REGIONAL INNOVATION PROJECT/PROGRAMME PROPOSAL

PROJECT/PROGRAMME INFORMATION

Title of Project/Programme:	Unlocking investments in gender and youth-inclusive early-growth stage adaptation Small and Medium-sized Enterprises in Kenya and Uganda
Country/ Countries:	Kenya, Uganda
Thematic Focal Area[1]:	Innovative adaptation financing
Type of Implementing Entity:	Multilateral Implementing Entity (MIE)
Implementing Entity:	United Nations Industrial Development Organization (UNIDO)
Executing Entities:	adelphi, Kenya Climate Ventures (KCV), Finding XY)
Amount of Financing Requested:	5,000,000 (in U.S Dollars Equivalent)

[1] Thematic areas are: Agriculture, Coastal Zone Management, Disaster risk reduction, Food security, Forests, Human health, Innovative climate finance, Marine and Fisheries, Nature-based solutions and ecosystem-based adaptation, Protection and enhancement of cultural heritage, Social innovation, Rural development, Urban adaptation, Water management, Wildfire Management.

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List of abbreviations

APT	Adaptation performance targets	**ICT**	Information and Communications Technology
ASAL	Arid & semi-arid landscapes	**IE**	Implementing Entity
ASAP	Adaptation SME accelerator Project	**IOM**	International Organization on Migration
BAU	Business as usual	**IPCC**	Intergovernmental Panel on Climate Change
CSA	Climate smart agriculture	**ITCZ**	Inter-Tropical Convergence Zone
DFIs	Development Finance Institutions	**MoFPED**	Ministry of Finance, Planning and Economic Development
EE	Executing Entity	**MSME**	Micro, Small and Medium Sized Enterprise
ESIA	Environmental and Social Impact Assessment	**NCAP**	National Climate Action Plan
ERS	Economic Recovery Strategy for wealth and employment creation	**NDC**	Nationally Determined Contributions
FAO	Food and Agriculture Organisation of the United Nations	**ROI**	Return on Investment
FI	Financial Institution	**SACCO**	Savings and credit cooperative organization
GDP	Gross Domestic Product	**SDGs**	Sustainable Development Goals
GoK	Government of Kenya	**SME**	Small and Medium-sized Enterprise
GoU	Government of Uganda	**SOC**	Soil Organic Carbon
SSP	Shared socio-economic pathways	**SSA**	Sub-Saharan Africa
TA	Technical Assistent	**UGEFA**	Ugandan Green Energy Finance Accelerator
ToC	Theory of Change	**WRI**	World Resource Institute
		WRUA	Water Resource Users Association

PART I: PROJECT BACKGROUND AND CONTEXT

1.1. Background and project context

This project takes an innovative approach in piloting a catalytic finance facility aimed to support early growth adaptation SMEs in Kenya and Uganda to scale their business models and adaptation impact on highly vulnerable target groups. The finance facility in combination with targeted business and post-investment advisory support will help these SMEs to overcome the missing middle financing gap and related challenges to grow and replicate their business operations, thus, widening the outreach and deployment of adaptation solutions to vulnerable groups. Vulnerable communities will benefit from an increased access to targeted and context-specific adaptation solutions, substantially increasing their resilience to climate change. The project will furthermore capacitate local FIs to gain a better understanding of adaptation solutions and technologies as provided by adaptation SMEs to raise their willingness and ability to provide tailored finance for adaptation businesses. Through its innovative approach, the project addresses both the finance supply (financial actors) and demand side (adaptation SMEs) to achieve transformational change in prevailing financing systems and mechanisms in the two target countries. A pre-screening of gender- and youth inclusive adaptation SME pipelines in Kenya and Uganda, the main target group of this project, conducted by the local executing entities (EE) showed that these SMEs operate across regions and counties, their adaptation business models tackling the diverse climate-related challenges of local customers and beneficiaries. At the same time, the SME market is highly volatile as business failures among early-growth enterprises are common and have been further exacerbated by the COVID-19 pandemic. The project will therefore take a cross-regional approach, inviting enterprises to apply from all regions in Kenya and Uganda. The final selection of participating adaptation SMEs will consider the extent the business model in question addresses specific vulnerabilities of the final customers/beneficiaries in the region of operation. To this end, a detailed scoring system with a positive list of eligible adaptation technologies/ approaches will be developed as part of the project's inception phase (see also Climate Risk and Adaptation SME Solution Matrix as a first guidance). Additionally, it is important to note that an initial gender assessment can be found in Annex 1 to give insight into how gendered challenges have been incorporated into the project planning and development. AA comprehensive assessment will be provided as part of the full proposal, together with a market analysis.

1. Geography & historical context: Located on the eastern coast of Africa, Kenya and Uganda lay adjacent to the rift valley and Lake Victoria. Kenya has a territory of approximately 580,000 km^2 and its landscape is predominantly characterized by drylands located in the north eastern and north western part of the country. In the south western part of the country mountain ranges, forested areas and large lakes define the main ecosystem structures. On the other hand, Uganda located west of Kenya is a landlocked country with relatively homogeneous landscapes of 241,555 km^2, characterized by large lakes, forested areas, savannahs and the White Nile. With high precipitation rates and large water bodies cover approximately 15% of the country surface area.
2. The populations within these two countries are young and rapidly growing (bottom heavy demographic models). According to the Kenya National Census (2019), the population was reported at 47.6 million people, a severe increase from the estimated 28.7 million in 2000[2]. Uganda's population was estimated at 40.3 million by midyear 2019 with an annual population growth rate of 3.1%[3]. This population is projected to double, making it one of the fastest growing nations in the world. Similarly, to Kenya the demographic model in Uganda is bottom heavy with children below the age of 15, constituting 48.1% of the population. Uganda also has a strong cultural diversity with the most recent census identifying 60 different tribal groups.
3. Over 38.73 million (KE) and 34.3 million (UG) are classified as living in rural areas, accounting for over 76% of households. Urban population, on the other hand, has significantly increased over the last 15 years as rural communities begin moving to urban areas in search of better economic opportunities that are non-agricultural based.
4. Economic structures and trends: The economic landscapes of both countries have followed similar growth trends since their independence. In 2020, Kenya's Gross Domestic Product (GDP) was 101 billion USD, and Uganda's was 37.6 billion USD, an increase of 694.73% and 505.43% since the year 2000, respectively. However, despite the rapid increase in GDP, not all parts of the population have experienced these financial gains. According to the GINI[4] index in 2019, income inequalities were classified as high as their scores of 41.61 (Kenya) and 42.80 (Uganda), clearly representing an unequal distribution of wealth. Despite this, there have been dramatic improvements in the amount of available wealth for individuals. Between 2000 and 2020 the Gross National Income (GNI) per capita increased from $3,159.2 to $4,267 in Kenya and by $1,239.4 to $2,138 in Uganda[5].
5. With growing wages, it is evident that communities have seen reductions in their financial vulnerability. However, rural and remote regions have not yet benefitted from these financial gains due to the lack of markets, price fluctuations for the crops they produce, and increasing climate threats leading to crop loss and poor harvest. Despite the substantial growth and improvement in the economic conditions within Kenya and Uganda, economic structures are predominantly dependent on rain-fed and non-mechanised agricultural production.
6. Agricultural production is central to Kenya's socio-economic success, agriculture contributes to approximately 80% of the workforce and 23.05% of the annual GDP. Similarly, in Uganda 25% of the country's annual GDP comes from agriculture and employs approximately 75% of the total labor force. In addition, women constitute the majority of this labor force, as highlighted by the World Bank (2020), recording 49.2% (Kenya) and 49% (Uganda) of women employed in the agricultural industry. Crop production is the largest component and most important for food security with sugarcane (6.8 million tons), maize (3.8 million tons) and potatoes (1.9 million tons) being the most produced crops in Kenya. Similarly, in Uganda, crops were also the largest contributor to this sector with sugarcane (3.9 million tons), plantain (3.8 million tons) and maize (2.9 million tons) being the three largest quantity produce[6].

[2] Kenyan national census. (2019). 2019 Kenya Population and Housing Census - Population by County and Sub-County - openAFRICA

[3] Uganda national census. (2019). THE STATE OF UGANDA POPULATION REPORT 2019 | Ministry of Finance, Planning and Economic Development

[4] The Gini coefficient is a measure of the income distribution of a population. Higher values indicate a higher level of Inequality and values closer to 0 represent more equally distributed income. Source

[5] World Bank, World Development Indicators. (2020). URL: Employment in agriculture (% of total employment) (modeled ILO estimate) | Data (worldbank.org).

[6] FAOSTAT. (2020). Crop and yield data. URL: https://www.fao.org/faostat/en/#data/QCL and https://www.fao.org/faostat/en/#data/QCL.

7. In Kenya, crop production predominantly occurs in Central, Rift Valley, Western and Nyanza provinces. Within these regions, there is large-scale production of coffee, tea, floriculture and smallholder production of essential food crops such as potatoes, beans, corn, and wheat. Areas in Uganda with similar climates, predominantly in central, western and eastern regions are the core agricultural production sites. Livestock farming is widely spread throughout Kenya and Uganda due to cultural and traditional practices in pastoralism. However, drylands in the North Eastern and North Western part of Kenya and the cattle corridor (Uganda) are regions where pastoralism is a main source of income and nutrition[7].

8. Agricultural production within Kenya and Uganda is heavily focused on crop production for staple foods or exportation. Yet, despite the vast number of agricultural exports coming from large-scale producers for products such as tea or coffee, small-scale production is primarily focused on supplying local markets and accounts for 78% and 80% of the total agricultural production in Kenya and Uganda, respectively. Currently, it is projected that smallholders (with plots ranging from 0.2 – 3 hectares) accounting for 78% and 80% of the total agricultural production in Kenya and Uganda, respectively[8].

9. <u>Climate</u>**:** Kenya and Uganda are located within a highly vulnerable area to climate change with increasing precipitation variability, extreme precipitation and droughts, and raising temperatures causing irreversible damage to the livelihoods of vulnerable communities. According to the Intergovernmental Panel on Climate Change (IPCC), the East Africa region, which includes Kenya and Uganda, has experienced a 1.5 °C increase in temperate since 1901 and projections foresee an increase by 1.7 ºC to 6 ºC by 2080. Uganda and Kenya have faced an increase in annual precipitation rates since the 1960s. However, the IPCC report of Africa established that "precipitation in East Africa [has shown] a high degree of temporal and spatial variability dominated by a variety of physical processes". For example, precipitation in north western Kenya has become less present and rather occurs in unexpected extreme precipitation events due to changes in the temperature of the Indian ocean9.

10. Kenya and Uganda are defined by a bimodal precipitation regime, with a short rainfall season occurring October- December (OND) and a long rainfall season between March and May (MAM). Precipitation in this region is controlled by the movement of the intertropical convergence tropical zone (ITCZ), an equatorial band of low pressure where northern and southern trade winds meet, causing heavy rainfall. Due to changes in the annual movement of the sun's solar position, the band moves either north or south depending on the time of year. For Kenya and Uganda, this means that regions above and below the equator can also experience altered intensity in rainfall during certain seasons[10].

11. The country's equatorial positions also create varying climatic conditions. Areas below and around the equator receive higher amounts of precipitation as southeast trade winds bring in moist air from the oceans that condenses and rises forming clouds in the area known as the doldrums. In these areas high temperatures create tropical environments where precipitation and temperature are high thus leading to dense vegetation formation. In northern parts of both countries drier conditions are observed as dry air that has been redirected falls towards the poles. Likewise, these regions also receive less rainfall due to their topographic structures. In Kenya and Uganda landscape altitude strongly contributes to precipitation patterns, hence highlands in the western proportion of Kenya and the central and eastern Uganda receive more precipitation[11].Precipitation in both countries controls the dominant vegetation types. Likewise, the geology/ topographic structures also control the extent of precipitation and water availability. Due to geological processes occurring along the great rift valley, landscapes like deep valleys, large lakes and mountain/volcanic ranges have been formed in the west of Kenya and throughout Uganda. These landscape features and the vegetation that exists within them have fostered safe socio-economic systems for regions. Water towers ensure that during dry seasons water captured in the forested areas is released into rivers and tributaries ensuring water availability at lower altitudes[12].

12. According to Walter and Lieth climate graph analysis of Kenya and Uganda's climate data between 1989 and 2019, Uganda and Kenya have similar bimodal climates, with annual mean temperatures of 23.3°C and 21.1° respectively (Figure 1 & 2 below). This is represented by the red line illustrating the average monthly temperatures. Evidently, due to the countries' equatorial position, mean seasonal temperatures do not fluctuate significantly. In terms of precipitation, the ITCZ results in bimodal precipitation structures, the two rainfall seasons are clearly depicted by the blue line which presents the monthly average rainfall. Areas with red dotted shading are dry period, and the blue line shading illustrates a humid period, and the full blue shading is present there Is a wet period. However, due to a variety of factors (direction of wind, altitude, etc.) both countries receive regional variations in precipitation. In Uganda, annual mean precipitation rates are at 1264mm with the majority of the year having humid and tropical rainfall events. Precipitation is much stronger in the central and western parts of the country and arid seasons occur in the southern and northern parts of the country. On the other hand, Kenya has a much lower annual mean precipitation at 701mm and an arid period occurring in
clear throughout Kenya with the exception of the arid regions in the east/northeast and north western arid and semi-arid regions where precipitation rates are much lower[13].

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[7] Waithaka, M., Nelson, G. C., Thomas, T. S., & Kyotalimye, M. (2013). *East African agriculture and climate change: A comprehensive analysis*. Intl Food Policy Res Inst.

[8] World Bank, World Development Indicators. (2020).

[9] Niang, I., O.C. Ruppel, M.A. Abdrabo, A. Essel, C. Lennard, J. Padgham, and P. Urquhart, 2014: Africa. In: Climate Change 2014: Impacts, Adaptation, and Vulnerability. Part B: Regional Aspects. Contribution of Working Group II to the Fifth Assessment Report of the Intergovernmental Panel on Climate Change. Cambridge University Press, Cambridge, United Kingdom and New York, NY, USA, pp. 1199-1265.

[10] Climate Risk Profile: Kenya (2021): The World Bank Group. URL: https://climateknowledgeportal.worldbank.org/sites/default/files/2021-05/15724-WB_Kenya%20Country%20Profile-WEB.pdf

Climate risk Profile: Uganda (2021): The World Bank Group. URL: https://climateknowledgeportal.worldbank.org/sites/default/files/2021-05/15464-WB_Uganda%20Country%20Profile-WEB%20%281%29.pdf

[11] Hadley cycles; Mugalavai, E. M., Kipkorir, E. C., Raes, D., & Rao, M. S. (2008). Analysis of rainfall onset, cessation and length of growing season for western Kenya. Agricultural and forest meteorology, 148(6-7), 1123-1135.

Everard, M., Vale, J. A., Harper, D. M., & Tarras-Wahlberg, H. (2002). The physical attributes of the Lake Naivasha catchment rivers. In Lake Naivasha, Kenya (pp. 13-25). Springer, Dordrecht.

[12] Wamucii et al. (2021). URL: https://hess.copernicus.org/articles/25/5641/2021/hess-25-5641-2021.pdf

[13] Climate Risk Profile: Kenya (2021)

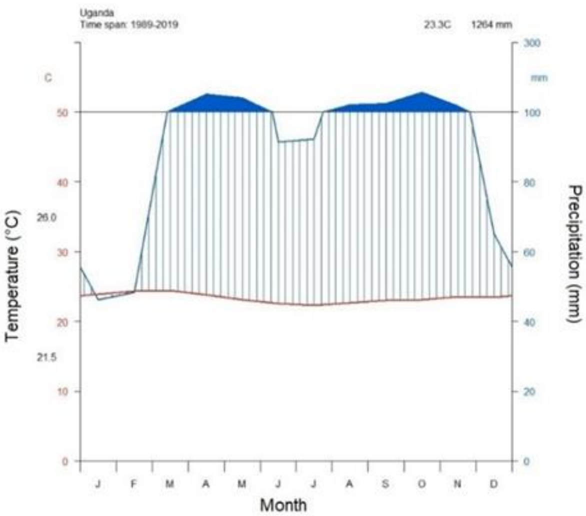

Figure 1. Climate graph Kenya

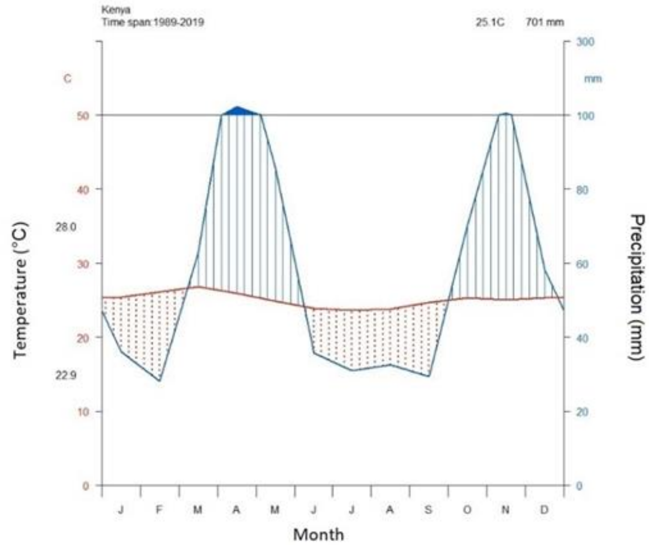

Figure 2. Climate Graph Uganda

1.2. Climate Change Vulnerabilities, Impacts and Risks

Climate trends and projections

13. Temperature: Extrapolating the World Bank Climate Portal data (2020) further, temperature variability plots indicate a statistically significant rise in temperature of 1.83°C (Uganda) and 1.7°C (Kenya) from 1901 to 2019. The data strongly suggest that a warming trend has occurred in both regions, which is in accordance with findings within (IPCC) reports, national and academic assessments, and several reports from non-governmental organizations.

14. Precipitation: Climate change poses a significant threat to East Africa's bimodal precipitation models, although mean annual precipitation variability plots indicate no significant trend changes in precipitation within the last 120 years. Anomaly plots derived from the World Bank Climate Portal (2020) show a trend to higher precipitation variability in recent years. Likewise, seasonal variability plots illustrate an altered seasonal occurrence of precipitation (Figure 3 & 4). In Kenya, both short dry seasons and short rain seasons are following a trend of increasing precipitation, whilst long rain seasons illustrate a slight reduction in mean seasonal rainfall over the time series. On the other hand, in Uganda all seasons presented an increasing mean precipitation trend, with the short dry season experiencing the most rapid and statistically significant increase. However, scholars have denoted three key variables that have changed in precipitation patterns in both Kenya and Uganda: (a) failure in the seasonality of rainfall, as precipitation is beginning to occur more erratically and outside of the defined bimodal seasonal structures; (b) higher frequency and severity of heavy rainfall events and droughts; (c) Increased occurrence of the El Niño and La Niña events[14] patterns[15].

[14] Niang et al. (2014)

[15] Kogo, B. K., Kumar, L., & Koech, R. (2020). Climate change and variability in Kenya: a review of impacts on agriculture and food security. Environment, Development and Sustainability, 1-21.

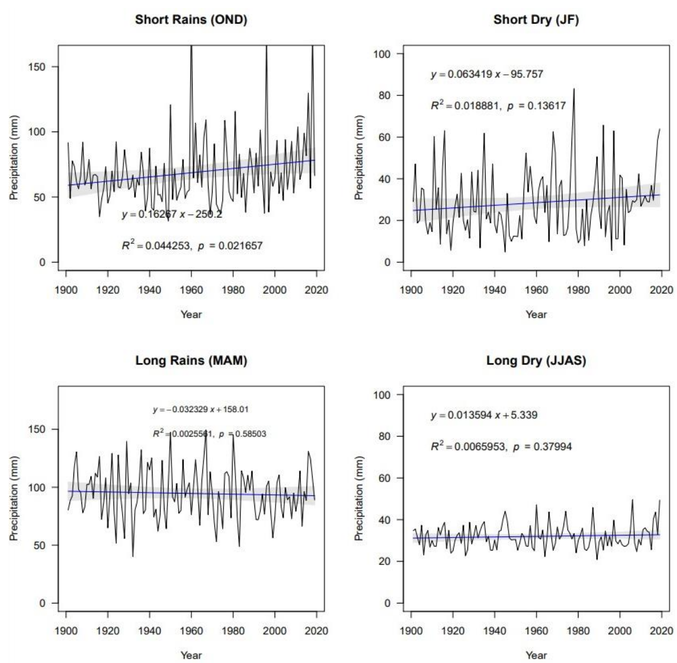

Figure 3. Mean annual seasonal precipitation trends in Kenya in the time series 1900-2019

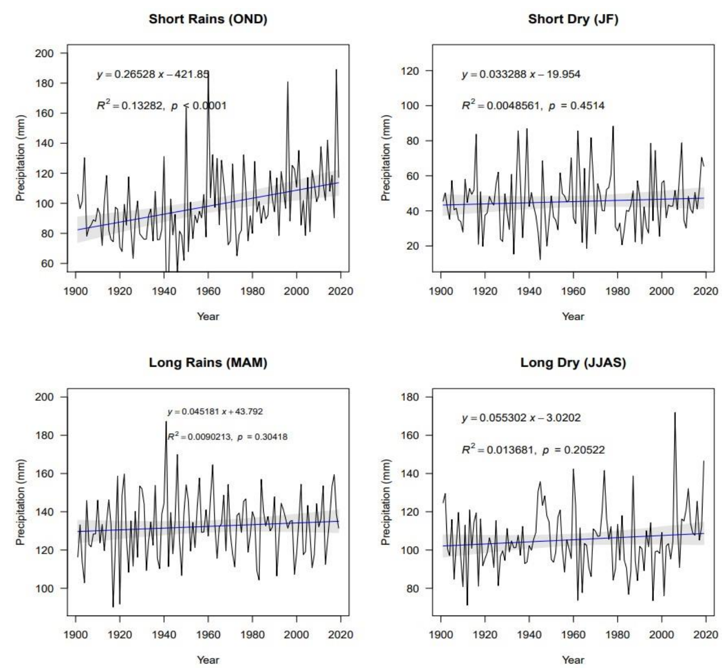

Figure 4. Mean annual seasonal precipitation trends in Uganda in the time series 1900-2019

15. Climate change projections: In terms of temperature, World Bank's shared socioeconomic pathways (SSP) projection 3 (Low mitigation efforts) projects a broadscale warming trend to continue, leading to average annual temperature of 27°C and 28.4°C by 2100 for Uganda and Kenya, respectively (Naing et al., 2014).[16] According to the World Bank, under all SSP scenarios Kenya and Uganda are projected to have a slight increase in temperatures towards the end of the century, particularly during the short rain season[17]. The World Bank and IPCC estimate that there shall also be an increase in "frequency duration, intensity and the proportion of heavy rainfall events" within both countries. However, the dry arid zones in northeastern and northwestern Kenya and northeastern Uganda are projected to experience a decrease in precipitation. Additionally, Kenya as a costal country faces pressures from changing sea level and flooding, it is especially at risk in the city of Mombasa (largest city in the province), Kwale, Mombasa, Kilifi, Tana River, Lamu[18].

Current and future vulnerabilities, risks and impacts of climate change

16. As presented above, Kenya and Uganda's economic structures are highly dependent on agriculture and the availability of water. These two sectors have been selected as their successes are paramount for ensuring adaptive capacity and resilience of vulnerable communities to current and future climactic changes. Kenya has a Human Development Index (HDI) value of 0.61 which puts the country in the medium range (142/189). Uganda ranked low on the HDI as it was valued at 0.483 (163/189). The difference in HDI scores can be attributed to variations in social support systems and economic success between the two countries. In Uganda GNI per capita values are low, with nearly half the value of per capital values in Kenya. As a result, the lack of financial resources halts access to natural resources. Financial availability has been strongly correlated with life expectancy, as individuals with lower incomes have less access to health care services, low food alternatives and high vulnerability to climate related food insecurity. The latter point particularly affects young children, new born and elderly as during moments of food insecurity they are most likely to face severe consequences[19].

17. However, currently both countries have similar life expectancy despite the differences in GNI per capita, as values were estimated at 64 (UG) and 67 (KE)[20]. Education scores relatively high with 88% (Kenya) and 89% (Uganda) of 15-24-year-old being literate. This has been correlated to growing incomes and increased availability in affordable education. Therefore, all in all both countries have had significant improvements in their social conditions, however, low incomes coupled with insufficient access and availability of affordable health care and frequent food insecurity issues have resulted in these numbers remaining relatively low.

18. The following section presents an analysis and justification of the vulnerability of specific sectors to climate change. The section utilizes data gathered from key informant interviews and stakeholder consultations, background desk research, and regional partner research to provide a concise characterization of the agriculture, water sectors and the vulnerability of groups that are dependent on these sectors.

19. Agriculture and climate change: With 75% to 90% of the population within Kenya and Uganda being dependent on rain fed agriculture as a means of livelihood strategies, climate change is a threat to livelihoods especially for small holder farmers[21]. The growing frequency of

[16] Under SSP2 - 27.04°C (KE) & 25.49°C (UG). Under SSP1 – 25.61°C (KE) & 24.41°C (UG)

[17] Climate Risk Profile: Kenya. World Bank (2021); Climate Risk Profile: Uganda. World Bank (2021)

[18] Think Hazard. (2022). Coast of Kenyan risk map. URL: Think Hazard - Coast

[19] World Bank, World Development Indicators. (2020).

[20] World Bank, World Development Indicators. (2020). URL: Employment in agriculture, female (% of female employment) (modeled ILO estimate) | Data (worldbank.org).

[21] World Bank, World Development Indicators. (2020). URL: Employment in agriculture (% of total employment) (modeled ILO estimate) | Data (worldbank.org).

droughts leads to collapse in food production systems as crops fail to grow and livestock die due to lack of water and pasture availability. These droughts have been a major driver of food insecurity and poverty rates throughout the whole of East Africa. The increasing occurrence of extreme precipitation events has caused erosion of crop lands and resulted in permanent alterations in crop productivity and yield potentials.

20. Climate change negatively affects crop production as (1) flash floods wash away crops and soil; (2) Unpredictability and out of seasonal precipitation coupled with warmer temperatures increased the presence of pest and diseases occurrences; (3) Erratic rainfall damages the post-harvest processes for crops that require drying; (4) Heavy rainfall causing erosion that permanently damages agricultural success; (5) Out of seasonal precipitation and cloud cover reduces growth rates by blocking solar radiation; (6) The increased frequency of drought experienced caused crop failure due to in reduced soil moisture, fertility and quality.

21. Although the above-described climate agricultural shocks are felt throughout both countries, its effects have considerably differing productivity impacts depending on the crops under scrutiny. Warmer temperatures in Kenya, for example, negatively affect maize yields but positively affect tea production. Vice versa, increased precipitation has a positive effect on maize and negative results on tea yields[22.] In addition, the climate impacts on agriculture also include the growing risks and challenges associated with pest and disease management[23]. For example, Jaramillo et al. (2011) found that with increasing temperatures came increasing prevalence of the pest berry borer on coffee plantations in East Africa.

22. Evidently, drought-prone areas are highly vulnerable due to agricultural producers' dependency on rain-fed agriculture in both Kenya and Uganda. Droughts and failure in seasonal rainfall are a major challenge for farmers, as during these events crops fail to produce sufficient yield or die due to heat and water stress. However, long-term trends can also result in permanent damages to yields, while frequent droughts and unexpected heavy rainfall events reduce the soil moisture content and quality thus reducing the potential for agricultural growth.

23. The above-described climate change and agriculture nexus can have further severe health implications. Food insecurity is directly linked to health in Kenya and Uganda as failure in agricultural production has a direct effect on communities' nutritional status, susceptibility to diet-related diseases, and overall health status. Currently, the majority of rural populations live below the poverty line and a further 70% is projected to live in food poverty. With changing climate conditions this region has become particularly sensitive to droughts or out of season rainfall. As a result, communities have seen an increase in prices of staple foods and reduced purchasing power due to lower incomes from crop failure. Parallel to this, the COVID-19 pandemic and the Ukraine-Russia conflict have further escalated price shocks and restricted movements within this region pressuring food prices to rise as supply reduced.

24. Water sector & Climate change: Altering seasonal precipitation patterns, extreme precipitation events, frequent droughts and floods are common problems that all sectors in Kenya and Uganda have to start creating adaptation practices towards. With rapid population growth, water availability is expected to dramatically decline in per capita availability regardless of climatic changes.[24] According to the World Resource Institute (WRI) Water Risk atlas, Kenya is considered categorized in a high-water risk scenario[25] with the exception of some areas in the rift value which are considered to have low water risk. On the other hand, Uganda is almost entirely in a medium water risk scenario, with the exception of regions around Lake Victoria.[26] Throughout both countries the following water-climate related challenges affect the population and water resources.

25. Water scarce regions' groundwater and freshwater supplies have been severely depleted or damaged by a failed water abstraction management leading to over-exploitation of water resources. Regions with limited or low water resource availability fail to incorporate co-management systems due to conflicting demands and requirements of different stakeholders. For example, in the cattle corridor, pastoralists migrating from region to region in search of vegetation and water result in growing conflicts between other pastoralists, water resources users, and management practices for regional water resources[27.]

26. Water availability in Kenya and Uganda is extremely variable across each region. The water resource in Kenya and Uganda is an integral part of vulnerable groups socio-economic standing. The majority of employment activities in these areas heavily depend on direct water availability (i.e. agriculture, tourism, energy, manufacturing industries). Currently, it is estimated that per capita freshwater availability is projected to decline by 80% and 73% for Uganda and Kenya respectively[28.] This loss is not primarily due to projected climate changes but the sheer projected mass population growth in both countries is expected to double by the year 2060, thus reducing the overall freshwater availability[29]. The primary driver of this increased water insecurity is the enhanced usage and demand for water resources despite altering precipitation models.

27. The desk research and stakeholder interviews have revealed key vulnerable groups are those in water scarce/ dryland regions. Within Uganda the cattle corridor is particularly vulnerable due to its frequency of droughts. The low-income earning community members requiring water for their cattle are particularly at risk. These communities have very little access to boreholes or water storage technologies due to technological and financial restraints. This is clearly seen on the WRI water stress atlas, as both countries are considered to have extremely high inability to access to improved water sources[30]. At the same time, they predominantly practice agro-pastoralism making

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[22] Ochieng, J., Kirimi, L., & Mathenge, M. (2016). Effects of climate variability and change on agricultural production: The case of small scale farmers in Kenya. NJAS-Wageningen Journal of Life Sciences, 77, 71-78.

[23] Jaramillo, J., Chabi-Olaye, A., Kamonjo, C., Jaramillo, A., Vega, F. E., Poehling, H. M., & Borgemeister,C. (2009). Thermal Tolerance of the Coffee Berry Borer Hypothenemus hampei: Predictions of Climate Change Impact on a Tropical Insect Pest

[24] GIZ: Climate Risk Profile Kenya (2020); GIZ: Climate Risk Profile Uganda (2020)

[25] This refers to the aggregation of all selected indicators from the Physical Quantity, Quality and Regulatory & Reputational Risk categories

[26] WRI. (2022). Aqueduct. URL: Aqueduct | World Resources Institute (wri.org)

[27] Nsubuga, F. N., Namutebi, E. N., & Nsubuga-Ssenfuma, M. (2014). Water resources of Uganda: An assessment and review. Journal of Water Resource and Protection, 6(14), 1297.

[28] GIZ: Kenya (2020); GIZ: Uganda (2020)

[29] Ahmadalipour, A., Moradkhani, H., Castelletti, A., & Magliocca, N. (2019). Future drought risk in Africa: Integrating vulnerability, climate change, and population growth. Science of the Total Environment, 662, 672-686.

[30] WRI. (2022). Aqueduct. URL: Aqueduct | World Resources Institute (wri.org)

them highly dependent on predictable precipitation events for livestock and crops success. Failures in precipitation tend to go hand in hand with increase food insecurity, poverty rates and malnutrition in both countries according to the FAO.[31]

28. Climate change further presents a specific challenge for remote regions with low water access as during extreme rainfall events, waste matter, pollutants, chemical compounds and dangerous biological organisms are washed down into water systems at a more rapid rate[32]. Coupled with increasing temperatures, water-borne diseases are able to develop faster and, in more regions. According to the WHO, water-borne disease is the leading cause of child mortality (children under the age of 5) in Sub-Saharan African countries.

Identified vulnerable regions

29. Coastal regions:[33] Kenya's coast is an important economic zone for East Africa as its ports connect the region's produce with international markets. Currently, the province provides living spaces for 4.3 million Kenyans according to the 2019 national census, and contributed approximately $5.7 billion to Kenya's GDP in 2019 (Kenya National Bureau of Statistics, 2019; Kenya National Census, 2019). However, for the majority of these economic activities operating near coastal regions, sea level rise is a particular concern as it can damage water systems, wash away agricultural land and increase the risk and spread of water borne diseases. In other coastal locations, sea level rise is likely to render more acute the current water supply and salinization problems, as freshwater aquifers are contaminated with saline water. Water logging of soils and the resulting salt stress is likely to reduce crop production. Kenya's broader economy is also at risk from rising seas as coastal and marine resources are critical to economic development through tourism, fisheries, shipping and port activities. Despite these threats the coast has yet to be severely affected, however future projections predict a sea level rise of 0.3 meters has been projected to submerge 4-6km of the largest coastal city, Mombasa [34].

30. Key River/Lake watersheds: A watershed can be defined as the dividing ridge between two different drainage areas. These features are important as they determine the availability of water for certain counties, this proposal has identified 12 (KE) and 18 (UG) counties where the watershed for several important lakes and river is located. According to the desk research conducted, climate change impacts occur differently within these regions. Watersheds areas define almost all areas of land in both countries. However, several watersheds are essential for the provision of water to other regions and communities but remain highly vulnerable to climate change. For example, Lake Naivasha has increased its volume by nearly 30% between 2017 and 2020 due to changes in the hydrological cycle, this caused severe impacts to wildlife, tourism, agricultural production and housing infrastructure. Low income earners located near the shores were most affected as their small holder agricultural plots, fishing grounds and houses were flooded[35].

31. Within these watershed areas, smallholder agricultural producers are the dominant and most vulnerable group. Due to cultural traits, such as the intergenerational distribution of land and the lack of key resources (in all regards), these agricultural producers have very low adaptive capacities. At highlands, producers face yield losses from heavy rainfall, reduced water availability, erosion driven soil quality reductions and landslides. However, at low altitudes agricultural producers face production shocks from floods, droughts, and landslides.

32. Arid/Semi-arid landscapes: Arid and semi/arid regions (ASALs) are landscapes that are characterized by low precipitation rates, high temperatures (during the day and low temperatures during the night) and limited alternative water sources, thus preventing the growth of plant and animal life. The arid/ semi-arid landscapes within Kenya range from Northwestern counties Turukana and Marsabait to the north east counties of Wajir and Mandera. In Uganda, drylands occur in both the northern and southern parts of the country in the central and Karamoja districts. Within both of these countries' dryland areas, smallholder subsistence agriculture and pastoralism are dominant forms of livelihood strategies. Pastoralism is estimated to constitute about 15%of the total agricultural GDP in Kenya and employ more than half of the agricultural labor force. In Uganda pastoralism occurs predominantly within the cattle corridor region (hosting 90% of all cattle in Uganda), which is a stretch of land (43% of Uganda's total area) that runs from the northeast of the country down to the southwestern section. This area hosts an abundance of agro-pastoralists, approximately 27% of the total population, that practice both small holder crop production and pastoralism[36].

33. ASAL regions in sub-Saharan Africa are beginning to experience more frequent occurrences of droughts, altered/shorter rainfall seasons, and higher temperatures. In Kenya and Uganda cyclic drought events have occurred and caused severe crop and livestock losses, famine and displacement. For example, despite food insecurity warnings in Uganda being relatively low this year, Kenya is set to experience a severe famine, as 26-50% lower rainfall was experienced in the OND rains at the end of 2021. Future projections for warmer temperatures, altered precipitation patterns and increased frequency of droughts are likely to hamper the availability of water resources, diminish livestock hers and increase competition over grazing lands in ASAL regions. Moreover, an insufficient land tenure system, poor infrastructure, and social factors (such as migration, low literacy and high poverty levels) limit the farmers' ability to cope with climate change and variability.

34. High Potential Agro-economic Zones: As most of the agricultural production is rain fed, yields are dependent on water availability from precipitation. Due to high operation costs, limited extension services, lack of credit, and insufficient supply of technical equipment, the adoption of irrigation related technologies has been low[37]. As a result of such factors, only 1% (KE) and 0.5% (UG) of cropland is irrigated in both countries (ibid). High potential agro-economic zones are responsible for ensuring steady supply of food in Kenya and Uganda, however, they are particularly sensitive to climate changes. These regions are located in central and western parts of Kenya, and are defined by moderate altitudes with bimodal precipitation structures (table 2). In Uganda, these agricultural zones are also spread throughout the central, western provinces and also adjacent to Lake Victoria (table 2).

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[31] FAO (2019)

[32] Wen, Y., Schoups, G., & Van De Giesen, N. (2017). Organic pollution of rivers: Combined threats of urbanization, livestock farming and global climate change. Scientific reports, 7(1), 1-9.

[33] As a landlocked country, this section is not relevant for Uganda

[34] Kebede, A. S., Nicholls, R. J., Hanson, S., & Mokrech, M. (2012). Impacts of climate change and sea-level rise: a preliminary case study of Mombasa, Kenya. *Journal of Coastal Research*, *28*(1A), 8-19.

[35] Odongo, V. O., van Oel, P. R., van der Tol, C., & Su, Z. (2019). Impact of land use and land cover transitions and climate on evapotranspiration in the Lake Naivasha Basin, Kenya. *Science of the total environment*, *682*, 19-30.

[36] FAO (2019)

[37] AQUASTAT (2002). URL: https://www.fao.org/aquastat/statistics/query/results.html

35. Climate changes occurring in Kenya and Uganda presents high potential agro-economic zones with similar production and yield challenges. Overall, the agricultural industry faces challenges ensuring yields as (a) out of season rainfall and cloud covers hampers growing success; (b) increased frequency of droughts and floods results in permanent damage to soil and crop growth potentials; (c) damage to crops during extreme rainfall events reduces soil quality and harms the plant. It is important to note that not all crops are projected to experience losses and regional distribution should be observed as an important factor, as crops like cassava are projected to increase yields by nearly 25% in Kenya and reduce by 12% in Uganda[38].

36. Major cities and urban agglomerations: Urban areas are known to be more resilient to climatic changes than rural areas as they have greater financial resources, they do not primarily depend on climate factors for economic success, and they have strong water governance measures on abstraction. However, climate change is expected to increase temperatures most severely in urban areas due to the urban heat effect. For example, according to the climate risk profile assessment by GIZ, Uganda's heat-related mortality is projected to increase by a factor of four by 2080 thus increasing those at risk from 0.2% to 9.5% of the total population. Similarly, projections for Kenya indicate that this figure will increase from 0.6% to 6.0% of the total population by 2080[39].

37. Urban areas are also at risk of floods. According to desk research the major cities including Nairobi, Mombasa, Kampala, Entebbe frequently face climate related floods and are areas of concern for the future. Table 2, has further clarified all high-risk areas that were identified in the desk research for each country. The community members most affected are those living in unregistered housing areas (slums) as their low housing quality, lack of drainage systems and close proximity to rivers results in direct impacts during heavy rainfall events.

Identified vulnerable segments of the population

38. Smallholder Farmers: Smallholders have been highlighted by both national governments, NGOs, and academics as key to ensuring food security in developing countries. Unfortunately, these smallholder producers are generally the most vulnerable to climate-related shocks due to their low adaptive capacities. This lack of capacities to adapt is due to their inadequate access to resources (financial, technological, human), unstable markets, poor infrastructure and insufficient access to external expertise to guide them on adaptation practices.

39. Pastoralists: In terms of livestock production, Kenya and Uganda have cultural and traditional traits that are linked to pastoralism. The dominant tribal groups who practice pastoralism are the Maasai, Kalenjin, Somali, Turkana, Oromo and Rendile in Kenya, this group is wide spready but 50% is based in the north western and north eastern provinces; and the Bahima/Abanyankole, Karamojong, Basongora, Itesot, Baruli and Banyarwanda in Uganda, interestingly, pastoralism is stretched across 42% of the country in a pastoralist bank known as the cattle corridor. However, animal husbandry is a highly climate sensitive industry as production success is determined by precipitation and grassland availability. With increasing frequency and severity in droughts and failure in seasonal rainfall, producing livestock has faced new challenges is accessing grazing lands, pressures from diseases (such as rift valley fever), or water sources from their animals to hydrate[40].

40. Women in agriculture: Although male and female farmers equally experience climate change-related effects, the adaptive capacities to climate change in agriculture vary significantly among male and female-headed households. This is as a result of cultural and customary law barriers that affect the interaction with agriculture. For example, Ugandan and Kenyan women usually grow annual crops that are of less value, earning less money, and these annual crops are mainly food crops. Men are engaged in planting mostly high value crops (that earn more money) e.g. coffee and tomatoes and are involved in cattle rearing. Therefore, when experiencing a climate shock, women tend to face larger financial burdens as their already limited financial resources is further restricted. Whereas, seeing men engage with higher value crops they are likely to be more financially equipped to tackle certain climate challenges.

41. In conjunction with this is their barrier to accessing financing from financial institutions (FI). FIs enable men and women to invest, improve and develop their agricultural resources to be further resilient to climate change. However, as men are the predominant owners of land they are able to take loans and utilize their land as collateral. However, women who already face restricted landownership, due to customary law, are unable to attain commercial finance due to their inability to provide collateral. This is a critical barrier for women as with reduced financial availability they are less likely to invest or develop their agricultural produce, especially during climate shocks.

42. Rural saving schemes (such as Chamma or Savings and Credit Cooperative Organisations (SACCOs) have been paramount to ensuring some form of financial services and lending for female farmers in Uganda and Kenya as they often offer more favorable lending conditions than commercial banks. This is due to the high interest rates from commercial financing and many times the business plans do not adequately account for women's labor which makes farming not as profitable for women and further hinders access to financing to implement CSA technologies and practices due to their high upfront costs. Additionally, spending patterns among male and female-headed households vary significantly. Informal loans were more likely to be utilized by female-headed households on food, health and education, while formal loans are more commonly utilized by male-headed households on agriculture/ livestock inputs, food and education.

43. Youth and agriculture: The success of agricultural production can have direct impacts on children and youths' abilities to live sustainable lives. In cases of agricultural failure, children can suffer from food-related illnesses that can directly affect their ability to perform in school or even lead to developmental delays. Parallel to this, failure in crop production can put financial constraints on family's abilities to pay school tuition for their children thus reducing their ability to search for other jobs outside of the agricultural or other low skilled jobs. As a result, youth in such scenarios tend to remain dependent on this subsistence agriculture if they choose not to migrate. Others may choose to move to urban centers with the hope of attaining higher paying stable jobs, however, the lack of education, low demand for low-skilled labor and high living costs tends to leave these individuals in low-income settlements. Therefore, strengthening the success, resilience and adaptive capacity of agricultural producers can help in protecting youth from more vulnerable situations.

[38] GIZ: Kenya (2020); GIZ: Uganda (2020)
[39] GIZ: Kenya (2021); GIZ: Uganda (2021)
[40] Twinomuhangi, R., Sseviiri, H., Mfitumukiza, D., Nzabona, A., Mulinde C. (2022) Assessing the evidence: Migration, Environment, and Climate change nexus in Uganda. Makerere university center for climate change and innovations.

44. Communities without access to improved drinking water: As presented above water access is highly dependent on individuals' access to drinking water, their regional location (urban/rural), the main ecosystem type (drylands, forested, etc.), and their requirements and demand for daily life. In Kenya and Uganda water access is strongly affected by the ecosystem type and evidently as presented above the arid/ semi-arid regions have the least available amounts of water. According UNICEF, 56% and 69% of people in Kenya and Uganda have access to safe drinking water.[41,42] Despite these values being relatively high, rural areas are more secluded from access to improved drinking water sources due to an insufficient government investment in remote water infrastructure and technological challenges relating to storage and maintenance of fresh water that occurs in these regions. In Kenya and Uganda ASAL areas and low-income urban areas are high risk areas due to the unavailability of improved water sources (Table 2).

1.3. Adaptation SMEs

45. **Role of SMEs in the economy of Kenya and Uganda:** A small and medium sized enterprise (SME)[43] operates on a relatively small scale, both in terms of employment and the economic outputs they create (assets and annual sales). The project will use the official definitions according to the Micro and Small Enterprises (MSEs) Bill 2012 of Kenya and the definition provided by the Uganda Investment Authority (UIA). Despite their small scale, SMEs play a fundamental role, especially in developing economies as they help reduce poverty rates through job creation and substantially contribute to economic growth. Likewise, they are fundamental for providing equitable jobs and entrepreneurship avenues for women, youth and other vulnerable groups. SMEs play quintessential role in reducing the gender gap as they promote and ensure the effective participation of women in national economies.

46. The SME sectors account for approximately 80% and 90% of the private sector and contribute 35% and 75% of the total GDP in Kenya and Uganda' respectively. Additionally, the SMEs in both the formal and informal sector have been found to be job engines. As a result, 14.9 million and +3 million people are estimated to be employed by this sector in Kenya and Uganda. Aside from the socio-economic importance of SMEs, these enterprises are spread differently in each country. In Kenya, according to recent survey by the Kenyan Banker's Association and JICA, these enterprises are spread throughout all sectors but were predominantly present in wholesale and retail trade, followed by information and communication technology and then agriculture. Similarly, in Uganda, enterprises are predominantly concentrated in the service sector, with agriculture closely following up. In addition, in both countries micro enterprises consist of the largest proportion of enterprises. Representing the lion's share of enterprises in the two economies, these SMEs operate on community level and increasingly target vulnerable populations at the bottom of the pyramid, consisting of customers, employees or partners along their value chain. They further provide adaptation solutions that are locally sourced, affordable and tailored to vulnerable communities' needs.

47. **SMEs as providers of local adaptation technologies, products and solutions:** National and large-scale approaches to generating adaptation solutions on a small-scale frequently fail to recognize the discrepancies that exist in different contexts[44]. Likewise, macro level planning has also been criticized for their failure to include marginalized groups. SMEs as the backbone of the Kenyan and Uganda economies are key to empowering vulnerable communities as they are aware of the context-specific climate challenges individuals and communities are facing. SMEs have local knowledge because they tend to operate, adapt and sell their products within the region they are based, this is particularly useful in terms of climate adaptation as they are aware of the intersections between location-specific climate, environmental and socio-economic factors and context-specific challenges communities are facing with regard to climate change. This can also be used as a force to educate as they can inform community members on the importance and benefits of operationalizing certain adaptation strategies[45].

48. Parallel to understanding the contextual challenges, SMEs provide products that are affordable and accessible to the surrounding community/ vulnerable target groups. SMEs can also frequently adapt and alter their products which makes them ideal providers of adaptation technologies, a feature that challenges larger corporates who must undergo bureaucracies that restrict timely changes. Furthermore, they develop market-based viable business models for the deployment of their adaptation products and services. All in all, SMEs that focus on providing adaptation solutions can ensure better integrated adaptation practices that support NCAP's and NDC's.

49. This project defines adaptation SMEs in accordance with the Adaptation Solutions Taxonomy framework developed by the Adaptation SME Accelerator Project (ASAP)[46] funded by the Global Environmental Facility (GEF): An Adaptation SME is a company providing technologies, products and/or services (TPS) that: Address systemic barriers to adaptation, by strengthening user's ability to understand and respond to physical climate risks and related impacts and/or capture related opportunities AND/OR contribute to preventing or reducing material physical climate risk and/or the adverse associated impacts on assets, economic activities, people or nature AND do no harm and generate long term value. The selection of adaptation SMEs for this project will be guided by the Climate Risk and Adaptation SME Solution Matrix (see Part I, Chapter 1.5) listing eligible adaptation solutions for the identified vulnerable regions and groups.

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[41] UNICEF. (2020). 'Make A Splash!' Partnership Progress Report. URL: Sanitation and Hygiene for All | UNICEF Kenya

[42] UNICEF. (2019). UNICEF Uganda annual report 2019. URL: UNICEF_UgandaAR2019-WEBhighres.pdf

[43] The project will facilitate access to finance for early-growth SMEs, excluding Micro enterprises as they are not be eligible for the loan sizes targeted nor in the position to absorb these. The project indirectly also benefits Micro enterprises as they form part of the beneficiary SME value chains respectively are their customers.

[44] Baker, I., Peterson, A., Brown, G., & McAlpine, C. (2012). Local government response to the impacts of climate change: An evaluation of local climate adaptation plans. Landscape and urban planning, 107(2), 127-136

[45] Naess, L. O., Newell, P., Newsham, A., Phillips, J., Quan, J., & Tanner, T. (2015). Climate policy meets national development contexts: Insights from Kenya and Mozambique. Global Environmental Change, 35, 534-544.

[46] https://lightsmithgp.com/wp-content/uploads/2020/09/asap-adaptation-solutions-taxonomy_july-28-2020_final.pdf

1.4. Climate Risk and Adaptation SME Solutions Matrix

50. The following matrix is a result of the Climate Risk and Vulnerability Assessment, as well as an in-depth market assessment of adaptation business models conducted in preparation of this Concept Note. It gives a preview of eligible adaptation solutions for the vulnerable regions and groups identified under Part I. The selection of adaptation SMEs to receive support under this project will be guided by the identified adaptation solutions

Table 2. Kenya's & Uganda's regional, sectoral and group vulnerability to climate change and identified solutions provided by adaptation SMEs

Region	Main counties	Main climate challenges	Most climate vulnerable socio-economic sector & group	Potential /Current solutions provided by adaptation SMEs
River/Lake watershed ecosystems	**Kenya:** Nakuru, Baringo, Kajiado, Busia, Homabay, Kakamega, Kisumu, Siaya, Kericho, Migori, Nyandarua, Tana River **Uganda:** Hoima, Masindi, Nebbi, Gulu, Apac, Lira, Soroti, Kumi, Pallisa, Mpigi, Masaka, Fort Portal, Bugiri, Iganga, Mukono, Luwero, Mubende	**Kenya:** **Overall**: Unstable hydrological flows **Main variables:** 1) Extreme weather events (droughts/floods) 2) Altered and more extreme hydrological cycles 3) Altered precipitation and cloud cover patterns **Uganda:** *High elevation:* 1) Heavy and out of season precipitation causing landslides, flooding, erosion, and soil degradation 2) Increased occurrence and frequency of droughts *Low elevation:* 3) Heavy precipitation events causing increased loading of chemical and organic compounds in lake ecosystems 4) Unstable precipitation patterns causing more variable lake and river ecosystems.	**Sector: Agriculture** • Reduced crop yields for lake ecosystem agricultural industries due to flooding and out-of-seasonal rainfall (1 & 2) • Crop failure from altered precipitation patterns (2 & 3) • Changes in fish availability due to reduced water quality, eutrophication and poisonous compounds flushed into river systems (1,2). *Key vulnerable actors:* • *Agricultural producers near lakes and rivers or in low elevation areas* • *Small holder agricultural producers without water storage or protected cultivation systems* **Sector: Water** • Lakes and rivers become more unstable from changing climatic conditions resulting in flooding and dropping water levels (1,2,3) • Flooding-related damages to infrastructure (1) • Low hydro-Energy Output (1 & 2) • Pooling of water increases risk for water & vector borne diseases such as malaria, typhoid bilharzia, etc. (1, 2) *Key vulnerable actors:* • *Hydro energy producers and low-income earning energy consumers. Failure in hydro production can lead to fluctuations in energy prices* • *Community members residing near lakes and rivers* • *New born children, pregnant women, elderly and young children are highly vulnerable to agricultural failures and water borne diseases*	**Agricultural production and fisheries:** • Weather & Climate Information Systems (WCIS, e.g. weather forecasting systems) • Protected cultivation systems (e.g. greenhouses) • Integrated Soil Fertility Management (IFSM, e.g. organic fertiliser) • Pest/disease and drought-resistant crops • Fish stock reloading services • Agricultural extension services • Bio pesticides • Media educational programs for climate smart agriculture • Index based livestock insurance • Farming Equipment Leasing **Water management** • Water storage and harvesting systems • Drip irrigation and hydroponic systems • Water resource regulation (e.g. riparian management) • Reforestation programs • Smart sanitation and water purification systems
High Potential Agro-economic Zones	**Kenya:** Likipia, Nakuru, Nyandarua, Kiambu, Nyeri,	**Kenya:** **Overall**: Unstable precipitation patterns **Main variables:** 1) Extreme rainfall events	**Sector: Agriculture** **Kenya:** • Agricultural producers experience crop failure, lower yields, damaged soils (moisture, quality, carbon), and increased pressure from pests	**Agricultural production** • WCIS (e.g. weather forecasting systems) • Protected cultivation systems (e.g. greenhouses)

<table>
<tr><th>Region</th><th>Main counties</th><th>Main climate challenges</th><th>Most climate vulnerable socio-economic sector & group</th><th>Potential /Current solutions provided by adaptation SMEs</th></tr>
<tr><td></td><td>Uasin Gishu, Embu, Makueni, Kajiado, Machacos,

<u>Uganda:</u>
Apac, Masindi, Lira, Jinja, Soroti, Kumi, Kamuli, Luwero, Mukono,Mbarare, Masaka, Rukungiri, Bushenyi, Kabale, Kisoro</td><td>2) Altered and more extreme hydrological cycles
3) Altered precipitation and cloud cover patterns
4) increasing frequency of droughts

<u>Uganda:</u>
Overall: Highest projected positive change in average temperatures, extreme heat
Main variables:
1) Extreme weather events (droughts/floods)
2) Altered and more extreme hydrological cycles
3) Altered precipitation and cloud cover patterns</td><td>and diseases during extreme and out of season rainfall events (1, 2, 3, 4).
<u>Uganda:</u>
• Reduced crop yields and quality (particularly for rainfed agriculture) due to higher temperature and/or lack of regular rainfall (1,3)
• Crops losses due to extreme weather events (2)
• Soil degradation due to increased temperatures and extreme weather events (1,2,3)
Key vulnerable actors:
• Small holder agricultural producers without water storage, protected cultivation systems and other essential adaptation technologies
• Women involved in agricultural production, especially single mothers.
Sector: Water
<u>Kenya:</u>
• Flooding related damages to infrastructure (1)
• Pooling of water increases risk for water & vector borne diseases such as malaria, typhoid bilharzia, etc. (1)
<u>Uganda:</u>
• Contamination of water sources (1, 2)
• Damage to already Insufficient water storage systems (1,2)
• Hydro-power production failures (1,2)
• Pooling of water increases risk for water & vector borne diseases such as typhoid and bilharzia, etc. (1, 2)
Key vulnerable actors:
• Damage to roads reduces access to markets for agricultural producers
• Young children, elderly and pregnant women are most susceptible to these diseases
• Community members residing near lakes and rivers (Uganda)</td><td>• ISFM
• Pest/disease and drought-resistant crops
• Agricultural extension services (including intercropping techniques, agroforestry, climate smart agricultural practices, sustainable agricultural practices)
• Farming equipment leasing
• Bio pesticides
• Media educational programs for climate smart agriculture
• Index based livestock insurance

Water management
• Flood protection technology
• Drip irrigation and hydroponic systems
• Smart sanitation and water purification systems</td></tr>
<tr><td>Arid/Semi-Arid Landscapes of Northern Kenya

For Uganda, specifically the “Cattle Corridor“</td><td><u>Kenya:</u>
Mandera, Wajir, Garissa, Isiollo, Marsabit, west pokot, Mandera.

<u>Uganda:</u>
Kotido, Moroto, Soroti,</td><td>Overall: Increasingly drier climate; Droughts are becoming more extreme and frequent

Main variables:
1) Increasing frequency of droughts
2) Altered precipitation and cloud cover patterns</td><td>Sector: Agriculture
• Crop failure and severe crop damage and livestock losses due to prolonged drought periods (1)
• Partial yield losses due to locust pests (3)
• Reduced soil quality due to intensified erosion dynamics (1, 2 & 4)
• Livestock losses and increased livestock stress due to lack of vegetation and water (1,2)
Key vulnerable actors
• Pastoralist and agricultural producing communities.</td><td>Agriculture production
• WCIS (e.g. weather forecasting systems)
• Locust warning systems
• Protected cultivation systems (e.g. greenhouses)
• ISFM
• Pest/disease and drought-resistant crops
• Animal feed storage facilities
• Farming equipment leasing
• Solar borehole solutions</td></tr>
</table>

Region	Main counties	Main climate challenges	Most climate vulnerable socio-economic sector & group	Potential /Current solutions provided by adaptation SMEs
	Lira, Apac, Kumi, Luwero, Kiboya, Kibale, Mubendu, Sembabule, Marare, Rakai	3) Cyclone driven locust swarms 4) rare but extreme rainfall events	• *New born children, pregnant women, elderly and young children are highly vulnerable to fluctuations in food availability.* • *Chronic dehydration can hamper childhood and prenatal development.* • *Pastoralists are at risk of conflict related mortality.* **Sector: Water** • Severe decline in fresh water availability both above ground and in underground storage (1) • Contamination of water sources (1,3) • Damage to already Insufficient water storage systems (3) *Key vulnerable actors* • *Pastoralist and agricultural producing communities with limited access to water sources.* • *Chronic dehydration can hamper childhood and prenatal development.*	• Bio pesticides • Improved seed and livestock breeds • Agricultural extension services (including intercropping techniques, agro forestry, climate smart agricultural practices) • Media education on adaptation avenues • Index based livestock insurance **Water management** • Water storage and harvesting systems • Drip irrigation and hydroponic systems • Smart sanitation and water cleaning systems • Drought and food security early warning systems
Major cities, urban and rural agglomerations	No specified county: predominantly low-lying areas High risk Cities Kenya: Nairobi, Mombasa, Naivasha, Kisumu, Nakuru, High risk cities Uganda: Kampala, Entebbe, Jinja, Soroti.	**Overall**: damage to local infrastructure and communities from extreme rainfall events and high temperatures **Main variables** 1) Increased frequency of extreme rainfall events causing flooding and landslides. 2) Severe warming caused by urban heat effect and Climate change 3) Altered and more extreme hydrological cycles (only Uganda) 4) Altered precipitation and cloud cover patterns (only Uganda)	**Sector: Agriculture** • Limited damage due to the little amount of producers *Key vulnerable actors* • *Urban crop producers face financial losses from production failures* **Sector: Water** • Long term damage to water systems and storage (1) • Communities living in low quality housing face damages and in some cases become displaced. These migrants face risks from food insecurity and other diet related issues. (1) • Pollution of drinking water systems increases the presence of water borne diseases. (1,2,3) • Old and young generations are at risk of heat stroke during high temperatures due to metal housing heat insulation (2). • Pooling of water increases risk for water & vector borne diseases such as malaria, typhoid bilharzia, etc. (1, 2) *Key vulnerable actors* • *Low income earners living in low quality housing areas (i.e. Kibera slum)* • *New born children, pregnant women, elderly and young children vulnerable to heat related mortality and water borne diseases.*	**Water management** • Water storage and harvesting systems • Improved drainage systems and flood barriers have been installed. • Improved housing infrastructure (including ventilation/cooling systems, concrete walls, etc.). • Irrigating gardens, urban farms-decentralised water storage facilities • Flood protection technology • Water infiltration and attenuation systems • sewer system clean-ups • Flood warning systems • Smart sanitation and water cleaning systems • Disease Surveillance Systems

1.5. Problem Statement

51. The proposed project aims to specifically address three key barriers in Kenya and Uganda:

<u>**Lack of coordinated approach towards role of adaptation SMEs**</u>

(1) **Vulnerable communities as identified in Part I have no or limited access to adaptation solutions** and are particularly susceptible to the negative effects of climate change due to insufficient adaptive capacities, a result of inadequate access to resources (financial, technological, human), unstable markets, poor infrastructure and insufficient access to external adaptation expertise. This is particularly relevant for vulnerable communities in high-vulnerability geographies such as ASALs or high potential agro-economic zones.

(2) **Kenya and Uganda's public institutions are overwhelmed by the task of increasing the resilience of vulnerable communities** due to the lack of funds, inadequate enforcement of national-level climate action policy frameworks and overlapping institutional competencies.

(3) The **private sector** has the potential to leverage climate change adaptation as an increasingly growing business case. **Its adaptation solutions, however, are not targeted towards the specific, contextualized needs of vulnerable groups**.

<u>**b) Lack of access to appropriate finance and support to support growth-stage adaptation SMEs**</u>

(4) **SMEs**, **Kenyan and Ugandan SMEs face severe challenges to sustain, grow and replicate their business models due to shortages in available capital** as they are largely underserved by FIs – referred to as the "missing middle" financing gap[47]. Below figure further highlights this "missing middle", depicting how early-growth stage SMEs are too big for micro-financing but too small for commercial banks. Concrete obstacles for such SMEs to access commercial loans or equity finance include collateralization, prohibitive risk ratings for young and small enterprises, and high interest rates. Hence SMEs are hampered to move beyond the scale of "micro" and expand business activities.

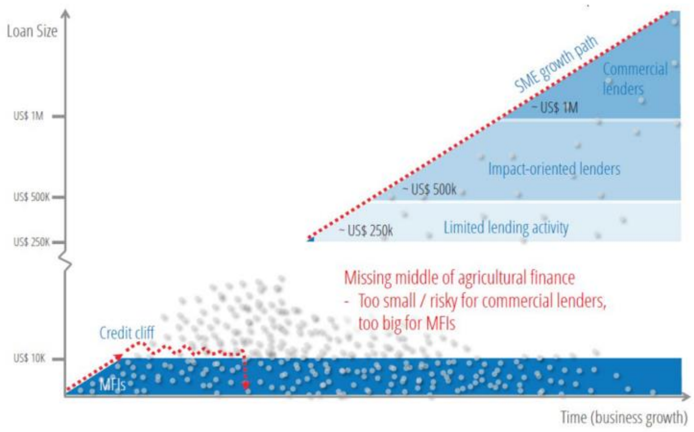

Figure 1: Finance opportunities of SMEs[48]

(5) The **lack of gender and youth inclusive investment opportunities is exacerbated,** as women and youth led enterprises mostly operating in the informal sector and suffering from a limited access to land and other collateral, lack of networks and knowledge resources, and legal and policy obstacles to business ownership and development.

(6) SMEs in the two countries also **lack tailored investment business advisory** for financial planning and management to move from grant and donation-based financing towards accessing commercial capital. Although there is a series of business incubators active in Kenya and Uganda, their focus is mainly on early-stage business support. Hence, there are few opportunities for SMEs offering pre- and post-investment support to develop the required financial records and management structures to access and absorb commercial capital investments.

<u>**c) Financing institutions do not support adaptation SMEs**</u>

(7) **High-impact SMEs that directly address climate change adaptation** through their tailored products and services **disproportionately experience the lack of appropriate commercial financing.** This is due in part to the unfamiliarity of FIs and investors with climate change-related business models and growth trajectories, which tend to involve (perceived) riskier technologies and longer timeframes to go to market. FIs and other investors struggle to understand and respond to the financing needs of adaptation SMEs with tailored financial products[49] that, for example, align lending requirements with readily available collateral, repayment periods with seasonality of businesses, enable investments in resource-efficient technologies and more.

(8) On the supply side of commercial capital providers, **available SME financing tends to be dominated by smaller ticket sizes, shorter repayment periods and a lack of diversity of financing models** tailored to SME needs[50]. Furthermore, larger-scale capital (above the scale of microfinance) needed to move beyond the start-up stage is mostly reserved for a small sub-set of high growth SMEs.

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[47] This gap in financing is estimated to affect between 50-70% of formal SMEs in emerging economies. Source: World Bank Group (WBG, 2019): World Bank Group Support for Small and Medium Enterprises.

[48] https://rootcapital.org/resources/how-impact-linked-financing-incentivizes-high-impact-investment-in-agricultural-smes/

[49] International Finance Corporation. (2017). MSME Finance Gap.

[50] International Trade Centre (ITC, 2019): Big money for small business. Financing the Sustainable Development Goals.

Despite varying definitions, the capital typically needed to address this financing gap is for investments of between USD 20,000 – 500,000 per enterprise with a medium to long-term time horizon or tenure – typically above the scale of microfinance and below that of traditional lenders and equity investors[51].

(9) As stakeholder consultation with FIs in Kenya and Uganda have shown, there is increasing commitment of the banking sector to comply with international sustainability frameworks while regulatory pressures are also building up to incorporate climate change considerations into bank operations. At the same time, **adaptation-based lending in the two countries is insufficiently anchored in FI investment strategies** as FIs lack climate (adaptation) strategies that lay out lending guidelines and indicators for adaptation-based finance in line with national climate action policies.

1.6. Proposed Solution and project objective

52. In light of these challenges, the project seeks **to realise the potential of adaptation SMEs to provide cost-effective and localised adaptation solutions to vulnerable communities in climate change-susceptible geographies** (both defined in Part 1) in Kenya and Uganda. It therefore aims at increasing vulnerable groups' climate change resilience through fostering and scaling commercially viable adaptation solutions offered by SMEs – thereby generating positive and sustainable economic externalities particularly benefitting vulnerable groups that are integrated in SMEs' value chains.

53. Addressing the lack of access to financing for adaptation SMEs in Kenya and Uganda to cater to deliver solutions to vulnerable groups, the project is centred around the design of an **innovative catalytic adaptation finance facility** (supply side) to facilitate adaptation SMEs' access to commercial investment capital. The facility is based on a **pioneering performance-based blended financing mechanism**, whose innovativeness lies both in its de-risking blended financing instruments with performance-based payments and its inclusive approach to co-creatively integrate local FIs, local impact investors and venture funds at design, investment and post-investment level. To increase the availability of targeted adaptation solutions for vulnerable communities, the project further **develops a pipeline of bankable market-based adaptation SMEs** (finance demand side).

54. At the same time, the project provides **capacity development and strategy support to local FIs** to anchor climate adaptation in their investment strategies. As an overarching pillar, the project will work towards an **enabling financial ecosystem and policy framework** that unlocks adaptation SMEs' transformative climate action potential. Given that the economies of Kenya and Uganda are predominantly made up of SMEs, the proposed project takes a specific **focus on gender- and youth inclusive adaptation SMEs as promoters of an increased local climate resilience** while also contributing to overcome gender and/or other socio-economic inequalities in the vulnerable communities they operate in.

55. Project Objective: The project objective is to achieve transformational change in local financial markets in Kenya and Uganda to become more inclusive towards early-growth women- and youth inclusive adaptation SMEs for them to realises their full potential in providing innovative climate adaptation solutions to highly vulnerable groups, enhancing local climate resilience in the agriculture and water sector while addressing and rectifying gender and/or other socio-economic inequalities exacerbated by climate change. The project seeks to have a transformational impact on the agriculture and water sector, making them more robust and mitigating climate change impacts by introducing sector-specific, innovative adaptation practices that are financially viable and have a standing track record with FIs in the two countries. The showcasing of bankable adaptation SME business models intends to have a spill-over effect within the two sectors, promoting good adaptation practices as a market opportunity for SMEs while opening new avenues for adaptation SMEs to grow and scale their business models.

56. The project will be structured around three Components:

I. Establishing a **Regional Coordination Platform (RCP)** that serves as a pioneering regional knowledge platform for Kenya and Uganda on adaptation entrepreneurship to connect actors in the fields of adaptation, climate-smart finance and entrepreneurship, promote knowledge management and cross-learning and encourage action to sustain and create markets for early-growth gender- and youth inclusive adaptation SMEs.

II. Pilot an innovative **performance-based blended financing scheme** to facilitate and leverage previously inaccessible commercial finance of partnering FIs to selected gender- and youth inclusive adaptation SMEs, supporting them to scale their adaptation impacts on vulnerable groups in Kenya and Uganda. A combination of unique financial instruments will be co-created and rolled out together with financers.

III. Promote a **conducive financial ecosystem** by increasing local FI's awareness and knowledge on gender- and youth inclusive adaptation SMEs' business solutions and financing needs, and supporting FIs to develop tailored financial products and institutional climate strategies to anchor climate adaptation in their investment portfolios and internal structures.

57. **Definition of focus target group for this project:** This project focuses on gender- and youth inclusive adaptation SMEs in Kenya and Uganda that provide climate adaptation solutions for the agriculture and water sectors in regions that are highly vulnerable to climate change. Gender- and youth inclusive adaptation SMEs combine characteristics typically associated with smaller enterprises such as local embeddedness and the inclusion of vulnerable communities in their value chains with an adaptation-geared business rationale. They contribute to rectify gender and/or other socio-economic inequalities by providing products and services that close gender gaps or meet the needs of women, girls or youth. Furthermore, they support gender diversity and the participation of youth (e.g. as part of the workforce) and strengthen inclusion and diversity across their value chains.

[51] Dutch Good Growth Fund (DGGF, 2016): New Perspectives on Financing Small Cap SMEs in Emerging Markets.

1.7. Project components and financing

Table 3. Project components and financing breakdown

Project Components	Expected Outcomes	Expected Outputs	Coun-tries	Amount (US$)
1. Regional coordination platform to connect adaptation, climate-smart lending, entrepreneurship, knowledge management and promote cross-learning	1.1 The project establishes a sustainable coordination, network and knowledge platform for and between adaptation entrepreneurs, adaptation stakeholders and (future) adaptation financiers across Kenya and Uganda	1.1.1 Establishing a multi-stakeholder Adaptation Action Steering Committee 1.1.2 An administrative and functional structure for the RCP is developed and endorsed	Kenya, Uganda	250,000
	1.2 Key stakeholders, ministries, financial institutions (FIs), adaptation SMEs and the end-users (vulnerable groups) create and sustain market for adaptation technologies, services and products	1.2.1 Regular regional Adaptation Action Events are organised 1.2.2 Annual Adaptation Finance Symposia are developed and held 1.2.3 Knowledge products on market-based adaptation solutions and impact of gender- and youth inclusive adaptation SMEs are developed (including the benefits for vulnerable communities and target sectors) and widely disseminated		
2. Innovative performance- based blended financing mechanism, investment brokerage services and direct enterprise support	2.1 Developing and implementing the project's enterprise support infrastructure	2.1.1 Scorecard (incl. final selection criteria) for the assessment of at least 100 early-growth gender- and youth-inclusive adaptation SMEs is co-created 2.1.2 Pipeline of at least 60 gender- and youth inclusive adaptation SMEs built for funding readiness support (100% of the SMEs will be women- and/or youth-inclusive, meaning they aim for a 50% gender and youth balance in their work force and/or their primary customer base)	Kenya, Uganda	121,000
	2.2 Supporting gender- and youth inclusive adaptation SMEs from funding readiness to investment and post-investment management	2.2.1 Two Catalyser Programme Cycles: Business advisory support to achieve funding readiness for 60 shortlisted gender- and youth-inclusive adaptation SMEs provided 2.2.2 Two Accelerator Programme Cycles: Post-investment support on growth and loan repayment provided for 30 gender- and youth-inclusive adaptation SMEs	Kenya/ Uganda	600,000
	2.3 Designing and implementing blended financing mechanism and performance-based payments for gender- and youth inclusive adaptation SMEs	2.3.1 Development and refinement of performance-based blended financing scheme 2.3.2 Mobilising at least 15 partner Financial Institutions (FIs) 2.3.3 Implementing performance-based blended financing instruments and portfolio management 2.3.4 Exit and scale-up strategy for innovative adaptation SME financing mechanism developed and operationalised	Kenya, Uganda	2,550,000
	2.4 Potential environmental and social risks of selected SMEs screened, assessed and monitored within the framework of the Environmental and Social Management System (ESMS)	2.4.1 A comprehensive ESMS for SMEs to receive technical and finance support is implemented	Kenya, Uganda	100,000
3. Local financing institutions support gender- and youth inclusive adaptation SMEs	3.1: Local financing institutions support the dissemination of adaptation technologies, products and services	Output 3.1.1: An Adaptation Finance Academy training concept is developed and implemented	Kenya, Uganda	350,000
4. Project/Programme Execution Cost				437,295
5. Total Project/Programme Cost				4,608,295
6. Project/Programme Cycle Management Fee				391,705
Amount of Financing Requested				5,000,000

1.8. Project calender

Table 4. Project Calendar

Milestones	Expected Dates
Project Inception Phase	October 2023
Start of Project Implementation	October 2024
Mid-term Review (if planned)	October 2026
Project Closing	October 2028
Terminal Evaluation	December 2028

PART II: Project JUSTIFICATION

A. Project components description

58. At the core of the proposed project lies the support of adaptation entrepreneurship based on a multi-directional project design. Key to this design is the three-pronged approach of
    1) Ensuring that adaptation entrepreneurship gains access to markets and partners and takes centre stage in national and regional policy and finance regimes (Component I)
    2) Piloting innovative and performance-based blended financing instruments coupled with targeted pre- and post-investment advisory support[52] (Component II) and thereby incentivising local FIs to bridge the missing middle financing gap for early-growth gender- and youth inclusive adaptation SMEs;
    3) Training FIs in adaptation finance to develop their own climate strategies and prototype innovative finance instruments[53] tailored for gender- and youth inclusive adaptation SMEs (Component III), thus broadening investment product portfolios and anchoring adaptation finance institutionally;

<u>Theory of Change</u>

59. By introducing an innovative approach for the delivery of tailored financial support to adaptation SMEs and establishing a pipeline of scalable adaptation SMEs, the project addresses the missing middle financing gap for SMEs. The project will systematically transform the financial ecosystem in Kenya and Uganda. This will enhance the delivery of private sector adaptation solutions that are localised, affordable and tailored to the needs of climate change-vulnerable communities, resulting in substantially improved adaptive capacities for groups susceptible to the negative socioeconomic effects of climate change.
The scenario of scaled gender- and youth inclusive adaptation SMEs support would have sizeable impact on the adaptive capacities of vulnerable groups in Kenya and Uganda – especially with regards to small-scale and rain-fed farmers as well as low-income communities susceptible to the effects of floods and droughts. Women and youth would directly benefit from the employment and economic empowerment opportunities that gender- and youth inclusive adaptation SMEs provide as well as from indirect effects of climate-induced shock mitigation.

60. Envisioned mid-term impacts foresee that FIs will invest in early-growth stage adaptation SMEs through an innovative catalytic finance facility that provides SMEs with investment advisory and finance to access markets and grow their business. At the same time, the national policy and regulatory environments in Kenya and Uganda foster adaptation solution investment and adoption in order toto increase resilience to climate change. On the Output and Outcome level, the project's Theory of Change is based on the following pathways of change and assumptions:

Component I: Regional Coordination Platform

- IF knowledge and awareness on the role of adaptation SMEs in increasing climate resilience and their finance- an market-related challenges is enhanced among key actors in finance, policy and business environment; and
- IF regional coordination on supporting adaptation SMEs in Kenya and Uganda is facilitated through networking and exchange (e.g. at Adaptation Action Steering Committee; Adaptation Action Events and Adaptation Finance Symposia); and
- IF a series of evidence-based knowledge products (e.g. Adaptation SME Taxonomy, Annual Impact Assessment, Action Plan Flagship Report) provides further insights into on the role of SMEs, their challenges and opportunities; and
- ASSUMING that the public and private sector in Kenya and Uganda fully recognise the potential role of adaptation SMEs in supporting the large-scale deployment of locally embedded adaptation solutions;
- THEN, a regional market of adaptation SMEs will be created, allowing them to scale and replicate their businesses.
- Which in turn, leads to national policy and regulatory environment fostering market-based adaptation solution investment and adoption.

Component II: Innovative performance-based blended financing mechanism, direct enterprise support and investment brokerage services

- IF an innovative performance-based blended financing mechanism is introduced in the Kenyan and Uganda market to bridge the missing middle financing gap;
- IF at least 60 outstanding gender- and youth inclusive adaptation SMEs are selected based on a thorough scorecard co-created together with FIs and other ecosystem stakeholders and receive funding readiness support; and
- IF a minimum of 15 local FIs are mobilised to participate in the catalytic finance facility and co-create innovative blended finance instruments tailored to the needs of gender and youth-inclusive adaptation SMEs; and

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[52] The co-creative prototyping methodology foundational to Component III's interdisciplinary Practitioner Labs and commercial bank-focused Finance Academy are refined from over a decade of experience in adelphi's SEED policy and financial product prototyping sessions with key financial actors in Africa and Asia. See also: https://seed.uno/programmes/ecosystem-building/practitioner-labs-climate-finance

[53] Building on adelphi's and Finding XY's proven financial readiness support in the framework of the European Union-funded Uganda Green Enterprise Finance Accelerator programme. See: https://ugefa.eu/

- IF at least 30 of the selected SMEs access innovative blended commercial financing instruments including a set of de-risking facilities coupled with performance-based payments, business advisory support and investment brokerage services
- THEN, at least 30 selected SMEs will be able to access tailored financial products and make investments to grow and replicate their business models
- THEN selected SMEs will scale the deployment of adaptation solutions across the two countries and enhance the adaptation impact they have on local communities;
- Which in turn, increases the familiarity and appetite of local FIs and other investors to invest in gender- and youth inclusive adaptation SMEs in Kenya and Uganda even beyond the project period.

Component III: Local financing institutions support gender- and youth inclusive adaptation SMEs

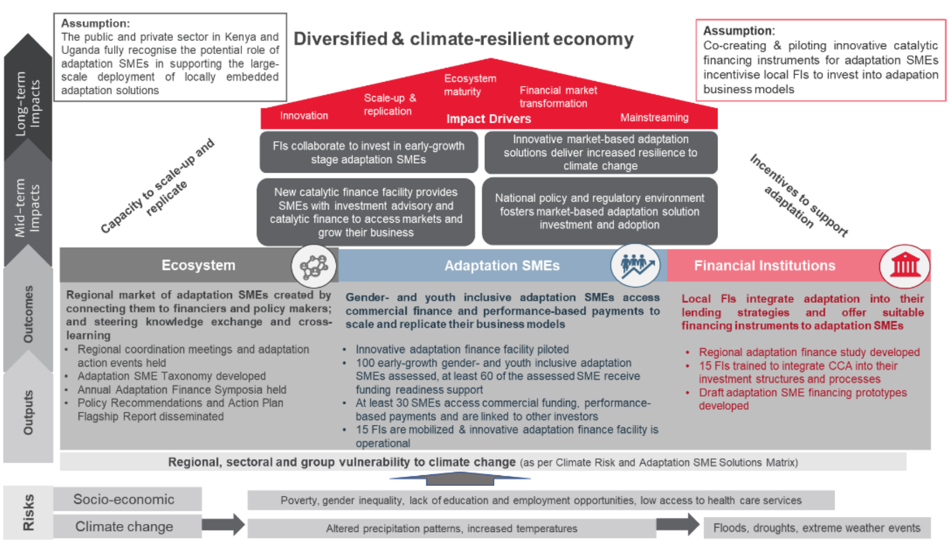
- IF a minimum of 15 local FIs receive guidance on how to develop their own climate (adaptation) strategy
- IF these local FIs understand the concept of climate adaptation (opportunities and risks) and how to integrate it into their investment structures and processes (operationalisation of climate strategy); and
- IF the FIs develop their own financial products targeting adaptation SMEs; and
- ASSUMING that through the co-creation and piloting of innovative catalytic financing instruments for adaptation SMEs (see Component II), local FIs are incentivised to invest into adaptation business models;
- THEN, pioneering local FIs integrate climate change adaptation into their lending strategies and offer suitable financing instruments to adaptation SMEs,
- Which in turn, leads to enhanced access to investment capital for adaptation SMEs in Kenya and Uganda and beyond.

61. The **regional approach** of the project will be key to the achievement of intended outcomes and impact as it provides the following added value to the project components:

- The Regional Coordination Platform (Component I) will establish a cross-country level adaptation entrepreneurship knowledge hub that extends Kenyan and Ugandan decision makers' national scope with insights on adaptation entrepreneurship insights and potential synergies between efforts and potential for collaboration. Through this, the project will support national policy makers and other ecosystem actors in Kenya and Uganda to provide conducive support systems and mechanisms to early-growth gender- and youth inclusive adaptation SMEs.
- Several of the FIs interviewed as part of the stakeholder consultation process provide financial services in both project countries. Including regionally active FIs into the project activities widens the scope of investment opportunities offered to the participating gender- and youth inclusive adaptation SMEs (Component II) and hence multiplies positive outcomes and impacts of this intervention.
- Kenya being counted as one of Africa's "big four" tech countries[54] provides enhanced market opportunities to adaptation SMEs, for instance in accessing agriculture or financial technologies. Based on similarities in climate change challenges experienced in both countries, a regional approach provides the opportunity for co-innovation and partnerships between Kenyan and Ugandan early-growth SMEs.
- Similarly, FIs in Kenya are often more advanced in anchoring climate (adaptation) considerations institutionally and as part of their investment portfolios. The proposed Adaptation Finance Academy (Component III) will allow for a peer-learning exchange between Kenyan and Ugandan to integrate strategic climate (adaptation) considerations.

An overview of the Theory of Change of the action can be found in the chart below.

Figure 5. Theory of Change of the proposed project



[54] Collins, T. (2022). Can Uganda's tech scene compete with Kenya?

Component I: Regional coordination platform to connect adaptation, climate-smart lending, entrepreneurship, knowledge management and promote cross-learning

62. **<u>Baseline situation</u>**: A core insight during the consultative process showed that early-growth gender- and youth inclusive adaptation SMEs in the region find it difficult to access finance due to 1) a lack of consideration by and visibility among finance, climate policy and business advisory actors, 2) insufficient coordination between actors in the ecosystem and 3) a lack of institutional knowledge on climate change adaptation and adaptation entrepreneurship (see Section J). Although consideration of adaptation action and SME support are two themes often identified in national development and adaptation plans and policies (see II.F and II.G, respectively), the nexus of adaptation and adaptation solution-oriented entrepreneurship is still nascent in the two target countries. Kenyan and Ugandan policy makers often develop national frameworks within the scope of their own organisational bodies, based on nationally-sourced information – inhibiting cross-country and -sector learnings to flow into policy development processes.

The dual lack of connections between adaptation action and the opportunities of private sector-based adaptation solutions as well as insufficient cross-country coordination translates into development and climate projects, that, although contributing substantially in supporting and coordinating sustainable SME solutions or adaptation projects, do not yet target adaptation SMEs as the common denominator. While climate finance is an increasingly important investment opportunity of FIs in both countries, climate-smart lending to SMEs is still an exception

63. **<u>Proposed interventions:</u>** Component I aims at establishing a Regional Coordination Platform (hereby RCP) that 1) connects actors in the fields of adaptation, (climate-smart) finance and entrepreneurship; 2) encourages action to sustain and create adaptation markets and 3) serves as a pioneering regional knowledge and coordination platform on adaptation entrepreneurship.

Outcome 1.1 The project establishes a sustainable coordination, network and knowledge platform for and between adaptation entrepreneurs, adaptation stakeholders and (future) adaptation financiers across Kenya and Uganda

Output 1.1.1: Establishing a multi-stakeholder Adaptation Action Steering Committee

64. To ensure that gender- and youth inclusive adaptation SMEs take a more central role and are targeted and supported by such actors, the EEs set up an RCP with a set of key functions:

1) Steer the interaction among different high-level stakeholders across countries, so as to encourage investments in proven adaptation technologies, products and services;
2) Organize regular Adaptation Action Events that link adaptation SMEs with other stakeholders to establish business linkages, access to markets and technologies and exchange knowledge;
3) Serve as a pioneering knowledge hub and distributor for profitable adaptation technologies and products in Kenya and Uganda, providing knowledge on the deployment and financing of adaptation products and services and offering replication business model profiles for future adaptation entrepreneurs

65. The RCP will be led and guided by the Adaptation Action Steering Committee, made up of core actors from finance, entrepreneurship, governmental institutions and representatives of vulnerable groups (such as youth-based organisations and rural women associations). The steering committee overlooks the vision and strategy of the project, guides the development and implementation of Adaptation Action Events and high-level Adaptation Finance Symposia and facilitates the exit strategy of the project.

Activity

<u>1.1.1.1 Formation of a multi-stakeholder Adaptation Action Steering Committee</u>

66. The steering committee's formation will be led by UNIDO in consultation with the governments from Kenya and Uganda as well as the EEs. This ensures a committee composition that is highly competent in the interrelated fields of adaptation and entrepreneurship, provides access to high-level public and private networks to leverage participation of key actors in the RCP activities, is endorsed by the respectively critical governmental institutions and includes concerns from representatives of vulnerable groups. To allow for a continuously committed and active committee, the list of committee members and overview of potential priority members will be reviewed and renewed on an annual basis.

Output 1.1.2: An administrative and functional structure for the RCP is developed and endorsed

Activities

<u>1.1.2.1 Endorsement of a strategic framework</u>

67. The Adaptation Action Steering committee is tasked to develop a sustainable strategic framework for the project duration and beyond. The strategic framework acts as a guide for project implementation and for future government organisations to carry on the project post project maturity. It includes:

- A rationale for achieving accurately defined project performance indicators such as gender- or youth-inclusive entrepreneurship based on the project's theory of change (ToC)
- A systemic analysis of the innovation mechanisms, focusing on regular feedback and refinement loops
- An outreach strategy to meet key objectives of increasing female and youth participation and developing outreach collaborations with representatives of vulnerable groups (CBOs, women organisations)
- An impact assessment strategy including a long-term vision of scale of impact, including the development of processes for government uptake post-project maturity
- An inclusion and participation strategy of vulnerable group representatives such as rural women-, youth- or migrant-focused groups into the project design and refinement phases
- A regularly enforced synergy scouting guideline to screen regionally for existing innovations and/or organisations to integrate them into the project
- A process handbook (developed prior to project maturity) to facilitate efficient project takeover

1.1.2.2 Digital platform for adaptation entrepreneurship practitioners and ecosystem actors

68. One core component of the RCP is its digital platform for adaptation entrepreneurship practitioners and ecosystem actors. The digital platform will serve four main purposes:

1) Providing a quantified database of profitable adaptation solutions with regularly updated and transparent journey insights (funding, impact, enterprise growth), sourced from regular impact assessments. This lends credibility to potential co-financiers and governmental organisations as future implementing entities.
2) Enabling regional community-building through participant profiles and contact information. This ensures that enterprises can reach out to each other, build networks and explore business linkages across countries. We would, however, refrain from integrating a fully-fledged communication operating system as maintaining communication on "new" systems is resource-efficient and tends to suffer from low usage rates. We thus opt for platform communication channels making use of existing communication tools such as WhatsApp, LinkedIn or emails.
3) Showcasing best practices of adaptation SMEs and offers access replicable business components. These originator profiles will include a step-by-step business development guideline as a "business-in-a-box" blueprint.
4) It serves as an openly available knowledge repository of relevant knowledge products (e.g. symposium reports, multimedia case studies etc.)

Outcome 1.2: Key stakeholders, ministries, financial institutions (FIs), adaptation SMEs and the end-users (vulnerable groups) create and sustain market for adaptation technologies, services and products

Output 1.2.1: Regular regional *Adaptation Action Events* are organized

Activity:

1.2.1.1 Adaptation Action Events

69. The RCP will feature regular events aiming to facilitate adaptation SMEs' access to networks, markets and finance. Event types are:

- *Adaptation Roundtables* – multi-stakeholder dialogue fora on adaptation SME challenges and opportunities. Roundtable agenda points are inspired by insights from vulnerable groups (farmer associations, cooperatives, women and youth associations) and supplemented by evidence gained through project knowledge products such as the Adaptation Finance Study (Activity 1.2.3.3) and impact assessments of the project's direct enterprise support components (Outputs 2.2.2 and 2.2.3). Roundtable discussions are video recorded and summary videos are uploaded to the project website.
- *Sectoral study tours* – Study tours are guided to showcase selected direct enterprise support alumni for non-enterprise roundtable participants between countries. This increases knowledge on adaptation entrepreneurship in practice and strengthens cross-country learnings. Sectoral study tours will also be offered between enterprises, as networking events and platforms to exchange ideas and explore linkages was a key finding of adelphi's currently ongoing Uganda Green Enterprise Finance Accelerator (UGEFA).
- Further event types that will be implemented are *radio podcast shows*; adaptation breakfasts that are informal cross-country exchanges between adaptation SMEs reflecting on commonly experienced challenges and opportunities; access to market events through which supported enterprises enhance their networks and explore business linkages.

Output 1.2.2: Annual Adaptation Finance Symposia are developed and held

Activity:

1.2.2.1 Annual Adaptation Finance Symposia

70. The Adaptation Finance Symposia will be annual multi-stakeholder events with high-level speeches, panel discussions, interactive break-out sessions, adaptation SME exhibitions[55] and pitches of the prototyped adaptation finance solutions developed during the Adaptation Finance Practitioner Labs (Activity 3.1.1.3). The symposia provide a platform for cross-country exchange between financiers, policy makers and adaptation SMEs. Aiming to be the leading adaptation finance knowledge hub in the region, the RCP's symposia will integrate into its agenda the presentation and dissemination of key insights of the Adaptation SME Finance Scoping Study (Activity 1.2.3.3) and Adaptation Market Analysis Report (Activity 1.2.3.1), as well as the developed evidence-based Adaptation SME Taxonomy (Activity 1.2.3.2).

Output 1.2.3: Knowledge products on market-based adaptation solutions and impact of gender- and youth inclusive adaptation SMEs are developed (including the benefits for vulnerable communities and target sectors) and widely disseminated

Activities:

1.2.3.1 Adaptation Market Analysis Report

71. Upon project kick-off, the EEs will develop an evidence-based study markets for adaptation solutions in Kenya and Uganda. The report will take account of vulnerable groups' climate change risks and adaptation priority sectors before exploring the challenges and opportunities of gender- and youth inclusive adaptation SMEs to scale their operations and adaptation impact for said vulnerable groups. The study expands on initial insights gathered during stakeholder interviews in the course of the consultative process. While its main purpose is to inform and tailor the direct enterprise support activities in Outputs 2.2.2 and 2.2.3, the report delivers critically needed insights into the still-nascent body of literature on adaptation entrepreneurship, and is thus suited for academia and practitioners active

[55] During the first symposium such exhibits are sourced from SEED's extensive enterprise database due to a lack of enterprise alumni at this project stage. The following symposia will feature enterprise exhibits with direct enterprise support alumni.

in this field, as well as for (future) adaptation entrepreneurs. It will be the first knowledge product to identify opportunities for successful adaptation entrepreneurship tailored to vulnerable communities as well as barriers to growth and scale for adaptation SMEs in the region.

1.2.3.2 Evidence-based Adaptation SME Taxonomy

72. Based on the pioneering taxonomy work on adaptation SMEs by the IADB's Adaptation SME Accelerator Project[56], this project will further refine and test the taxonomy assumptions with real enterprise data prior, during and after project completion. This ensures that definitional scopes of adaptation entrepreneurship and their provided adaptation solutions remain distinct and applicable in the context of enterprise support eligibility criteria. It therefore establishes a structured approach for transparently determine whether an SME qualifies as an "Adaptation SME" based on the type(s) of technologies, products and services offered. The adaptation taxonomy is integrated into the Adaptation Finance Academy curricula.

1.2.3.3 Adaptation SME Finance Scoping Study

73. Prior to the first Adaptation Finance Symposium (Activity 1.2.2.1), the EEs will conduct an interview- and desk research-based report on the state of adaptation SME finance in Kenya and Uganda. The study will be published onto the project's digital platform, integrated into the Adaptation Finance symposia's curricula and used to inform the direct enterprise support activities in Component II as well as the Finance Academy (Output 3.1.1). It will provide key insights on:

- The financing needs of gender- and youth inclusive adaptation SMEs (e.g. ticket sizes, repayment periods, financial product type)
- The volume of adaptation finance and the inclusion of the private sector
- An analysis of current green and adaptation finance product portfolios in the two countries
- A status quo analysis of current adaptation finance policies and frameworks and their implications
- The knowledge and view of FI executives on the financial needs of adaptation SMEs

1.2.3.4 Multimedia case study films to showcase adaptation business models and their impacts

74. The case studies to be developed have the objective to promote and showcase the contribution of selected gender- and youth inclusive adaptation SMEs to the achievement of NDCs and SDGs. The case studies serve to provide visibility for actor groups with limited exposure to the lived realities, struggles and potentials of gender- and youth inclusive adaptation SMEs on the ground. Based on experience with case study films in previous projects, this product also serves as a critical advantage for enterprises, as they often use these films for marketing purposes and to attract finance.

1.2.3.5 Policy Recommendations and Action Plan Flagship Report

75. Insights on the needs of adaptation SMEs and solution pathways to effectively address those needs will be synthesized into a set of tangible policy recommendations for policy makers in Kenya and Uganda in the form of an Action Plan Flagship Report. Information is derived from the project's knowledge products (e.g. Activities 1.2.3.1, 1.2.3.3), impact assessment (Activity 1.2.3.6) and Adaptation Action (Activity 1.2.1.1) as well as Adaptation Finance Academy Events (Component 3). The report will be published on the RCP's digital platform.

1.2.3.6 Annual Impact Assessment

76. The project will include both an internal and external impact assessment, aiming at analysing and showcasing the efficient contribution of the project to the achievement of improved access to finance for adaptation SMEs to reach their potential. To increase adaptation action measurability and design robust performance and impact indicators, the project will develop a transparent and publicly available impact data section as part of on the digital platform. This will be led by the Adaptation Action Steering Committee, who will establish an Impact Assessment strategy (as part of Activity 1.1.2.1), at its core serving as the project's impact framework. This includes:

- *Impact Methodology Strategy* – This strategy will detail how existing EE impact tools can be further tailored, improved and mainstreamed across the project
- *Impact Dashboard Tool* – for supported enterprises, supporting the planning, measurement and management of their economic, social and environmental impacts. This tool will include tailored indicators to measure adaptation impacts. These impact dashboards will be filled by adaptation SMEs in the course of the capacity building support and on an annual basis post support, contributing to the monitoring of the additional long-term outcome KPIs.
- *Control groups* – Control groups will be established to be able to measure impacts of the direct enterprise and financial support vis a vis non-support. Shortlisted enterprises that are not selected for the programme are well suited to form a control group.

77. *Lessons learned and Impact assessment reports* – Lessons learnt will continuously feed into the program design and implementation throughout the project implementation period. Impact Assessment Reports will provide an evidence foundation for both internal learning and external communication activities during and after this project.

78. *Integration of feedback loops from vulnerable groups as customers of adaptation SMEs*: to gain insights on the impact the project and its concomitantly disseminated adaptation solutions have on vulnerable communities in Kenya and Uganda, the project will regularly collect adaptation SME customer feedback (disaggregated by vulnerability variables such as income, occupation, gender, age). The data generated through feedback loops be important markers for the re-adjustment of project components and activities, such as scorecard criteria (Activity 2.1.1.1).

[56] Trabacchi, C., Koh, J., Shi, S., Guelig, T. (2020) Adaptation Solutions Taxonomy.

Component II: Innovative performance-based blended financing mechanism, investment brokerage services and direct enterprise support

79. **Baseline situation**: There is a gap in the entrepreneurial support systems when it comes to SMEs phasing from grant-based funding to commercial growth-stage investments. Especially for adaptation enterprises, access to concessional finance is challenging[57] as described in the Problem Statement (see paragraph 59).) From a financial market perspective, climate change-related investments by international climate funds and multilateral development banks have increased,[58] but there is still a lack of suitable finance mechanisms to deploy the money through local FIs targeting early-growth SMEs. Climate adaptation is a nascent field for bankers and is perceived as high-risk given the climate-induced uncertainties of adaptation market opportunities, lack of clear impact measurement frameworks and the innovative character of adaptation technologies or solutions that lack benchmarks. At the same time, the financing instruments offered by local FIs are barely suited for the SME market as they are often not accessible (e.g. because of high collateral requirements) nor attractive (e.g. due toto high interest rates) for these small market players. Lastly, commercial banks in Kenya and Uganda lack a suitable pipeline of bankable adaptation SMEs.

80. **Proposed interventions:** Component II constitutes an innovative financial mechanism bridging gender- and youth inclusive adaptation SMEs' 'missing middle' financing gap in the two target countries. A performance-based blended financing mechanism will be pioneered together with funding facilitation instruments, addressing the main accessibility barriers to commercial finance. The innovation of this approach stems from 1) the unique combination of de-risking blended financing instruments with performance-based payments to specifically scale and replicate highly impactful adaptation business models; and 2) the highly inclusive approach involving not only local FIs but also impact investors and venture funds in Kenya and Uganda in a co-creation process from design to investment and post-investment stage.

81. The mechanisms core modules and processes are:
    1) *Selected pipeline of gender- and youth inclusive adaptation SMEs receive TA:* The EE will select a pipeline of eligible gender- and youth inclusive adaptation SMEs based on a thorough scoring process focusing on main financial, innovation, adaptation and socio-economic impact criteria (see Output 2.1.1). The selected adaptation SMEs receive tailored business advisory to achieve financial readiness.
    2) *Matchmaking between local FIs and supported gender- and youth inclusive adaptation SMEs:* A pipeline of eligible adaptation enterprises will be matched with a selection of local FIs to apply for loan funding.
    3) *De-risking of commercial bank financing*: In order to facilitate the financing agreements between participating adaptation SMEs and local FIs, the EE provide a certain amount of grant financing to blend the loan. The design of blended financing mechanisms will be shaped upon during inception phase in a co-creation process with the local FIs (see different financing options under Output 2.3.1).
    4) *Performance-based payments:* Upon achievement of individual APTs, the participating adaptation SMEs receive performance-based grant payments. Performance-based grant payments can be used for loan repayment and/or for additional investments.
    5) *Additional de-risking and incentivising components* may be built in as needed to further tackle investment-related challenges (e.g. to value collateral as a prerequisite for the loan agreement).
    6) *Leveraging complementary investments by impact investors/ venture funds:* In order to diversify the pool of investors and achieve a greater value of leverage, the project will also work with impact investors and venture funds (e.g. the EEs own venture funds) that offer patient facilities like convertible debt and equity. Investments by this group of financiers will complement the investments by local FIs (commercial banks, microfinance institutions) as they might not be able to solely satisfy the demand for capital by the participating SMEs. Impact investors and venture funds also support participating adaptation SMEs with due diligence costs (and other admin charges), thus, increasing their finance-readiness further. Impact investors and venture funds will not receive any direct financial incentives by the project but they will be involved in the co-creation of the financing facility.

Outcome 2.1: Developing and implementing the project's enterprise support infrastructure

Output 2.1.1 Scorecard (incl. final selection criteria) for the assessment of at least 100 early-growth gender- and youth-inclusive adaptation SMEs is co-created

Activity:

2.1.1.1 Scorecard co-creation

To select a pipeline of gender and youth-inclusive adaptation SMEs for the catalytic financing scheme, a scorecard with a set of robust and fit-for-purpose criteria will be developed jointly with experts from the Adaptation Action Steering committee (Output 1.1.1) and the participating FIs (Output 2.3.3). A positive list of eligible adaptation technologies/ solutions, taking into consideration regional vulnerabilities and socio-economic structures (see also Climate Risk and Adaptation SME Solution Matrix/ Part I, Chapter 1.5), will form the basis for discussion with FIs/ investors to ensure their eligibility for asset finance and the resulting loan products offered. The following overview provides an indication of the proposed scoring categories:

Table 1: Draft scoring categories, as a foundation of the newly-developed selection scorecard.

Non-Financial scorecard criteria		Financial scorecard criteria	
Impacts	Adaptation products/ services	Financial Status	Annual turnover
	Environ. Safeguards/Maladaptation		Gross & operating profit

[57] Cowan, A. (2019). The SME finance gap in Kenya: how are investors missing the 'missing middle'?

[58] https://afdb.africa-newsroom.com/press/multilateral-development-banks-mdbs-climate-finance-rose-to-66-billion-in-2020-joint-report-shows?lang=en

	Monitoring, assessment & reporting	Financial Systems	Debt Ratio
	Gender & Youth inclusiveness		Quality of financial projections
Business Model	Value Proposition		Financial controlling systems
	Product / Service		Financial Statement
	Growth Potential	Investment Plans	Clarity of investment proposal
	Target Market		Loan ticket size in line with project
Team & Expertise	No and expertise of Staff		Investment influencing on business growth
	Ratio full time / temporary		Job creation potential
	No of financial staff		

After the first financing cycle, the scorecard will be critically reviewed vis-à-vis the selected and supported enterprises to consider lessons learned for the second cycle.

Output 2.1.2: Pipeline of at least 60 gender- and youth inclusive adaptation SMEs built for funding readiness support (100% of the SMEs will be women- and/or youth-inclusive, meaning they aim for a 50% gender and youth balance in their work force and/or their primary customer base)

2.1.2.1 Outreach campaign

82. Through a dedicated outreach campaign, a pipeline of high-quality applications will be generated for the intake into the two cycles of the funding program. The action is promoted through a launch event and information campaign among relevant multipliers in the Ugandan and Kenyan ecosystem, making use of the contacts and network of the Adaptation Action Steering Committee (Output 1.1.1). In both countries, well-established incubator programs focusing on green and climate-smart enterprises offer a suitable pipeline for this project[59]. Women and youth groups (including village-based savings and loan groups) will be specifically targeted. Women- and youth-led / -owned companies from the EE's current portfolios will provide leads and networks. Existing women/ youth empowerment programs like Kenya Women Finance Trust will be a source of targeted adaptation SMEs.

2.1.2.2 Set-up of online application system and pre-application support

With the EE having implemented various selection schemes (e.g. adelphi has implemented the SEED global selection scheme[60] for almost 15 years, having handled over 6,000 applications, the Uganda Green Enterprise Finance Accelerator processed over 2,500 registrations; KCV has implemented a digitalized expert-managed investment applications platform for the past 6 years, with 100-150 applications annually). Building on these lessons learnt, applications will be handled through an online application system with user accounts, which allow for editing the application until the application deadline. A backend interface will be established to manage and monitor the online applications and to provide technical assistance remotely. One-day pre-application workshops will be offered to support applicants to clarify their business concepts and submit comprehensive and consistent applications.

2.1.2.3 Selection of funding-ready gender- and youth inclusive adaptation SMEs

83. Through an elaborated online scoring system and selection process each application is evaluated independently by two to three analysts from the EE along a scorecard that will be based on the publicly communicated eligibility criteria. The assessment is undertaken along four guiding principles: four/six eyes principle (each application is evaluated independently; where the two analysts' scores differ extraordinarily, a third analyst is drawn in); shared benchmark principle (prior to the evaluation period the facility objectives and the eligibility criteria are thoroughly introduced to each engaged analyst); capacity principle (analysts are engaged for sector and technology expertise, while an interdisciplinary composition of the team ensures an excellent delivery of the task); documentation principle (all inputs, changes and comments are documented).

Outcome 2.2: Supporting gender- and youth inclusive adaptation SMEs from funding readiness to investment and post-investment

Output 2.2.1: Two Catalyser Programme Cycles: Business advisory support to achieve funding readiness for 60 shortlisted gender- and youth-inclusive adaptation SMEs provided

Activity

2.2.1.1 Catalyser enterprise support programme (2 cycles)

84. At least 60 selected adaptation SMEs will receive capacity-building support based on the proven EE's toolkit which consists of five peer-learning workshops in small groups combined with individual support for each enterprise. The support is delivered by the locally-based EEs with support and backstopping provided by the international EE (adelphi). The content of the capacity building support will be aligned with the specific needs of shortlisted applicants and will include:

- **Business planning:** Development of growth strategy with gender- and/or youth-related milestones, e.g. with regard to vulnerable groups as primary customer segments, their engagement along SMEs' value chains as well as inclusive approaches to increase the number of direct beneficiaries of adaptation products and services
- **Financial Reporting**: Review of financial systems/improvement of financial controlling and management
- **Financial Planning,** based on the developed growth strategy, and risk management
- **Investment Planning:** Financial growth scenarios, profitability analysis of planned investments

[59] Incubators and accelerators from Kenya/ Uganda: E4Impact - https://www.e4iaccelerator.org/; Pangea Accelerator - https://www.pangeaa.com/; Kenya Climate Innovation Centre - https://www.kenyacic.org/; Sinapis - https://www.sinapis.org/; Nailab - https://nailab.co/; Catalyst Fund - https://bfaglobal.com/catalyst-fund/; Selected Transaction Advisors for SMEs in Kenya & Uganda: Open Capital Advisors: https://opencapital.com/; PFAN: https://pfan.net/

[60] For details please see https://seed.uno/

- **Impact Assessment:** Setting up an impact assessment framework, validating adaptation impact assumptions
- **Loan Application Preparation**, including pitching and loan negotiation training

85. The Catalyser programme will also focus on enhancing the competitiveness of the selected enterprises. Gender equality and the inclusion of marginalised groups (including women and youth) will be facilitated by tailored tools to further sensitise the participating SMEs for gender aspects and the inclusion of marginalised groups. Based on 20 years of experience in supporting green and inclusive enterprises, adelphi has developed an easy-to-use advisory methodology and toolbox, which is continuously updated.

2.2.1.2 Developing Adaptation Performance Targets (APT)

86. An integral part of the Catalyser advisory package will be the development of the adaptation SME's theory of change, drafting of adaptation impact chains and identification of outputs and outcomes along their individual adaptation-related impact dimensions, taking into consideration the vulnerabilities of their target customers/ beneficiaries. Based on the theory of change, the EEs and the participating adaptation enterprises will agree on Adaptation Performance Targets (APT) to be achieved within a certain time-frame (e.g. 5km of drip irrigation pipeline sold to vulnerable smallholder farmers within the next 1.5 years). The selected APT will form the basis for the performance-based payments (Outcome 2.3).

87. APTs need to be ambitious and meaningful to avoid the risk of setting goals, that if met, would not reflect a genuine improvement of the final beneficiaries' climate resilience. They need to be fit for purpose to ensure that the underlying adaptation metric is material to the SME's core business. Especially for businesses operating in the agriculture and to some extent also in the water sector, it will be crucial to build in precautionary measures to manage risks associated with extreme events (e.g. weather or other natural hazards), especially with the project focus being on highly vulnerable regions. To that end, several sets of targets may be developed to provide flexibility for performance-based payments.

88. APTs are verified by an external service provider looking back at the enterprise historical trajectory (e.g. turnover and sales number in the past three years) and benchmark against industry peers, if available. As part of the advisory, adaptation enterprises will also develop a sound concept how to measure and monitor adaptation impacts and targets using an impact planning dashboard including KPI's/indicators and an individual M&E framework to monitor their APTs in a cost-effective manner.

Output 2.2.2: Two Accelerator Programme Cycles: Post-investment support on growth and loan repayment provided for 30 gender- and youth-inclusive adaptation SMEs

Activity

2.2.2.1 Business model and financial management advancement through one-on-one advisory (2 cycles)

89. Throughout two funding cycles (year 3 and year 4 of project implementation), the Accelerator Programme enables adaptation enterprises to secure loan funding moving them towards financial resilience and growth, building their in-house financial management capacities and processes, thus putting them in a better position to create jobs while contributing to an enhanced climate resilience. The accelerator support will apply a one-on-one support methodology.

90. The accelerator support will be provided to all enterprises receiving finance under this project, accompanying the financial support process throughout with the following key activities:

- Strengthening financial management capacity and financial management systems according to FIs requirements
- Advancing and validating the enterprise growth strategy, investment roadmap and financial assumptions

Outcome 2.3: Designing and implementing blended financing mechanism and performance-based payments for gender- and youth inclusive adaptation SMEs

Output 2.3.1: Development and refinement of performance-based blended financing scheme

Activities

2.3.1.1 Co-creative financial facility design

91. To achieve alignment between the project's financing facility and the standard procedures at partnering FIs and investors and tailor the instrument to both their requirements as well as adaptation SME needs, a well-conceptualized co-design process will be implemented to develop and test the most effective blended financing instruments for the Kenyan and Ugandan market. Such instruments mainly need to remedy eligibility knock out criteria, such as irregular cash flows, and de-risk loan agreements with target enterprises from the view of the financing institution as well as increase affordability of finance to the enterprises. To overcome those key barriers to finance, a number of prototype-stage ideas have been developed:

Option 1: Partial Repayment Scheme: Reducing both the risk of default for the FIs as well as the cost of finance for the enterprise, a grant of 25 – 33% of the total loan amount that is unlocked with any eligible loan agreement. This reduces the outstanding loan amount (principal) immediately after loan approval and thus allows the enterprise to access higher ticket sizes, reduces collateral requirements and the total interest amount to be paid by the enterprise.

Option 2: Loan Guarantee Scheme: Guarantee schemes buffering the risk of loans have worked well in various programs in Kenya and Uganda so far, sometimes hindered by exaggerated bureaucracy. A dedicated guarantee fund or, saving transaction costs and ensuring long-term sustainability, cooperation with an existing fund can work well to facilitate the flow of small-scale loans to green enterprises. Both individual, and portfolio guarantee instruments will be considered.

Option 3: Origination costs incentives: Time and cost-intensive due diligence and loan appraisal processes can be an obstacle for FIs to take on new SME borrowers, especially when they are not familiar with the dynamics in a new value chain or market. Financial incentives to cover these costs upfront can lower the barrier for FIs to look into new SME markets and business segments for investing.

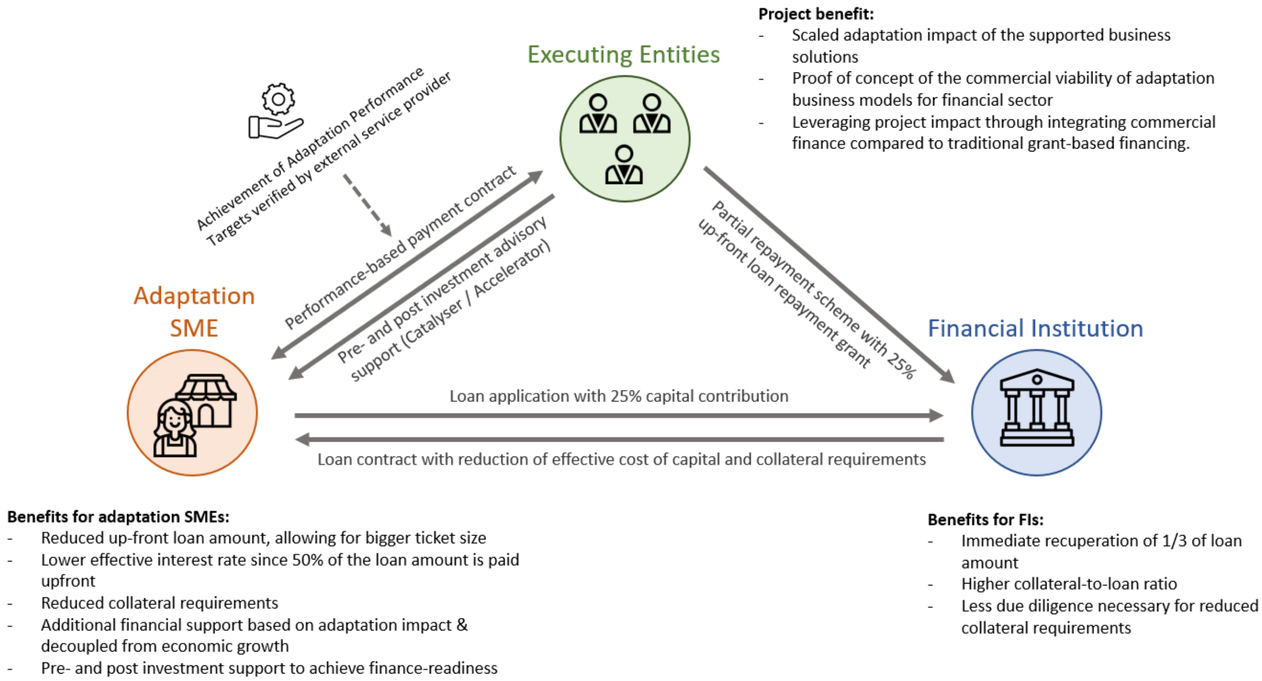


Figure 2: Exemplary set-up for Loan-Attached Repayment Grants and Performance-based payments.

92. In a dedicated workshop with FIs these prototypes will be refined for implementation also capturing potentially promising new ideas for other approaches and instruments. Involvement of FIs in this process will not only guarantee alignment with existing processes and structures within the FIs, but also create ownership among FIs. Interested impact investors and venture funds may provide additional capital for the selected gender- and youth inclusive adaptation SMEs, either in the form of ex-ante/ follow-on investments or as dedicated co-financing agreements. Several promising instruments will then be applied in collaboration with partnering FIs and investors to facilitate loan and equity financing. Based on evaluation of the first cycle, instruments may be further refined, with a final evaluation at the end of the project. The action will aim to result in a solid and tested mechanism with potential to be scaled and/or replicated both nationally in Kenya and Uganda, and internationally.

93. Complementary to the blended financing instruments the EE will pilot additional performance-based and incentive mechanisms for participating adaptation SMEs to make commercial investment capital accessible and scale their adaptation impact further:

94. **Option a: Support SMEs to value collateral**: Covering costs for determining the collateral value (3-5k USD) as a prerequisite for the loan application which can be a prohibitive factor for SMEs to apply for financing.
Option b: Cash-Flow Gap Cover: A cover for up to three months to continue repayment in times of low liquidity can close short-time gaps and upon successful repayment of this cover funding it can be accessed repeatedly by any eligible enterprise.
Option c: Covering due diligence and other loan preparation costs: The selected adaptation SMEs may receive support with required due diligence and other cost involved in preparing their loan application.
Option d: Performance-based payments: Upon achievement of individual APTs, the participating adaptation SMEs receive additional performance-based grant payments that will cover up to 15% of the overall loan size and can be used for the repayment of the loan and/or for additional investments.

95. Any combination of these instruments can be applied, whereas option 1 – 3 instruments aim at funding facilitation and option a-d as additional incentivizing and enabling instruments.

Table 2: Overview of instrument options and grant amounts.

Instrument	No of SMEs	Grant amount per SME	Total Grant amount (for 30 SMEs)	Leveraging effect**
Option 1: Partial Repayment Scheme	30	*25 - 33 % of loan ticket size** / 18.750 - 24.750 USD	562.500 - 742.500 USD	1.687.500 – 1.507.500 USD Factor 2 – 3
Option 2: Guarantee Scheme		*35% portfolio or individ. guarantee*	787.500 USD	1.462.500 USD Factor 1,9
Option 3: Origination costs incentives		*Average appraisal subsidy*	600.000 USD	1.650.000 USD Factor 2,75

		20.000 USD		
Performance-based and incentive mechanisms				
Option a: Grant for collateral valuation	30	3.000 - 5.000 USD	90.000 - 150.000 USD	-
Option b: Cash Flow Gap Cover		*20% of Partial Repayment Scheme* 3.750 - 4.950 USD	112.500 - 148.500 USD	-
Option c: Due Diligence & Loan Prep. Grant		5.000,00 USD	150.000 USD	-
Option d: Performance-based payments		*Up to 1515% of loan ticket size** 11.25011.250 USD	675.000 USD	-

*Assumption: Average ticket size: 75.000 USD.

** The leveraging effect describes the amount of private capital, which is leveraged by the grants provided through this project. Calculated as: Number of loans * average ticket size - (total grant amount)

Output 2.3.2 Mobilising at least 15 partner Financial Institutions (FIs)
Activity

<u>2.3.2.1 Building a portfolio of contractual partnerships with FIs and impact investors/ venture funds</u>

96. Formalized partnerships will be sought with at least 15 local FIs and impact investors/ funds that have already been part of the design process. The EEs will leverage their well-established networks with commercial banks and impact investors in Kenya and Uganda. The Kenyan EE, KCV Limited being an investment management company with an established fund to invest in climate-smart, early growth-stage enterprises, will be one key partner here. Specific alignment to the internal procedures, risk scorecards, due diligence and loan appraisal requirements of the partnering FIs and investors will be considered in jointly designing the catalytic financing facility.

97. For the implementation of blended financing instruments, a detailed outline of roles, responsibilities and transactional procedures will be agreed upon and refined over the course of the project. Memorandums of Understanding will be signed before the first presentation of enterprises to FIs and impact investors/venture funds. In the second cycle, also new partner institutions will be invited to come on board to increase outreach into the ecosystem and to enable these to benefit from the experience and learnings from the pilot stages, and any conceptual refinements already implemented.

Output 2.3.3 Implementing performance-based blended financing instruments and portfolio management
Activities

<u>2.3.3.1 Performance-based blended financing implementation</u>

98. Adaptation SMEs that have successfully completed the Catalyser program (Output 2.2.1) will be linked to the partnering FIs and impact investors/ venture funds to apply for funding. At least 30 participating SMEs successfully sign a financing agreement with an FI/investor and thus, become part of the Accelerator programme.

99. For each successful financing agreement, the EEs will sign individual contracts with the borrowing adaptation enterprises to agree on the performance-based grant payment that will be tied to the achievement of Adaptation Performance Targets (APT). APTs may relate to different business aspects such as sales targets, vulnerable customers/ beneficiaries served, women/youth representation in the enterprise value chain (e.g. as sales agents) etc. The individual amounts of performance-based grant payments will be determined based on the categorization of participating gender- and youth inclusive adaptation SMEs according to their growth and impact potential. Gender- and youth inclusive adaptation SMEs with a medium growth potential but a high adaptation impact potential, for instance, would receive higher performance-based grant payments than high-growth/low-to-medium impact profile enterprises.

<u>2.3.3.2: Portfolio management:</u>

100. Portfolio management of funding-eligible enterprises is coordinated through a central database for progress monitoring and documentation, supported by local EEs providing the business support, in order to ensure that enterprises work effectively towards meeting FIs/ investors requirements on funding-readiness in terms of financial management systems and realistic investment plans along funding-readiness action plans. An external service provider will be contracted to monitor the borrowing SMEs' adaptation-impact performance, e.g. by reviewing and verifying self-reporting efforts by SMEs. Regular reporting on the status of achievement of APTs by this service provider to the EEs will be an integral part of the performance-based financing system to ensure that individual contract stipulations are met. The Accelerator Support, as well as dedicated contingency planning sessions for enterprises benefitting from the cash flow gap cover instrument will mitigate the risk of defaults as much as possible. Since this financial facility engages and leverages funding provided by market-based financial institutions in an innovative manner, the facility can rely on due diligence and repayment monitoring processes conducted by financial institutions themselves.

Output 2.3.4 Exit and scale-up strategy for innovative adaptation SME financing mechanism developed and operationalised

<u>2.3.4.1 Exit and scale-up strategy development</u>

101. Both the financing facility, which will raise the appetite and familiarize FIs with adaptation business models, products, services and technologies, as well as the Adaptation Finance Academy (outlined in 3.1.1) will prepare local banks and other FIs to deploy international climate finance capital provided by (international) DFIs. FIs will gain first-hand experience with adaptation SMEs, their investments and the integration of adaptation-related criteria into loan appraisal processes and scorecards.

Outcome 2.4: Potential environmental and social risks of selected SMEs screened, assessed and monitored within the framework of the Environmental and Social Management System (ESMS)

Output 2.4.1 A comprehensive ESMS for SMEs to receive technical and finance support is implemented
Activity
2.4.1.1 Application of an Environmental and Social Management System (ESMS)

102. A comprehensive ESMS will be set-up and implemented specifically for the screening, assessment and monitoring of environmental and social risks that potentially result from the activities of the SMEs that will be selected to receive targeted technical and financial support through the project. The methodology of the ESMS will be developed and presented at fully developed proposal stage, in line with the environmental and social principles as defined by AF's Environmental and Social Policy.

103. Further, this will include assessing any potential risks for maladaptation as a result of the SMEs introducing adaptation solutions such as any negative impact /externality on other groups, potential for future conflict, unwise trade-offs, short vs long term benefits, path dependencies or a technology lock-in that eliminate choices of future generations, or higher risk on other areas that the farmers livelihood depends on, etc. If the screening results in a high or moderate risk category for the sub- project, then additional steps might be taken to avoid or mitigate such risks.

104. Project and safeguard information will be disclosed to public and relevant stakeholders for their information and engagement. Regular monitoring of the compliance with required environmental and social management plan will be carried out and documented in the annual progress reports.

Component III: Local financing institutions support gender- and youth inclusive adaptation SMEs

105. **Baseline situation**: The financing of gender- and youth inclusive adaptation SMEs in Kenya and Uganda is limited by the lack of awareness and knowledge among local FIs about the business opportunities of accessing adaptation finance and channelling it into adaptation entrepreneurship. To enable effectively funnelled adaptation finance to locally-led adaptation entrepreneurs who target those most vulnerable to climate change, local FIs need to be capacitated and empowered in understanding adaptation, its funding criteria, and business cases.

106. **Proposed interventions:** The Adaptation Finance Academy serves as an events-based knowledge hub to tackle the insufficient FI portfolio of adaptation finance instruments tailored to gender- and youth inclusive adaptation SMEs, as well as to contribute to increasing efficiently channelled adaptation finance to local interventions and adaptation entrepreneurs. Adaptation Finance Trainings will provide tailored information and knowledge on climate adaptation and the private sector and the specific role of adaptation SMEs in building local resilience. The trainings will be held back-to-back to Climate Strategy Workshops that will anchor strategic adaptation considerations within participating FIs, serving as the strategic foundation for adaptation action. The Adaptation Finance Practitioner Labs, are co-creative multi-stakeholder workshops in which innovative adaptation finance instruments tailored to early-stage gender- and youth inclusive adaptation SMEs are designed by local FIs.

Outcome 3.1: Local financing institutions support the dissemination of adaptation technologies, products and services

Output 3.1.1: An Adaptation Finance Academy training concept is developed and implemented

Activities
3.1.1.1 Adaptation Finance Trainings

107. The banking sector in the two target countries is generally lacking awareness in the concept and prospects of adaptation finance as well as what financial products and services are required for gender- and youth inclusive adaptation SMEs to scale. The Adaptation Finance Trainings offers the opportunity to expand on nascent knowledge on adaptation finance and entrepreneurship as a lever for new financial business opportunities.

108. The interactive hands-on trainings will be facilitated by experienced advisors and target local FIs participating in small teams of three to four members. A specific focus of the trainings will be on gender-lens and inclusive financing to create additional awareness on the obstacles of women, youth and other marginalised groups to access finance. The workshops also act as showcasing events for gender- and youth inclusive adaptation SMEs as blueprints for investable business models. Furthermore, subnational government officials are invited to discuss possible cooperation for joint locally implemented adaptation finance projects.

3.1.1.2 Climate Strategy Workshops

109. In order to ensure that the suggested funding facility will be strategically anchored within partner FIs, Climate Strategy Workshops will be implemented, capacitating them to develop Climate Strategies, outlining strategic pillars for climate action, action fields for operationalisation as well as clear climate targets, both on mitigation and adaptation. The Climate Strategy Workshops will engage representatives from different departments, ranging from sustainability and partnership managers to communication teams as well as product developers, client solution managers and commercial departments to embark on co-creation sessions to jointly design Climate Strategies for their banks. Participants will further benefit from capacity building on climate impact measurement, to support sustainability-related reporting.

110. These Climate Strategy Workshops will aim at providing the foundation of stimulating the appetite of commercial banks and other FIs to engage with green clients. Furthermore, they will create awareness and stimulate interest to include an assessment of green investments (with a focus on adaptation impacts) as part of loan appraisal processes. In order to increase cross-country learning and exchange, leading commercial banks from Kenya, with a Climate Strategy already in place, will share their experiences in developing and operationalising climate actions.

3.1.1.3: Adaptation Finance Product Innovation – Practitioner Labs

111. Practitioner Labs aim at prototyping adaptation finance instruments which tackle barriers to access finance facing gender- and youth inclusive adaptation SMEs. These adaptation finance instruments will provide innovative approaches to deploy and operationalise adaptation finance by investing in adaptation enterprises. Based on interactive and innovative learning and prototyping methodologies, the Labs will facilitate the development of instruments and products which increase access to adaptation finance for SMEs in Kenya and Uganda. The Practitioner Labs will emphasise the specific obstacles and needs of women, youth (and other vulnerable groups) entrepreneurs to access finance and seek the integration of inclusive financing elements in the prototyped financial instruments.

112. Prototyping is a bottom-up, demand-driven, iterative and human-centred approach to develop targeted and effective instruments, creating ownership among the prototype developers while ensuring that the needs of the target group are met. The Practitioner Labs will leverage the local and thematical expert knowledge and extensive networks of leading FIs and fortify a community of practice through hands-on and collaborative peer-learning opportunities. To maximise the chance of adoption, the validated prototype solutions are pitched and further discussed in high-level annual Adaptation Finance Symposia (Output 1.2.2).

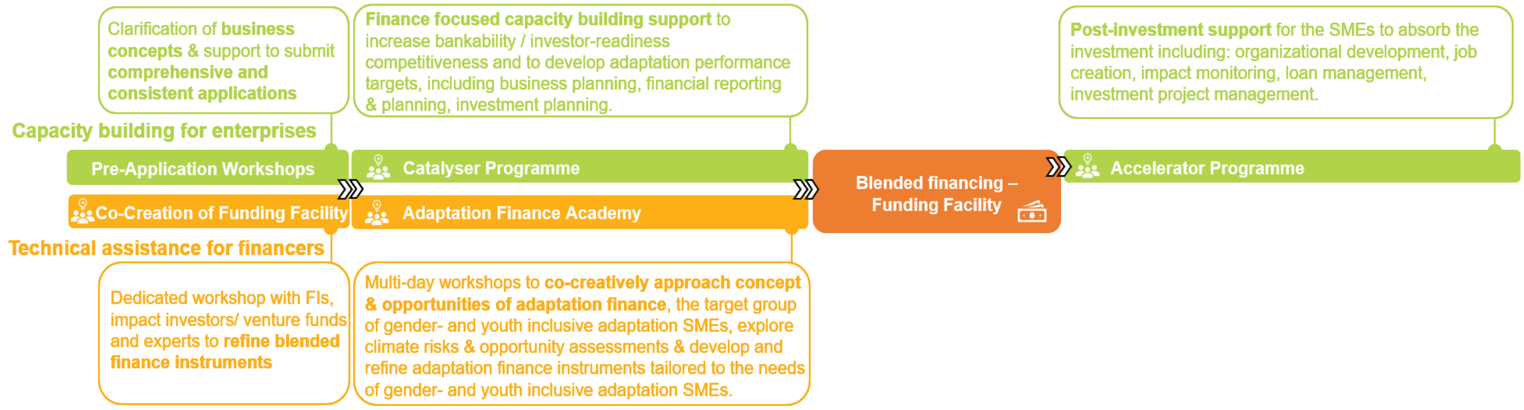


Figure 3: Intervention logic.

B. Promotion of innovative solutions to climate change adaptation

113. The project will pilot and test an innovative combination of blended financing instruments with a performance-based payment scheme while training local FIs in climate-smart financing. By both combining capacity building formats with financial support and providing tailored support to SMEs as well financers, it truly bridges the "*missing middle finance gap*" of adaptation SMEs in Uganda and Kenya. The project will not only replace "traditional" grants for enterprises by innovative and unique funding facilitation instruments which leverage private sector funding amounting up to more than two to three times the amount of grant funding provided, it will also apply an inclusive market-based approach of stimulating and scaling viable and sustainable private sector adaptation solutions with lasting impacts. In doing so, the project seeks to achieve a transformational change in the prevailing SME financing and support mechanisms. The innovation of tailored financing instruments will be sought through a co-creation process involving all core parties. The prototype financing instruments will then be tested throughout two financing cycles to distil those best fit-for-purpose. Access to tailored finance will allow adaptation SMEs to make the necessary investments in order to grow and scale their operations, leading to scaled deployment of adaptation solutions. The project seeks to achieve collaborative innovation, while at the same time building a community of practice across borders, ensuring the sustainability of the action.

114. The project will select the most innovative, finance-ready adaptation solutions offered by early-growth SMEs in Uganda and Kenya through regional calls for applications to participate in the catalytic financing scheme. All adaptation SME applications will be assessed against a set of adaptation **innovation criteria** including:

- **Fit-for-purpose**: The applicant's adaptation solution addresses the prevailing key vulnerabilities in the respective regions they operate in (see Climate Risk and Adaptation SME Solution Matrix). For example, enterprises offering/ running protected cultivation systems to address crop failure and severe crop damage due to prolonged drought periods in the arid/semi-arid landscapes of Northern Kenya.
- **Market viability**: The adaptation product or service offered by the applicant meets the needs of the target market as the final beneficiaries.
- **Financial sustainability**: The applicant needs to demonstrate financial sustainability of the adaptation business model.
- **Different or Better** The market-based adaptation solution offered is an improvement over existing solutions or a new solution that is different from the existing adaptation solutions. It must have an added value over and above what the target beneficiary is currently using/practicing to address the adaptation problem faced. These innovative solutions comprise not only new technologies and approaches, but also build on and/or revive traditional knowledge of indigenous peoples and local communities. The application should also show potential for systemic and sustained improvement of such practices or approaches.
- **Scale-up and replication potential:** The adaptation solution has a track record in the market. It has been tested and refined to meet the demands of the target market with the potential to reach out to new markets or regions. The applicant must provide proof of concept (growth plan) on how scale-up and replication of the product or service will be rolled out with the intended financing amount.

- **Transformational change potential**: The applicant's adaptation solutions provides proof of concept of system change or transformations achieved, disrupting existing default social biases that have an adverse effect on local climate resilience. For instance, this may refer to SMEs creating alternative livelihoods for marginalised pastoralist communities suffering from loss of cattle due to longer dry spells or businesses providing their product or service to remote and underserved markets.

115. The EEs understand innovation as an impact-oriented, context-specific concept and innovations promoted by the action adhere to achieve a systemic change to disrupt prevailing socio-economic structures or local procedures that have an adverse impact on local climate resilience. Innovation will therefore be assessed under the overarching vision of the action to achieve adaptation impact at scale.

116. Design thinking, prototyping and other highly collaborative formats will also be used for ecosystem building events such as the Adaptation Action Events or Annual Adaptation Finance Symposia to ensure that the ideas, knowledge and expertise of various ecosystem stakeholders are leveraged, while fostering cross-sectoral and cross-regional collaboration and facilitate peer-networking.

117. The regional approach of the project will allow to identify and promote innovations across borders, e.g. by co-inventing new adaptation solutions by SMEs from Kenya and Uganda. It also widens the scope of markets, investment and support opportunities for gender- and youth inclusive adaptation SMEs to share innovations for specific sectors and replicate these in different geographical areas.

C. Roll-out of successful innovative adaptation practices, tools and technologies

118. In order to create sustainable impact and meaningful benefits through innovative adaptation practices, tools and technologies; it is key to not only focus on developing, identifying, and promoting innovation but to also put emphasis on the roll-out and sustainability of such innovations. Therefore, the EEs will make use of a comprehensive and integrated approach to innovation that creates a bridge and flows from innovation sourcing and promotion (see above – Chapter B) to sustainability and long-lasting impact (see below – Chapter M). The EE's vision for the project is to achieve impact at scale through a multi-pronged approach to innovation roll-out.

119. There are several key elements how the roll-out of successful innovations will be supported. Firstly, at the core of this project is the financial system innovation which refers to the **piloting of the funding facilitation instruments, combined with performance-based blended financing mechanisms** (Output 2.3.1). The co-creatively designed pilot will test the financing mechanism in the market and demonstrate its value to FIs for long-term usage, potential replication by other FIs and full-scale roll-out of such an instrument for financing early-growth stage gender- and youth inclusive adaptation SMEs.

120. The pilot will benefit from the experiences of the EEs with climate-smart and green financing instruments for the SME sector in Uganda and Kenya, for instance through the Uganda Green Finance Accelerator programme[61] led by adelphi in cooperation with Finding XY, and KCV's established fund to invest in climate-smart, early growth-stage enterprises in Kenya. Based on the learnings of the EEs and in a co-creation process with local FIs, blended financing instruments in combination with performance-based payments will be tested and refined during the proposed project implementation.

121. The testing of the pilot together with comprehensive monitoring and impact assessment will enable reconfiguring and incrementally refining the innovative finance mechanism in the process of two financing cycles to make full-scale roll-out as impactful as possible and encourage FIs to scale-up their lending to gender- and youth inclusive adaptation SMEs with proven and tested innovative mechanisms. Complementary to piloting these new financing approaches with local FIs, the same FIs are supported to strategically anchor adaptation finance within their institutional set-up and operations.

122. A second key pillar for rolling out innovation will be the **support to the selected adaptation SMEs** themselves which builds on the selection criteria for SMEs described above (see Chapter C). Via the Catalyser (Output 2.2.2) and especially the Accelerator (Output 2.2.3), gender- and youth inclusive adaptation SMEs will be assisted in the scale-up and large-scale roll-out of their business model innovations and innovative adaptation products/services, tools and technologies in both target countries. Beyond the financing itself, the two non-financial pre- (Activity 2.2.1.1) and post-investment support elements will be instrumental for enabling adaptation SMEs to develop a clear growth strategy and scale-up plan that reinforces the roll-out potential and long-term viability of respective innovations in a sustainable manner and self-financed in the long run. Put differently, gender- and youth inclusive adaptation SMEs create new solutions and seek innovations. The project selects such enterprises to support the design and development of market-based, innovative and viable solutions through technical support while the enterprises pilot and demonstrate their products and services. The project then provides support to scale adaptation solutions and to replicate it in other areas and to reconfigure it wherever evidence from the piloting suggests the need for it.

123. Thirdly, the project will facilitate **system innovation through its multi-stakeholder approach** spanning across both target countries and beyond. Through various formats for network building, multi-disciplinary collaboration, and creation of sector linkages, a new regional system of support and community of practice for innovative adaptation SMEs with the participation of the private, financial and public sector will be mobilised and strengthened. With the support of the Adaptation Action Steering Committee and facilitated by the RCP, the project will develop a solid foundation for the roll-out of these system innovations and long-lasting networks and cooperation opportunities that are set to remain active after the duration of the project and will be sustainable drivers of support and innovation in the adaptation space.

124. Beyond these three pillars, the project will have overarching and cross-cutting principles and systems in place for scaling up and rolling out successful innovative adaptation practices, tools and technologies. The system of continuous monitoring and impact assessment will provide a strong basis for the EE's principle of reiterative cycles of innovation, learning, testing, and improving in preparation and throughout the roll-out of innovations. For this reason, the project will have an approach with two implementation cycles in which insights and learnings from the first cycle inform the improvement of the second one. Examples include the selection criteria for identifying the right SMEs or the reconfiguration of the piloted innovative financing mechanisms.

125. This idea of constant optimisation as a driver for effective scale-up of innovations will be fostered by the RCP and the regional approach of the project across the two countries that will facilitate cross-border learning. Through comprehensively analysing and collecting learnings as well as documenting and broadly sharing these, the project will make best practices, lessons learned, and tested innovations

[61] https://ugefa.eu/

available to a wide set of stakeholders. This will be instrumental for reconfiguring early stage innovations and developing new innovative solutions that are effective and market-ready on the basis of existing evidence, knowledge, and learnings.

126. Pathways to scale this project beyond this pilot to be funded by Adaptation Fund will be paved during project implementation: The capital injection facilitated through the project will result in catalysing enterprises to qualify for next-level finance (e.g. higher loan ticket sizes, impact / equity investments etc.). The financing facility as well as the Adaptation Finance Academy will prepare FIs to access and deploy international green finance and related climate finance instruments (such as green and sustainability bonds, blended finance, green credit lines, insurance microfinance, etc.), since they will not only be able to demonstrate an increased understanding of the climate finance landscape, instruments and requirements, familiarity with ESG assessments and a track record in deploying climate finance to adaptation enterprises. Once established and operational, the financing facility will set the benchmark of revolutionizing access to finance interventions for adaptation SMEs. The EE entity in cooperation with Finding XY and KCV, will explore further possibilities to scale its operations.

D. Economic, social and environmental benefits

Based on the analysis of climate change risks for the focal sectors and the resulting challenges for the affected vulnerable groups (Part I), the EEs have identified various economic, social and environmental benefits the project will provide to direct beneficiaries that include gender- and youth inclusive adaptation SMEs and FIs and the indirect beneficiaries of vulnerable groups and communities who make up suppliers and consumers in the SME value chains as well as their wider communities.

127. **Economic benefits:**

Benefits for the direct beneficiaries include:

- Enable gender- and youth inclusive adaptation SMEs to increase their resilience to climatic or economic shocks in the future.
- Capacity Building and financial support for gender- and youth inclusive adaptation SMEs to maintain and create additional local jobs in their communities, reaching out to additional vulnerable groups to generate local income and integrating communities into local economies and value chains.
- Increased access to adaptation finance for early-growth stage gender- and youth inclusive SMEs through training provided for FIs (Component III) on climate adaptation finance (e.g. incorporating ESG criteria in loan appraisals).

Benefits for the indirect beneficiaries include:

- Stabilises and improve incomes and future livelihoods, ultimately strengthening the local and regional economy
- Increased access to a wider variety of green and climate adaptive products and services.
- Partake in knowledge exchange and dissemination as well as set examples to other non-participating local SMEs and communities to become more resilient to climate risks through the RCP and its digital platform and events.
- Active decision making and influence in the design and implementation of the project components through consultative and co-creative formats. Active decision making and influence in the design and implementation of the project components through consultative and co-creative formats.

128. **Social benefits:**

In general, increased climate resilience of businesses, local communities, and marginalised groups not only creates direct positive existential social impacts but also leads to a wide variety of social co-benefits ranging from health and education impacts to poverty reduction, equality, and livelihoods. Some of these, for indirect beneficiaries, are further highlighted below.

- Reduction of food poverty and the stabilisation of food and water security for vulnerable groups will be improved tremendously through stable incomes.
- Develop resilient and stable food and water supply to communities and/or self-supporters through dissemination of innovative water and agricultural adaptation solutions.
- Improve the overall health and well-being of vulnerable groups and communities by freeing up time and resources typically spent on providing basic needs for themselves and enabling especially the youth and women to attend schools and other educational institutions for capacity building and upskilling.
- Contribute to eliminating key reasons for social inequalities that women, youth and marginalised groups face, through provision of access to financing and know-how about adaptation business development.
- Reduction of eco-social conflicts between settled communities and moving communities, like agri-pastoralists, on food and water resources through supported adaptative technologies and systems on irrigation, water storage, soil treatment and drought-resistant crops.
- Reduce the risk or need for forced migration of communities since using adaptative technologies and systems makes communities less likely to degrade the land or water resources.

129. **Environmental benefits:**

Positive environmental impacts are at the core of the project through the roll out of an innovative mechanism for climate adaptation finance and invigoration of ecosystem investors and FIs with an interest in investing in green and climate finance. Additionally, the RCP will play a strong role in documenting and disseminating good practices, lessons learned and tested solutions for climate adaptation and further sustainability- and climate related impacts.

- Eliminating conflicts between mankind and wildlife which will accelerate wildlife protection through the fostering of green adaptation solutions that reduces the distress on natural resources (e.g. water, soil, biodiversity).
- Increase the application of nature-based solutions that in turn replace other harmful technologies and systems.
- Support the regeneration of natural resources and also support biodiversity conservation through green products and services provided by local SMEs. SMEs
- Lead to more considerate and efficient usage and interaction with a fragile environment and scarce resources.

The non-financial support provided to the selected adaptation SMEs will include several specific tools for maximizing the positive environmental impact of the businesses as well as measures to assess and evaluate potential negative effects. In addition, the project will prepare and establish an Environment and Social Risk Management Plan which will be implemented and monitored by the EEs for the project implementation (as basis for this see risk analyses in Chapter N).

E. Cost-effectiveness analysis

130. The project's cost-effectiveness was a key consideration of the overall project design. Therefore, the project will only select high-impact gender- and youth inclusive adaptation SMEs. Hence, every dollar spent on this project will have a higher impact and better cost-effectiveness compared to other projects that support average impact SMEs. This means that the overall gender- and youth inclusive adaptation SMEs project portfolio will aim to achieve the highest possible adaptation impact.

131. In order to make sure that the selected gender- and youth inclusive adaptation SMEs achieve the best possible impact, the project will make use of performance-based payments. The performance-based payments will not only allow to track the adaptation impacts achieved, but will also allow to emphasize the financing of activities that generate the best possible impact with each dollar spent. The performance-based payments will hereby build on a robust impact monitoring and the quantification of results against each dollar spent.

132. The project will focus on activities characterised by a high scale-up and replication potential. This will not only generate best possible impacts which can be tracked at the end of the project but will also fuel impacts at scale beyond the project period. All adaptation SME solutions piloted and validated with the project financing will – with the further expansion of the SME growth – be multiplied and consolidated with the life-time of the supported gender- and youth inclusive adaptation SMEs.

133. Beyond the cost-effective use of the money spent, the grant will be used to leverage private sector capital. This means that with each selected adaptation SME that receives financial support, additional private sector capital (provided by FIs) will be leveraged. The "leveraging factor" will be an integral design criterion for the financial instruments designed, ensuring that every dollar spent catalyses additional capital, thus scaling the impacts of this project. The capital leveraged will be equally tracked by the project being an integral part of the performance-based payment tracking.

134. A break-down of the budget shares dedicated for financial support to SMEs, technical assistance and project management is given below.

Table 3: Budget break-down and leveraged private sector capital.

No of direct beneficiaries	Budget for financial support to SMEs	Budget for technical assistance & ecosystem activities	Project Management Fee	Leveraged private sector capital
30 adaptation SMEs At least 15 FIs	1,4 – 2 Mio USD*	3.208.295 Mio – 2.608.295 USD*	391.705 USD	2,8 – 6 Mio USD*
	28 - 40% of overall budget	**64 - 52% of overall budget**	**8% of overall budget**	

* Depending on design and combination of financial instruments

135. The cost-effectiveness will be further strengthened by minimising transaction costs at all levels. This will be of crucial importance for FIs as providers of investment capital for adaptation SMEs. Their financing process will follow their well-established procedures. The project will support their decision making and selection process by supporting the banks in their due diligence and later on, through the performance-based tracking of impacts.

136. By building on existing processes, structures, toolkits and relationships of the EEs, the project will further minimise transactions costs allowing the project partners to have a head start and effectively start from day one with the project implementation. This will reduce the overall programme set-up costs and will allow the project partners to focus on the implementation of programme activities to maximise the impacts of the supported gender- and youth inclusive adaptation SMEs.

137. The regional approach of the project will allow the project partners to use learnings and results from the target countries and replicate these within the scale-up of the project activities in the second financing cycle across the target countries. The grant spent within one country will herewith benefit the cost-effective implementation in the second target country. This will also allow for a benchmarking of results across the two countries.

138. Where possible, the project will aim to benchmark the project results across other SME adaptation portfolios. In order to do this, the EEs will research the cost-effectiveness of other programmes at the start of the project. This benchmarking shall emphasize the cost-effective ambition of the EEs throughout the project.

F. Consistence with national/ sub-national sustainable development strategies

139. With the deterioration of living standards and underperforming economic systems, in 2003, the Government of Kenya (GoK) formulated and implemented Kenya's Economic Recovery Strategy for Wealth and Employment Creation (ERS), built with the objection of restoring high economic growth, accelerating in industry success and improving the quality of life of its population. In addition, this strategy created a paradigm shift where for the first time in economic planning vulnerable groups and important sectors lay at the heart of economic planning as the government began prioritizing education, development and implementation of social support in arid and semi-arid region, and improving living conditions of urban dwellers in low quality housing infrastructure. With the great success of the ERS, Kenya then began expanding its vision "to sustain the recovery and move into a higher growth and development path". In 2008 the GoK announced its 'blueprint plan' for accelerating transformation into an industrialized middle-income nation by 2030. The vision 2030 agenda was anchored on several strategic principles to improve the social, economic, and governmental standings of Kenya and its vulnerable communities.

140. In early 2010 Uganda announced its first national scale development plan with their vision 2040 agenda "strengthening Uganda's competitiveness for sustainable wealth creation, inclusive growth and employment," to ensure the country reaches middle income status by 2040. Unlike Kenya, Uganda has taken a sectoral approach to achieving its vision 2040, prioritizing the following six sectors:

Agriculture; Tourism; Minerals, Oil and Gas; Infrastructure; and Human Capital Development. An additional planning document of the vision 2040 agenda was created known as the Uganda Green Growth Development Strategy 2017/18 – 2030/31 and aiming for an "inclusive low emissions economic growth process that emphasizes effective and efficient use of the country's natural, human, and physical capital while ensuring that natural assets continue to provide for present and future generations" (Vision 2040, 2017:8).

141. This project strongly relates to the national agendas of Kenya and Uganda as it strives to improve climate change resilience of vulnerable communities, who usually have low social indicators (e.g. life expectancy, poverty ratio, income), by improving their access to adaptation solutions through locally embedded adaptation SMEs. It also promotes a gender- and youth-inclusive approach to enhance inclusion and livelihoods of women and young people. Additionally, through the promotion of adaptation enterprises this project likewise contributes to the development and diversification of the country's economies, a feature that both governments have highlighted as an integral part of their planning.

142. The tables below give an overview of all relevant policies and strategies identified, and a brief description of how the project is consistent with core strategic points.

Table 4: Overview of relevant policies and strategies, and project alignment.

Plans/ strategies/ policies	Relevant strategic points and alignment with the project
Regional cooperation	
East African Community (EAC) Vision 2050: Recognizes the role of MSEs in regional industrial development agendas, underscoring the need for enhanced competitiveness through innovation and value addition to tap into intra and inter-regional trade opportunities. **EAC Development Strategy & EAC Agriculture and Rural Development Policy**: Achieve food security by increasing output, quality and availability of food and rational agricultural production through promoting complementarities and specialization under sustainable use and management of soil, water, fisheries and forests in order to conserve the environment.	The project fosters regional exchange on SME support and finance mechanisms with regards to the coordination of policies, strategies and efforts of public, private and civil society actors (Output 1.1.1) as well as by knowledge exchange and peer-learning within and between sectors and markets (Output 1.2.1/ 1.2.2, Output 1.3.1).
Agriculture	
Kenya Agricultural Policy 2021: Attain household and national food and nutrition security through innovative and sustainable interventions linked to the country's long-term development targets. Increase productivity and income growth, especially for smallholders; enhanced food security and equity, emphasis on irrigation to introduce stability in agricultural output, commercialisation and intensification of production especially among small scale farmers; appropriate and participatory policy formulation and environmental sustainability. **Agricultural Sector Transformation and Growth Strategy: Towards Sustainable Agricultural Transformation and Food Security in Kenya 2019-2029**: 3 core principles: (1) Increase small-scale farmers, pastoralists and fisherfolk incomes; (2) Increase agricultural output and value added; (3) Increase household food resilience to improve food security, the economic viability of agriculture and its resilience to climate change	The project will promote gender and youth inclusive adaptation SMEs with a focus on the agriculture (and water) sector. According to the county-based vulnerabilities displayed in the Climate Risk and Adaptation SME Solution Matrix (see Part I, Chapter 1.8), the selected adaptation SMEs (Outcome 2.1) will provide innovative adaptation solutions that – by further scale-up and replication of these business models (Outcome 2.2. and 2.3) - will specifically benefit smallholder farmers in rural and remote areas to enhance their productivity and competitiveness while being severely affected by climate-induced risks. At the same time, these SMEs will promote gender equality and the inclusion of youth and other marginalized groups, creating employment opportunities and enhanced household incomes. Moreover, preference will be given to nature-based solutions, catering to the principles of organic agriculture production. By improving the coordination of SME support approaches through multi-stakeholder networking and platform building and the dissemination of knowledge products and good practices (Outcome 1.1), the project will contribute to develop an enabling environment to strengthen agricultural services towards small and medium-sized business actors.
Uganda National Agricultural Policy (NAP) 2013: As overall objective, achieve food and nutrition security and improve household incomes through coordinated interventions that focus on enhancing sustainable agricultural productivity and value addition; providing employment opportunities, and promoting domestic and international trade. **Uganda Agriculture Sector Strategic Plan 2016**: The plan seeks to operationalise the NAP 2013 by transforming the sector from subsistence farming to commercial agriculture towards a competitive, profitable and sustainable sector. Four strategic objectives guide this process: 1) Increase production and productivity of agricultural commodities and enterprises; 2) Increase access to critical farm inputs; 3) Improve access to markets and value addition and strengthen the quality of agricultural commodities; and 4) Strengthen the agricultural services institutions and the enabling environment. **Uganda National Agricultural Organic Policy 2019**: Eight strategic targets formulated, among them the Increase in the annual growth rate in Organic Agriculture production (i); Reduce degradation of the ecosystems (iii); Increase in the contribution of Organic Agriculture sub sector to the GDP (iv); Reform and streamline extension supportive services and policy and legislative frameworks (vii). As cross-cutting principle the expansion of opportunities for business and employment in Organic Agriculture enterprises for both women and youth shall be facilitated.	
Water sector management	
Kenya Water Act 2012: Provide for the management, conservation, use and control of water resources a) to satisfy basic human needs (b) to protect aquatic ecosystems in order to secure ecologically sustainable development. **Kenya Irrigation Act 2019**: Development, management and regulation of irrigation, to support sustainable food security and socioeconomic development in Kenya.	This project specifically relates to these national objectives as it will focuses on gender- and youth inclusive adaptation SMEs from the water (and agriculture) sector. The selected and supported SMEs under this project (Outcome 2.1, 2.2., 2.3) create improved water availability through the provision of technologies that improve storage, purification and reduced agricultural water usage systems including drip irrigation and hydroponic systems. Selected SMEs also improve access and availability of water resources for women, youth and other marginalized groups.
Uganda Water Act 1997: Allow for the orderly development and use of water resources for domestic use, watering of stock, irrigation and agriculture, industrial, commercial, […], fishing, preservation of flora and fauna in ways which minimize harmful effects to the environment. **Uganda National Irrigation Policy 2017**: Vision of an additional 1,500,000 Ha under irrigated agriculture by 2040 by adhering to principles such as promotion of IWRM, commercial and market orientation, environmental principles, gender and equity and water use efficiency.	
Women and Youth	

Kenya National Policy on Gender and Development (NPGAD) 2000: Legitimate point of reference for addressing gender inequalities at all levels of government and by all stakeholders; avenue for gender mainstreaming across all sectors in order to generate efficient and equitable development outcomes **Kenya Labor Act 2002**: Legal improvements in women labor by increasing wages, implementing gender divisions in unions, and expanding maternity leave. **Kenya Youth Development Policy 2019**: Develop and improve the state of vulnerability of youth in the country **Uganda National Gender Policy 2007** (first introduced in 1997): Ensure improvements in gender equality regarding: Income, decision making, accessing justice systems, public and health care services, education, gender-based violence, access to land and financial systems. **Uganda National Youth Action Plan (UNYAP) 2016**: Improve youths' income, education status, health status, participation to foster better socio-economic performance for youth	Contributing to the national priorities of Kenya and Uganda, this project will provide support for women, youth and other marginalized groups that are highly vulnerable to climate change in two ways: 1) Specific focus on women and youth entrepreneurs as they have greater restriction to financial instruments and other resources. 2) Women, youth and other vulnerable groups are the primary beneficiaries of the adaptation solutions provided by gender and youth-inclusive SMEs supported.
SME development	
Kenya Vision 2030: Strengthening SMEs to become key industries of tomorrow by improving their productivity and innovation **Kenya Micro and Small Enterprises Policy 2020**: Provide an integrated enabling business environment for the growth and development of productive MSEs that make significant socio-economic contributions. Enhance skills & capacity development, aaccess to domestic and export markets, access to a diversified and affordable range of financial products and services, access to decent and affordable infrastructure, enhanced coordination and implementation of support programmes. **Uganda Vision 2040**: SMEs are a keystone to macroeconomic planning that takes an emphasis towards development of new industries. **Uganda Micro, Small and Medium Enterprise (MSME) Policy 2015**: Create a critical mass of viable, dynamic and competitive MSMEs, significantly contributing to the socio-economic development under the guiding principles of (among others): Policy coherence; Promoting intra and inter regional trade, Environmentally friendly and cleaner consumption and production technologies.	In accordance with national priorities in Kenya and Uganda, the project has a specific focus on supporting adaptation SMEs (Component II) as well as to create enabling conditions for these SMEs (Component I) to scale up and replicate their business models. The project will enhance the skills and knowledge of selected SMEs to become finance ready while facilitating access to affordable commercial finance. It creates SME role models for transformation of SME support mechanisms, especially of financial systems to provide accessible and affordable instruments for SMEs in the two countries (Component III).
National Climate (Adaptation) Strategies	
Kenya Nationally Determined Contribution (NDC) 2020: Agriculture and water sectors are among 13 priority sectors. Focus on agriculture includes: Mainstream climate smart agriculture; Build resilience of agricultural systems; Strengthen communication systems on climate smart agriculture and agro-weather issues. **Kenya National Adaptation Plan 2015-2030, 2016**: Priority adaptation actions, among others, are economic growth, increase in employment opportunities and improved wages of Kenyans. Sub-actions to achieve this include capacity building on 'green jobs' and enterprises, access to the Kenya Climate Fund for climate proofing investments for SMEs and upscaling of climate resilient enterprises. **Uganda NDC 2007**: Priority adaptation strategies that reduce land degradation, improve metrological services and water management practices. **Uganda NDC 2022 (interim draft)**: Provision of current baselines of important data points and desired targets for 2030. Multifaceted and multi sectoral approach to ensure climate resilience but to also support (not hinder) their vision 2030 and vision 2040 development agendas. Water and agriculture being core focal sectors. **Uganda National Adaptation Programmes of Action 2007**: Agriculture and water resources identified as highly vulnerable sectors; among the 10 intervention areas by participating communities, indigenous knowledge documentation and awareness creation, water resources and weather and climate information ranked among top 4 priorities. **Uganda National Adaptation Plan for the Agriculture Sector (NAP-Ag)** 2008: Among others, objectives are the promotion of: Climate resilient cropping and livestock production and value chains; Climate smart agricultural innovations; Knowledge of good practices and partnerships to reduce agricultural vulnerability; gendered climate smart agriculture programme to reduce the vulnerability of women, youth and other groups.	The intended impact of the project is in line with the overall objectives of national climate adaptation strategies as it proposes to support gender and youth inclusive adaptation SMEs in Kenya and Uganda to improve the vulnerabilities of local communities with a specific focus on marginalized groups. The project will focus on the water and agriculture sector, identified as two of the main priority sectors by the respective strategy documents and plans. According to the Climate Risk and Adaptation SME Solution Matrix (see Part I, Chapter 1.8), supported adaptation solutions will be selected on the basis of county-level vulnerabilities. Furthermore, preference will be given to gender- and youth-inclusive business models, solutions that are based on local/ indigenous knowledge, nature-based solutions/ eco-system-based approaches and business models that have awareness raising/ capacity development elements as an integral part (see also selection criteria under Output 2.1.1).

G. Relevant national technical standards

143. The actions undertaken within this project will be at all times in full compliance with the relevant national environmental and social safeguards and technical standards applicable in Uganda and Kenya. Based on the analysis of the most vulnerable sector groups (see Part I, 1.5 "Climate Risk and Adaptation SME Solution Matrix") and the possible adaptation solutions, for each country a range of relevant national policies and laws were identified for the project to comply with:

Table 5: Overview of relevant technical standards.

Sectors	Uganda	Kenya
Agriculture	• The Animal Breeding Act, 2001 • The Fish (Amendment) Act, 2011 • The Fish Act, 1951 • The Fish (Aquaculture) Rules, 2003 • National Agricultural Organic Policy, 2019 • The National Seed Policy, 2018 • National Agricultural Policy, 2013 • The National Animal Feed Policy, 2004	• The Agriculture Act, 2012 • The Irrigation Act, 2019 • The Crops (Amendment) Act, 2019 • The Seed and Plant Varieties (Amendment) Act, 2015 • The Agriculture and Food Authority (AFA) Act, 2013 • The Livestock bill, 2021 • National Agriculture Insurance policy, 2021 • National Livestock Policy, 2019 • The National Irrigation Policy, 2015 • The National Livestock Policy (Sessional Paper Number 2 of 2008)
Water and land	• The Water Act, 1995 • The Water Resources Regulation, 1998 • Water Act (General Rates) Instrument, 2017 • The Land (Amendment) Act, 2010 • The Land (Amendment) Act, 2004 • The Land Act, 1988	• The Water Act, 2012 • Water rules, 2012 • Water Quality Regulations, 2006 • The National Land Policy (Sessional Paper Number 3 of 2009)
Health	• Second National Health Policy, 2010	• The Biosafety Act, 2009 (as amended in 2018) • National Food and Nutrition Security Policy, 2011
Biodiversity	• The National Environmental Act, 2019 • National Forestry and Tree Planting Act, 2003 • The National Environment (Environmental and Social Assessment) Regulations, 2020 • National Environment (Minimum Standards for Management of Soil Quality) Regulations, 2001 • National Environment (Wetlands; River Banks and Lake Shores Management) Regulations, 2000	• The Environmental Management and Co-ordination (Amendment) Act, 2015
Electricity	• The Electricity Act, 1999 • The Renewable Energy Policy for Uganda, 2007	• The Energy Act, 2019 • The 2021 FiT Policy

144. Compliance with national technical standards and laws will mostly be relevant for the supported adaptation SMEs to legally conduct their businesses and to be eligible for obtaining external financing. Especially for activities such as fishery, livestock and forestry, permits or licences issued by governmental agencies are required, both in Kenya and Uganda. To hold the relevant licences and/or permits is an important factor to consider a business model as finance-ready since a missing licence/permit bears the risk of fines or shut-down. Hence, a screening by the EEs whether a licence/permit is required for an activity will be performed in the scope of Output 2.2.2 to support the shortlisted applicants to comply with all relevant regulations.

145. In Uganda, the National Environmental Act (1999) provides a legal framework to protect, develop and manage environmental sensitive areas. For the prevention harming the environment through any business or activity, together with the National Environmental Regulations (2020) it implies the obligation to conduct an environmental and social impact assessment (ESIA) for specific activities carried out in protected areas or utilizing natural resources.

146. The project aims to support the shortlisted SMEs to decide whether an assessment is required and with the preparation of such. As part of Catalyser programme (Output 2.2.2), the local EEs will utilize their expert knowledge and networks to analyse on a case-by-case basis whether an ESIA is needed. Another compliance check in regards to required licenses and/or impact assessments will be made when the supported SMEs apply for financing as part of the FIs legal due diligence procedures.

H. Duplication of project with other funding sources

147. During the design of this project and at the time of conducting stakeholder consultations, it was ensured that there is no duplication of project interventions in the two target countries. The regularly enforced synergy scouting guideline developed under Activity 1.1.2.1 further ensures continued screening for existing projects to integrate possible synergies and cooperation throughout project implementation. The project complements a series of other projects within the target countries. Therefore, the EEs will engage with such initiatives upon project approval to scope potential linkages. Among the screened initiatives so far, we find no significant evidence for risk of duplication. Further duplications will be continuously investigated throughout project implementation. Some of the projects and/or initiatives identified that the proposed project will complement in Uganda and Kenya are listed below.

Table 6: Complementarity with ongoing projects.

Other currently ongoing projects	Summary of project	Complementarity and synergies
Regional/Global		
Adaptation Fund-UNDP Innovation Small Grant Aggregator Platform (ISGAP) under Adaptation Fund Climate Innovation Accelerator - Grant funding for Not-for-Profit entities from developing countries to develop and diffuse innovative adaptation practices, tools, and technologies	Provides grants to promote innovative adaptation practices, business models and technologies at both ideation and scale-up stages. Provides grant funding on a competitive basis to from Not-for-profit, Civil Society Organisations (CSOs) including Non-Governmental Organisations (NGOs), and Business Member Associations (BMOs).	ISGAP project excludes for-profit entities and there is no concrete focus on building investment readiness of the grantees, which the proposed project targets. The ISGAP grant provision also has no commercial co-finance component, thus financial leverage is limited. Lessons learned will be explored during inception phase.
Africa SME Programme by the African Development Bank (AfDB) (2013-2023) https://www.afdb.org/en/topics-and-sectors/initiatives-partnerships/access-to-finance-for-smes-through-fis	Supports local FIs with long term liquidity and technical assistance to successfully provide relevant financing to local SMEs. Supports SME clients to ensure better loan application preparations. A key eligibility criterion is adherence to best practices in social and environmental protection.	AfDB does not finance SMEs directly. AfDB supports local FIs so they will increasingly consider SMEs for market opportunities. It focuses on increasing the capabilities and expertise of FIs to provide necessary services to SMEs which has a complementary aspect to the proposed project (Output 3.1.1).
Adaptation SME Accelerator The Adaptation SME Accelerator is an initiative led by the Lightsmith Group, in partnership with the Inter-American Development Bank, the Global Environment Facility, and Conservation International.	Builds an ecosystem for early-stage companies in emerging markets with technologies, products, and services that build resilience to the impacts of climate change. Includes the identification of adaptation SMEs, the development of a taxonomy to define "climate resilience & adaptation solutions", regional conferences for adaptation SMEs and other stakeholders, and partnerships with incubator and accelerator programs to develop adaptation, resilience and social impact-focused curriculum.	The Adaptation SME Accelerator connects companies and related stakeholders with SMEs that provide climate adaptation solutions through regional conferences, a community platform, and directory. The proposed project's regional coordination platform will rather promote knowledge management and cross-learning between SMEs and involves other components that complement the networking opportunities. Cooperation for knowledge products will be investigated, especially methodologies for supporting adaptation SMEs in developing and expanding their businesses
Climate Resilient Agribusiness for Tomorrow (CRAFT) (2018-2023) of the Netherlands Ministry of Foreign Affairs, implemented by SNV	Increases the availability of climate smart foods for the growing population in Kenya, Tanzania and Uganda. Targets small and medium entrepreneurial farmers, SME agribusinesses, and SME service providers, as well as FIs and government agencies who create an enabling environment toto foster large-scale roll-out of climate smart agriculture.	CRAFT´s activities include similar areas such as business case development and facilitating access to finance with FIs, however only target business opportunities that address climate risks in agriculture. Synergies with agricultural enterprise support will be explored.
USAID Feed the Future initiative in Kenya and Uganda	Equips small-scale producers and MSMEs (especially women- or youth-owned)) with capacities to participate and engage in agricultural market systems. Includes expanding access to markets, increasing access to finance as well as expanding demand-driven, market-oriented training programs to build skills for entrepreneurship and workforce development.	USAID´s Initiative has a strong focus on agriculture market systems and MSMEs operating within these systems. The strategy of the program follows a centralized approach and does not seek to induce cooperation or knowledge-sharing between stakeholders. The particular focus on women- and youth-led businesses provides a synergy opportunity with the proposed project.

Africa Biodigester Component (ABC) (2020-2025) project of SNV, GIZ, Netherlands Enterprise Agency, is a 5-year programme that builds on the results of the Africa Biogas Partnership Programme (ABPP) in Kenya, Uganda and Burkina Faso and helps develop and strengthen demand and supply to create sustainable biodigester markets.	Improves the end-user business case with existing agricultural programmes; increases access to finance for end-users and enterprises; strengthens biogas business case through development services and result-based finance incentives; increases support for suppliers of prefabricated biogas technology helping them enter markets and expand their activities.	TABC program targets biogas enterprises that will receive business development support as well as result-based financing. Given the specific scope of action of the ABC incentives, there is little thematic nor strategic overlap with the proposed project.
Adaptation Private Sector Initiative (PSI) project by UN Framework Convention on Climate Change (UNFCCC)	Increases the involvement of the private sector in the wider adaptation community. Developed a PSI case study database, featuring good practices and profitable climate change adaptation activities by private companies from a range of regions and sectors.	Both the proposed project and the PSI database offer a platform of private sector engagement with adaptation solutions. While the PSI database focuses on corporates (such as Nestlé and Microsoft), the proposed project focuses on MSMEMSME adaptation business models. Opportunities for cross-learning will be explored.
Uganda		
Uganda Green Enterprise Finance Accelerator (UGEFA) financed by the European Commission and the Delegation of the European Union to Uganda, implemented by adelphi. 2020-2023	Business Development Support for green enterprises to build their financial capacity and strengthen their business models. Works with banks to co-create opportunities to increase accessibility and tailoring of loans to green business models and technologies. Facilitates access to tailored finance for green SMEs, to scale their sustainability impacts, including the creation of green jobs. Reduces the risk of financing change by working together with commercial banks to provide green SME lending.	Both UGEFA and the proposed project seek to enhance access to finance for green MSMEs by working with FIs to raise awareness on green lending opportunities. Both projects also offer a financing mechanism to SMEs. However, UGEFA promotes increased access to finance for green SMEs, without focusing on a specific sector or climate focus, whereas the proposed project focuses on adaptation technologies. The proposed project also has a regional focus, fosters peer-learning between stakeholders in Kenya and Uganda to share learnings in the East African region. The UGEFA project will be in the concluding stages once the proposed action will take off and the project will benefit from UGEFA learnings and networks.
Mastercard Foundation Young Africa Works (2018-2030) with country-specific strategies to tackle youth un- and underemployment.	Focuses on finding solutions for Africa's youth employment challenge. Supports agri-food systems and agribusiness through the commercialization of agriculture; strengthens Uganda's tourism and hospitality sector; improves vocational training and expands access to financial services for MSMEs working in construction; unlocks domestic and international investments to spur growth in MSMEs.	The Young Africa Works project seeks to improve the conditions for youth employment in Kenya and focuses on the training and development of young people entering the domestic labor market. There are activities that support SMEs but there is no direct focus on improving the financial ecosystem to facilitate financing opportunities for climate adaptive SMEs. Collaborations to tap into the foundation's network and potential pipeline of youth-inclusive enterprises will be explored.
Kenya		
End Drought Emergencies (EDE-CPIRA) (2020-2023) implemented by ASAL communities, the Government of Kenya, SNV, and Water Sector Fund Kenya – with funding from the European Union (EU).	Implements Public-Private-Community Partnerships to improve the functionality and climate resilience of rural water systems. Engages the local private sector as service contractors, managers, investors, or innovative technology providers to improve water service delivery.	SNV involves private enterprises in the management of rural water systems and thus improves their revenue enhancement and cost reduction strategies, as well as climate mitigation and adaptation mechanisms. There is no direct overlap with the proposed project, however, the EEs will reach out inquire about market opportunities for adaptation SMEs to join public-private partnerships and engage in the water management sector (Activity 1.2.3.1).

Water & Energy For Food (WE4F): A Grand Challenge for Development (2020-2023) implemented by GIZ as a joint international initiative of the German Federal Ministry for Economic Cooperation and Development (BMZ), the European Union (EU), the Ministry of Foreign Affairs of the Government of the Netherlands, Sweden through the Swedish International Development Cooperation Agency (Sida), and the U.S. Agency for International Development (USAID).	Focuses on environmentally sustainable innovations aiming to improve energy and water efficiency in the agricultural sector, implemented through several Regional Innovation Hubs that facilitate regional exchange and local activities. Strengthens the skills of the selected innovators, develops skills for end users and multipliers, improves access to suitable financing, improves political and sectoral framework conditions, and strengthens exchange among specialists ((regional and global).)	Both WE4F and the proposed project follow a decentralised approach to enhance regional cooperation and improving the local framework conditions for MSMEs. The proposed project furthermore involves cross-community and cross-country exchanges. The WE4F program puts a strong focus on innovations within the water-agriculture-food nexus. The EEs will reach out to the WE4F project executives to scope potential synergies and cooperation opportunities for innovation showcasing and innovator network access.
USAID **Kenya Investment Mechanism (KIM)** is facilitating investment in key sectors of Kenya's economy, including agriculture and provides regional trade and investment opportunities. 2018-2023	Addresses insufficient quality consulting services and limited availability of tailored financial products. Uses smart incentives to mobilise finance in targeted sectors including agriculture, clean energy, and women-owned businesses in the health, water, and trade sectors. Builds the capacity of FIs and business advisory service providers through training and technical assistance to facilitate private finance and investment for smallholder farmers and SMEs. Leads policy reform efforts focused on removing barriers inhibiting large-scale investment into these sectors. Serves as an investment platform that mobilises capital from the private sector and builds partnerships between stakeholders in the financial ecosystem.	KIM allocates a substantial amount of financial support in the capacity-building of FIs to improve the structure and framework conditions of financial markets in Kenya. The trade and investment efforts focus on two-way trade and investment between the United States and Africa. The EEs, will engage with KIM executives to explore potential linkages in the framework of FIs capacity building implemented under Output 3.1.1.

I. Learning and knowledge management component

148. Iterative learning through **feedback loops** and knowledge management will be key principles of the approach for the collaboration with early-growth gender- and youth inclusive adaptation SMEs, FIs, vulnerable groups and public stakeholders.

149. Within the project team and structure, the EEs will ensure learning and knowledge management through the promotion of regular exchange and feedback. All project team members will develop systems and means to promote learning and knowledge management, including in terms of capacity building, project management and institutionalisation of knowledge. A fully-fledged **Knowledge Management (KM) strategy** including adaptive management approaches, dedicated project activities that ensure KM and the dissemination of lessons learned, learning objectives and specific indicators will be presented at full proposal stage.

150. Looking at the specific project activities, Component I focuses on the Regional Coordination Platform (RCP), which, at its core, fosters multi-stakeholder interactions, **sharing and learning through cross-community and cross-country exchanges.** A regional learning and knowledge management approach is critical for this project since Kenya and Uganda face similar climate risks with regards to agriculture and water sectors. Therefore, the learning and knowledge generation will allow learning from each other, sharing experiences among the countries and replicating successful approaches. The knowledge products developed in this context will be disseminated through national, regional, and international fora by the EEs, UNIDO outreach unit, and other networks.

151. The RCP will serve the purpose of knowledge provision, management and exchange through steering interactions between different stakeholders, offering regular **Adaptation Action Events, and acting as a knowledge hub** and distributor for profitable adaptation technologies and products. This will be guided by a multi-stakeholder Adaptation Action Steering Committee.

152. The Adaptation Action Events will link gender- and youth inclusive adaptation SMEs with other stakeholders and facilitate the exchange of adaptation entrepreneurship knowledge and learnings. Examples of such planned events are adaptation roundtables, sectorial study tours, and access to market events. Beyond this, high-level Adaptation Finance Symposia will be organised to increase knowledge of adaptation finance among key finance actors and policy makers as well as to allow for exchange and dissemination of new ideas and approaches. The piloted performance-based blended financing instruments under Component II will serve as a key source of information for the Adaptation Finance Symposia.

153. Another key pillar of learning and knowledge management covers **documenting and disseminating the impact of the roll-out, opportunities and barriers of adaptation technologies and products** by gender- and youth inclusive adaptation SMEs. This includes elements such as an Adaptation Market Analysis Report, an Evidence-based Adaptation SMEs Taxonomy, an Adaptation SME Finance Scoping Study, multimedia case study films to showcase adaptation business models and their impacts, and a digital platform for adaptation entrepreneurship practitioners and ecosystem actors. A database of adaptation products, services and technologies will facilitate cross-country replication of suitable business models.

154. Crucially, via its annual impact assessment, the project will provide single, double and triple learning loops. The impact assessment will offer evidence for project impact delivery and its efficacy (both regarding scaling of adaptation SME impact and its effect on vulnerable groups) and re-assess the necessity and appropriateness of delivery of adaptation solutions to vulnerable groups. Participatory and multi-perspective evaluation of impact assessment data is ensured by the inclusive set-up of the leading organisational body, the Adaptation Action Steering Committee. Impact assessment learnings are shared on the RCP's digital platform. Lastly, policy recommendations on developing the market for gender- and youth inclusive adaptation SMEs will be developed and disseminated in the form of Action Plan Flagship Report.

155. The RCP will further provide a comprehensive **process guidebook** that consolidates all relevant learnings and processes developed in the project for potential project takeover.

156. The design of the co-creatively (with FIs) designed pilot performance-based blended-finance mechanism, central to Component II, is guided by learnings derived from the Adaptation SME Finance Scoping Study. The mechanism will be evaluated after completion of its first investment cycle, and refinement areas will be identified and implemented to ensure a validated and efficient mechanism for the second cycle and further scale-up in a potential project extension. The mechanism's detailed processes are further subject to regular scrutiny – e.g. the adaptation SME scorecard will be incrementally refined based on the annual impact assessment, in which one section critically explores vulnerable groups' adaptation needs.

157. As part of Component III, the cross-country Adaptation Finance Academy will serve as an events-based knowledge hub to tackle the insufficient portfolio of adaptation finance products tailored to (gender- and youth inclusive) adaptation SMEs. Climate strategy workshops allow local FIs to learn from their more advanced peers to anchor strategic adaptation considerations within participating FIs, serving as the strategic foundation for adaptation action.

158. Knowledge management will be continuously integrated into the processes in the form of efficient live documentation. The project will make use of interactive digital tools such as Mural and Miro, and the focus will be on multimedia documentation. Furthermore, the project team will systematise the learning products and store them in a shared storage system / platform that is easily accessible to the client and key partners. This shared storage will contain all documents created during project implementation. In addition, management tools such as the actor landscape, the steering system, the timetable of activities, etc. will also be stored here. In this way, the stakeholders get both a general overview of the project implementation and access to findings and results, and can discuss this knowledge with the project team in trainings or regular meetings.

159. The very strong partnership approach of this project proposal is a further success factor for effective learning and knowledge management. Through a wide set of partnerships with international and national stakeholders learning and knowledge management can be promoted and boosted. Beyond the networks of SMEs and FIs and the strong and diverse project team, partnerships with a particularly strong relevance for learning and knowledge management include collaborations with other key actors from the adaptation finance, enterprise, and innovation ecosystem.

J. Consultative processes

160. A wide range of stakeholders were consulted by the Kenyan and Ugandan EEs for the design of this project, in compliance with the Adaptation Funds' ESP and GP. The consultations focused on government agencies, private sector actors and civil society organizations directly engaged with SMEs in the agriculture and water sectors, respectively working with vulnerable groups such as women and youth as the final beneficiaries of the targeted adaptation SMEs. SMEs from different sectors as the main target group of this project were consulted to find out about current challenges and opportunities in the Kenyan and Ugandan market.

161. The National Focal Points in Kenya (MoEF – Office of the Cabinet Secretary) and Uganda (MoFPED Uganda) were consulted throughout the design process and gave valuable feedback on the draft concept note. In addition, the local EEs held consultation sessions with government agencies such as the Ministry of Finance (MoFPED) in Uganda or the Water Resources Management Authority in Kenya and a series of international organisations promoting private sector development such as UNDP, RTI International/ USAID, WWF. Due to the prevailing COVID-19 pandemic, most of these consultations were held virtually.

162. As to the specific target group of this project, gender- and youth inclusive adaptation SMEs, consultations with a series of this type of SMEs were conducted to seek clarity on their specific challenges. To this end, the local EEs interviewed adaptation SMEs that are women-led and/or owned, such as for Uganda, Hamwe Enterprises (digitalisation of agriculture for smallholders), Bhundu Base Limited (sustainable tourism) and Barbets Davids Farms (land restoration and holistic livestock management); and for Kenya Mace Foods (food processing), Hydroponics Africa Limited (hydroponic farming technology) and Acacia Innovations (eco-briquettes). The majority of these enterprises also has a strong focus on youth employment as part of their business models. Specific challenges mentioned with regards to access to finance were related to the lack of collateral many women entrepreneurs face, hence, the project should pay close attention to women ownership of resources and explore alternative approaches such as movable collateral. Another important point mentioned here was the lack of access to information and data, faced by women smallholder farmers that often lack the necessary technology and face language barriers (e.g. if information is only provided in English).

163. In order to also reach out the final beneficiaries of this project, highly vulnerable groups with a specific focus on women and youth, the local EEs spoke to a series of non-governmental organisations and government authorities involved with these focus groups. For Uganda, for instance, Finding XY was in close touch with MAAIF engaged in supporting women through the village saving groups and SACCOs and with Sustainable Development Systems (SDS) Africa, working with poor women groups in remote areas on livelihood creation and economic diversification. Likewise, in Kenya, KCV interviewed WUSC and AGRA, both supporting youth employment and women empowerment. Issues raised here related to the purposeful inclusion of women and youth in both, urban and rural communities, as their vulnerability is closely linked to water access (e.g. water prices in urban areas make women more vulnerable than in rural communities where water units are cheaper). It was also said that existing initiatives to support youth should be linked to financial support for them to gain market access.

164. In the course of a mission to Kenya by the international EE, adelphi, in March 2022, a series of FIs were interviewed with the objective to identify success factors to support the SME sector in Kenya to scale their contributions to a green and circular economy, biodiversity conservation and climate mitigation and adaptation. At the same time, the mission aimed to explore the most salient challenges for green SMEs to access growth finance in Kenya to identify the most suitable interventions (capacity building & financial support) to unlock growth finance for green SMEs to scale their sustainability contributions. For that purpose, the interviews were geared to understand the level of experience and interest in green sector financing, specifically the strategic importance and the integration of Environmental Social Governance (ESG) criteria in lending decisions.

165. On the other hand, KCV is implementing a revolving risk capital facility fund in Kenya through which climate adaptation enterprises access early stage capital and business growth support. For 6 years, KCV investments have been leveraged by FIs like, Equity Bank, NCBA, KCB, RaboBank and Cooperative Bank of Kenya; and impact investors/ venture funds like, Root Capital, OPES LCEF, RaboRural Fund and KfW; and Capacity developers like, Open Capital Advisors, Africa Management Institute.

166. As a result, the following insights were found on the SME finance situation in Kenya:
- Regulatory pressure for banking sector: Requirement to develop, implement and disclose appropriate climate-related information
- Pledges and commitment of banking sector to international sustainability frameworks. However, tailored green financial products are missing
- Scattered support landscape for (green) SMEs and financial sector: Anecdotal matchmaking between SMEs & commercial banks, but no systemic solutions
- Missing link between finance demand & supply: (Green) SME Support and Green Finance Technical Assistance
- Enabling entrepreneurship environment: Kenya Start-up Bill 2021 (forthcoming) to foster entrepreneurship

167. The EEs are also closely involved with the Ugandan banking sector as adelphi and Finding XY are currently implementing the Uganda Green Enterprise Finance Accelerator (UGEFA). In the course of this engagement, a series of FIs from Uganda has taken part in the Green Finance Academy Uganda, implemented in March 2022 (please see table below for full list). At this occasion, a survey on challenges to deploy green finance to SMEs in the Ugandan market has been conducted. The following insights from the workshop and survey have been taken up for this concept note as part of the stakeholder consultations:
- Ugandan FIs struggle most with complex nature of green business models and the lack of respective appraisal processes.
- There is a substantial lack of pipeline of bankable green business models
- The banking sector overall has a low awareness or interest in financing green SMEs as they are considered high-risk and complex in nature.

168. Furthermore, the FIs interviewed at the workshop stated that they see climate change rather as a business opportunity than a risk for the Ugandan banking sector and 21 out of 28 participants stated that they expect their organisation to have a climate strategy within the next three years. Among the green sectors seen as most promising for the future, agriculture ranked as the top sector (above energy and waste management).

169. The process of interactive consultation has been highly successful, and it is planned to continue in the same spirit of collegial technical collaboration among project stakeholders and their representatives for the preparation of the proposal.

Date	Scope and Outcome of Consultation	Stakeholders Consulted
March-April 2022	Discussion relating to the role of governments and the vulnerability of communities to climate change Outcome: • Government programs have attempted to address the drivers of climate vulnerability; however, they have focused mainly on disaster minimization and less of adaptation and capacity building • Women and youth are particularly vulnerable due to their lack of access to money and jobs.	**KENYA** **Government actors**: Kenyan Ministry of Environment and Forestry, Water Resources Management Authority, Nairobi Securities Exchange **UGANDA** **Government actors**: Ministry of Finance, Planning and Economic Development (MoFPED) – National Focal Point; Ministry of Agriculture, Animal Industry and Fisheries (MAAIF); National Planning Authority (NPA)
March 2022	Discussion about barriers and opportunities related to climate adaptation financing Outcome: • Ugandan FIs struggle most with complex nature of green business models and the lack of respective appraisal processes • Substantial lack of pipeline of bankable green business models • Low awareness or interest of banking sector in financing green SMEs as they are considered high-risk and complex in nature.	**KENYA** **Financial institutions:** Pula Advisors, Equity Group, East African Development Bank, Stanbic Bank Foundation, Kenya Bankers Association, African Guarantee Fund, E4Impact, ANDE, DANIDA **UGANDA** **Financial institutions**: Bank of Africa, Centenary Bank, Equity Bank, Finca Uganda, Housing Finance Bank, NCBA Bank Uganda Limited, Opportunity Bank, United Bank for Africa, Stanbic Bank, Yako Bank, Uganda Development Bank
June 2022	Discussion about drivers of the vulnerabilities and potential avenues to reduce pressures on these groups. Outcome • Lack of access to capital especially from banks and other financial institutions are a main reason for the existence of all vulnerable groups • Competition from larger existing businesses which stifle the growth of enterprise owned by vulnerable community members (especially women and youth). • Climate change is the greatest challenge for small holder farmers, pastoralists and communities with low access to water. Understanding the issues and addressing them is multifaceted and complicated.	**KENYA** **Vulnerable groups:** Enterprise Development Officers and key representatives of Pastoralists, Communities without access to safe drinking water, Women in Agriculture, smallholder farmers, youth in agriculture consulted in the counties of Wajir and Bungoma **UGANDA** **Vulnerable groups:** Uganda Women Entrepreneurs Association Limited, Farming groups of smallholder farmers in Luweero District/ Central Region and Kitenga Sub-County, Uganda Red Cross (Wastepreneurship programme for Youths, Food and Livelihoods Program for CBOs in Moyo & Yumbe, Adjumani and Karamoja),
March-April 2022	Discussion about the role of NGOs and international organizations and the type of climate adaptation support/ programs they offer Outcome: • Mitigation and disaster reduction have dominated climate action, more effort needs to focus on developing early warning systems, flood protection, etc • There is a great opportunity to take climate smart products to scale but consumers lack awareness of the products and their benefits • There has been a low mobility of climate finance that jeopordizes the opportunity for MSME development • Due to both financing constraints and market challenges there a few adaptation MSMEs present in Uganda and Kenya	**KENYA** **Non-Governmental Organisations / International Organisations:** World University Service of Canada, WWF country office **UGANDA** **Non-Governmental Organisations / International Organisations:** CHEMONICS (USAID/Uganda strategic investments activity), UNDP Uganda, UNFCC (Regional collaboration center (RCC) Kampala), Red Cross Red Crescent Climate Centre, Sustainable Development Systems (SDS)
March-April 2022	Discussion on the barriers and opportunities related to SME development both within and outside the climate adaptation sphere Outcome: • MSMEs face strong financial and market challenges that compromises their ability to be developed. • Red tapes (paper work and documentation) are complicated and people tend not to formalise their organizations. The compounded effect of this and lack of collateral restrict enterprises from accessing FI	**KENYA** **Business association:** SME Support centre, Alliance for a green revolution in Africa **UGANDA** **Business association:** National union of coffee, agribusiness and farm enterprises (NUCAFE)
May 2022	Discussion related to the barriers and opportunities to developing adaptation enterprises Outcome: • There is an abundance of opportunities for developing adaptation MSMEs in Kenya and Uganda, enterprises just lack access to finance and technical training • Financial institutions need to become more accessible to ensure promotion of such enterprises. • Women face specific challenges with attaining collateral	**KENYA** **Adaptation enterprises:** Acacia innovation limited, Sistema bio limited, hydroponics Africa limited, Good farmland management limited, Mace foods limited, Sunken limited **UGANDA** **Adaptation enterprises:** Hamwe enterprise, Bhundu Base Limited, Barbets Davids Farms (all women-led enterprises)

170. Given the relevance of multiple actors for the proposed activities under this project, a multi-level consultation process will be initiated during the development phase of the full proposal. Each country will hold consultative meetings and workshops with relevant business associations, adaptation enterprises and their value chain partners (including micro enterprises and informal sector) as well as customer and beneficiary groups.

171. A specific focus will be on gender- and youth-focused SMEs as the primary target group of this project. As a result of the interviews and additional research, an adaptation SME market assessment for Kenya and Uganda will be developed that identifies the main challenges and opportunities for gender- and youth-focused adaptation SMEs and compiles a first pipeline of eligible adaptation SMEs for the proposed action. It should be noted that vulnerable groups such as women, youth, marginalised groups and indigenous peoples will be effectively integrated into the consultative process.

172. At the same time, the EEs will get back to the consulted FIs in both countries to seek Letters for Expression of Interest to participate in the project activities. In the course of these follow-up meetings with FIs, the EEs will present in more detail the conceptual outline of the proposed performance-based blended financing mechanisms to discuss potential financial products to be offered by FIs under the project. A specific focus will be laid on gender and youth lens investing to take into consideration gender-based factors and specific obstacles for youth to access and better inform investment decisions. This will inform the planned co-creation process to develop new and innovative performance-based blended financing instruments in the project's inception phase.

173. The project grievance mechanism will also be presented and promoted during these consultations. This approach permits to meet the needs of the stakeholders and adjust the project activities at the national levels. The inputs from these workshops will be combined and aggregated by EEs for the validation of the project document. National focal points will be invited to a regional session to present the project outline in detail and seek their feedback and advice.

K. Multiple perspectives on innovation

174. The EEs methodology is fundamentally guided by its validated focus on building multi-stakeholder and co-creation structures and processes. Co-creation as a collaboration principle of participatory design, development and implementation; fundamentally benefits from a multitude of views, positions, explicit and implicit knowledge as well as expert and non-expert participation. By integrating local expertise on lived realities, opportunities, challenges and vulnerabilities; the innovation output of such participatory action is enhanced with integrated, inclusive and customised solutions aligned with local complexities.

175. The proposed project is informed and led by multi-stakeholder and co-creative structures and processes in multiple ways: Firstly, the Adaptation Action Steering committee, the guiding body for the activities in Component I and supporting element in Component II, will consist of key actors from finance, entrepreneurship and governmental institutions as well as representatives of vulnerable groups (such as rural women associations and youth-based organisations, 1.1.1). This ensures both that 1) the RCP's activities are designed and implemented in an inclusive manner incorporating the wishes and concerns of vulnerable communities and 2) that project oversight is not blind to potential issues due to silos of expertise and particular interests. Specifically, vulnerable groups will be consulted for the Market Analysis Report, the SME Finance Scoping Study and other knowledge products.

176. Secondly, the RCP's activities are structured by its strategic framework. Within this framework, the formulation of strategic inclusion and participation safeguards will be ensured as well as the incorporation of adherence to multi-perspective and inclusivity elements for all activities throughout project implementation.

177. Thirdly, the ecosystem building Adaptation Action Events (1.2.1) and Annual Adaptation Finance Symposia (1.2.2) are highly collaborative formats enriched by valuable inputs of adaptation (entrepreneurship) practitioners that ensure that ideas, knowledge and expertise of ecosystem actors from a variety of sectors and geographies are leveraged. Cross-sectoral and cross-country collaborative events within these sub-components strengthen a holistic view on adaptation entrepreneurship and finance as well as foster peer-learning and -networking. Through dedicated formats such as panel discussions, exhibitions and roundtable discussions, each of these events will give a stage and voice to vulnerable groups.

178. Fourthly, co-creation processes in particular depend on an active engagement, trust and input by participants from different organisations and levels. Based on adelphi's validated method of co-creating meaningful and innovative outputs with FIs together with other actor groups (such as entrepreneurs and vulnerable communities), the EEs will implement the Adaptation Finance Product Innovation Practitioner Labs and Adaptation Finance Trainings. By being made conscious about the actual issues of adaptation entrepreneurs on the ground (and the needs of those most affected by climate change), financial products are prototyped in an inclusive and multi-perspective fashion. The EE acknowledge the potential of participatory design thinking process and its potential to create ownership for developed solutions among involved actors.

179. Fifthly, the financial mechanism developed under 2.3.1 will be designed in a highly collaborative manner in a co-creation process between the EEs and partnering FIs.

180. Lastly, and based on the eligibility criteria defined in the scorecard used to select enterprises (2.1.1.3), gender- and youth inclusive adaptation SMEs that 1) offer business models and adaptation impacts that address regional vulnerabilities and 2) have a gender- and youth focus are likely to represent the majority of supported and funded enterprises and, thus, offer innovative products, technologies or services tailored to their local target customers, who are predominantly climate change-vulnerable communities. As many aadaptation solutions have been agriculture-focused in previous projects supported by the EEs, it is further estimated that a significant share of supported entrepreneurs will have some touchpoints with the agricultural sector representing one of the most vulnerable sectors while at the same time, forming the backbone of Kenya's and Uganda's economy. As part of the capacity building, adaptation SMEs will be supported to develop customer and community engagement strategies.

L. Justification for funding

181. The project aims to promote a shift away from the baseline scenario characterised by

- Women and youth in Kenya and Uganda often lacking access to resources to absorb climate-related stressors appropriately, being most severely affected by climate change
- Missing middle financing for (adaptation) SMEs as they lack access to adequate financing
- Insufficient awareness and knowledge of local FIs on climate adaptation concepts and markets, resulting in insufficient investment opportunities provided for gender- and youth inclusive adaptation SMEs
- Lack of coordination and exchange on adaptation entrepreneurship opportunities between policy, financial and other supporting actors in Kenya and Uganda and across countries

182. The table below outlines the baseline and the alternative adaptation scenario that the Adaptation Fund will help materialise in targeted areas and focal sectors.

Table 7: Baseline scenarios and AF Impact.

Baseline scenario	Adaptation Fund impact
Component I	
Climate change: Kenya and Uganda's economic structures being highly dependent on agriculture and the availability of water are increasingly threatened by rising temperatures and the prevalence of extreme weather events. Precipitation is becoming more and more unpredictable, droughts and extreme rainfall events are more severe and frequent, thus drastically altering agricultural yields and leaving communities with low access to water. Smallholders constituting the main agricultural producers in both countries are particularly vulnerable due to their lack of financial resources, technological integration, awareness and training on climate change, climate adaptation solutions, and distance from urban centres. **Women and youth:** Female-headed households in Kenya and Uganda are less likely to take part in commercial farming as they mostly plant low-value crops. Women are also often the main victims of climate change-induced social, political and economic tensions, resulting in hikes in gender-based violence. Kenya's and Uganda's youth are highly vulnerable to change-related stressors such as floods or droughts, as they lack resources to absorb shocks appropriately. **National and regional responses:** Although consideration of adaptation action and SME support are two themes identified in Kenya's and Uganda's National Development and Climate Strategies and Plans (see Part II, Chapter F), the nexus of climate adaptation and adaptation solution-oriented entrepreneurship is still nascent in the two countries and the wider region. Due to the insufficient awareness among financiers, policy makers and other ecosystem stakeholders of the adaptation impact potential of early-growth gender- and youth inclusive adaptation SMEs in the region, these lack financing opportunities. There is furthermore a lack of institutional knowledge and coordination between the above-mentioned actor groups with respect to the right mechanisms to support adaptation SMEs for scale up and replication.	**Market-based adaptation solutions**: By supporting the scale-up and replication of gender- and youth inclusive adaptation SMEs in Kenya and Uganda through a catalytic financing mechanism, the project will collect evidence-based good practices and approaches to successfully support market-based adaptation solutions. The information will be made accessible through an online database and tailored knowledge products to inform policy makers, financiers and other adaptation entrepreneurship practitioners and ecosystem actors accordingly. A series of multi-stakeholder dialogues and peer-learning events will facilitate adaptation SME access to critical networks, markets and finance. **Women and youth**: The project will specifically empower gender- and youth inclusive adaptation SMEs providing products and services that close gender gaps or meet the needs of women, girls or youth, supporting gender diversity and the participation of youth through internal policies, practices and participation in the workforce, and strengthening inclusion and diversity with regards to women and youth across the value chain. As a result of the offered gender- and youth inclusive adaptation solutions, the targeted SMEs increase women and youth's resilience to climate change. **Cross-border coordination and knowledge exchange**: A Regional Coordination Platform (RCP) will be established to raise the awareness and knowledge of key stakeholders and to foster cross-country exchange about the role of gender- and youth inclusive adaptation SMEs and their adaptation impacts. The RCP connects actors in the fields of adaptation, (climate-smart) finance and entrepreneurship, encourages action to sustain and create adaptation markets and serves as a pioneering regional knowledge platform on adaptation entrepreneurship. The RCP will be led and guided by the Adaptation Action Steering Committee, made up of core actors from finance, entrepreneurship, governmental institutions and representatives from of vulnerable groups. The committee will develop a sustainable strategic framework to guide the project implementation and serve as a manual for post-project engagements of core actors.
Component II	
Missing middle financing gap: SMEs generally and adaptation SMEs in particular suffer from a substantial financing gap (see Part I: Adaptation SMEs and Part 2: J). Adaptation SMEs are disproportionately affected by the 'missing middle' financing gap between financiers and SMEs as their 1) investments often require longer time horizons to capitalise and 2) a lack of monetary indicators for returns on adaptation business models among financial products further limits their attractiveness to local FIs. In Uganda and Kenya, there is a substantial lack of finance products that (adaptation) SMEs can access. **Women and youth**: Although women in Kenya and Uganda provide an important contribution to agriculture, female-headed households still have a lower output and are less likely to take part in commercial farming as they mostly plant low-value crops. They tend to have a very low access to land in terms of ownership and management choices resulting in lack of collateral that is a prerequisite to access commercial financing.	**Catalytic financing for gender- and youth inclusive adaptation SMEs**: Through Component II, the proposed project will implement a performance-based blended financing mechanism to allow gender- and youth inclusive adaptation SMEs in Kenya and Uganda to access concessional finance on favourable terms to scale up and replicate their businesses and adaptation impacts. The AF grant will be utilised to blend existing loan products offered by local FIs that are often not eligible for these SMEs. The provision of targeted non-financial support towards investment readiness combined with blending elements will lower the investment risk for local FIs. **Women and youth**: The business advisory and investment brokerage support offered under Component II is targeted at adaptation SMEs that intentionally seek to rectify gender and/or other socio-economic inequalities in the sectors and geographical areas they operate in. Complementary to selecting this specific target, the business advisory support offers tailored tools and modules to specifically promote finance-readiness of gender- and youth-led adaptation SMEs.
Component III	
Limited financing portfolios: The financing of gender- and youth inclusive adaptation SMEs is limited by the lack of awareness among FIs in Kenya and Uganda about the business opportunities of accessing adaptation finance and channelling it into adaptation entrepreneurship. At the same time, adaptation-based lending is insufficiently anchored in FI investment strategies as many FIs in Kenya and Uganda do not have guiding climate (adaptation) strategies that lay out lending	**Adaptation-based lending**: Local FIs in Kenya and Uganda will be trained in climate adaptation concepts and methodologies while showcasing to them successful adaptation business models and raising their awareness on adaptation SME markets and business opportunities. By participating in the proposed Adaptation Finance Academy, local FIs will 1) be trained on climate adaptation concepts and adaptation SME market opportunities, 2) be capacitated to develop Climate Strategies, outlining strategic pillars for climate action, and 3)

guidelines and indicators for adaptation-based finance in line with national climate action policies.	be guided through a co-creative multi-stakeholder process to prototype innovative adaptation finance instruments.

M. Sustainability of the project

183. While the project activities are developed for the duration of the support, all components and outcomes are inherently designed to ensure long-term sustainability. Not only are impacts expected to continue beyond the closure of the project but a strong orientation towards vertical and horizontal scale-up is also a key intention and design feature of the project which further fuels project sustainability at an even larger scale. Sustainability of the project is based on two principles:

184. (1) **Scaling Up:**

Scaling adaptation SMEs' business models: Through the unique combination of capacity building and financial support, truly bridging the missing middle finance gap, the project effectively supports adaptation SMEs to scale their impacts. With its focus on viable business models, instead of adaptation project relying on grant funding, the target group has an intrinsic motivation to ensure long-term sustainability.

Stimulating lenders' appetite in adaptation SMEs: The Adaptation Finance Facility, complemented by the technical assistance provided to FIs as part of the Adaptation Finance Academy, will familiarise FIs with the needs, technologies, products and services offered by adaptation SMEs, their growth journeys and investment needs. It will catalyse the appetite and familiarity of loan officers to extend debt finance to adaptation SMEs and will strategically anchor the topic of climate adaptation in corporate strategies and commitment on management level of participating FIs.

(2) **Replication:**

Business model replication: In order to avoid that aspiring entrepreneurs, have to re-invent the wheel, adaptation SMEs will be selected according to their replication potential, characterised by easy-to-understand, adaptable business models with relatively low upfront investment costs to start a business. Replication blueprints ("adaptation business-in-a-box") will be shared through various channels, including the RCP, capacity building formats provided to SMEs and the website.

Financial instrument replication: Involved FIs will be engaged in joint fundraising to replicate the adaptation finance instruments developed as part of the project in order to ensure long-term sustainability beyond the project duration.

185. Under Component I, the established RCP will continue to create linkages between the private sector and FIs to ensure the long-term growth and support of adaptation SMEs. Also, the facilitated networks and linkages are expected to result in self-sustaining partnerships and informal communities of practice that will generate their own dynamics and lead to sustainable benefits and impacts for adaptation SMEs. In that sense, the project will act as a trigger and leverage that mobilizes and unleashes the potential of better collaboration and synergy creation in the sector, leading to long lasting impacts and self-reinforcing mechanisms of cooperation. Sustainability is achieved through the RCP's strategic framework, which acts both as a guide for project implementation and for future government organisation to carry on the project after the project duration. It also included an impact assessment strategy including a long-term vision to scale impact, a process handbook to facilitate efficient project takeover, as well as an open-source adaptation solution database (*institutional sustainability*).

186. The documentation and dissemination of knowledge, best practices, innovations, and lessons learned of performance-based blended lending to early-growth adaptation SMEs will play an important role in showcasing how financing for these companies could be systematically approached. This will help stakeholders to create appropriate financing instruments that will benefit more enterprises in the two countries and region, even after the duration of the project. Furthermore, the project will closely coordinate with other similar international efforts, players, and initiatives as to share and document best practices and gained knowledge.

187. The innovative Adaptation Finance Facility with its funding facilitation and performance-based financial instruments and investment brokerage services foreseen under Component II will enforce this long-term growth and support by providing early-growth adaptation SMEs with bespoken advisory support and catalytic financing. This will leverage the systematic strengthening and long-term sustainability of adaptation SMEs in order to unlock further investments for them to operate in difficult, changing and different markets beyond the project. It is expected that the innovative financing mechanism will showcase to FIs the business opportunities in financing early-growth SMEs, with a specific focus on gender- and youth-inclusive SMEs, and will sustainably encourage the scale-up of their lending to such companies in the future (*economic sustainability*).

188. One aim of this piloting approach is to provide a tested and proven mechanism to DFIs and other FIs with an interest in channelling adaptation finance capital via commercial banks and other local FIs to SMEs. This can be instrumental for mobilising green finance for adaptation SMEs in the future and will create sustainable impacts beyond the project itself. Connected to this aspect, a key sustainability-related outcome of this approach will be the unlocking of capital for adaptation enterprises in future and the creation of links to various follow-on investors beyond the ones included in the pilot of the project itself (*financial sustainability*).

189. Specific additional key features of the project activities in Component II that will lead to enhanced sustainability include the screening, shortlisting, and selection criteria of early-growth adaptation SMEs that will be included in the scorecard. Beyond viability and financing requirements, particular attention will be paid to their potential for business scale-up and impact of their adaptation technologies, products and services in order to ensure long-lasting sustainability of project support. The inclusiveness of the business will be another key selection criterion, as the project aims to support SMEs that have a transformational impact on local socio-economic structures by including highly vulnerable groups – with a focus on women, youth, marginalised groups and indigenous peoples – actively in their value chains and/or as final customers or beneficiaries. In addition, the provision of catalytic business development support at pre-and post-investment levels to the early-growth adaptation SMEs will be instrumental for their future ability to approach relevant investors and access finance which will create sustainable benefits and significantly improve their investment readiness and potential for growth and scale (*social sustainability*))

190. More specifically, the Catalyser (Output 2.2.2) will focus on shortlisted SMEs and improve their business management capacity and assists them in developing a comprehensive business plan in order to achieve funding readiness. The Accelerator (Output 2.2.3) then focuses on strengthening and scaling-up existing adaptation SMEs through support in securing funding, improving their financial resilience, catalyzing growth, developing finance readiness, and building in-house financial management capacities. The combination of these support activities and the additional one-on-one support elements demonstrate the strong focus of the project on long-lasting impacts and the development of resilient, growing, and flourishing enterprises way beyond the duration of the project itself.

191. The achievement of positive environmental impacts will be part of the DNA of selected adaptation SMEs. Besides their adaptation impacts, these SMEs have developed nature-based solutions and business models, reducing greenhouse gas emissions, and applying circular approaches to reduce and reuse waste, water and the consumption of other scarce resources. By supporting these SMEs to grow, the project ensures long term environmental sustainability (*environmental sustainability*).

192. With respect to achieving a transformational change in the current financial market structures in Kenya and Uganda that lack appropriate and affordable financial products for SMEs and awareness of climate adaptation related market opportunities and business models, Component III will complement the efforts of Component II in developing new and innovative financing approaches. The Adaptation Finance Academy (Output 3.1.1) will offer Kenya's and Uganda's banking sector the opportunity to expand on their nascent knowledge on adaptation finance and entrepreneurship as a lever for new financial business opportunities. Climate Strategy Workshops will be one element to ensure that the suggested funding facility (Component II) will be strategically anchored within partner FIs beyond the project duration. Cross-country learning and exchange between more advanced FIs (mainly from Kenya) that already have climate strategies in place and those FIs interested in developing such strategies will further contribute to fostering regional networks and collaborations beyond project implementation.

193. Regular monitoring and evaluation of project activities according to the project's Monitoring and Evaluation Framework (to be developed for the full proposal submission), coupled with an annual impact assessment of the direct enterprise support components will continuously inform project implementation to foresee any risks of achieving the expected outcome and sustainability of the project. In line with this, the Adaptation Action Committee will develop an Impact Assessment strategy (as part of Output 1.1.2), including methods, tools and scorecards at the beginning of the project.

194. Lastly, any training material developed will continue to be used after the end of the project by the local EEs. Good practices of adaptation business models and financing pathways will further be disseminated through the RCP to stakeholders interested and involved in similar business support activities. In general, the RCP will span across the two focus countries and beyond and will thus increase the potential reach of project impacts and of the supported companies as they scale up their operations after the end of this project.

N. Environmental and social impacts and risks

195. The project is designed to fully align with the Adaptation Fund's Environmental and Social Policy (ESP). Below is a summary of the evaluation and assessment process carried out against AF's Policy to evaluate the potential environmental and social risks and impacts of the project. The objective of this project is to facilitate investments and capacity building in early growth stage SMEs that operate climate adaptative business models in order to support them in rolling out adaptation solutions and scale their operations, ultimately building community resilience to climate change. With a particular focus on supporting female- and youth-inclusive enterprises, the project is designed to generate positive economic, social and environmental impacts through the three key Components and the respective Outputs (activities) and Outcomes (see Project Components and Financing table).

196. A risk screening was conducted for the planned activities under Components I, II and III and as a result the project is categorised as low risk (Category C) with no adverse environmental or social impacts. However, specific activities in component II, e.g. the selection of SMEs which will receive support to effectively deliver localized adaptation solutions on the ground, constitute unidentified sub-projects. As per AF ESP Policy, unidentified Sub-Projects are classified as activities or components that are not identified at the proposal stage to the level where adequate and comprehensive environmental and social risk assessment is possible. Hence this requires the project to screen, assess and monitor the unidentified subprojects accordingly in the course of the implementation period.

197. In line with the AF ESP policy the methodology of the Environmental and Social Management System (ESMS) will be developed during the fully developed proposal stage. The ESMS will contain a process for identifying environmental and social risks for the unidentified activities/sub-projects and, when needed, the development of commensurate environmental and social management elements that will complement and be integrated in the overall Environmental and Social Management Plan (ESMP). The project/programme ESMS will specify any other related procedures, roles, and responsibilities.

198. In addition to the assessment against AF's Environmental and Social Policy, an assessment against the UNIDO Environmental and Social Safeguards Policy and Procedures (ESSPP) which is a framework developed to help UNIDO decide whether a project or programme should be supported and if any environmental and social risks should be addressed along the project has been undertaken. As per UNIDO Environmental and Social Safeguards Policies and Procedures (ESSPP), the proposed project is likely to have minimal or no adverse social and/or environmental impacts and as such has been categorised as "Category C". The project will fully mainstream ESS considerations into its design. This will be achieved through the development of an Environmental and Social Management System (ESMS) as outlined above. The ESMS will guide the E&S risk screenings and assessments for any subprojects (SMEs) that will be supported through this project and will incorporate additional site-specific mitigation measures in the overall ESMP, if needed. This approach will ensure that all subprojects avoid, minimise, and/or mitigate any potential adverse E&S impacts that may emerge from their interventions/ activities across all stages of their respective project cycles (planning, implementation, post-implementation).

199. The table below provides an overview of the assessment against AF's Environmental and Social Policy. Principles that require management and mitigation actions are subsequently discussed in more detail. The mitigation measures to address the potential risks highlighted in the principles above are captured in the table below.

AF Environmental and Social Principles	Further assessment required?	Potential impacts and risks – further assessment and management required for compliance
Compliance with the Law	No	The proposed project is in full compliance with Kenyan, Ugandan and international laws and regulations. It also has the endorsement of Kenyan Ministry of Environment and Forestry (Office of the Cabinet Secretary) and Ugandan Ministry of Finance, Planning and Economic Development. Every unidentified subproject (SME) that will be supported through this project will be assessed for its compliance with national law.
Access and Equity	Yes	Components of the proposed project support locally-led, early-stage gender- and youth inclusive adaptation SMEs. Considering existing gender gaps in regards to access to resources for business (such as financing opportunities and land access), there is a low risk that the project may exacerbate these inequities. Notably, the project is also designed to focus on improving access to finance and capacity building for marginalised climate adaptation business owners. Any forthcoming unidentified subproject (SMEs) that will be supported through this project will be screened for their access and equity as it will be determined in the ESMS.
Marginalised and Vulnerable Groups	Yes	The proposed project has an extended focus to support gender- and youth inclusive adaptation SMEs led by women and/or youth in the community. It supports gender- and youth inclusive adaptation SMEs who operate within existing default social biases, and may pose a minor risk of excluding marginalised groups in the implementation of the project activities – whether as direct beneficiaries or indirect beneficiaries of the project activities. Any forthcoming unidentified subproject (SMEs) that will be supported through this project will be screened for its impact on marginalised and vulnerable groups as per ESMS
Human Rights	No	No activities in the proposed project will impede on international human rights. Unidentified subproject (SMEs) will be screened for their impact on human rights as a part of the ESMS
Gender Equality and Women's Empowerment	Yes	The proposed project targets communities where the gender gap is significant, and may pose a risk that women may not benefit equally from the project activities. Positive social impacts of the project are also dependent on receiving sufficient applications and participants from female (and youth) led SMEs as well as SMEs with business models that empower women and youths through provision of climate change adaptation solutions (gender- and youth inclusive adaptation SMEs).). Unidentified subproject (SMEs) will be screened for their impact on gender equality as a part of the ESMS.
Core Labour Rights	Yes	It may be likely that a large number of early-stage gender- and youth inclusive adaptation SMEs targeted by the project may operate informal businesses and utilise informal contracts when hiring staff, lack compliant working conditions, or lack enforcement for occupational health and safety standards in line with International Labour Organisation standards.
Indigenous Peoples	Yes	The proposed action has an extended focus to support gender- and youth inclusive adaptation SMEs that increase the resilience of vulnerable groups including indigenous peoples, where applicable.[62] The peoples who identify with the indigenous movement in Uganda face risks from the creation of conservation areas and mining activities that deny them access to land, livelihoods, protection and democratic rights. In Uganda, indigenous people all face land and resource tenure insecurity, poor service delivery, poor political representation, discrimination and exclusion. While the action aims to support locally embedded adaptation SMEs that promote socially-inclusive business models aiming to increase not only local climate resilience but also providing socio-economic co-benefits such as alternative income or job creation, there is a risk that selected SMEs operate within existing default social biases that exclude indigenous peoples to partake in the promoted business activities, thus denying them the improvement of livelihoods or business services. Unidentified subproject (SMEs) will be screened for their impact on indigenous peoples as a part of the ESMS.
Involuntary Resettlement	No	Activities in the proposed project will not cause involuntary settlement of local communities. Unidentified subproject (SMEs) will be screened to avoid supporting any projects leading to resettlement as a part of the ESMS.
Protection of Natural Habitats	Yes	The project's direct activities are not expected to have any adverse impact on the environment or natural habitats. However, while working with early-stage gender- and youth inclusive adaptation SMEs that offer products and services to help communities increase resilience to climate change, we recognise it may be likely that they operate business activities that may cause harm to natural habitats.

[62] The peoples who identify with the indigenous movement in Kenya and Uganda are mainly pastoralists and hunter-gatherers, including for Uganda mainly Benet, Batwa, Ik and the Karamojong and Basongora pastoralists – while the latter are not recognized specifically as Indigenous Peoples by the government. For Kenya indigenous peoples include the hunter-gatherers Ogiek, Sengwer, Yiaku, Waata and Awer (Boni) and pastoralists Turkana, Rendille, Borana, Maasai, Samburu, Ilchamus, Somali, Gabra, Pokot, Endorois and others. (Berger et al., 2022).

		For example, as a result of lack of resources and technology, they adopt poor waste management in the value chain, leading to pollution of local water ways and ecosystems. Unidentified subproject (SMEs) will be screened for their impact on natural habitats as a part of the ESMS.
Conservation of Biological Diversity	Yes	The project is not expected to have any adverse impact on the environment or biodiversity. Similarly, early-stage gender- and youth inclusive adaptation SMEs offer products, services and employment that help local communities increase their resilience to climate change effects. However, in doing so, they may risk overlooking maladaptation practices (e.g. doing reforestation with invasive species). These are often caused by the lack of complete information or lack of resources in implementing business activities, where businesses resort to the cheapest or quickest option available. The project aims to address these support gaps through the proposed components and activities. Unidentified subproject (SMEs) will be screened for their impact on biodiversity as a part of the ESMS.
Climate Change	Yes	The project is designed to recognise, incentivise and support gender- and youth inclusive adaptation SMEs with business models that generate climate-adaptation benefits for the local community. It will not generate significant and/ or unjustified increase in greenhouse gas emissions or other drivers of climate change. Moreover, mitigation co-benefits provided by the applying adaptation SMEs will be considered as an asset. However, the gender- and youth inclusive adaptation SMEs may still engage with conventional production activities such as the employment of carbon-intensive machinery that produces GHG emissions. Given that the project will give preference to business models that increase the adaptative capacity, respectively decrease the sensitivity of customers/ beneficiaries, the risk for the project to cause maladaptation is perceived low. Specific Assessment Frameworks will be used to identify maladaptive action and to derive scoring criteria for the selection of adaptation SMEs under the project (see Part II, Chapter A, Activity 2.1.1.3 Screening and shortlisting of applicants). In addition, a detailed set of additional mitigation measures will be outlined in the environmental and social risk management plan at full proposal stage (see Part II, Chapter N for initial concepts). Unidentified subproject (SMEs) will be screened for their impact on biodiversity as a part of the ESMS.
Pollution Prevention and Resource Efficiency	Yes	It may be the case that the value chains of early-stage gender- and youth inclusive adaptation SMEs still employ resource inefficient production methods and are unable to minimise material use effectively, due to constraints such as lack of finance to obtain modern low carbon machinery. Notably the proposed project aims to work with these SMEs to improve sustainability in their value chain to be able to attract green finance opportunities. Unidentified subproject (SMEs) will be screened for their impact on biodiversity as a part of the ESMS.
Public Health	No	No activities in the proposed project are foreseen to generate any significant negative impacts on public health.
Physical and Cultural Heritage	No	No activities in the proposed project are foreseen to cause any alteration, damage or removal of physical cultural resources, cultural sites, and sites with unique natural values. Neither does it permanently interfere with existing access and use of such physical and cultural resources. Unidentified subproject (SMEs) will be screened for their impact on biodiversity as a part of the ESMS.
Lands and Soil Conservation	No	The proposed project supports local gender- and youth inclusive adaptation SMEs that promote climate-adaptation for local populations in Kenya and Uganda, including promoting soil restoration and conservation as well as avoiding further degradation or conversion of productive lands. Unidentified subproject (SMEs) will be screened for their impact on biodiversity as a part of the ESMS.

Timeline for Risk Management and Monitoring Implementation

200. Details of each of the mitigation measures will be developed during project design and planning and revisited with all relevant implementing partners during the kick-off of each project component. For example, the setting of indicator benchmarks will be done at this stage. Monitoring will be conducted throughout project implementation, in particular, during regular jour fixe meetings. During the monitoring process, should new risks arise or further mitigation efforts are required, this will be addressed before the next stage of project implementation begins through an iterative and inclusive process. After the complete implementation of each programme component, a risk management and monitoring assessment will be conducted again to check that mitigation measures were successful in avoiding or reducing identified project risks.

201. adelphi is Europe's largest think-and-do-tank based in Germany, working on the intersection of green entrepreneurship and green finance in various countries around the globe. adelphi is committed to a just transition and creating a liveable, sustainable society and works together with financial institutions, green enterprises and policy makers to unlock finance at scale to secure a climate-neutral and resilient tomorrow. Partners and clients include the European Union, European Investment Bank, AFD, KfW, the International Development Finance Club, the Federal Ministry for Environment, Nature Conservation and Nuclear Safety, the Government of Flanders and IKEA Foundation. adelphi is leading the Uganda Green Enterprise Finance Accelerator (funded by the European Union) and the Circular Economy Catalyst Kenya (funded by IKEA Foundation). Based on adelphi's experience in the implementation of green entrepreneurship programmes in more than 35 countries globally, and its portfolio of tested and proven toolkits for SMEs and FIs, adelphi will be responsible for the conceptual and methodological approach, superficially the development of the SME selection mechanism and approach, the development of training methodologies and toolkits, the co-creation of the financial instruments as well as the set-up and implementation of the Adaptation Finance Academy. Furthermore, adelphi will provide backstopping and quality management as well as M&E support.

202. Founded in 2017, Finding XY is an innovation center that designs and implements innovative programs that provide access to low-risk capital, capacity development and markets-based research. Through our services we want to create communities where there is no Poverty (SDG1), with Gender Equality (SDG 5), creating opportunities for economic growth with decent work (SDG 8) and empowering SMEs through innovation (SDG 9). This is achieved through building global partnerships with the goal of mitigating climate change and conserving the environment. (SDG 13 and 17). Finding XY is based in Kampala, Uganda.

203. Kenya Climate Ventures. KCV is an impact investment venture fund providing innovative, targeted, and performance-based blended risk financing, bespoke technical assistance, and business growth support to enterprises, to achieve successful rollout and scale up of climate-smart solutions in Kenya. KCV has over 50 years of cumulative experience in early-stage SME financing, impact investing, application of risk capital and blended financing, climate investing, gender lens investing, sector aligned and nexus investments, enterprise development, and advisory services for sustaining SMEs growth, market stability and impact. KCV is based in Nairobi, Kenya.

204. Finding XY and Kenya Climate Ventures will be responsible for local outreach and the creation of a pipeline of relevant SMEs for the project, the delivery of the Catalyser and Accelerator Support to selected enterprises (Finding XY: Uganda; KCV: Kenya), the set up and coordination of the RCP and Adaptation Action Committee as well as the coordination of all local ecosystem activities as well as local M&E in Uganda and Kenya respectively.

PART IV: ENDORSEMENT BY GOVERNMENTS AND CERTIFICATION BY THE IMPLEMENTING ENTITY

A. Record of endorsement on behalf of the government[8] *Provide the name and position of the government official and indicate date of endorsement for each country participating in the proposed project / programme. Add more lines as necessary. The endorsement letters should be attached as an annex to the project/programme proposal. Please attach the endorsement letters with this template; add as many participating governments if a regional project/programme:*

Dr. Chris Kiptoo *Principal Secretary* *Ministry of Environment and Forestry* *Office of the Cabinet Secretary* *Kenya*	Date: *5th July 2021*
HonMatia Kasaija, *Minister of Finance, Planning and Economic Development* *Uganda*	Date: *17 August 2021*

B. Implementing Entity certification *Provide the name and signature of the Implementing Entity Coordinator and the date of signature. Provide also the project/programme contact person's name, telephone number and email address*

I certify that this proposal has been prepared in accordance with guidelines provided by the Adaptation Fund Board, and prevailing National Development and Adaptation Plans (Kenya's NAP, NCCRS and INDC, Uganda Vision 2040, Uganda's NAP, NAPA and the Climate Smart Agriculture Program (2015-2025)) and subject to the approval by the Adaptation Fund Board, commit to implementing the project/programme in compliance with the Environmental and Social Policy of the Adaptation Fund and on the understanding that the Implementing Entity will be fully (legally and financially) responsible for the implementation of this project/programme.	
Mr. Akos KOSZEGVARY Implementing Entity Coordinator	
Date: *August 4, 2022*	Tel. and email: +43 1 26026 4573 A.Koeszegvary@unido.org
Project Contact Person: Mr. Alois Mhlanga	
Tel. And Email: +43 1 26026 5169; a.mhlanga@unido.org	

[8] Each Party shall designate and communicate to the secretariat the authority that will endorse on behalf of the national government the projects and programmes proposed by the implementing entities.

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Ref: MEF/EMC/6/VOL.VIII/85

5th July, 2021

The Adaptation Fund Board
c/o Adaptation Fund Board Secretariat
Email: Secretariat@Adaptation-Fund.org

Letter of Endorsement

ENDORSEMENT FOR "UNLOCKING INVESTMENTS IN EARLY-GROWTH STAGE ADAPTATION MSMES IN KENYA AND UGANDA"

In my capacity as designated authority for the Adaptation Fund in Kenya, I confirm that the above regional project/programme proposal is in accordance with the Government's National priorities in implementing adaptation activities to reduce adverse impacts of, and risks, posed by climate change in the region.

Accordingly, I am pleased to endorse the above project/programme proposal with support from the Adaptation Fund. If approved, the project/programme will be implemented by the United Nations Industrial Development Organization and executed by Kenya Climate Ventures and Uganda Green Enterprises Finance Accelerator, in close collaboration with the relevant Government Agencies under the coordination of the Climate Change Directorate.

Dr. Chris Kiptoo, CBS
PRINCIPAL SECRETARY

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In any correspondence on
this subject please quote No. ALD 72/251/02

THE REPUBLIC OF UGANDA

Ministry of Finance, Planning &
Economic Development
Plot 2-12, Apollo Kaggwa Road
P.O. Box 8147
Kampala
Uganda

17th August 2021

The Adaptation Fund Board
C/o Adaptation Fund Board Secretariat
Email: secretariat@Adaptation-Fund.org
Fax: 202 522 3240/5

ENDORSEMENT FOR A PROJECT PROPOSAL: UNLOCKING INVESTMENTS IN FEMALE AND YOUTH-LED EARLY-GROWTH STAGE ADAPTATION MICRO, SMALL AND MEDIUM-SIZED ENTERPRISES (MSME) IN KENYA AND UGANDA

I have the honor to refer to your call for proposal under the Large Innovation Grants to support innovations and enhanced direct access.

With the support of the United Nations Industrial Development Organization (UNIDO), Uganda has developed a project proposal aimed at Unlocking investments in female and youth-led early-growth stage adaptation Micro, Small and Medium-sized Enterprises in Kenya and Uganda. The Project aims at;

1) Developing Regional coordination platform to connect adaptation, climate-smart lending, entrepreneurship, knowledge management and promote cross-learning
2) Developing Innovative blended financing mechanism and investment brokerage services
3) Building Capacities of Local financing institutions to support adaptation MSMEs

In my Capacity as the appointing Authority of the Designated Authority for the Adaptation Fund in Uganda, I confirm that the above project proposal is in accordance with the National Climate Adaptation Priorities of the Government of Uganda.

Accordingly, I am pleased to endorse this project proposal for support from the Adaptation Fund. If approved, the project will be executed by the Uganda Green Enterprise Finance Accelerator and Implemented by the United Nations Industrial Development Organization.

Matia Kasaija (M.P)
MINISTER OF FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

Copy: -The Permanent Secretary/ Secretary to the Treasury
-The Country Representative, UNIDO Uganda Office

Annex 1: Preliminary Gender Assessment

205. In general, MSMEs are highly inclusionary as they create avenues for youth, women and vulnerable groups to be included in national economies. Women and/or youth-inclusive adaptation enterprises as a sub-group and primary target group of this project are intrinsically motivated to overcome existing gender and/or other socio-economic inequalities in the socio-economic systems they operate in, aiming for a 50% gender and youth balance in their work force and/or their primary customer base, and/or providing products that address the needs of women, girls or youth. The promotion of such enterprises ensures greater inclusion of women and youth in economic activities and local value chains while increasing their climate resilience. The initial gender assessment presented here utilized in-depth desk research, key informant interviews and regional expert consultations to clarify (a) the current challenges and opportunities women face to their involvement in entrepreneurship; (b) specific vulnerabilities women face in their communities and economic sectors; (c) how the project design can be further improved to ensure greater favorability for their inclusion. This preliminary gender assessment will be further clarified and discussed in the full proposal.

Figure 5. Project gender inclusion approach

206. According to the SME Survey conducted by the Central Bank of Kenya in 2016, the distribution of SMEs by gender of business owners in Kenya was as follows: 47.9% of the licensed establishments were owned by males; 31.4% owned by females; and 20.7% were jointly owned. Further, 60.7% of unlicensed establishments were solely owned by females[63]. Whilst no data on such distributions was found for Uganda, it can be assumed that similar structures exist in Uganda. Despite the presence of women ownership of SMEs, women experience several barriers towards engaging with entrepreneurship. 1) Due to customary law and patriarchal structures women are less involved within the labor force as they are often restricted to child care and household management roles. As a result, they tend to be more involved in smallholder agricultural practices, where they have limited control over their agricultural and financial resources. 2) Women are also less likely to access financial services offered from banks such as loans. This is a crucial barrier to SMEs success. In a sample survey on the Ugandan SME sector 23% claimed that access to finance was their largest obstacle to success.

207. In summary the challenges faced by women to developing SMEs in Kenya and Uganda that will be tackled by the proposed project are as follows:

1. They fall in the missing middle of enterprise finance as their needs are too large for micro-financing but too small and risky for commercial lenders;
2. Commercial markets do not serve these early-growth stage companies because of inherent risks and unattractive returns;
3. They operate on low margins (e.g. grow low value crops, are culturally not involved in cash crop farming/ cattle rearing) and cannot afford to pay interest rates that would cover the operating costs and risks inherent for financial institutions to provide the seasonal working capital these businesses need;
4. They lack meaningful collateral as they often do not have customary rights to land;
5. They do not have the requisite credit track record (e.g. as they operate in the informal sector).

208. At its core this preliminary gender assessment sought to ensure that the project design was adjusted to ensure sufficient and accurate gender sensitivity and inclusion. The research aided in guiding 4 main areas of project planning that would be adapted for greater inclusivity.

a. Inclusion criteria: This project has recognized the importance of ensuring the selection criteria of SME have specific sections that seek to maximize the inclusion of women, youth and vulnerable groups. This is specifically done by setting the target to ensure that 50% of the company's employees or target group are women or youth.
b. Inclusive design thinking methodologies: Despite SMEs generally being considered highly inclusionary, part of the nonfinancial technical support this project offers will also include gender, youth and vulnerable group components to ensure the business models can be adapted to ensure these groups are more accurately included.
c. Inclusive loaning systems: Seeing a lack of collateral and gendered barriers (as presented above) were the main identified factors that restricted women from accessing finance, as part of the projects collaboration with banks, components will be created to inform banks on improving their inclusivity.
d. External support for participants: As mentioned above female participation in projects and workshops can be affected by patriarchal and child caring structures within these societies, in order to counter these subsidies for parental care and travel costs will be included in the project to improve this groups access to workshops.

[63] Central bank of Kenya. (2016). SME survey [2016 Micro, Small and Medium Enterprises (MSME) Survey Basic Report - Kenya National Bureau of Statistics (knbs.or.ke)]

MINISTRY OF ENVIRONMENT AND FORESTRY
Office of the Principal Secretary

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P. O. Box 30126 – 00100
NAIROBI

Ref: MEF/EMC/6/VOL.VIII/85

5th July, 2021

The Adaptation Fund Board
c/o Adaptation Fund Board Secretariat
Email: Secretariat@Adaptation-Fund.org

Letter of Endorsement

ENDORSEMENT FOR "UNLOCKING INVESTMENTS IN EARLY-GROWTH STAGE ADAPTATION MSMES IN KENYA AND UGANDA"

In my capacity as designated authority for the Adaptation Fund in Kenya, I confirm that the above regional project/programme proposal is in accordance with the Government's National priorities in implementing adaptation activities to reduce adverse impacts of, and risks, posed by climate change in the region.

Accordingly, I am pleased to endorse the above project/programme proposal with support from the Adaptation Fund. If approved, the project/programme will be implemented by the United Nations Industrial Development Organization and executed by Kenya Climate Ventures and Uganda Green Enterprises Finance Accelerator, in close collaboration with the relevant Government Agencies under the coordination of the Climate Change Directorate.

Dr. Chris Kiptoo, CBS
PRINCIPAL SECRETARY

P.o. Box 30126 - 00100 Nairobi

24 JUN 2021

PS OFFICE

RECEIVED

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION

OFFICE OF THE UNIDO REPRESENTATIVE TO KENYA, ERITREA, SOUTH SUDAN, COMOROS AND SEYCHELLES

UNITED NATIONS OFFICE AT NAIROBI, GIGIRI

P.O. BOX 41609, 00100 GPO NAIROBI, KENYA

TELEPHONE: (+254 20) 7624369/70   FAX: (+254 20) 7625286 E-MAIL: office.kenya@unido.org

File: AF/01/2021

25 May 2021

Dear Dr. Chris Kiptoo,

Subject: Request for endorsement letter to the Adaptation Fund for the unlocking investment in early growth adaptation MSMEs in Kenya and Uganda proposal

UNIDO presents its compliments to the Ministry of Environment and Forestry and has the honor to thank you for your continuous support, guidance, partnership and trust.

UNIDO was recently accredited to the Adaptation Fund (AF), which means that the organization can now submit proposals for funding. The Adaptation Fund has recently issued a call for Large Innovation Grants: https://www.adaptation-fund.org/adaptation-fund-launches-call-for-proposals-for-projects-up-to-us-5m-to-support-innovation-and-enhanced-direct-access/.
The application and endorsement of the Large Innovation Grants does not reduce the country allocations under the Adaptation Fund.

In response to the call for proposals, UNIDO has developed the attached draft proposal that seeks to unlock funding for early-growth adaptation MSMEs in Kenya and Uganda. As we work towards finalization of the proposal and as per the Adaptation Fund guidelines on their submission, we kindly request an endorsement letter from you, as the Designated Authority, confirming that the proposed activity is in accordance with government adaptation priorities. Templates for endorsement letters are available on: https://www.adaptation-fund.org/generic/government-endorsement-letter-template-submitted-through-niesriesmies/

We will be happy to schedule a call to discuss the proposal.

Yours Sincerely,

for Kawira Bucyana,
UNIDO Country Representative, OIC

Dr. Chris Kiptoo, CBS
Principal Secretary,
Ministry of Environment and Forestry,
Nairobi.

Telephone : 256 41 4707 000
: 256 41 4232 095
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: 256 41 4343 023
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Website : www.finance.go.ug

In any correspondence on
this subject please quote No. ALD 72/251/02

THE REPUBLIC OF UGANDA

Ministry of Finance, Planning &
Economic Development
Plot 2-12, Apollo Kaggwa Road
P.O. Box 8147
Kampala
Uganda

17th August 2021

The Adaptation Fund Board
C/o Adaptation Fund Board Secretariat
Email: secretariat@Adaptation-Fund.org
Fax: 202 522 3240/5

ENDORSEMENT FOR A PROJECT PROPOSAL: UNLOCKING INVESTMENTS IN FEMALE AND YOUTH-LED EARLY-GROWTH STAGE ADAPTATION MICRO, SMALL AND MEDIUM-SIZED ENTERPRISES (MSME) IN KENYA AND UGANDA

I have the honor to refer to your call for proposal under the Large Innovation Grants to support innovations and enhanced direct access.

With the support of the United Nations Industrial Development Organization (UNIDO), Uganda has developed a project proposal aimed at Unlocking investments in female and youth-led early-growth stage adaptation Micro, Small and Medium-sized Enterprises in Kenya and Uganda. The Project aims at;

1) Developing Regional coordination platform to connect adaptation, climate-smart lending, entrepreneurship, knowledge management and promote cross-learning
2) Developing Innovative blended financing mechanism and investment brokerage services
3) Building Capacities of Local financing institutions to support adaptation MSMEs

In my Capacity as the appointing Authority of the Designated Authority for the Adaptation Fund in Uganda, I confirm that the above project proposal is in accordance with the National Climate Adaptation Priorities of the Government of Uganda.

Accordingly, I am pleased to endorse this project proposal for support from the Adaptation Fund. If approved, the project will be executed by the Uganda Green Enterprise Finance Accelerator and Implemented by the United Nations Industrial Development Organization.

Matia Kasaija (M.P)
MINISTER OF FINANCE, PLANNING AND ECONOMIC DEVELOPMENT

Copy: -The Permanent Secretary/ Secretary to the Treasury
-The Country Representative, UNIDO Uganda Office

ADAPTATION FUND

Project Formulation Grant (PFG).

Submission Date: 08.August 2022

, Adaptation Fund Project ID: AF00000276
Country/ies: Kenya, Uganda
Title of Project/Programme: Unlocking investments in gender and youth-inclusive early-growth stage adaptation Small and Medium-sized Enterprises in Kenya and Uganda
Type of IE (NIE/MIE): Multilateral Implementing Entity (MIE)
Implementing Entity: United Nations Industrial Development Organization (UNIDO)
Executing Entity/ies: adelphi, Kenya Climate Ventures (KCV), Finding XY)

A. Project Preparation Timeframe

Start date of PFG	**November 1, 2022**
Completion date of PFG	**March 30, 2022**

B. Proposed Project Preparation Activities ($)

Describe the PFG activities and justifications:

List of Proposed Project Preparation Activities	Output of the PFG Activities	USD Amount
Coordinate with project Executing Entities to finalize project outline and develop implementation arrangement, including micro-assessments of the Executing entities	Finalization of the project outline and definition of implementation arrangements	15,000
Finalize the gender assessment and development of the Environmental and Social Management System	Gender Assessment Report Environmental and Social Management System	10,000
Further stakeholder consultation and validation of the final project outline	Validation of the project outline through a consultative process, including the respective community consultation reports	5,000
Total Project Formulation Grant		30,000

C. Implementing Entity

This request has been prepared in accordance with the Adaptation Fund Board's procedures and meets the Adaptation Fund's criteria for project identification and formulation

Implementing Entity Coordinator, IE Name	Signature	Date (Month, day, year)	Project Contact Person	Telephone	Email Address
Mr. Akos KOESZEGVARY		August, 4, 2022	Mr. Alois MHLANGA	+43 1 26026 5169	A.Mhlanga@UNIDO.org