
	credit sales can increase the economic viability of climate projects in operating in commercially challenging markets such as sustainable agriculture, allowing them to secure up-front investment or fund long-term operations. Read more about carbon finance for agriculture here.	with international standards bodies to generate carbon credits.
Structured finance mechanisms	Securitization divides projects into different financial tranches with varying degrees of risk and return to match specific investors' risk-return appetite. Although complex, securitization helps to reduce the overall cost of financing and to broaden the capital pool available to the project.	Although securitization is a complex financial instrument, it has already been used in the energy sector in the region, including for off-grid solar systems (which share similar market conditions with the agriculture sector). For example: • In 2020, the NEoT Offgrid Africa (NOA) investment platform set up a securitization program for loans to finance off-grid energy projects in Côte D'Ivoire. The program will equip more than 100,000 households in the country with solar home kits, mainly in rural and peri-urban areas.
Results-based financing	This is an approach in which financing terms are linked to the delivery and verification of predetermined results (i.e., outputs or outcomes). For example, these instruments can apply more favorable interest rates if certain results are achieved or delay disbursements until predetermined performance indicators are verified. By making funding conditional to performance and having results verified by an independent third party, results-based funding reduces counterparty risk and the need for data gathering upfront.	Results-based financing (RBF) has been used in various African countries to finance the off-grid solar sector and increase energy access. Some examples include: • EnDev's RBF Facility in Tanzania, implemented by SNV since 2013, focused on accelerating the development of a local market for improved cook stoves and off-grid solar energy. • Kenya Off-Grid Solar Access Project (KOSAP), started in 2018 and aimed at accelerating energy access through mini grids and standalone solar systems for local community facilities, enterprises, and households.