Private Sector Engagement to Address Climate Change and Promote Green Growth

KEY MESSAGES

- Development Assistance Committee members are increasingly engaging the private sector to mobilise green investment, promote green private sector development, and harness skills and knowledge for addressing climate change in developing countries. Efforts include developing clean infrastructure, reducing energy and water use, improving the climate resilience of cities and communities, and supporting natural capital and ecosystems.
- Challenges for private sector engagement on the environment include a lack of evidence on environmental outcomes, moving beyond demonstration projects to scale up successful approaches and the need to strengthen links with partner country priorities.
- Emerging good practice spans ways to communicate the business benefits of addressing environmental issues (e.g. cost savings, reduced risks), understand and address the barriers to private sector engagement on environmental issues, promote sound business models and adopt a holistic approach that includes support for the enabling policy environment for investment and business.

INTRODUCTION

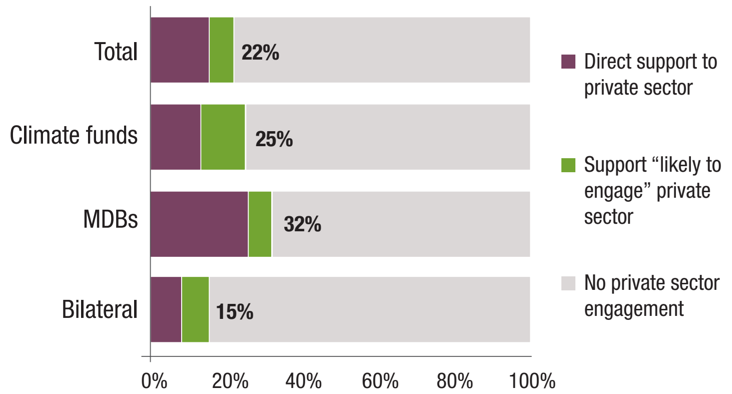
The Sustainable Development Goals and Paris Agreement reconfirm that growth and development cannot continue without all countries tackling climate change and boosting environmental sustainability. Transitioning from the current development pathway to a low-carbon, climate-resilient one will require significant investment and innovation and, more importantly, a shift in the way governments and the private sector make decisions. To support partner countries in this context, development co-operation providers will need to better engage with the private sector to mobilise resources, knowledge and innovation for addressing climate change and promoting green growth.

The importance of tackling climate change and other environmental issues is now well recognised by different parts of the private sector. The financial sector has acknowledged that addressing global environmental challenges, such as climate change, is key to managing business risks and ensuring long-term returns on investment (Carney, 2015). Optimising resource use and improving environmental performance also help companies reduce costs, streamline operations and increase efficiency. In addition, the need for innovative solutions in the areas of climate change mitigation and adaptation is an opportunity for companies to develop new products and services and serve new markets. Finally, there is increasing emphasis on corporate social responsibility and responsible business conduct among multinational companies. Addressing environmental risks and impacts is a key part of their efforts.

LESSONS

The private sector will be a critical partner in delivering effective development co-operation on environmental issues in partner countries. Business practice has been associated with environmental pollution and degradation, especially in countries where safeguard systems and environmental governance need strengthening. Yet, companies also play an important role in driving green growth in developing countries. Multinational companies can promote greener behaviour across the supply chains that they manage, investors and banks are potential sources of investment for clean infrastructure, and businesses and entrepreneurs provide the skills and knowledge leading to innovation in clean technologies and resource efficiency.

FIGURE 1. **CLIMATE-RELATED DEVELOPMENT FINANCE SUPPORTING PRIVATE SECTOR ENGAGEMENT ACROSS DEVELOPMENT FINANCE PROVIDERS, 2013**



Note: Bilateral providers include Development Assistance Committee members; multilateral development banks (MDBs) include the African Development Bank, Asian Development Bank, European Investment Bank, European Bank for Reconstruction and Development, Inter-American Development Bank and World Bank; climate funds include estimates from the Adaptation Fund, Climate Investment Funds, Global Environment Facility, International Fund for Agricultural Development and Nordic Development Fund. Estimates are based on USD commitments for 2013.

Source: OECD DAC Statistics in Crishna Morgado et al. (forthcoming)

Recognising this, development co-operation providers are increasingly engaging the private sector to promote green growth. A review of development finance flows shows that up to 20% of climate-related development finance in 2013 supported activities to engage the private sector, with the majority of finance being deployed toward climate change mitigation *(see Figure 1)*.

Mobilising Green Investment

Development co-operation providers deploy different approaches to mobilise private finance to combat climate change. Where political and commercial risks reduce returns on investment, they use loans and blended finance to attract private capital and make use of guarantees to de-risk private finance for renewable energy technologies. Led by a group of bilateral development finance institutions, the Interact Climate Change Facility serves as one example of a mechanism that pools finance from different development finance institutions and co-invests in renewable energy and energy efficiency projects in partner countries.

Development co-operation providers are also increasingly using grant financing in more catalytic ways. For example, matching grant schemes support particularly innovative companies that would otherwise not have access to financing in playing a role in climate change mitigation and adaptation. A special window on renewable energy within the Africa Enterprise Challenge Fund provides grant financing through an open competition for projects based on low-cost clean energy and climate technologies that help smallholder farmers access energy services and adapt to climate change. Businesses are required to provide matching funds to ensure that grants are catalytic and financial risks are shared between partners.

Promoting Green Private Sector Development

Development co-operation providers work with partner countries to improve the enabling policy environment for private climate investments. This support includes, for instance, policy reforms such as helping phase out fossil fuel subsidies, which in turn increases the profitability of clean energy investment, and creating feed-in tariffs for specific renewable energy technologies. More broadly, this support promotes building new markets and much needed institutional and technical capacity in partner country governments, which enables these governments to mobilise and sustain green investment over time.

Efforts are also underway to shape policies and programmes to improve the environmental performance of businesses in partner countries as a way of supporting sustainable and inclusive growth. Small businesses in particular face several barriers in addressing climate change, including a lack of capacity and access to tools needed to green their businesses, poor access to finance for low carbon technologies, and inadequate awareness of the business case for increasing efficiency and improving resilience.

Emerging approaches by development co-operation providers take a market systems approach to promote green growth through the development of value chains and markets for environmental products and services.

GIZ's Employment for Sustainable Development in Africa programme, for example, provides finance to support public-private partnerships with local companies in order to generate employment in key value chains that will contribute to a greener economy in areas such as water, energy and waste management. GIZ supports vocational training and skills development so that poorer segments of populations can engage in these value chains.

Programmes also target improved access to finance in order to encourage uptake of low carbon technologies and improve the environmental performance of businesses. One major area of donor effort is the use of credit lines to incentivise businesses to invest in environmental solutions. The multi-donor **Green for Growth Fund** provides concessional finance to public and private financial intermediaries in order to set up and demonstrate the viability of financing for low carbon technologies in the Middle East and North Africa. The fund includes technical assistance to financial institutions, business associations and businesses, and government partners to build capacity and raise awareness of green finance.

Harnessing Skills and Knowledge for Green Growth

Through dialogue, policy discussions and formalised partnerships, development co-operation providers engage the private sector to harness skills and knowledge to address environmental issues. For example, through the Swedish Leadership for Sustainable Development network, the Swedish International Development Cooperation Agency co-ordinates 20 Swedish or Swedish-rooted companies that meet regularly and discuss opportunities to promote global leadership in addressing sustainability issues.

CHALLENGES

Private sector engagement on the environment faces a number of key challenges.

Evidence of Impacts

There is a general lack of evidence on the extent to which private sector engagement efforts have resulted in wide-ranging environmental outcomes, beyond the mobilisation of private investment. The United Nations Framework Convention on Climate Change negotiations have focused on mobilising climate finance within the context of financial commitments made by developed countries to address climate change in developing countries. This has resulted in high visibility for tracking the amounts of private capital mobilised, but less attention to the effectiveness and impacts of these efforts. In addition, development co-operation providers' efforts to improve the environmental performance of businesses increasingly involves working through intermediaries such banks, business and professional associations, and companies with extensive supply chains. While this approach may be a necessary and effective way of reaching out to companies, especially small and medium-sized enterprises, it leads to significant difficulties in monitoring and verifying environmental impacts and outcomes.

Supporting Partner Country Priorities

Private sector engagement approaches also need to make stronger links with national development plans and priorities on climate change and the environment. Approaches to promote clean technologies in partner countries are sometimes combined with efforts by Development Assistance Committee member countries to promote their own private sector, and therefore favour technologies from their own countries. While such approaches may be effective in delivering environmental benefits at the project level, like fuel savings or reduced emissions, they do not necessarily contribute to supporting the development of local technologies or longer-term solutions. Also, it is unclear whether they would promote the most cost-effective approaches. In addition, the eventual roll-out of clean technologies past the pilot stage is less likely when partner country governments are not engaged adequately and therefore complementary policy reforms do not take place.

Realising Scale

While there are several examples of successful innovative ways to engage the private sector in promoting green growth, there is still a need to scale up such approaches. One of the biggest challenges facing infrastructure investors is the limited flow of bankable projects in clean infrastructure such as renewable energy or low-carbon transport, despite many of these technologies being proven at a small scale.

GOOD PRACTICE

Find Common Ground

To engage the private sector in partner countries where there may be a lack of awareness and understanding of environmental issues, development co-operation providers need to find ways of communicating with private sector partners that highlight win-win solutions. In the context of private sector engagement on the environment, this approach involves focusing on the benefits of improving environmental performance such as increased competitiveness, reduced costs and reduced exposure to risks, rather than environmental benefits per se.

Understand Private Sector Needs

Private sector engagement to support green growth should be centred on a good understanding of demand from the private sector for development co-operation support. In other words, approaches should be rooted in an understanding of how development co-operation providers can better address the barriers that companies face in pursuing market opportunities for green technologies, products and services in developing countries.

To drive lasting positive environmental change, private sector engagement needs to promote sound business models for environmental protection that deliver environmental outcomes, are financially feasible and create decent jobs.

Adopt a Holistic Approach

Mechanisms to leverage green private investment will only result in improved long-term environmental performance if an adequate enabling policy environment exists in partner countries. To scale up successful project cases to programmes or sustainable market level, it is important to adopt a holistic approach to private sector engagement on climate change and green growth. This approach involves supporting a range of policy reforms and regulations to promote climate change mitigation and adaptation and improved environmental performance – the enabling policy environment for private climate investments – along with use of limited public finance for mechanisms to leverage green private investment.

REFERENCES

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