



LOCAL DEVELOPMENT FINANCE

GLOBAL CHALLENGES, LOCAL SOLUTIONS

THE CHALLENGE

Many of the world's 48 Least Developed Countries (LDCs) are amongst the fastest growing economies and have made significant progress in recent years towards the achievement of the Millennium Development Goals (MDGs). As the momentum is building for the post-2015 agenda and the Sustainable Development Goals (SDGs), the focus shifts towards critical development challenges that remain. Over 1 billion people continue to live on less than \$1.25 a day and whilst absolute levels of poverty are falling, regional and national inequalities are increasing. Additionally, external shocks such as natural disasters, changing climate patterns and globalized economic relationships are testing the resilience of local communities.

The result is a more uncertain and differentiated world in which many localities are not reaping the benefits of growth. The significant resources needed to address these development challenges will require a **new thinking that goes beyond a focus on overall economic growth of LDCs** towards a more sustainable and transformative approach that mobilizes domestic public and private resources for investment in resilient local economies and societies. **How can domestic resources be reinvested locally to build resilience, reduce inequalities and stimulate inclusive growth?** This is the question that UNCDF seeks to answer through its work in Local Development Finance.

UNCDF is the UN's capital investment agency for the world's 48 least developed countries. UNCDF invests its seed capital and technical assistance to promote increased capital flows to the local level, reducing inequalities, improving basic services and increasing opportunities for sustainable economic development. UNCDF's Local Development Finance Practice does this through innovation and testing in new public and private financial systems that mobilize, allocate and invest additional resources and promote transparency and accountability in their use. The overall impact of UNCDF's work in local development finance is measured in terms of the increase in local fiscal space and the increase in local fixed capital formation that is triggered, or leveraged by UNCDF's investment.

For UNCDF, **local development is about improvement in the quality of life at the grassroots level.** This involves local governance and the decision-making process in a given locality. Yet, local development is more than local governance and decentralized provision of basic services. It is about the spatial, institutional and economic linkages within a locality. It is about how local institutional, economic and social conditions affect the spectrum of human needs: Shelter and housing, food security, education and health, safe infrastructure, aesthetic and resilient environment, citizen empowerment and representation, fulfilling and rewarding economic activity.



OUR APPROACH TO LOCAL DEVELOPMENT FINANCE

Transformative Impact Financing (TIF), uses UNCDF's Local Development Finance tools and instruments to unlock domestic capital (public or private) for local economic development, infrastructure and service delivery and entrepreneurship, with an emphasis on the transformative impact as a measure for success.

Working through local authorities and local stakeholders, TIF promotes locally born pipelines of investable projects and public investments with an impact on development such as job creation, women's economic empowerment, resilience to climate change and increases in food security. The combination of investment in the productive sector, investment in public infrastructure and strengthened local financial management releases the latent potential of the local economy and stimulates responsive public service delivery, private sector development, and local business growth. **TIF promotes local economic development that retains value within the local space.** It is measured in terms of the increases in the local fiscal space and in the local fixed capital that is triggered or leveraged by the local development finance tools and instruments.

TIF requires strengthening the capacity of existing public and private institutions and the procedures they use, as well as providing the seed capital itself.

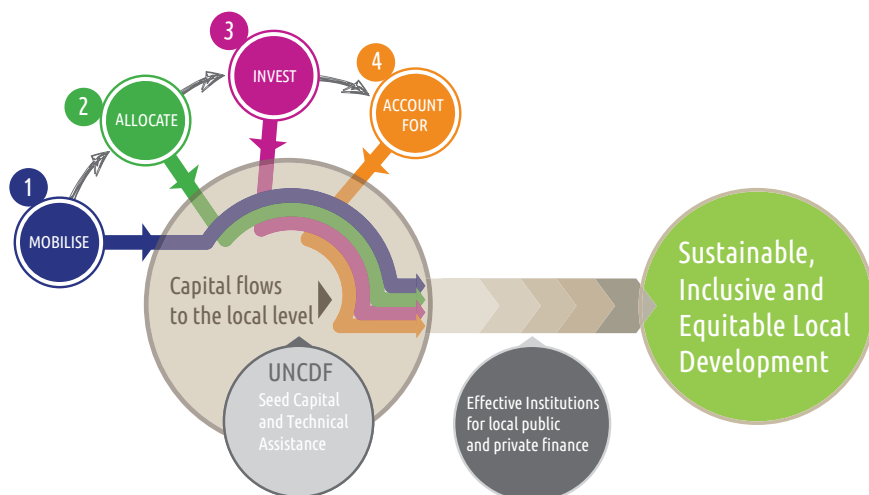


Figure 1 illustrates that the purpose of local development finance is poverty reduction through sustainable, inclusive and equitable local development.

To this end, UNCDF's Local Development Finance programmes mobilize, allocate, invest and make accountable increased capital flows to the local level through improved and strengthened local public and private institutions.

The diagram at the left shows how UNCDF seed capital and technical assistance is applied towards this end. The term "capital" is applied in its wider sense, encompassing its multiple definitions as a factor of production, an accounting term in public finance, a large scale fiscal or financial flow, an income generating resource, and finally a valuable and / or expendable resource. LDFP seed capital leverages these flows to the local level, promoting poverty reduction through local development.



LOCAL DEVELOPMENT FINANCE INVESTMENT INSTRUMENTS

Local Development Funds: Are fiscal transfers provided to local governments for investment purposes. LDFs can be fully discretionary or can be ring fenced for specific activities. The use of Minimum Conditions / Performance Measurement funding systems provide strong tools for improving local government performance while encouraging compliance with regulations, identifying capacity gaps in different functional areas, and strengthening general monitoring and evaluation systems through annual assessments.

Structured Project Finance: This financing instruments provide structured non-recourse financing solutions, in the form of collateral guarantees, for development projects as part of local development programmes. The aim is to unblock sources of local domestic finance for small and medium infrastructure projects by reducing private sector risk for selective, strategic and catalytic local economic development projects. These include industrial infrastructure projects such as energy projects, transport, warehouses, and food processing plants.

SME Cluster Finance: Designed to support local economic development by grouping their existing and potential enterprises into clusters with connected value chains, labour market requirements and other linkages. This enables economies of scale and the unlocking of domestic capital for the enterprises within the targeted cluster. This enables the addition and retention of value within the local economy, the diversification of the labour market and the stimulation of complementary activity such as legal and accounting services.

Municipal Finance: Rapidly growing towns and cities face the challenge of financing their infrastructure needs. This will require creative solutions of blended finance that include local taxes, support from central government, municipal borrowing, bond issues, public private partnerships and innovate forms of remittance and crowd sourcing finance. UNCDF supports towns and cities in least developed countries to design and test out workable solutions and business models that can be taken to scale.

LoOKING: A national diagnostic tool that examines the challenges and opportunities for local development and charts a roadmap for the introduction of scalable models of Transformative Impact Financing that will leverage increases in the local fiscal space and the local fixed capital formation. LoOKING is carried out in collaboration with governments and can contribute to the design of national strategies for local development that unlocks domestic resources to finance productive investment, infrastructure and service delivery at the local level.

HOW UNCDF IS USING ITS INVESTMENT TOOLS

Decentralisation and Citizen Empowerment: UNCDF works with local governments, promoting financial and fiscal accountability of the local state to its citizens through local development funds, performance-based grant systems, the strengthening of the local revenue streams, local procurement and accountable planning, budgeting and decision making. Local Development Funds are sustainable systems of local public investments leading to strengthened local economies and local services.

Climate Change Adaptation: UNCDF offers its local development finance core approach to local governments to help reduce vulnerability of local communities to the adverse effects of climate change through global programmes like the **Local Climate Adaptive Living Facility (LoCAL)**, which uses a performance-based climate resilient grant (PBCRG) system to channel global financial flows to address climate change to the local level.

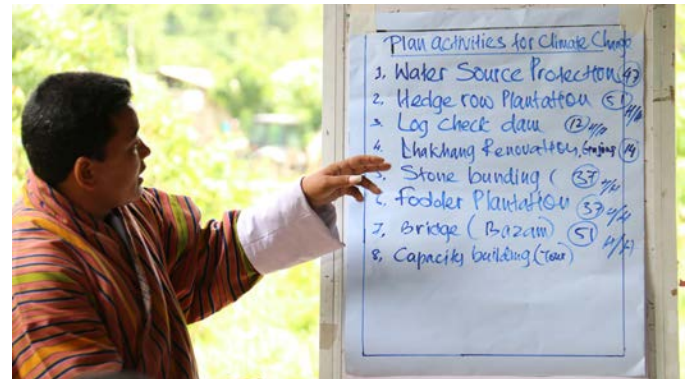
Food Security: Together with governments, UNCDF is implementing a global programme that uses a Local Food Systems (LFS) approach. **Finance for Food (F4F)** seeks to fill gaps in the local system in which food is grown, transported, processed and consumed, in order to reduce dependence on food imports and enhance local productive capacities. This programme is implemented in collaboration with the Belgian Fund for Food Security (BFFS) and the International Fund for Agricultural Development (IFAD).

Women's Economic Empowerment: The **Inclusive and Equitable Local development (IELD)** programme, implemented in partnership with UNDP and UN Women, uses a range of financial instruments (including SME cluster finance and structured project finance) to invest in infrastructure and local private sector initiatives that have a transformative impact at the local level on women's economic empowerment.

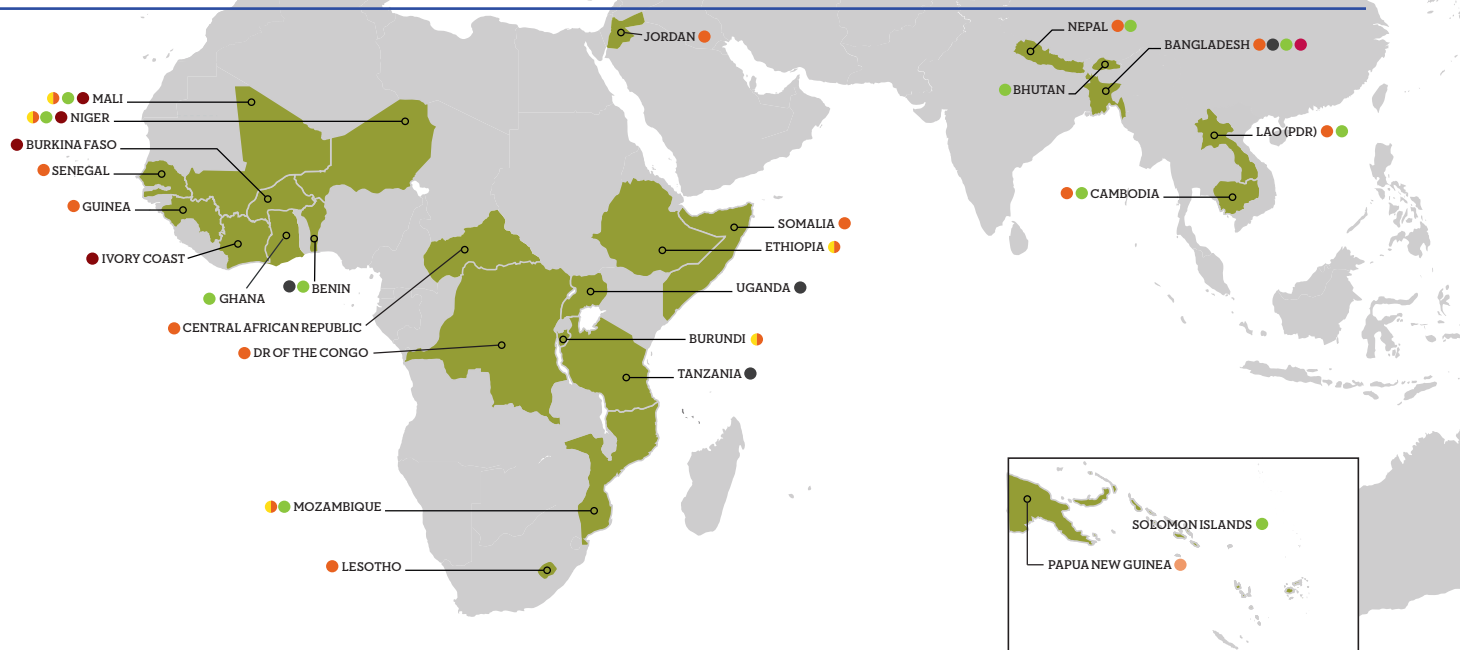
Local Economic Development: Transformative Impact Finance is about local economic development that transforms local economies. UNCDF promotes national platforms that enable domestic resources to invest in local projects with measurable impact. The approach links local government financing of public economic goods (like roads) with 'missing link' private investments like cold storage warehouses. This local intervention creates incentives for economic activity.

Cross Border Development: UNCDF supports cooperation between local authorities on either side of a national border. The **Local Cross Border Initiative (LoBI)** provides a financing mechanism for infrastructure and services that have cross-border impact and reach. LoBI provides impetus for economic integration, which can act as a foundation for maintaining and building stability in regions often characterized by conflict and volatility.

Post-conflict environments: The UNCDF approaches described above, in particular the Local Development Fund have proved particularly effective in post conflict environments. Local investments provided through accountable local institutions, and local taxes for local services build trust between the citizens and the state at the grassroots level.



UNCDF'S WORK IN LOCAL DEVELOPMENT FINANCE



- LOCAL DEVELOPMENT FINANCE COUNTRY PROGRAMME**
- IELD** - INCLUSIVE AND EQUITABLE LOCAL DEVELOPMENT
- LOOKING** - LOCALLY OWNED KNOWLEDGE= INSTITUTIONAL GROWTH

- F4F** - FINANCE FOR FOOD PROGRAMME
- LOBI** - LOCAL CROSS-BORDER INITIATIVE
- LoCAL** - LOCAL CLIMATE ADAPTIVE LIVING FACILITY
- LFI** - LOCAL FINANCE INITIATIVE

The United Nations Capital Development Fund (UNCDF) is the UN's capital investment agency for the world's 48 Least Developed Countries (LDCs). UNCDF uses its capital mandate to help LDCs pursue inclusive growth. UNCDF uses 'smart' Official Development Assistance (ODA) to unlock and leverage public and private domestic resources; it promotes financial inclusion, including through digital finance, as a key enabler of poverty reduction and inclusive growth; and it demonstrates how

localizing finance outside the capital cities can accelerate growth in local economies, promote sustainable and climate resilient infrastructure development, and empower local communities. Using capital grants, loans, and credit enhancements, UNCDF tests financial models in inclusive finance and local development finance; 'de-risks' the local investment space; and proves concept, paving the way for larger and more risk-averse investors to come in and scale up.



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