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Partnership for Environment and Growth

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INTERNATIONAL CONFERENCE:

UNLOCKING PRIVATE FINANCE

FOR ENERGY EFFICIENCY AND GREENER, LOW-CARBON GROWTH

in the Eastern Partnership and Central Asia countries

SUMMARY RECORD

OECD BETTER POLICIES FOR BETTER LIVES | UNECE | UN environment | UNIDO

UNLOCKING PRIVATE FINANCE FOR ENERGY EFFICIENCY AND GREENER, LOW-CARBON GROWTH

CAN PRIVATE INVESTORS FINANCE THE GREEN, LOW-CARBON AND ENERGY EFFICIENT DEVELOPMENT IN EASTERN PARTNERSHIP AND CENTRAL ASIA COUNTRIES

International Conference

Brussels, 29-30 June 2017

Summary Record

The conference was part of the EU-funded "Greening the Economies in Eastern Neighbourhood Countries" (EaP GREEN) project, implemented by the OECD in co-operation with UNECE, UN Environment and UNIDO. It was also supported by the German Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety.

Discussion highlights

In the context of European Union's neighbourhood and development policies, the Conference discussed initiatives and financial vehicles relevant for green finance in the Eastern Neighbourhood and Central Asia countries. The aim was to define how such finance could be scaled up. The scope of “green finance” referred to those investments that provide environmental benefits in the broader context of environmentally sustainable development such as investments in clean / renewable sources of energy, energy efficiency, reductions in air, water and land pollution, recycling and waste management, and clean transport.

The key points from the discussion include:

- ***While policy frameworks are becoming more supportive of green economies, bolder, faster, and more coherent policy action is needed to unlock green finance in the partner countries:*** The partner countries have, most importantly, undergone significant energy sector and energy subsidy reforms. However, they can do more to improve transparency and accountability of public support going to the energy sector by, among others, adopting better subsidy reporting methodologies, improving data collection and undertaking regular reporting. Focus needs to be placed on energy affordability for the poorest parts of the population and turning subsidies into clean investments, as evidenced by Ukraine's experience. Carbon pricing through a carbon tax or Emission Trading Schemes could be considered. Important lessons in this regard are provided from the EU and Kazakhstan's experience. Stricter enforcement of environmental policies and laws is also vital.

- ***Capacity for investment planning requires urgent improvement:*** Insufficient capacity to prepare and implement realistic long-term investment strategies and plans and develop green bankable projects persists. It remains one of the key bottlenecks to the scaling up of green financing in the partner countries. Given that there are substantial funding needs, international finance will not suffice to finance all green investments. Therefore, governments can seek to strengthen their green public finance systems by designing and implementing green public investment programmes in accordance with good international practices and by improving the project appraisal and selection practices of their public finance institutions.

- ***The mechanisms that are used to facilitate green investments will gain from better coordination:*** The role of International Finance Institutions (IFIs) as well as the EU-supported facilities that provide funding to green investments in the region both in infrastructure and energy efficiency and renewables (including through environmental credit lines), is crucial. The Green for Growth Fund and the Green Climate Fund are seen as opportunities to bring the major IFIs together, make them cooperate, and use these Funds’ financing to mobilise investment from donors, IFIs and the private sector. There is a need for better coordination across the IFIs and for harmonisation of the financial products they offer to commercial banks.

- ***Local financial markets require support in order to evolve into greener markets:*** Local commercial banks need to diversify and further green their portfolios if they want to stay aligned with new green market transformations and reduce their risks related to future “stranded assets”. Greening the financial sector and working through national banks is yet another opportunity for governments to stimulate green finance. Building a financial market in a country/region (e.g. lending or bonds issuance for energy-efficiency/renewable energy investments) will clearly take time but needs to start without delay.

- ***Small and medium-sized enterprises (SMEs) will need particular attention in conjunction with green finance:*** SMEs are the backbone of countries' economies while being most dependent on bank finance. Banks, with support by IFIs and donors, can design and put in place financial products that better respond to SMEs needs. On the other hand, governments need to facilitate SMEs access to finance (e.g. through targeted subsidies, setting special guarantee schemes and tax incentives, introducing regulations which support the development of other finance sources such as bonds, leasing or energy service companies).

The conference provided an opportunity to touch upon emerging topics, which are not yet on the agenda of policy makers in the partner countries. These included: implications of a green economy transition and the risk of stranded assets; development of green bonds markets and the role of the banking and monetary policy of Central Banks in stimulating green investments in the countries. Several countries expressed interest to learn more about the green bonds market and what Central Banks can do to help shape the green transition agenda. The European Commission suggested carrying on the debate and organising another regional event next year and similar events at the national level, in particular in conjunction with the roll out of the European External Investment Plan and the focus of the European Commission on promoting low-carbon development.

International conference on

Unlocking private finance for energy efficiency and greener, low-carbon growth

29 – 30 June 2017, Brussels

SUMMARY RECORD

Background, meeting objectives and participants

The current document presents a synthesis of the main issues that were discussed during an international Conference on avenues for unlocking private finance for energy efficiency and greener, low-carbon growth in Eastern Partnership (EaP) and Central Asia countries. This event took place on 29-30 June 2017 in Brussels and gathered about 120 participants representing several sectors and stakeholder groups. Primarily, these included officials from ministries of environment, economy, finance and energy, as well as from domestic public financial mechanisms, such as national development banks and energy efficiency / renewable energy funds. Experts from domestic commercial banks and lending institutions also took part in the Conference along with those from international finance institutions (IFIs) and EU-supported financial vehicles. This event was also attended by the European Commission, OECD, UN Environment, as well as the private sector, academics and non-governmental organisations.

The main objectives of the Conference were to:

- ✓ Take stock of relevant initiatives, policy changes and financial vehicles in the partner countries;
- ✓ Identify key challenges and ways forward to better align financial mechanisms with policy reforms;
- ✓ Highlight emerging topics that may need further advancement on the green growth policy agenda.

A Discussion Paper prepared by the OECD provided a background for the discussion. Two additional OECD reports, prepared under the EU “Greening Economies in the Eastern Neighbourhood” (EaP GREEN) Project, namely: "Energy subsidies in the EaP countries" and "Energy efficiency financing in Ukraine" were also circulated as support materials for the discussion. All documents related to the conference are available electronically and can be accessed here.

The Conference was co-organised by the European Commission and the OECD. It was financed by the European Union through the EaP GREEN Project, which is being implemented by the OECD together with UNECE, UN Environment and UNIDO. The Conference was also supported by the German Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety through its International Climate Initiative.

This conference was the final regional event envisaged as part of EaP GREEN work on green investments and finance and provided an opportunity to present work done by OECD over the past several years within the project and beyond. This covered issues such as the role of IFI-supported environmental credit lines disbursed by commercial banks in the partner countries; leveraging private resources through targeted public investment programmes in the transport sector; analysis of climate-related development finance in the partner countries, as well as analysis of their energy subsidies.

Opening session: Taking an integrated view

This session featured high-level speakers from the European Commission, the Eastern Partnership (EaP) and the OECD who discussed the most recent policy developments and trends in green investments and finance for an energy-efficient, low-carbon and green economy in the context of international cooperation.

Katarina Mathernová (Deputy Director General, DG NEAR) opened the conference and introduced the ***current agenda of the European Union with regard to green investment and its link to EU's neighbourhood and development policies***. Ms. Mathernová stressed that it is, first of all, the enormous benefits from energy-efficiency action that can drive the green transformation in the European Union and beyond. She pointed out that the EaP and Central Asia countries have a significant potential to grasp such benefits and enjoy strong support from the EU and its Member States to do so. Ms. Mathernová confirmed the willingness of the European Union to continue to accompany the partner countries in their efforts to move towards a greener and more sustainable path of economic development. She also explained that energy efficiency will be among the key areas of policy dialogue in conjunction with the upcoming Eastern Partnership Head of States Summit, which will be held in November 2017 in Brussels. This stems from the fact that energy connectivity and sustainable energy are important elements of energy security as identified at the Riga Summit in 2015. To support progress in this area, Commissioner Hahn launched a high level energy-efficiency initiative in 2016 together with the European Bank for Reconstruction and Development (EBRD), European Investment Bank (EIB), World Bank, International Finance Corporation (IFC) and International Monetary Fund (IMF), in which IFIs agreed to actively collaborate to bring to scale energy efficiency reforms and investments. This initiative has a specific focus on energy efficiency in buildings as buildings account for up to 40% of energy consumption in many countries in the region. Targeted work was already launched in selected pilot countries, which include Ukraine and Georgia. On a broader scale, by combining financial assistance with policy dialogue to enable investments, in the energy sector, among others, the EU External Investment Plan will help achieve significant improvements as set by the Sustainable Development Goals and the Paris Agreement on climate action.

Mykola Kuzio (Deputy Minister of Ecology and Natural Resources, Ukraine) spoke about the ***main policies that his government had put in place to help drive green transformation in Ukraine*** including policies related to macro-economic stabilisation, consolidation of the banking system, EU Association Agreement, ratification of the Paris Accord on Climate Change. Mr. Kuzio stressed that environmental consciousness had been an important part of the preparation of a comprehensive policy process and national reform agenda in his country. He also brought up a number of challenges with regard to green policy reform which the government of Ukraine needs to focus its further efforts on. Some of these challenges include: improving environmental taxation, strengthening the environmental enforcement and compliance system, introducing carbon pricing and green procurement, reducing fossil-fuel subsidies. Mr. Kuzio stressed the need for improved cooperation between IFIs and local commercial banks in order to better leverage costly credits and ensure sustainable and accessible financing for green investments. While IFIs help create clean energy markets, domestic commercial banks need to make further efforts to sustain these markets. Mr. Kuzio also underlined the role of state-owned banks as first movers in this direction.

Simon Upton (OECD Director for Environment) addressed participants though a video message and acknowledged the ***EU's and Germany's long-standing relations with the OECD in supporting the greening of economic growth in the EaP countries and Central Asia***. Mr. Upton pointed out that while the partner countries had made significant progress in terms of political, economic and social transformation, they remain very energy and carbon-intensive and continue to rely on fossil fuels as a key driver of their economic growth and as a source of government rent. Such underlying conditions often create resistance to low-carbon transition and governments need to ensure that green policy making is aligned with the imperatives of the new climate agenda. Mr. Upton spoke about the transitional consequences of green transformation for companies, investors, governments and communities. This transition represents a significant economic opportunity for the countries creating prospects for new investments in low-carbon and energy-efficient growth. Mr. Upton underlined the decisive role of governments in providing the right conditions and incentives that can stimulate financial and capital markets to invest in green projects.

He concluded that since these investments will influence our future over the next 20 - 40 years, the transition has to be well and thoughtfully managed in order to ensure that its possible negative effects on people and their everyday lives should be adequately mitigated.

Jürgen Keinhorst (Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety, Germany) spoke about the ***main challenges that the countries of the EaP and Central Asia have to address in order to put their economies on a greener*** path. Some of these challenges include: aging infrastructure, low finance for infrastructure operation and maintenance, technology backlog, low productivity and high-carbon intensity. He listed the key factors of success including political and economic stability and regulatory predictability, good governance, stable and capable administration, a broader use of economic incentives in green policies. Mr. Keinhorst stressed the need to exploit the energy-water-food nexus as a vehicle for integrating climate and green policies and make them part of the long-term country development strategies. In addition, he emphasised that IFI and donor support has a catalytic effect in mobilising finance but the bulk of resources should come from the countries themselves. Mr. Keinhorst also underlined the need for continuous donor support to capacity development particularly to those sectors / policy areas where countries could not succeed on their own. Germany has put in place about 70 twinning projects for both new EU member states and other countries and Mr. Keinhorst encouraged participants to consider such twinning opportunities as a way to increase capacity for policy development in their countries.

In summary, the main points that emerged from the interventions of the high-level speakers were:

- The green transition represents a significant economic opportunity creating prospects for new investments in low-carbon and energy-efficient economic growth. Investments in energy efficiency are “a low-hanging fruit” and a significant driver of the green transformation in the European Union and beyond.
- Governments need to ensure that green policy making is aligned with the imperatives of the new green and climate agenda. Investments made today will influence our future over the next 20 - 40 years, therefore the transition has to be thoughtfully managed in order to mitigate possible negative effects on people’s lives.
- Governments have a decisive role to play in providing the right conditions and incentives that can stimulate financial and capital markets to invest in green projects. While IFI and donor support has a catalytic effect in mobilising finance the bulk of resources should come from the countries themselves. At the same time, there is a need to improve cooperation between IFIs and local commercial banks in order to better leverage costly credits and ensure sustainable and accessible financing for green investments.
- Donors need to continue to support capacity development particularly in those sectors / policy areas where countries cannot succeed on their own. The EU and its member states expressed their willingness to continue to support the partner countries in their efforts to move towards a greener and more sustainable path of economic development.

Session 2: Lessons learned from mobilising capital markets

This session focused on the role of capital markets, and how these markets have responded to the new green and climate-related challenges in the EaP and Central Asia countries.

Matthew Savage (Consultant to EaP GREEN, Oxford Consulting Partners) presented the ***main findings and conclusions of an OECD study on lending to corporate energy efficiency in Ukraine*** conducted as part of the EaP GREEN project and also supported by Germany. The study looked particularly at the experience of the state-owned Export-Import Bank of Ukraine (Ukreximbank) with designing and managing environmental credit lines provided by IFIs and on-lent to end borrowers. Ukreximbank is the largest intermediary recipient of IFI energy-efficiency finance in the region. Ukreximbank has taken more than EUR 500 million in 6 credit lines from 5 IFIs and other financing bodies. Mr. Savage stressed that the high energy intensity of the economy underpins the attractiveness of Ukraine as a suitable place for energy-efficiency lending. However, the expansion of energy-efficiency lending is constrained by a number of wider macro-economic and regulatory challenges faced by local financial institutions. These are compounded by a series of demand side barriers (e.g. unstable energy pricing, lack of awareness of benefits of energy-efficiency investments, demanding collateral requirements). Mr. Savage also explained that there were several reasons that contributed to Ukreximbank's success: initial technical support provided by the IFIs along the credit lines, Ukreximbank's senior management commitment and resources, new regulatory and policy reforms (e.g. increases in industrial energy prices).

Jan-Willem van de Ven (EBRD) spoke about the ***EBRD experience with setting Green Economy Financing Facilities (GEFF) in a number of countries in the region***. The main objective of the GEFFs is to help mainstream green finance into the operations of local banks and their clients by stimulating the uptake of high-performance green technologies, services or practices. Mr. van de Ven noted that the EBRD partners with local financial institutions to lower market barriers for early movers by providing technical assistance and incentive payments to borrowers and making risk-sharing arrangements with banks. While the EBRD is helping local banks to create new markets by developing new products (credit lines, mortgages, climate-related financial backing), credit lines alone cannot ensure a systemic change. Prior to financing, there is a need to increase awareness of benefits of new clean technologies both across banks and borrowers (which is often the highest transaction cost in financing such investments). Mr. van de Ven pointed out a particular problem related to energy-efficiency (EE) audits. Given that audit costs are usually high, such audits are undertaken mostly by large companies where the possibilities for savings from EE measures are also large (USD 10 - 40 million on average). For small and medium-sized enterprises (SMEs), households and other end-users, there is a need to develop simpler web-based tools (e.g. lists of eligible pre-selected equipment such as pumps, boilers or motors) which could help such clients select the right technologies themselves and reduce their costs.

Christopher Knowles (Green for Growth Fund (GGF) shared some "***Lessons learned from mobilising private capital for energy efficiency (EE) and renewable energy (RE) investments***" that have emerged from the operations of the Green for Growth Fund in the region. Mr. Knowles highlighted the importance of GGF support for the full-cycle of the energy finance process. He pointed out that the GGF was created to bring all IFIs together and make them cooperate and harmonise their products. Mr. Knowles explained that it is the Fund's capital structure (public-private partnership) that increases the effectiveness of donor funding by bringing in additional private capital from both multilateral and private institutional investors that might not otherwise be attracted to the sector or the region. Mr. Knowles also pointed out that GGF experience shows that when establishing a new financial vehicle it is not good to rush through the process as the first tangible results can usually be expected 4-5 years after the launch of the operations of the vehicle. To scale up the Fund's impact, Mr. Knowles noted the need for additional public and private capital, increased bankability of RE projects or currency solutions in some countries in the region (Azerbaijan, Georgia, Ukraine). He also pointed out that capital will come when there is demand.

Jakob Thomä (2° Investing Initiative) presented the ***experience of EU markets with regard to giving SMEs access to green finance***. Mr. Thomä spoke about the differences in the banking structure across Europe (commercial, cooperative and public banks) and how these differences influence domestic loans market shares (bank lending vs. non-bank lending). It is mostly public and cooperative banks that lend to SMEs and households and offer loan maturities longer than 5 years. On the supply side, there is a need to diversify commercial banks' portfolios and better align IFIs' investments with local commercial lending. On the demand side, it is vital to demystify investment in EE: EE is not so much about interest rates but about financial and environmental savings that can be achieved as a result of such investments. Developing a proper business case for EE investments can help reduce the perception of risks and increase demand for green lending. Mr. Thomä also pointed out the clash between the conspicuous role of SMEs in the (green) economy and their limited access to (not only green) finance. One particular issue related to tracking CO_2 emissions in green investments and of concern to banks is the cost of data needed to assess banks' climate-related equity portfolios. These costs have been rapidly declining over the past several years in the EU and the USA (due to data available from the Emissions Trading Schemes). However, due to the current low carbon price in the EaP and Central Asia countries full carbon accounting in lending institutions may not happen soon.

The main highlights from this session included:

- Commercial banks in the EaP countries and Central Asia continue to dominate financial markets but green lending is not yet a consistent part of their corporate portfolios. Public and private equity funds and venture capital firms, both of which provide equity capital allowing companies to leverage debt from commercial banks, are still immature. It is mostly IFIs and various EU-supported facilities (e.g. Green for Growth Fund, E5P) that provide green finance. Environmental credits lines established by the IFIs in selected domestic banks aim to create a sustainable market for green lending. However, commercial banks need to diversify and further green their portfolios if they want to stay aligned with new green market transformations and reduce the risks related to future “stranded assets”.
- IFI-supported environmental credit lines alone however cannot ensure a systemic change in financing green investments. Prior to financing, there is a need to increase awareness of benefits of new clean technologies at both domestic banks and borrowers. Donors, governments and civil society organisations can do more to support IFIs' efforts in awareness-raising and knowledge-sharing.
- On the demand side, it is vital to demystify investment in EE. Investing in EE is not so much about interest rates but about financial and environmental savings that can be achieved as a result of such investments. It is also about the quality of project preparation. Well-designed projects have better chances to get financing. Donors and governments can more pro-actively support the identification and preparation of projects which make a good business sense.
- SMEs which are the backbone of region's economies and are most dependent on bank finance need particular attention. Banks, with support by IFIs, can design and put in place financial products that better respond to SMEs needs. Banks will always perceive lending to small businesses as higher risk. For this reason, access to alternative sources of funding for such businesses and support from government is so important.

Session 3: Unlocking private finance for green investment: The role of public authorities

The discussion during the first day underlined the importance of capital markets in financing green projects. At the same time everybody recognises that governments have a certain role to play in helping unlock private finance for green investments. What governments can do and what instruments they can use (regulatory, financial) to help stimulate higher demand for green finance were the main issues discussed during the third session of the conference. Two specific instruments were presented namely setting a carbon price through emission trading and providing targeted public support for investments in clean transport. Both examples came from Kazakhstan.

Anna Pegels (German Development Institute) spoke about ***government interventions aimed at creating demand for and mobilising green private investments***. Ms. Pegels outlined various policy instruments that governments have at their disposal (including financial and market-based instruments, regulatory mechanisms, coordination platforms, or soft information measures) to help lower risks and increase returns on green investments. Ms. Pegels also spoke about the political economy of green transformation. As such transformation involves major economic restructuring there are a lot of actors who have vested interests in the process and the main question of who wins and who loses as a result of the change needs to be carefully analysed. Both big actors (e.g. oil and gas companies) and small players (e.g. households who protest again fossil-fuel reforms) can have powerful political influence on policy reform through their veto powers. A successful policy package put forward by governments aimed at mobilising green private investments should consider stakeholders' interests along with the feasibility of proposed actions and the capacity of all actors to implement them.

Sabyr Assylbekov (Ministry of Energy, Kazakhstan) presented ***Kazakhstan’s experience with setting up an Emissions Trading Scheme (ETS)***. Mr. Assylbekov explained the main elements of the ETS which is considered one of the main instruments to achieve the country’s climate targets under the Nationally Determined Contribution. The ETS was launched in 2013. After the second trading period of 2014-2015 when it experienced some challenges, ETS is now being prepared for a re-launch in 2018. Mr. Assylbekov informed participants of the progress in re-launch preparations including new methodological work, trading permits, legal documentation. Contrary to the first two phases which used the "grandfathering" approach (based on historic amounts of CO_2 emissions) to allocate carbon permits across participating enterprises, the third phase (2018–2020) is designed to use a benchmarking method. This method is based on the EU ETS system and is designed to reward more efficient companies. However, as Mr. Assylbekov explained, benchmarking is not without problems as it may lead to the shutdown of some high GHG emitting companies. Kazakhstan has learned a lot from the EU ETS but in designing its own scheme, the government has taken into account Kazakhstan's economic, development and climatic specifics. Among the major challenges to ETS implementation, Mr. Assylbekov mentioned inflexible legal framework, low (or unclear) carbon unit price, unreliable data provided by companies, untimely issuance of certificates by the authorities. He also noted that the President of Kazakhstan invited all countries from the Eastern Partnership and Central Asia to join forces and establish an integrated regional emissions trading scheme.

Rafal Stanek (Consultant to OECD, KommunalKredit Public Consulting) and Bakhyt Bayanova (National Expert, Kazakhstan) presented the work the OECD has done (and financed by Germany) to support the Ministry of Energy of Kazakhstan to ***prepare a clean public transport investment programme aimed at reducing GHG emissions and air pollution in selected cities***. The programme is designed to support the shift to modern public transport powered by clean fuels, such as compressed natural gas and liquefied petroleum gas, in the major urban centres in the country. Mr. Stanek introduced the main elements of the programme, including among others, its objectives, specific targets, financial instruments. He also spoke about the Excel-based model developed as part of the project which helps calculate the main programme elements (e.g. costs of the programme given certain targets, possible emission reductions, optimal level of subsidy that can be provided to potential beneficiaries). Mr. Stanek noted that the aim of this work is to demonstrate in practice how to use scarce public funds to leverage private resources for socially important projects (aka blending). He underlined the need for a set of clear criteria allowing the public financier to select the most cost-effective projects for financing. In her turn, Ms. Bayanova highlighted some issues related to further programme implementation both in terms of opportunities (e.g. good cooperation with stakeholders at a local level, interest by bus producers) and challenges (lack of centralised environmental data, insufficient monitoring of fuel quality, need for better cooperation across government bodies). She also noted that this investment programme is the first such programme at a state level in Kazakhstan designed to provide public support to private sector actors in a competitive manner.

The main points that emerged from this discussion were:

- Governments have a broad array of possible instruments - both regulatory and financial - to create higher demand for green investments. A successful policy package aimed at mobilising green private investments should consider not only the economic, financial and technical feasibility of proposed actions and different actors' capacity to implement them but also the individual interests of all stakeholders involved.
- Putting an explicit price on carbon is the first best option to stimulate more demand for green investments but as experience from Kazakhstan shows this is not an easy task. Establishing a well-functioning ETS may take years and face resistance from different economic groups. EaP and Central Asia governments could consider introducing price on carbon (through a carbon tax or ETS) while learning from the EU and Kazakhstan's experience (from both what works and what does not). However, it is important that in setting ETS governments take their time to work with key stakeholders as well as take into account country's economic, development and climatic specifics.
- Governments will always have competing demands on their public resources. However, governments can use subsidies in a smart way and as an incentive to mobilise resources from the private sector (known as blending). Designing public investments programmes which allow governments to achieve country's green and climate-related objectives in a cost-effective and efficient manner is possible, as exemplified by the clean public transport investment programme in Kazakhstan. Other countries in the region may want to consider developing such programmes with

support by the OECD and donors as a way to green their public finance systems and strengthen the management capacity of their public finance institutions (e.g. public funds, development banks).

Session 4: Accessing international climate-related development finance

While governments can help create the right regulatory environment and provide the right incentives for enterprises, households and investors to implement green projects, international climate-related development finance also plays an important role in mobilising further private- and public-sector green finance in the EaP and Central Asia countries. Issues related to challenges to accessing international climate-related development finance were at the focus of the discussion during session 4.

Takayoshi Kato (OECD) talked about the ***evolving landscape of climate-related development finance in the EaP countries and Central Asia*** based on past and on-going OECD work (supported by Germany). Using the example of Georgia, Mr. Kato stressed that development finance has been – and will most likely remain in the near future – a crucial part of the green finance landscape for many countries in the region. Mr. Kato stressed that accessible low-cost finance can help improve the risk-return profile of investments, and that well-functioning financial markets should be developed in a way that are also conducive to green finance over time. On the other hand, he emphasised that care needs to be taken that concessional finance should not crowd out private sector investment or delay needed regulatory reforms, such as reforms on energy subsidies and environmental standards.

Andreas Lunding (Green Climate Fund (GCF) outlined various ***support schemes and financial instruments that GCF can provide (concessional debt, equity, guarantees and grants)***. With the Fund's primary focus on long-term funding, its main objective is to help unlock private climate finance for micro, small and medium-sized enterprises. To achieve this objective, as Mr. Lunding explained, the Fund takes on considerable risk which helps make climate projects viable. In this context, Mr. Lunding presented a new USD 500 mln GCF call for proposals aimed at mobilising private capital (called "Pitch for the Planet"). The Fund is inviting the submission of both mitigation and adaptation projects (such as climate-proof infrastructure, urban energy efficiency, ecosystem services or agriculture). Mr. Lunding stressed the importance of the minimum concessionality criterion for private sector deals (in order to prevent the crowding out of private sector investments) as well as the Fund's collaborative approaches with IFIs, development agencies and local (national) entities. He also highlighted the commitment of institutional investors, local financial intermediaries or corporates to co-invest in projects jointly with GCF. Of the countries of the region, Armenia, Moldova and Tajikistan have already benefited from support from the Fund.

Tatiana Chernyavskaya (UNIDO) and Marko Van Waveren (UNIDO Consultant) presented ***UNIDO's work on resource efficient and cleaner production (RECP) in the manufacturing sector in the EaP countries with a focus on financing RECP measures at SMEs.*** On the basis of specific projects developed by UNIDO, Ms. Chernyavskaya demonstrated the environmental and financial benefits that small and medium-sized companies can achieve as a result of implementing RECP projects. She also highlighted the major challenges faced by SMEs in the region in accessing bank finance such as high interest rates, demanding collateral requirements, currency risks, awareness and finance literacy gaps. She explained that both commercial banks and IFIs' credit enhancement programmes are primarily targeted at big companies which makes it very difficult for SMEs (particularly in the agricultural sector) to access capital. Mr. Van Waveren discussed possible ways to improve the access to RECP finance for SMEs. He stressed the importance of tackling both the main hurdles of bank lending as well as exploring alternative sources of finance such as leasing, ESCOs (energy service companies), supply chain financing, microfinance. In addition and based on examples from the EU countries, Mr. Van Waveren presented some innovative green finance solutions such as sustainability bonds, community funds and crowdfunding which could also be considered as potential new sources of financing green investments.

The main highlights that came out of this session were:

- OECD analysis shows that currently climate-related development finance in the EaP and Central Asia countries is, and most likely will remain in the near future, a crucial part of the green finance landscape in the region. While low-cost finance can help improve the risk-return profile of green investments it is important that IFIs and donor concessional finance should not crowd out private sector investment or delay needed regulatory reforms.
- Additional sources of finance, such as the Green Climate Fund, Green for Growth Fund or the Eastern Europe Energy Efficiency and Environment Partnership (E5P), are emerging and have the potential to become important players and help unblock private finance. EaP and Central Asia governments need to do more to raise awareness of these new opportunities in their countries, working with business associations and other relevant stakeholders interested in investing in green projects.
- SMEs face particular challenges in accessing both commercial banks' loans and development finance sources. While IFIs can help put in place SME-tailored financial products at commercial banks and donors can provide technical assistance aimed at improving project preparation, the main responsibility lays with national governments. Governments need to do more to facilitate SMEs access to finance (e.g. through targeted subsidies, setting special guarantee schemes and tax incentives, introducing regulations which support the development of other finance sources such as bonds, leasing or ESCOs (energy service companies) and make sure SMEs are aware of such opportunities.

Session 5: Aligning policies for the transition to a green economy

Scaling up green investments will not happen sufficiently rapidly unless governments adjust existing policies and regulations and align them with the imperatives of the new low-carbon and green growth agenda. The current economic system continues to foster reliance on fossil fuels as a main driver of economic growth and short- and medium-term profits. Moving to a greener economic path of development requires new ways of policy making and new policy tools. Setting adequate price on carbon emissions, reforming environmentally-harmful and economically-wasteful energy subsidies and redirecting them to green investments as well as decarbonising financial flows lie at the heart of the green growth agenda. The de-carbonisation of the industrial base and related financial impacts resulting from new climate-related policies pose a particular concern to companies, investors and policy-makers. All these issues form part of the debate on policy alignment and were at the focus of the discussion during the fifth session of the conference.

Nelly Petkova (OECD) presented the results from the study on ***"Energy subsidies in the EaP countries"*** implemented as part of the EaP GREEN project. This analysis looks at government support to both producers and consumers of fossil fuels, including coal, oil and petroleum products, natural gas but also electricity and heat generated on the basis of these fuels. The study also analyses support that goes to energy efficiency and renewable energy sources in the EaP countries. Ms. Petkova stressed that while in absolute terms the amount of government support to fossil fuels in these countries is relatively small (except in Ukraine), in relative terms the picture is quite different. For example, in 2014, in most countries (Azerbaijan, Belarus, Moldova, and Ukraine) the amount of quantified fossil-fuel subsidies as a share of GDP was larger than these countries' national budget deficits as a share of GDP. Ms. Petkova pointed out that further reforming such subsidies can lead to better budgetary outcomes. She also indicated that public support to EE/RE is negligible compared to fossil-fuel subsidies. Ms. Petkova also spoke about data constraints as a particular concern in preparing the analysis. One main finding of the study was that governments in the region generally do not produce tax expenditure reports which can show the revenue foregone for the budget as a result of various tax benefits provided to different economic actors in different economic sectors, including energy. She pointed out that these challenges hamper adequate decision making and governments can do more to increase transparency as a prerequisite for further reforms in the sector. Ms. Petkova underlined the fact that countries in the region have already undergone significant energy sector and energy subsidy reforms and these reforms continue to evolve.

Sarah Duhr (Federal Ministry for the Environment, Nature Conservation, Building and Nuclear Safety, Germany, Consultant) spoke about ***Ukraine's experience with turning subsidies into energy-efficiency investments in the municipal heat and gas sector.*** Ms. Duhr explained that savings from reduced energy-related social subsidies after energy-efficiency investments are implemented create a revenue stream which is consolidated through a newly established Energy Efficiency Fund. She presented a multi-year calculation of investment volumes vs. subsidy savings for Ukraine where high energy losses and inefficiencies multiply the negative impacts of increased energy prices. Ms. Duhr stressed the double socio-economic aspect of energy-efficiency measures: households will not only make direct savings as a result of lower energy and electricity bills but this will also lead to reduced subsidies that state/municipal budgets need to pay. These budgetary savings can then be used either for scaling up energy-efficiency measures or as a social subsidy provided to the most vulnerable social groups in the country.

Artem Kuznetsov (Prime Minister’s Office and Ministry of Regional Development, Building and Housing and Communal Services of Ukraine) continued the presentation started by Ms. Duhr and discussed ***progress with establishing the Energy Efficiency Fund whose investments will support the modernisation (thermal insulation) of residential buildings in Ukraine***. Mr. Kuznetsov explained that the Law on the Energy Efficiency Fund was adopted recently by the Parliament. While the main preconditions for the Fund's operations are in place some additional legislation still needs to be enacted (e.g. Law on energy efficiency in buildings, Law on housing and utility services). Apart from direct positive financial impacts on households and state/municipal budgets, Mr. Kuznetsov noted that implementing EE measures will have a broader impact on the economy (both in terms of contracts for renovation businesses or higher property values for real estate owners), Ukraine’s foreign policy (energy independence) and, not least, the environment (reduced CO_2 emissions). The Fund is expected to catalyse the development of the residential housing renovation market with a total investment potential of more than EUR 40 bln. Mr. Kuznetsov also mentioned that a number of donors and IFIs have already committed to contribute to the Fund’s activities and support investments (EU and Germany) or provide technical assistance.

Dr. Isabel Blanco (EBRD) presented the ***preliminary results from a study on the fiscal implications of a green economy transition with fiscal and budget recommendations for fossil-fuel rich countries and with a specific focus on Kazakhstan***. Dr. Blanco identified some challenges to green economy transition for countries where oil and gas sectors have not only been key drivers of economic growth (and major source of income for budgets) but also where fossil-fuel reserves and related assets are owned (controlled) by the national or local governments. She pointed out that the transition will affect investments beyond the oil and gas sector but also power generation, transmission and distribution, roads and ports, cement and steel industry. The transition will also have an impact on governments’ policy agendas (fiscal policy, climate change, economic policy). Dr. Blanco stressed that the green economy transition will generate both fiscal opportunities and risks. She discussed several options with regard to fiscal policy (tax reform, subsidy reform, changes in ownership structures) and the budget process (better planning, monitoring or reporting) that countries could consider in order to mitigate the risks the transition might bring about (revenue losses, increased indebtedness). On Kazakhstan, preliminary quantification shows that there is a period of around 10 years to implement relevant measures before the fiscal implications become fully felt.

Dr. Alexander Golub (World Bank, Consultant) framed ***the debate around "stranded assets" in terms of development challenges to carbon-dependent countries.*** Stranded assets are discussed in the context of capital investments made in fossil-fuel infrastructure which will not be recovered over the operating lifetime of the physical asset because of reduced demand or reduced prices as a result of climate policy. As part of this work, the World Bank has modelled various policy and development scenarios of the "stranded assets" impact in 15 different regions and countries, including in Kazakhstan. In his presentation, Dr. Golub underlined the importance of cooperation under uncertainty and asset diversification in the transition to a knowledge-based economy. To eliminate double dependency on fossil fuels (export and domestic consumption) Dr. Golub underlined that traditional diversification of products and exports may not be sufficient to achieve resilience to future technological and policy shocks, augmented by climate change. Under such conditions, investments in human capital and institutions may generate higher returns than investments in natural resources and carbon-intensive sectors alone (due to higher labour productivity and consumption). The resistance of traditional industries and the lack of good governance will pose, according to Dr. Golub, major barriers to the green transition, while cooperation on climate policy could support the timely adjustment to transformations on the global market. Not least, Dr. Golub warned against the danger of overlooking technological innovations and mistaking structural transformation for cyclical fluctuations.

The main points that emerged from this discussion were:

- OECD analysis shows that fossil-fuel subsidies in the EaP region have significant economic, social and energy security implications. Developing a good understanding of where such subsidies exactly go (who benefits) and how big and costly they are is a first step in designing appropriate reform plans. However, data availability of and reporting on subsidies are largely lacking in the region and need to be meaningfully improved to serve adequate policy decision making. Governments can do more to improve transparency of public support going to the energy sector by, among others, adopting better subsidy definitions and reporting methodologies, improving data collection and undertaking regular reporting.
- Better targeting support to poor people and re-directing fossil-fuel subsidies to energy-efficiency investments, as exemplified by the work that is currently being carried out in Ukraine, shows one possible direction for energy-subsidy reform. It will be interesting to learn further from Ukraine's experience. Governments in the region may want to consider such an option and discuss with donors possible support in this direction.
- The issue of stranded assets does not seem to be on the policy agenda of most of the countries in the EaP and Central Asia countries. There is little awareness among governments, companies and local investors of the fiscal and financial implications of future climate policies. The global climate agenda advances fast and governments in the region need to be better prepared for the transition to a low-carbon model of economic growth. In order to better cope with future challenges, governments need to develop adequate strategies that could help them diversify away from the current resource-intensive patterns of production and consumption. The work carried out by the EBRD and the World Bank in this area can be used as a model to conduct further analysis on this issue and identify key policy adjustments, including with regard to investments in human capital and institutions, which may be needed. Donors have a crucial role to play in supporting such efforts.

Session 6: Exploring new avenues

Traditional sources of private capital, such as commercial bank loans, are not the only source of financing green economy transition. Other sources of capital such as public/private equity and green bonds can be used for this purpose. Institutional investors, including Pension Funds and Sovereign Wealth Funds, and banking and monetary policy can be further tailored to promote the financing of green investments. Session 6 looked at these other sources of finance and discussed their relevance for the EaP and Central Asia countries.

Frank van Lerven (New Economics Foundation, UK) presented the ***role of banking and monetary policy in financing the transition to a green economy***. Mr. van Lerven stressed that climate change poses a systemic change to the financial system. However, generally, central banks have not aligned their policy objectives with the threats of climate change. Mr. van Lerven emphasised the increasing importance of central banks in promoting green transition, an issue that until now has largely remained unexplored in mainstream debates. He outlined several policy instruments available to central banks such as macro-prudential regulation (aimed at reducing economic shocks), credit creation and quantitative easing (QE)[1]. When used responsibly these instruments can help promote green transition. Mr. van Lerven presented examples from different countries which demonstrate that greening Central Bank instruments is possible and they can be used to stimulate commercial banks to direct a higher share of their lending operations to green investments (e.g. lower capital requirements for those commercial banks that support green investments, providing

[1] QE is an expansionary monetary policy whereby a central bank buys predetermined amounts of government bonds or other financial assets from commercial banks in order to increase money supply and stimulate the economy.

green credit guidance to commercial banks, introducing limits on "brown lending" or green credit quotas). Working with and through banking regulators and associations is yet another opportunity for governments to stimulate green lending products and services.

Manuel Adamini (Climate Bonds Initiative (CBI), UK) talked about ***green / climate bonds and how accessing debt capital markets can help finance climate solutions at a low cost***. Mr. Adamini stressed that despite the fact that the global green bond market has been growing at a considerable pace green bonds still represent a small fraction of global bond issuance annually. Mr. Adamini explained that when multilateral development banks participate in such deals either as issuers or as investors their participation can help lower project-risk exposure and boost the credibility of the deal. Similarly, when green bonds are issued by governments this has a demonstration effect and can help unlock the market. Green bonds are particularly suited to finance infrastructure investments as such investments match demand by long-term investors. Experience with issuing green bonds in the EaP and Central Asia region is rather limited. However, some countries (e.g. Belarus, Ukraine, and Kazakhstan) are already considering this financing option.

Liesel van Ast (UNEP Finance Initiative) presented the ***work the UNEP Finance Initiative (FI) has been carrying out on sustainable finance in partnership with financial sector actors, including banks, insurance companies, asset managers, and asset owners***. In her presentation, Ms. van Ast emphasised the importance of integrating Environmental and Social Governance (ESG) criteria into investment analysis and decisions as well as the need to develop green and inclusive products and services in the financial sector. She shared UNEP FI experience with implementing the recommendations of the Task Force on Climate-Related Financial Disclosures[2] in the banking and insurance sectors in selected. In doing so, UNEP FI has worked with a pilot group of banks and helped them adapt and green their strategies and portfolios. Ms. van Ast also spoke about a new UNEP FI initiative to help financial institutions in Eastern Europe directly access the Green Climate Fund (GCF). In addition, UNEP FI is in a position to provide support to selected National Designated Authorities in the region and help them nominate financial institutions for GCF accreditation as well as identify and prioritise funding proposals. Ms. van Ast also announced a Regional Roundtable on “Scaling up Sustainable Finance across Banking, Insurance and Investment in Europe” which UNEP FI is holding on 16 – 17 October 2017 in Geneva.

Hülya Kurt (Escarus – TSKB Sustainability Consultancy) shared ***Turkey's experience with financing green investments and the achievements of the Development Bank of Turkey (TSKB) in moving to sustainable banking practices***. Ms. Kurt spoke about TSKB green investments in both renewable energy, energy-efficiency and resource-efficiency projects. While investments in hydro dominate the TSKB portfolio, loans for solar projects are on the rise. Investments in industrial EE are also important. Given Turkey’s growing and energy-intensive economy (largely based on coal), much more needs to be done in the public buildings sector where the energy savings potential is very high. Ms. Kurt also spoke about the first green bond in Turkey (USD 300 million) issued by TSKB in 2016. The bond comes along with specific advantages for climate bond investors, such as preferred fiscal treatment and a feed-in tariff for solar fixed for a 10-year period. In addition, Ms. Kurt mentioned that in 2014 the Banks Association of Turkey issued voluntary Sustainability Guidelines for the banking sector. The Guidelines were prepared to provide commercial banks with guidance on how to address the environmental and social dimensions of the investments they finance and how to increase transparency of their activities.

The main points that emerged from the discussion during this session included:

- Given central banks' ability to influence financial flows and commercial bank lending and as experience from different countries shows aligning banking and monetary policies with the threats of climate change provides yet another opportunity for governments to green the financial sector and stimulate financing of green investments. Governments in the EaP and Central Asia may consider working with their Central Banks and Banks Associations to explore this option also in

[2] The Task Force is part of the Financial Stability Board which is a body that monitors and makes recommendations about the global financial system.

cooperation with international partners (e.g. World Bank, International Finance Corporation, UNEP FI, OECD).

- More generally, governments in the region should seek to encourage commercial actors, such as banks, insurance companies, asset managers, to adopt relevant environmental, social and governance risk-rating criteria and adequately reflect risk in their financial decisions. This could contribute to raising awareness across the financial services industry of possible business opportunities. Combined policy-support and industry-led initiatives may be the right strategy to pursue.
- Green bonds represent yet another source of capital to finance green investments. Experience with issuing green bonds in the EaP and Central Asia region is rather limited. Governments in the region need to explore this possibility further as green bonds are particularly suited to finance green infrastructure investments. Sovereign bonds issued by governments have a demonstration effect and can help scale up the market. Governments can cooperate with IFIs as multilateral development banks have significant experience and can provide the necessary policy advice.

Session 7: Closing session

In this session, the OECD and the European Commission summarised the discussion at the Conference. They highlighted new policy issues that may need to be considered for further analysis in supporting the EaP countries and Central Asia in their efforts to transition to an energy-efficient and low-carbon economy.

In summarising the discussion ***Kumi Kitamori*** (OECD) and ***Vassilis Maragos*** (EC, DG NEAR) thanked the presenters and the participants for the fruitful discussions over the two days. They acknowledged the diversity of stakeholders and their views. They also underscored the countries' commitments to seize the opportunities to green finance and investment which have to be closely connected to, and measured against, an enhanced quality of life of citizens. They stressed that experience shows that green investments can bring more jobs and contribute to higher growth.

Ms. Kitamori and Mr. Maragos pointed out that the discussion showed that reforms are actually taking roots in the region leading to concrete actions related to green policies and investment. These include the development of green growth strategies as well as specific instruments to facilitate green investment, such as Emissions Trading Systems, initiatives to turn environmentally-harmful subsidies into green investment, and increased green lending by country public and, increasingly, commercial finance institutions. The exchange at the meeting also demonstrated the growing body of experience of working with IFIs and donors on facilitating commercial lending to green projects. They reiterated the need for a better co-ordination across various sources of finance, including innovative financial instruments, and the need to pull together instruments and tools, public and private, in order to work at scale. They also stressed the importance of investing in people through private sector, business development and banking support and exchange programmes as well as the value of monitoring green financial flows in order to assess progress and learn from experience.

Ms. Kitamori and Mr. Maragos also spoke about the vital role of domestic capital (public and private) and the need to demystify investments by reducing the perception of risks associated with lending to green projects and developing proper business cases to demonstrate green lending benefits. They highlighted the importance of sustainable in-country processes building on the EU experience so far. The EU can lead by example but countries need to make comprehensive "greening" processes part of their national reform agendas. Ms. Kitamori and Mr. Maragos reiterated, among other things, the need to remove environmentally-harmful subsidies; reinforce environmental taxes to motivate more environmentally-sound behaviour; strengthen enforcement and compliance mechanisms as well as joint IFI and commercial bank programmes that would provide a sustainable basis for green private finance. They also pointed out that in order to implement these new policies and programmes the countries need to develop both administrative and absorptive capacities, recognising the particular challenges faced by SMEs.

In highlighting possible future work in the Eastern Partnership countries and Central Asia the following steps were suggested for implementation by the OECD, EU and their partners:

- ✓ Reinforcing links between policies / regulations and demand for capital, including clarification of benefits from green investments and analysis of costs of inaction and further work on enforcement and compliance to generate demand and a level-playing field;
- ✓ Development of menu/analysis of less known financial sources and instruments that already exist and that can possibly be used on the basis of experience from the EU/OECD countries;
- ✓ Analysis of how to scale up IFIs investments to leverage further domestic finance in a timely fashion;
- ✓ Strengthening domestic finance capacity for green investments by:
    - Supporting selected countries in designing clean investment programmes that can be financed by public sources as a way to mobilise private sector investment;
    - Providing methodological and practical support to domestic public/development banks and other public finance institutions financing green investments on risk assessment and green project appraisal (e.g. Development Bank of Kazakhstan);
- ✓ Working on accounting and reforming of energy subsidies with a focus on energy affordability for the poorest parts of the population and turning them into clean investments;
- ✓ Improving the absorptive capacities and country ownership by also strengthening project preparation capacity;
- ✓ Providing a platform for sharing experience and knowledge transfer on a regular basis at the regional and country level.

Ms. Kitamori and Mr. Maragos expressed the OECD's and the European Commission's support for further dialogue on these important topics in the same (or similar) format in the future. They called for a reinforced discussion at the national level which should be supported by concrete actions that can mobilise public and private funding and engage the private sector and citizens' organisations in order to ensure increased feasibility and transparency of financing arrangements.

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