Source: CANVA

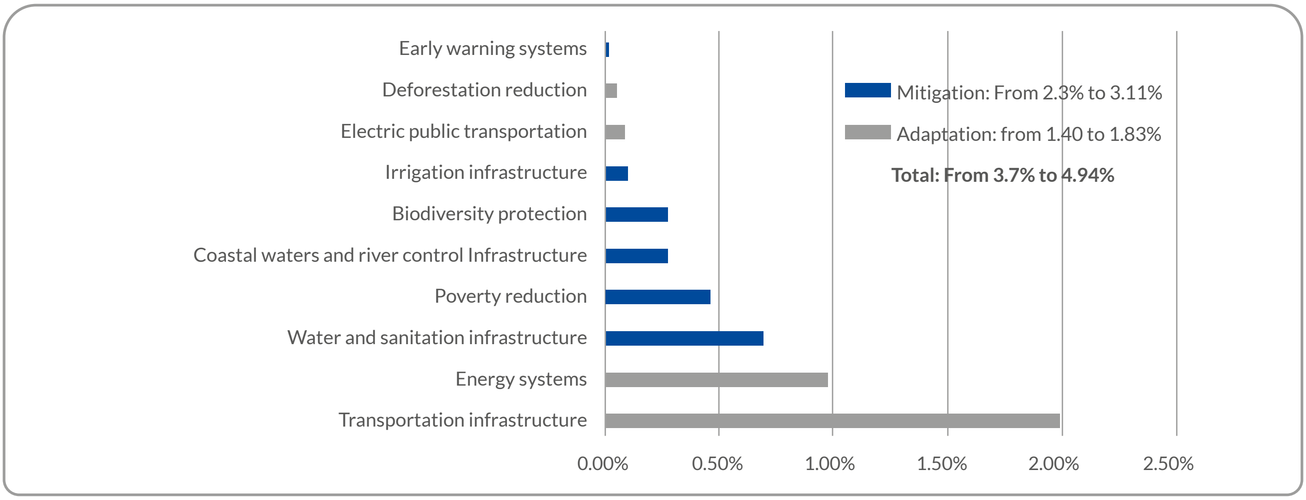
Climate transition financing in **LAC public development banks**

Public development banks (PDBs) in Latin America and the Caribbean view climate transition as an opportunity for investment, but according to the new ALIDE-EIB survey, confront challenges like the shortage of long-term financing and the limited awareness of their customers regarding the options for investment.

The Latin America and Caribbean (LAC) region is confronting one of its most serious climate crises, marked by high physical vulnerability to extreme events. Although its contribution to global greenhouse gas emissions is minimum, its economies frequently suffer the impact of disasters like hurricanes, forest fires and droughts. Faced by this challenge, the joint study recently conducted by the Latin American Association of Development Financing Institutions (ALIDE) and the European Investment Bank (EIB) «Climate financing in Latin America and the Caribbean: how public development banks are contributing to supporting the climate transition», points up the role played by PDBs in the region, as essential institutions for raising the necessary funds with which to effect the transition toward a low-carbon and climate resilient economy.

LAC is experiencing a disproportionate impact of climate change: the frequency and seriousness of natural disasters have increased, negatively affecting both the lives and economies of its inhabitants. According to data published by the International Monetary Fund (IMF) and the Economic Commission for Latin America and the Caribbean (ECLAC), coping with these challenges will cost between US$110 and US$290 billion a year, an investment representing from 1.9 to 4.9% of the region's gross domestic product (GDP). The investment priorities are to be found on two

Figure N.º 1: Annual investment needed to fulfill Latin American and Caribbean climate action commitments up to the year 2030 (% of GDP)



Source: ECLAC (2023a).

fronts: mitigation, in order to reduce physical vulnerability to extreme climate events, and adaptation, which means building up the most exposed infrastructure and economic sectors, like agriculture, infrastructure and tourism.

The countries of the region, however, are confronted by a restrictive macroeconomic context, marked by low growth, high debt levels and limited fiscal margins. This hampers their access to sufficient funds with which to finance the green transition, limiting the capacity of the governments to make sustainable climate investments.

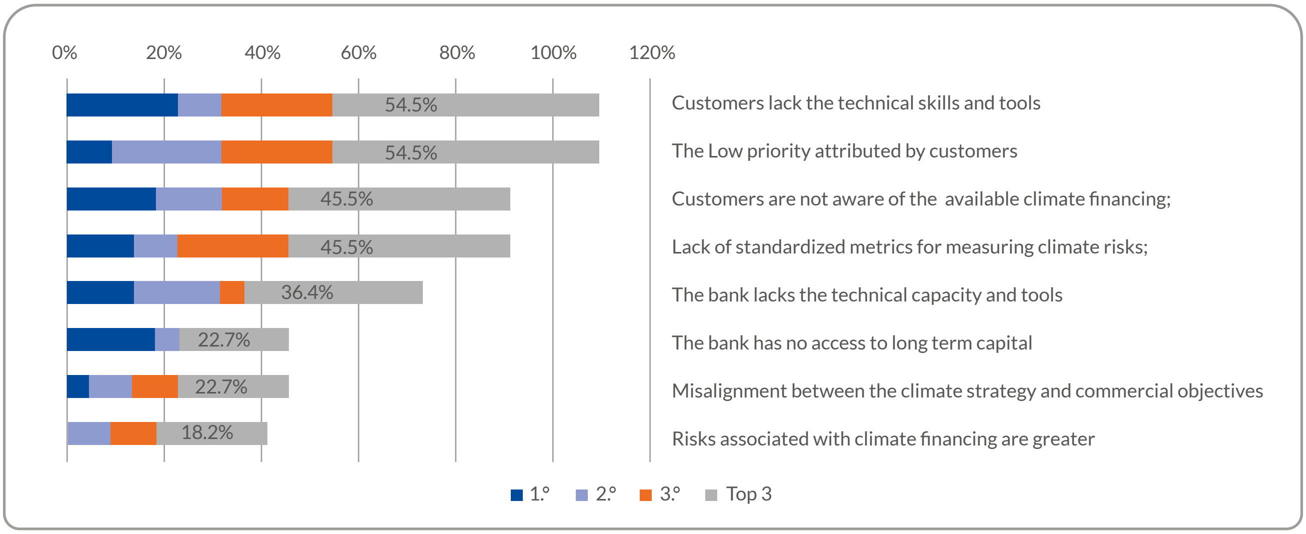
Public development banks are particularly important in LAC, where, in some cases, they account for nearly 50% of the banking system and, as a result, of those countries' total credit. Their importance stems from their capacity to raise funds and to catalyze investments in sectors of high climate priority, where the private sector tends to be reluctant to assume risks, due to the lack of guarantees or short-term profit.

The study conducted by ALIDE and the EIB reveals that these banks consider climate financing to be a strategic opportunity. Some 93% of the public development banks view climate transition as an opportunity, rather than a risk, and 77% state that they incorporate international climate-related standards, like the UN Sustainable Development or the Paris Agreement Goals, in their practices.

Even so, gaps continue to exist in the public development banking sector in regard to their alignment with a climate strategy and access to financial mechanisms, such as green loans. The principal barriers that have been identified include the low priority assigned by their customers to green

Source: CANVA

Figure N.º 2: Proportion of public development banks that mentioned Each factor among the three main limitations (% of public development banks that responded)



Source: EID-ALIDE Climate Survey, 2024.

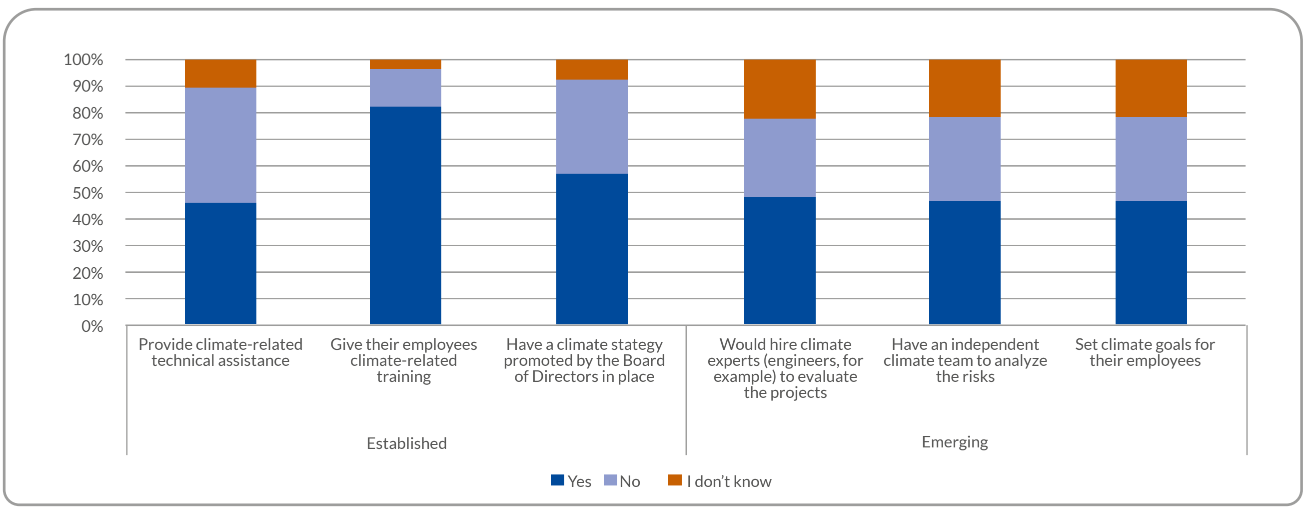
investments, the lack of technical capacity on the part of both the banks and their customers, and the scarcity of long-term financing in line with climate project characteristics.

The banks also face internal barriers, like the absence of standardized metrics for monitoring climate risk and the lack of accessible financing in the long term, which are critical aspects for making climate investments viable. Improvement of the regulatory and data infrastructure is essential for mobilizing the private sector to make green investments.

Public development banks have made progress in what are considered to be «established» climate-related banking practices, but much remains to be done in confronting climate risks fully. At present, 46% offer their customers technical assistance, 82% train their staff members in climate issues and 57% have a climate strategy in place approved by their boards of directors. Nonetheless, a study of emerging trends reveals that only 48% employ climate experts, 46% have a team dedicated to all aspects of climate risk and another 46% have incorporated climate goals as key indicators of personnel performance.

On the other hand, Latin America and the Caribbean already pay a high cost for the effects of climate change, particularly the Caribbean, where small landlocked countries face

Figura N.º 3: Proportion of public development banks that ... (% of banks that responded



Source: EIB-ALIDE Cimate Survey, 2024.

Figure N.º 4: Proportion of public development banks that experienced damage to their physical assets due to extreme climate events (% of public development banks that responded)

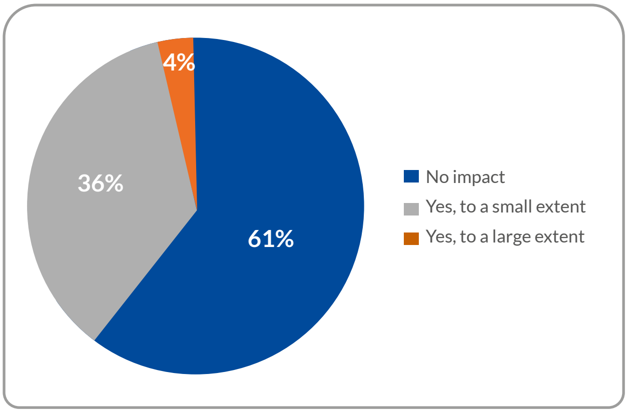
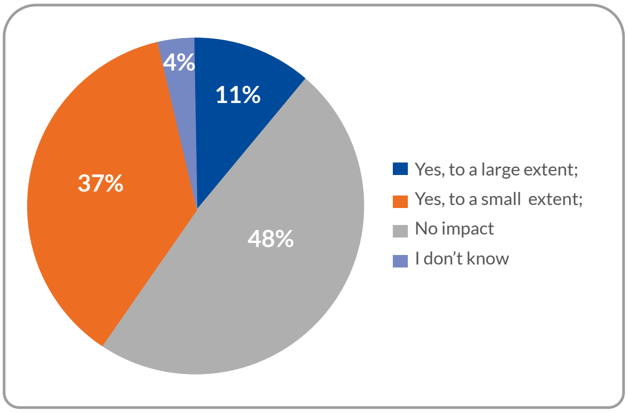


Figure N.º 5: Proportion of pubic development banks that reported deterioration of the quality of their assets due to extreme climate events (% of banks that responded)



Source: EID-ALIDE Climate Survey, 2024.

impacts that are disproportionate, considering their size and emissions. Public development bank exposure to these physical risks is significant at the national level. In 2023, 40% of these banks reported damage to their physical assets and 59% adduced the deterioration of their portfolio quality due to extreme climate events. The sectors most adversely affected are the micro, small and medium enterprises, together with infrastructure, which reflects the vulnerability of these sectors to climate phenomena.

The study emphasized that in order to overcome those challenges, collaboration must be improved among governments, the private sector and public development banks in the region, in order to raise the necessary financial resources and reach the climate transition goals. These include national policy alignment with international commitments, like the Sustainable Development and Paris Agreement Goals. The establishment of clearly-defined regulatory frameworks and appropriate incentives could contribute to increasing private sector participation and promote further integration of green investment in the region.

It is in this context that Latin American and Caribbean development banking is to be found at a decisive moment in its course toward becoming economically sustainable and climate-resilient. The public development banks are called upon to lead this transition, and their capacity for adapting to and innovating and collaborating with the private sector and international institutions will be vitally important for surmounting existing barriers and activating a turn toward a low-carbon and climate impact-resistent future.

Source: CANVA

1 For the reader's ease of understanding, the array of actions taken by a bank to facilitate climate transition were divided into two groups: "established" – those not involving any structural change in banking practices and that are commonly found in the banking sector, and "emerging" – those for which less examples are available in the industry and that could involve a modest change in the way of doing business.

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