

# Unlocking potential: green finance in the Middle East, North Africa and Central Asia

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*Check against delivery.*

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## 1 Climate change – not a distant threat

Good afternoon everyone.

I am delighted to kick off your discussions on how to make financial sectors more resilient to climate-related risks and how to scale up climate finance. They come at the right time.

Countries in the Middle East, North Africa and Central Asia are particularly vulnerable to the impact of climate change. Not tomorrow but today. We are in the midst of a climate emergency.

For example, the devastating floods that hit Pakistan in 2022 affected 33 million people and drove up food inflation. The Asian Development Bank estimated the costs for rehabilitation of land and reconstruction of infrastructure to be at least US\$16.3 billion.<sup>[1]</sup>

Elsewhere in the region, water scarcity is a big problem, for instance in Egypt. Only about 3% of the country's surface is arable land, i.e. land on which crops can be grown, mostly along the Nile. Heat waves, water stress and salinated soil already put pressure on Egypt's agriculture.[2] Climate change will further exacerbate these existing vulnerabilities with implications for food prices and food security.

Climate change will have significant effects on food prices all over the world according to a recent study by the European Central Bank (ECB) and the Potsdam Institute for Climate Impact Research (PIK). Globally, food inflation could increase by 3.2 percentage points per year by 2035. Headline inflation could rise by 1.18 percentage points annually.

The study underlines the greater vulnerability of many countries in the Middle East, North Africa and Central Asia where the effects might exceed the global averages. The study also suggests that, as temperatures continue to rise, these inflationary effects are likely to worsen.[3]

This means for central banks and supervisors it is high time to be prepared for the huge economic impact of climate change and the associated upward pressure on prices, and to raise awareness among governments about the massive economic impact.

## **2 Time's up for fossil fuels**

Given that climate change is here, and here to stay, responses ought to be two-pronged. First, adaptation, i.e. responding to what is already happening. Second, mitigation, i.e. accelerating global decarbonisation and fast-tracking the green transition.

In other words: we need to prevent the worst while addressing the bad that is already happening.

I know that we ought to be realistic and pragmatic. The world economy is still very dependent on fossil fuels and will continue to be for some time. Take oil, for instance. According to a recent analysis by the International Energy Agency (IEA), global oil demand is growing more slowly, after a strong post-pandemic rebound.[4]

The IEA expects global oil demand to peak by the end of this decade. However, the IEA also acknowledges that in many cases it is still difficult to find alternatives to oil. It also states that under current policies, oil demand could remain near current levels for some time.[5]

But the trend is clear: many regions across the world are weaning their economies off fossil fuels. The IEA also projects that global demand for natural gas will peak by 2030.[6] For instance, last year, natural gas consumption in Europe fell by 7% and reached its lowest levels since 1995.[7] At the same time, global investment in clean energy has been outpacing investment in fossil fuels. According to the IEA “for every US\$1 US spent on fossil fuels, US\$1.7 is now spent on clean energy”. In 2019 this ratio was 1 to 1.[8]

These global developments will have a particularly pronounced effect in the Middle East, North Africa and Central Asia, where the emissions intensity of economic activities is higher than in other emerging market and developing economies.[9] This makes companies and financial institutions – especially those exposed to carbon-heavy activities – vulnerable to transition risks. In light of these global trends and developments, it is essential to plan for a post-fossil fuel future.

### **3 Green finance in emerging market and developing economies**

We need to scale up climate finance significantly, both for mitigation as well as for adaptation. Climate adaptation measures, such as developing heat-tolerant crops or making public infrastructure “climate-proof”, are an essential pillar of addressing the climate crisis. At the same time, decarbonisation efforts will also require large-scale investment, for example, to develop low-carbon technologies.

The climate-related financing needs for mitigation and adaptation in the Middle East, North Africa and Central Asia are substantial, at least US\$1 trillion by 2030 to achieve the Nationally Determined Contributions (NDCs), according to the IMF. [10] Comparing the financing needs with the actual supply of green finance across the region shows a large financing gap. This is where the region’s financial sectors must play a major role.

Attracting substantive amounts of private capital will be essential to plug the financing gap. Blending public and private capital can be one viable option to mobilise green finance. Unfortunately, emerging market and developing economies especially tend to struggle to get private investors on board.

In a challenging global macroeconomic and geopolitical environment, investors appear to prefer investing in advanced economies that often offer more attractive risk profiles.

This is especially true after central banks in advanced economies increased interest rates to bring down inflation. Many emerging market and developing economies have started to cut rates. By contrast, central bank rates in many advanced economies, for example in the United States and the euro area, have plateaued. This has further reduced the interest rate differentials between emerging market and developing economies, on the one hand, and advanced economies, on the other. At the same time, overall, political risk in emerging market and developing economies has increased.

All in all, investments in emerging market and developing economies have become less attractive in recent years. That means emerging market and developing economies need to improve their risk-return profiles to attract investors.

## **4 The NGFS Blended Finance Handbook**

In this context, let me showcase some of the work carried out by the global Network of Central Banks and Supervisors for Greening the Financial System – the NGFS. Some of you are members of this network, which aims to support the transition of the financial system towards sustainability.

### **4.1 Barriers to blended finance**

At COP28 in Dubai, the NGFS published a handbook that identifies key barriers to blended finance in emerging market and developing economies.[11] Let me give you a few examples.

First, structural issues, such as gaps in the legal and institutional frameworks of the countries concerned. This often translates into issues for private investors. For instance, country ratings falling below the often required investment-grade thresholds or foreign exchange hedging becoming too expensive.

Second, limited investment opportunities and a lack of viable climate projects. Typically, such projects are small in scale, require longer timelines and therefore have high due diligence costs. This makes them unattractive to international private investors.

Third, data gaps: investors need to be able to effectively price in climate-related risks. A lack of robust frameworks, standards and taxonomies makes this very difficult.

### **4.2 Policy recommendations**

The NGFS handbook also provides several policy recommendations to address these barriers. To name just a few:

First, put in place policies that make emerging market and developing economies more attractive for investors. This includes, for example, climate policies such as carbon pricing, which can be very effective in shifting capital flows into climate investments.

Second, policymakers should promote ways to better manage and diversify risks and strengthen the catalytic role of multilateral development banks to attract private capital. For example, diversifying risk through risk pooling and tranching, could help attract different sources of private capital.

Third, investors need decision-useful information and planning certainty. Credit rating agencies and ESG data providers can play an important role here. It is essential that they align their practices and products with blended finance realities in emerging market and developing economies.

Implementing these recommendations and resolving the obstacles to green finance in emerging market and developing economies will require the collaboration of multiple stakeholders. Policymakers, multilateral development banks and private financial institutions all need to get on board.

In this context, let me highlight the role of the large sovereign wealth funds that some countries of the region have. Thanks to their long-term investment horizons and their large size, they are uniquely placed to act as catalysts for green finance and to crowd in private capital. Some sovereign wealth funds are already involved in climate mitigation projects in the region. But overall, this involvement is still quite low.<sup>[12]</sup> According to the IMF, reasons for that include many of the obstacles I mentioned earlier, such as a lack of standards and data quality, a perceived lack of investment opportunities and low returns as well as uncertainty around government green finance policies. Drawing on the recommendations and the experience from the demonstrative projects that the NGFS handbook compiles could prove a good starting point to tackle these challenges.

## **5 Concluding remarks**

The Middle East, North Africa and Central Asia face a host of climate-related risks. These risks range from damage due to extreme weather events to sizeable transition risks due to the reliance on fossil fuels and the exposure to carbon-intensive activities.

Addressing these risks makes multitasking necessary. Countries will have to adapt to climate change, while also mitigating it to prevent further damage and losses.

Climate adaptation and mitigation require substantial investments that cannot come from the public sector alone. This offers great potential for the financial sectors in the region to play a prominent role in financing these dual efforts. To fully unlock this potential, work is needed on a range of barriers to investment that persist. Pooling its expertise from all regions of the world, the NGFS can do its bit to help make this happen, together.

**Footnotes:**

1. Asian Development Bank (2022): By the numbers: Climate change in Central Asia.
2. Asian Development Bank (2022): By the numbers: Climate change in Central Asia.
3. Carnegie Endowment for International Peace (2023): Climate change in Egypt: Opportunities and obstacles.
4. Kotz et al. (2024): Global warming and heat extremes to enhance inflationary pressures, *Communications Earth & Environment*, Vol. 5 (116).
5. International Energy Agency (2024): Oil demand growing at a slower pace as post-Covid rebound runs its course.
6. International Energy Agency (2024): Oil demand growing at a slower pace as post-Covid rebound runs its course.
7. International Energy Agency (2023): World Energy Outlook 2023.
8. International Energy Agency (2024): Gas Market Report Q1 2024.
9. International Energy Agency (2023): World Energy Investment 2023.
10. International Monetary Fund (2024): Preparing financial sectors for a green future: Managing risks and securing sustainable finance.
11. International Monetary Fund (2024): Preparing financial sectors for a green future: Managing risks and securing sustainable finance.
12. International Monetary Fund (2024): Preparing financial sectors for a green future: Managing risks and securing sustainable finance.
13. Network for Greening the Financial System (2024): Scaling up blended finance for climate mitigation and adaptation in emerging market and developing economies.
14. Network for Greening the Financial System (2024): Scaling up blended finance for climate mitigation and adaptation in emerging market and developing economies.
15. International Monetary Fund (2024): Preparing financial sectors for a green future: Managing risks and securing sustainable finance.