

ENVIRONMENT FOR EUROPE MINISTERIAL CONFERENCE

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DRAFT KEYNOTE ADDRESS BY BRIGITA SCHMOGNEROVA¹

Opening remarks

- 1.** Sixteen years after the Environment for Europe process was originated Central and Eastern Europe, the Caucasus and Central Asia are still facing important environmental challenges.

Many of them cross borders: like air and water pollution. Addressing them requires strong international cooperation. International cooperation remains essential to achieve environmentally sustainable development in our region.

It is well recognised in the SEE where achieving sustainable energy solution is hardly thinkable without close cooperation of all SEE countries. But there are many environmental challenges which cross borders in Central Europe, Central Asia and Caucasus that call for multilateral solutions as well.

- 2.** In addition to international cooperation the provision of adequate levels of financing for environmental improvement is absolutely critical. To provide appropriate funding with regards to an amount and pricing is a shared responsibility between governments, donors, international financial institutions and a private sector. Tight budgetary resources often have to be complemented by private funding which on the other side might provide comfort that funds are spent in the most efficient way. The

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Government should be encouraged to cooperate with commercial banks and combine local or international funding (like the EU funds) with private funding.

3. Providers of international finance, including the private sector and IFIs must respond to new opportunities and challenges in the region. This requires them to be innovative in the development and the use of financing instruments to support environmental improvements.

The most common financing instrument is project-based lending. This is also true for the EBRD. Through investment projects, EBRD is a major provider of environment-related finance in the region. In 2006 alone EBRD invested €976 million in environmental investments. A significant proportion of this figure - €872 million, representing 18% of total EBRD investment - was for projects with a specific environmental focus such as energy efficiency, renewable energy, water and sanitation and solid waste management. Between 2001 and 2005 EBRD provided 48% of IFI environmental investment and 53% of IFI technical assistance for environmental investments in Eastern Europe, Caucasus and Central Asia.

High volume of environmental investments underlines the EBRD mission as environmental sustainability is central to EBRD's mandate. The EBRD mandate is to help partner countries to make the transition from unsustainable, centrally planned economies to efficient, equitable and sustainable market economies. A sustainable natural environment and the efficient use of resources and energy are fundamental to achieving sustainable economic growth.

Equity investment is a less frequent financial instrument in which investor shares a major part of risk. On the other side, depending on the size of the investment, it allows to have a bigger say in the client company. If the investor is committed to sustainability, it is an excellent opportunity to promote environmentally friendly behaviour of the client.

4. Pricing of loans is often critical. Some IFIs like the World Bank and the ADB, provide concessional cheap loans much welcomed by the governments. This is not the case of the EBRD. EBRD normally lends on a non-concessional basis, based on current market interest rates - which is built into its mandate. However, in cooperation with donor funding additional value added can be provided like the TA in project preparation and project implementation.

5. Cost recovery is not only essential for a sound banking but it is closely linked to a sustainable development. Subsidised water and energy is not an environmentally friendly solution. Cost recovery should be an integral part of investments. The appropriate pricing of environmental goods, encourages conservation and more efficient use of resources and energy. Furthermore, it incentivises clients to develop sustainable institutional structures to meet, maintain and enforce higher environmental standards. At the same time, the social implications of tariff increases can not be ignored and affordability analysis where necessary should be conducted. In order to make a gradual implementation of cost recovery prices socially acceptable, different mechanisms have been developed. However, so called investment grants may accelerate the environmental investments without compromising sound banking and putting additional burden on low income groups.

6. Innovative financing instruments are required. Recent years have seen a number of innovations in the field of environmental financing. As a global concern about climate change increases, trading carbon credits generated by projects that reduce greenhouse gas emissions, has provided an important new source of environmental finance.

In order to help our partner countries to take advantage of these opportunities, EBRD, together with the European Investment Bank, launched the Multilateral Carbon Credit

Fund at the end of last year. Through this Fund, governments and private enterprises can buy carbon credits from emission-reduction projects.

However, it is not yet clear what international action will be taken after the Kyoto Protocol ends on 2012. This uncertainty threatens the viability of the carbon credit market. It is imperative that the international community reaches agreement on a post-Kyoto framework for greenhouse emissions trading.

Financial sector should also consider other options like:

- a) Piloting the establishment of water quality markets to create incentives for reduced water pollution discharges through permit trading.
- b) Working with enterprises to pioneer biodiversity offsets in the region.
- c) Exploring the potential for conservation banking through supporting biodiversity cap and trade systems allowing trading of endangered species credits to offset negative impacts on endangered species.

7. In recent years, EBRD has also provided a number of special purpose financing lines designed to promote sustainability. The EBRD has issued a €64 million energy efficiency and renewable energy credit line in Bulgaria and similar credit lines are to be developed in up to ten other countries in Central and Eastern Europe. Working with financial intermediaries exposes IFIs to additional environmental risks.

The financial intermediaries have limited capacity to undertake environmental due-diligence, monitoring and reporting. In response to this credit lines have to be complemented with support for training and capacity building. Since 1995 EBRD has supported 298 financial intermediaries in 29 different countries.

8. The context for environmental finance is changing. Increasingly, environmental improvements are being regarded as a business case for investment and sustainability is becoming part of mainstream investment. The development of carbon trading markets in recent years shows that the financial community is beginning to pay closer attention to environmental issues. Traditionally, if environmental due diligence recognises some environmental issues, investment is accompanied by EAD to mitigate possible negative impact. But increasingly major loans for environmental upgrades are issued financing purely to achieve better environmental performance. Good examples are: a \$100 million loan for the Mittal Steel Temirtau Coal Mine Modernisation project in Kazakhstan, and a \$300 million environmental loan to Russia's Lukoil.

9. The EBRD is drafting its new Environmental and Social Policy, due to be approved by early 2008 and is working on its Sustainability Initiative which will recognise these recent trends, including advances in energy efficiency, carbon trading, renewable energy, biodiversity and social issues including labour and gender. It will also emphasise the need for new, innovative initiatives in support of environmentally and socially sustainable development, including innovative financing instruments that will deliver environmental benefits. New financing facilities could be developed in the area of water and sanitation, in sustainable agriculture, biodiversity etc.

10. Closing remarks:

The Environment for Europe process is entering a new phase. I would like to reiterate that multilateral cooperation remains necessary to address the numerous environmental challenges in the region. In the need to address challenges of the climate change multilateral cooperation is an eminent part of the solution.

EBRD has been an active participant in the Environment for Europe process since its inception. Our close relationship with the Project Preparation Committee, and the donor support that has been channelled through it, has enabled to develop investment portfolio in areas such as water and sanitation, energy efficiency and biodiversity. Since the Kiev Conference, the PPC has supported EBRD projects with an investment value of €443 million.

The EBRD welcomes internalisation of the PPC Secretariat inside EBRD. It is understood as an important opportunity to strengthen the EBRD capacity to be proactive and innovative in the financing of environmental improvements and develop opportunities for promoting environmental sustainability.

Finally as the Environment for Europe process, and the region as a whole, enters a new phase, the EBRD remains committed to the principles of the process.

We look forward to continuing to work closely with our partners to ensure that the environmental sustainability remains a central objective of international cooperation in the region. We are considering initiating a regular "EBRD Environmental Forum" which could provide a platform for coordination in the area of environment and sustainability.