4 Recommendations for policymakers

This chapter draws on the challenges and solutions identified in Chapters 2 and 3 to set out recommendations to increase and accelerate the mobilisation of private finance, and the role that international public finance providers can play to this end. The chapter identifies three key action areas that policymakers should prioritise: i) tailoring project- and country-level interventions to de-risk projects and markets; ii) scaling up the use of cross-border financing mechanisms and improving co-ordination to channel global finance; and iii) enhancing international institutions to maximise the mobilisation potential of public climate finance.

The analysis presented in Chapters 2 and 3 suggests there is considerable scope to improve the effectiveness of public climate finance in mobilising larger volumes of private finance. Climate finance cannot operate in a vacuum; as highlighted throughout this report, a wide range of country-specific, sectoral, and project-level factors affect the potential for private finance mobilisation. The scope of this report, and the recommendations below, however, are primarily focused on the actions that bilateral and multilateral providers of climate finance can take by shifting the nature and direction of their financing and technical assistance. These will need to be co-ordinated with action from a wide set of stakeholders across partner countries and the private sector.

The recommendations below are presented in general terms. Their applicability will, however, vary considerably across different contexts, reflecting different provider mandates and priorities, beneficiary country-specific challenges and priorities, and varying challenges across different climate-relevant sectors and technologies. Their ease of application, impact in mobilising additional private finance for investment in climate action, and timescale of impacts will also vary, as set out in the indicative judgements presented in Figure 4.1, below.

4.1. Action area 1: Tailor project- and country-level interventions to de-risk projects and markets

Recommendation 1: Tailor public finance interventions to reflect the rapidly-shifting commercial dynamics in key sectors, including scaling up blended finance and other mobilisation approaches in more mature sectors

There is evidence that many critical investments in decarbonisation, particularly in clean energy, are already or close to being commercially viable in some developing countries. Meanwhile, there remain significant investment needs in climate action areas where the potential for commercial investment is much more limited, including investments in adaptation which are difficult to commercialise, and investments in agriculture and forestry where the climate imperative is often misaligned with commercial opportunities.

Private finance mobilisation should become the default approach for public finance directed towards climate investments in sectors where the commercial dynamics have evolved to improve the prospects of private sector participation, for example where new technologies have become more mature and risks and returns better understood. A large portion of international public climate finance remains dedicated to clean energy investments, notably renewable power generation, with the vast majority of this finance provided in the form of conventional loans, which mobilise relatively small volumes of private finance. Notwithstanding the urgency and importance of scaling up investment in clean energy, the rapidly shifting commercial dynamics of energy investments open the opportunity to reorient public climate finance to more effectively crowd-in private finance (see Recommendation 2). Specifically, climate finance providers should consider private finance mobilisation as the default approach for their support in renewable power, and consider, where appropriate, whether any direct public support remains required at all. In turn, much greater volumes of public climate finance could then be dedicated towards the development of blended finance instruments that crowd-in private finance in other sectors, including industry, transport, agriculture, and forestry, or in low-income countries. Given mobilisation approaches aim to reduce public finance deployed over time, such a shift has the potential to free up capital for a larger number of interventions, including wider climate investments in sectors and markets where commercial options are more limited, such as least developed countries, and towards wider sustainable development objectives.

International public climate finance should be used to de-risk sectors and asset classes that are currently beyond the scope and investment criteria of commercial finance. As set out in the complementary paper (OECD, 2023[1]) on *Scaling up adaptation finance in developing countries: challenges and opportunities for international providers*, bilateral and multilateral public climate finance providers should take steps towards increasing the mobilisation of private finance towards adaptation, including by (i) allocating their development finance with a clear objective to mobilise private finance for adaptation, particularly in sectors favourable to private sector engagement, such as agriculture; (ii) exploring, piloting, and subsequently scaling tailor-made approaches, such as portfolio approaches, risk-sharing mechanisms, and the issuance of bonds like Green, Social, and Sustainability (GSS) bonds; (iii) considering the unfamiliarity of private financiers with adaptation and the challenges of small-scale transactions, utilising intermediaries, such as development actors and private fund managers, to unlock private finance for adaptation projects through portfolio approaches and risk-sharing mechanisms; and (iv) adjusting currently bankable projects with cash-flow certainty to contribute more to adaptation, for example by integrating climate resilience into the design of new infrastructure. Increased efforts in mobilising private finance for adaptation should be anchored by the development of standardised metrics for blended finance transactions that are capable of effectively monitoring and evaluating their impact on climate adaptation (OECD, 2023[1]).

Recommendation 2: Within more mature sectors and markets, reorient loans and other debt instruments towards private finance mobilisation

Loans account for the vast majority – a yearly average of USD 43.6 billion between 2016 and 2021, or 71% – of public climate finance provided by developed countries through bilateral and multilateral channels; yet only USD 12.3 billion per year of private finance was mobilised by leveraging mechanisms that involve debt-related public finance instruments (including direct investment in companies and special purpose vehicles, simple co-financing, syndicated loans, and credit lines). This points to the potential of reorienting lending to more effectively mobilise private finance, including through shorter loan tenors where appropriate (see Recommendation 5), and scaling up the use of other non-debt blended finance approaches where appropriate.

Syndicated loans, including subordinated debt, can be particularly effective in mobilising private finance in many climate action areas, for example towards large clean energy projects with high up-front costs. However, such loans currently mobilise relatively small sums, suggesting they are underutilised. Credit lines are another form of debt instrument that have the scope to be significantly scaled up. They are particularly applicable to smaller projects with investments undertaken over a longer time horizon, for example investment in energy efficiency and sustainable agriculture.

Recommendation 3: Scale up the use of guarantees at the project and portfolio levels, and enhance providers' institutional capacity to provide guarantees

Guarantees have demonstrated strong private finance mobilisation potential, mobilising an average of USD 2.6 billion yearly between in 2016 and 2021. Along with equity investments, scaling up the use of guarantees, including to optimise the terms and conditions of debt through extended maturities and lower interest rates, can help address the high cost of capital in contexts where debt distress and wider risks deter private investment.

Specific structures that have demonstrated a strong record in mobilising private finance include MIGA's various forms of guarantees against a range of political and credit risks. Guarantees can be particularly impactful when combined with other mobilisation approaches, for example the Swedish International Development Cooperation Agency's (SIDA) guarantee of the first-loss tranche in the IFC's Managed Co-Lending Portfolio Program (MCPP).

In April 2023, members of the OECD's Development Assistance Committee adopted new rules to better reflect donor effort in measuring credit guarantees in official development assistance (ODA). This methodology is expected to open to the door to a greater use of guarantees to mobilise private finance for development and climate. Continued discussions should ensure revised ODA directives give clarity on the full breadth of guarantees provided by donors, including in relation to the operations of MDBs and other multilateral institutions.

Recommendation 4: Provide tailored capacity-building to support improved enabling conditions for investment and the development of project pipelines

There is a need to address the persistent institutional and capacity challenges that limit the scope for private finance mobilisation in many developing countries. While these efforts need to be country-led, international climate finance providers have a critical role to play in supporting the creation of the required enabling environments for investment by scaling up policy support and technical assistance through the provision of grants and concessional finance where appropriate. Such support is particularly appropriate in sectors and countries where attracting private capital is still too challenging, such as in low-income countries and fragile contexts, and areas such as adaptation and resilience, biodiversity, and social sectors, amongst others. Governments and climate finance providers also need to ensure that capacity development and policy reforms are systematically undertaken with a view to maximising the flow of finance towards climate projects.

Even in more mature sectors and markets, technical assistance to further improve enabling environments and support project demonstration can help maximise the subsequent private finance mobilisation potential of public climate finance at the portfolio and project levels. As outlined in Chapter 3, the availability of projects with balanced risk-return profiles remains a major impediment to private investment in climate action; technical assistance for project pipeline development can support private finance catalysation. Additionally, in the context of rapidly evolving technologies and markets for climate action investments, regulatory policy and frameworks need to keep pace; technical assistance is critical in supporting developing countries to this end.

The relatively small sums of private finance mobilised towards low-income countries underscores the need to start by supporting capacity development, in order to improve their enabling conditions for investment. Such support should be closely linked to wider assistance for broader sustainable development objectives, which are themselves critical to improving investment conditions, capital market development, and stimulating cross-border and domestic private sector investment in climate action.

Recommendation 5: Progressively exit projects once they become commercially viable to free up financial resources for new climate change mitigation and adaptation priorities and projects

Traditional infrastructure development finance has largely been characterised by an “originate-and-hold” model, with development finance providers supporting and financing project origination, development, and construction, and then holding assets in order to recoup their investments and make a return. Loans, which comprise the vast majority of international public climate finance, have an average maturity of 23 years. This approach, however, is capital intensive and locks significant volumes of limited public climate finance into projects that may have achieved commercial viability.

Linked to Recommendation 1, development finance providers should routinely and frequently assess the commercial landscape of their investments and explore opportunities to reduce their financial exposure by bringing in greater volumes of commercial investment when the conditions allow, in line with the OECD’s *Blended Finance Principles* (OECD, 2020[2]). This could include selling their equity exposures at the project level entirely, securitising multiple exposures (through the structures discussed in Recommendation 6), or selling parts of their loan books to the private sector.

4.2. Action area 2: Scale up the use of cross-border financing mechanisms and improve co-ordination to channel global finance

Recommendation 6: Expand the use of public climate finance to support the development of financing structures that crowd-in institutional investment at scale

The small scale of projects and transactions and information asymmetries remain major barriers to cross-border investment towards developing countries across all climate action areas. The nature of many climate investments, for example off-grid renewables, energy efficiency, and agriculture, are small in scale individually, but have major climate mitigation and adaptation potential collectively. International investors lack the in-country presence and local experience, due diligence capacity, as well as financial appetite to invest in small projects.

Investors have, therefore, repeatedly called for the development of secondary assets that aggregate a number of smaller constituent projects in developing countries into larger, rateable, tradeable assets. Relatively small amounts of public climate finance can be used to support structured finance, including aggregation and securitisation, alongside support for standardisation of contracts and project documentation, to address capacity constraints amongst commercial investors and mobilise private finance. Such instruments can support climate finance providers to more rapidly exit projects once they are commercially viable (see Recommendation 5).

However, such instruments (shares in collective investment vehicles), accounted for only 7% of private finance mobilised towards climate action, suggesting they remain underutilised. This reflects the relative novelty of these approaches, but nevertheless suggests there is significant scope to increase public support towards such structures. These efforts should be combined with support for local capital market development, to draw on and expand the critical role of local financial institutions in deploying international finance for climate action on the ground.

Recommendation 7: Strengthen co-ordination and collaboration between bilateral and multilateral climate finance providers, domestic actors, and the private sector

A range of international partnerships have been trialled over time. Country platforms are emerging as potentially promising new ways to strengthen collaboration between the public and private sectors at the country level and mobilise the needed domestic and international finance to support developing countries' transitions to low-carbon and resilient development pathways. Collaboration between and amongst bilateral and multilateral providers can be scaled up, including by increasing co-investment approaches between bilateral and multilateral providers, as well as standardising processes and project documentations and sharing pipeline development and due diligence.

Experience with country platforms, including *Just Energy Transition Partnerships (JETPs),* so far is fairly limited. Nevertheless, some partial lessons learnt have emerged. Strong country ownership, in line with best practice on development effectiveness, and credible political commitment by all parties are essential to establishing clearly-defined, ambitious long-term visions and interim targets, as well as to sustaining platforms or partnerships over time. Country platforms need to be initiated, designed, and implemented ensuring inclusive, meaningful dialogue with and participation of all stakeholders involved or impacted, including civil society organisations.

Upfront transparency on project pipelines is required in order to effectively mobilise private investors, alongside efforts to develop those pipelines (see Recommendation 4). Early identification of areas where concessional finance can be most catalytic versus where it might crowd-out private finance, in line with the sector- and project-level considerations outlined in Recommendation 1, should inform the early conception, design and composition of country platforms.

The sectoral scope of country platforms, most prominently the JETPs, has been limited to the energy sector in middle-income countries. There is, therefore, scope to consider using similar models in other countries and sectors, including adaptation and nature, tailoring the partnership to the specific needs the target country and sector(s). Moreover, financial and other support through JETPs has to date been dominated by G7 donors; this should be expanded to bring in a wider range of development partners.

4.3. Action area 3: Enhance international institutions to maximise the mobilisation potential of public climate finance

Recommendation 8: Request clearly-defined institutional private finance mobilisation targets from MDBs, while safeguarding development objectives and avoiding unintended consequences

As shareholders of multilateral development banks (MDBs), bilateral providers should request MDBs to explicitly define private finance mobilisation corporate strategies and incentives as part of their core mandates. As mobilisation is not an end in itself, but rather a means to increase the resources available to support development, climate, environmental and social objectives in partner countries, mobilisation targets should have differentiated objectives for specific sectors and country contexts, and be revisited on a regular basis to adjust and, where appropriate, reduce, the role of public finance as the commercial landscape for investment improves over time. Such objectives should also define specific mobilisation targets, taking into account that the scope for the mobilisation of private investment might be limited in sectors and regions that face relatively high barriers to investment, for example low-income countries, investment in nascent technologies and public goods. Mobilisation targets will, therefore, need to be made with careful consideration of wider MDB mandates, ensuring that greater efforts to mobilise private finance do not come at the expense of supporting sustainable development objectives more broadly, including fulfilling basic development needs in the poorest countries. Moreover, scaling up mobilisation requires enhanced collaboration between different specialists within MDBs, bringing together corporate strategy, structuring, operational and climate teams.

Recommendation 9: Encourage MDBs to further use or develop risk transfer mechanisms and provide local currency financing

MDBs can use risk transfer mechanisms to free up risks from their balance sheets and increase lending in development priority areas, such as climate-related investments. Co-lending approaches and syndication platforms are useful mechanisms that MDBs can use to attract institutional investors' capital.

Approaches to optimise the capital efficiency of MDBs, however, should not be considered as a substitute for capital increases[1] where needed, especially to support the investments and activities of MDBs' concessional operations. These efforts would be complemented by enhanced dialogue and knowledge-sharing among MBDs as well as with shareholders, credit rating agencies, commercial and institutional investors.

Recommendation 10: Further improve data disclosure and transparency on accounting methodologies relating to public climate finance and the private finance it mobilises

There remain significant data gaps, which limit the ability to assess the private finance mobilisation record and potential of international public climate finance, including in the data and analysis presented in this paper. This presents major impediments to policymakers seeking to understand what has worked in various sectors and geographies. More granular data reporting on the nature of public climate finance – including on whether interventions are expressly designed and *intended* to mobilise private finance, through which leveraging mechanisms, and the role of complementary technical assistance – would help provide a more complete picture both of private finance mobilised on aggregate, as well as the merits of individual transactions.

As a complement, efforts should be made to share the data that does exist. For example, the Global Emerging Markets Risk (GEMs) database could be improved (including with more data on recovery rates, adding equity transactions and providing more granularity on project-, sector-, and country-level characteristics) and made public in full. This would help close information asymmetries on country-specific investment risks in developing countries by giving investors access to historic data on development finance providers' transactions.

Figure 4.1. Summary of recommendations

Challenges	Recommendations and delivery channels	Applicability to challenges	Type of impact	Timescale of impact
Project and country-level challenges • Public climate finance does not currently reflect commercial dynamics in many climate action areas. • Mobilisation approaches/ blended finance make up a relatively small share of interventions. • Enabling environments in many developing countries remain weak, stifling investment in climate action.	**Action area 1: Tailor project- and country-level interventions to de-risk projects and markets**			
	1. Tailor public finance interventions to reflect the rapidly-shifting commercial dynamics in key sectors. ***climate finance providers***	●	**Mobilisation**	Short term
	2. Within more mature sectors and markets, reorient loans and other debt instruments towards private finance mobilisation. ***climate finance providers***	● ●	**Mobilisation**	Short term
	3. Scale up the use of guarantees at the project and portfolio levels, and enhance providers' institutional capacity to provide guarantees. ***climate finance providers***	● ●	**Mobilisation**	Short term
	4. Provide tailored capacity-building to support improved enabling conditions for investment and the development of project pipelines. ***climate finance providers***	● ●	**Catalytic effect**	Medium-long term
Private sector challenges • Scale and accessibility of investments in developing countries remains limited. • Governments, climate finance providers, and private finance remain disjointed.	5. Progressively exit projects once they become commercially viable to free up financial resources for new climate change mitigation and adaptation priorities and projects. ***climate finance providers***	● ●	**Mobilisation**	Medium term
	Action area 2: Scale up the use of cross-border interventions and improve international co-operation to channel global finance			
	6. Expand the use of public climate finance to support the development of financing structures that crowd-in institutional investment at scale. ***climate finance providers with financial intermediaries***	●	**Mobilisation**	Short term
	7. Strengthen co-ordination and collaboration between bilateral and multilateral climate finance providers, domestic actors, and private sector. ***recipient governments, climate finance providers, private sector***	● ●	**Catalytic effect**	Medium term

Challenges	Recommendations and delivery channels	Applicability to challenges	Type of impact	Timescale of impact
Institutional challenges	**Action area 3: Enhance international institutions to maximise the mobilisation potential of public climate finance**			
• Mobilisation is not a core objective for most MDBs. • Mobilisation approaches are under-utilised relative to potential. • Data on public finance and mobilisation is misaligned and weak.	8. Request clearly-defined institutional private finance mobilisation targets from MDBs, while safeguarding development objectives and avoiding unintended consequences of such incentives. ***MDB shareholders, MDBs***	●	**Catalytic effect**	Medium term
	9. Encourage MDBs to further use or develop risk transfer mechanisms and provide local currency financing. ***MDB shareholders, MDBs***	● ● ●	**Mobilisation**	Short term
	10. Further improve data disclosure and transparency on accounting methodologies relating to public climate finance and the private finance it mobilises. ***climate finance providers***	●	**Catalytic effect**	Medium term

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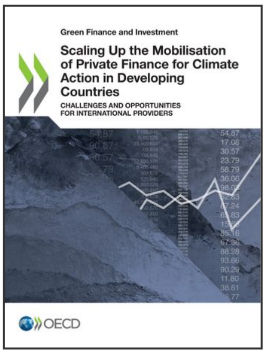
OECD (2023), *Scaling up adaptation finance in developing countries: Challenges and opportunities for international providers*, https://doi.org/10.1787/b0878862-en. [1]

OECD (2020), *OECD DAC Blended Finance Principle 2 Guidance*, https://www.oecd.org/dac/financing-sustainable-development/blended-finance-principles/principle-2/Principle_2_Guidance_Note_and_Background.pdf. [2]

Note

[1] A capital increase is an increase of shareholders capital subscription, usually including both paid-in capital and callable capital, to enable an MDB to increase its lending. A general capital increase occurs when all shareholders increase their subscriptions while keeping the same shareholding structure. A selective capital increase for a subset of shareholders increases the MDB’s available capital while changing shareholders’ relative weight in their voting power (Boosting MDBs’ investing capacity, 2022[3]).



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