

Executive Summary

International Climate Finance (ICF) is a core component of the United Kingdom's contribution to developed countries' shared goal of mobilising US\$100 billion of public and private climate finance a year by 2020. Significant amounts of private investment will be key to achieving a sustainable, low-carbon climate-resilient (LCCR) transition where the private sector is driving a long-term solution to climate change. ICF therefore focusses its investments upon demonstration which will mobilise private finance, aiming to make catalytic investments that can be scaled up and replicated by private finance.

This evaluation seeks to establish whether private investors are influenced by evidence from ICF-supported projects (i.e. by demonstration effects) into investing in LCCR projects, without or with less development finance, directly and/or through funds.

We focussed on a sample of 20 ICF programmes, 10 of which were investigated in depth, which intended to mobilise private finance through demonstration effects into follow-on projects, outside the ICF programme.

During our evaluation we interviewed 154 individuals, including teams working on ICF supported-programmes, implementing partners, businesses and developers, and a range of investors including development finance institutions. We also interviewed key sector experts, reviewed programmes and other documents, and focussed on two areas where transformational change was indicated.

How ICF has used demonstration effects with the intention of mobilising private finance

Nearly all our sample programmes intended to use demonstration effects to mobilise private finance into follow-on projects. In their business cases, many described plans to communicate the results of their programmes. However, most business cases did not have a clear plan for how they would use demonstration effects to mobilise private finance. Few of the programmes were monitoring mobilisation of private finance through demonstration effects, although some had plans to do so.

We found that programmes are intending to demonstrate that:

- There is a market;
- A financial or investment model works;
- There are favourable enabling conditions; and/or
- Others are investing.

Most programmes are actively communicating the demonstration effects through formal, programme-led communications. Other methods of communication include word of mouth from programme partners, learning and networking through conferences and industry bodies. Market participants are alert to new information and we found evidence of informal communications in all programmes in the final sample.

How much private finance has been mobilised through demonstration effects, by whom and for what purposes

From four of the 10 programmes in our in-depth investigation, we identified US\$430 million (£350 million) of private finance that has been mobilised into 21 LCCR projects through demonstration effects. We found five other cases of mobilisation where the amount of the investment was unavailable. Around half of the total amount (US\$208 million) was invested in renewable energy projects and a similar amount (US\$217 million) was invested in businesses supplying solar systems for homes, businesses and mini-grids. 1% of the overall investment was in resilience and none was in energy efficiency.

In the other six programmes in the in-depth review, we found interim outcomes such as raised ambition and replication with the same level of concessionality. These interim outcomes can be seen as an indication that private finance may be mobilised in the future or that some progress towards that goal has taken place.

How and for whom demonstration effects work to mobilise private finance

We identified six types of demonstration effect, that is, six ways in which a programme can show to potential investors that such investments represent viable propositions:

- **Demand** – giving investors confidence in the scale of the opportunity.
- **Business model** – will be effective in satisfying the demand at a profit.
- **Track record** – of reliable financial and environmental returns.
- **Compliance** – will meet investors’ reporting standards.
- **Risk** – can be assessed with acceptable levels of confidence.
- **Trust** – in the judgement of other credible actors already investing.

We identified four types of investor: businesses and developers, direct investors, fund managers, institutional investors. Each uses demonstration evidence for different purposes and in different ways, which we summarise below:

- Where the demand for LCCR products and services is unproven and/or something about the business model for satisfying that demand is uncertain, demonstration effects encourage **businesses and developers** to pursue LCCR opportunities because they give them confidence that their business can succeed and will be able to secure investment.
- Where investors do not have enough information to assess LCCR investment opportunities then demonstration effects provide **direct investors** with confidence in the likely returns and enable them to assess the risk associated with the investment more accurately. As a result, they are more likely to invest.
- Where **fund managers** have no experience of managing LCCR funds, demonstration effects provide fund managers with confidence that the model is viable as they will be able to secure funding and find suitable opportunities for investment. Consequently, they invest time and resources in extending existing or establishing new funds.
- Where **institutional investors** have a mandate for sustainable investment but do not have experience of investing in LCCR funds, evidence from demonstration projects provides them with confidence in fund managers’ abilities to secure investment, find opportunities and deliver acceptable returns.

Each effect for each type of investor has been assessed as ‘convincing’, ‘plausible’ or ‘tentative’ depending on the strength of evidence for the contribution of demonstration effects to the mobilisation of private finance. N/A indicates that no evidence was found. This is shown in the table on the next page.