

When blue becomes

green:

A new bank for a low-carbon future



Roman Marshavin, World Bank, Executive Director for Russia *Alexey Morozov, World Bank, Advisor*

Climate change is one of the greatest challenges of the 21st century. The latest report of the International Panel on Climate Change projects that in the coming decades the world will be facing increasing heat waves, longer warm seasons and shorter cold seasons. As we are witnessing with our own eyes, climate change also causes longer patterns of unpredictable and extreme weather. One can argue about the reasons behind the energy crisis in Texas during the winter of 2021, but one thing is obvious — Texans had not experienced such a prolonged, freezing winter for

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a long time. A few months later, the winds in the North Sea suddenly stopped blowing, sending the UK into an energy crisis and pushing several domestic energy suppliers out of business in several days. To tackle the climate change challenge, the global community long ago joined efforts towards finding ways to minimize humans' impact on nature.

Finally, on November 4, 2016, the Paris Agreement entered into force, aiming to limit global warming to well below 2°C compared with pre-industrial levels. Countries have been actively working ever since on accelerating climate action — the latest example being the COP26 summit which took place between October 30 and November 13, 2021. International organizations and especially financial institutions stepped in to support the climate agenda, and among them the World Bank Group (WBG),

by playing a leading role in helping to shape the climate dialogue and support climate financing. In 2021, the WBG launched the Climate Change Action Plan 2021–25 (CCAP), which sets out the ambitions and objectives of the WBG leadership on climate change adaptation and mitigation financing for adaptation, including increasing climate financing targets to 35 per cent on average over the fiscal years 2021–25. In its 2021 Energy Policy to Support Energy Access and a Low-Carbon Transition in Asia and the Pacific, the Asian Development Bank announced its ambition to deliver \$100 billion in cumulative climate financing from its own resources between 2019–30.

Investment needs

As renewable energy is considered to be an important component of the green transition, a substantial share of funds provided by Multilateral Development Banks (MDBs) is aimed at increasing renewable capacities, especially in developing economies — the main clients of those institutions. And yet, investment needs are still enormous.¹ Tackling the green transition comes at a price. According to the World Bank (WB), the cost of meeting growing energy demand while transitioning aggressively to low-carbon pathways in large and middle-income economies in Asia alone could be in the range of \$650 billion annually or \$13 trillion over 20 years. Between 2015 and 2020, the WB provided \$9.4bn in financing for renewable energy and energy efficiency projects in low- and middle-income countries. While this amount is significant, it is obvious that the efforts of the WB and other existing MDBs will not be sufficient to fund a green transition.

At the same time, while recognizing the importance of the climate agenda, decision-makers cannot lose sight of the development goals facing humanity, and especially the poorest. It would be a grave mistake to sacrifice

development exclusively for the sake of lowering emissions. According to the United Nations Conference on Trade and Development (UNCTAD), at the current level of investment in SDG-relevant sectors, developing countries face an annual gap of \$2.5tr. Estimates for total investment needs in developing countries alone range from \$3.3tr to \$4.5tr per year for basic infrastructure (roads, rail and ports; power stations; water and sanitation); food security (agricultural and rural development); climate change mitigation and adaptation; health and education.

At today's level of investment, both public and private, in SDG-related sectors in developing countries, the average annual funding shortfall over 2015–30 is expected to be around \$2.5tr.² This does not leave developing countries much room to maneuver, as the fiscal space is rapidly shrinking. Governments would need to make tough choices and set their priorities straight. Although the cost of renewable generation has been falling, deploying wind or solar generation still requires quite sensitive budget sacrifices and significant baseload build up. By channeling scarce public and international funds into deployment of renewable technologies, a real possibility looms that in addition to not making a significant impact on solving climate change challenges, those governments may end up depriving their populations of financing that could be used for more immediate, basic purposes, like health care, education and food security.

Ensuring a just transition

As far as energy is concerned, switching to gas-to-power (especially combined with carbon capture technologies) is considered by many to be a reliable, affordable and environmentally prudent option that could enable a just transition without causing abrupt and risky sacrifices.

This is true not only in least-developing countries, but also in middle-income and even high-income economies. In the US, for example, the growth of wind and solar (126 TWh) between 2015 and 2018 was accompanied by a similar increase in gas-fired power production capacity (134 TW).³

In Germany, a report by Wartsila Oyj shows that to phase-out coal power plants by 2038 the country would need as much as 12 GW of new natural gas-fired power plants.⁴ When a lightning strike led to the blackout of an extensive portion of the UK grid in London in 2019, it ignited conversations on the need for resilience in the grid, as it became apparent that battery storage alone will not be enough to guarantee security of supply in light of the increasing penetration of renewables in the energy mix.⁵ “With nuclear unsuitable for providing anything but baseload due to the time and expense required to kick a reactor into gear, the CEO of Statera, a UK power supplier noted, fossil fuel gas offers the best route — even if counter-intuitively — to a carbon-neutral future for the UK.”⁶ Two years later, when the wind stopped blowing in the North Sea, the UK faced one of the biggest energy crisis in its history. Gas and coal-fired electricity plants were called to provide baseload electricity, sending electricity prices to \$395/MWh. This even resulted in the restarting of a coal power plant in Nottinghamshire — one of the very few left, and slated for closure by 2024.

While industry experts may have different opinions regarding how long natural gas will remain a transition fuel helping to lay the path towards a green future, the majority of them agree that gas-powered generation will continue to play a key role in the energy transition, at least for some time. Mohammad Sanusi Barkindo, the OPEC Secretary General, mentioned that “oil and gas will continue to have an important role to play well into the future ...” and “... it has much to offer in this regard, including some of the world’s cost cutting-edge technologies and advanced innovations, which can all be leveraged to promote a lower-carbon future.”⁷

According to the International Energy Agency (IEA), “the links between electricity and gas markets are not going to go away any time soon. Gas remains an important tool for balancing electricity markets in many regions today ... and ... will remain an important component of electricity security.”⁸

According to Deloitte: “The hydrocarbon business model still has a lot to offer, especially for resources at the bottom of the cost curve, and can adapt with new

clean energy technologies (eg, carbon capture and hydrogen-based energy storage) that abate emissions on a significant scale.”⁹

And yet, finding MDB financing even for development of gas-to-power plants is becoming more difficult. The WBG and the European Investment Bank have dropped their support of upstream oil and gas in 2019 and financing of gas-to-power projects has been declining. Over the last few years, major shareholders of the MDBs have been vocal in slowing down their support of gas-related projects. To get their approval, those projects have to be located in low-income countries with no economically and technically feasible alternatives to clean energy sources in sight. These projects would also need to have a significant positive impact on energy security, energy access and development.

As a result, such projects are often facing greater scrutiny from MDB stakeholders compared with green-labelled investments. On top of that, MDB staff are often discouraged from coming up with conventional fossil fuel-based projects, even when all or most of the applied conditions can potentially be met. Commercial financing is also shrinking as institutional investors, who traditionally have been the supporters of long-term investment projects, are becoming increasingly ESG-concerned, gradually disposing of their holdings in projects that have any connection to fossil-fuel powered generation.

As interest in gas-to-power projects in the eyes of MDBs and institutional investors is shrinking significantly, while demand for baseload generation is apparently continuing to grow, it is unclear who is going to assist developing countries in transitioning toward a green future. Even worse, underfinancing creates a real possibility of future market movements that could lead to a deficit of fossil-based products (in the end even Tesla cars still use a lot of plastic in their construction).

Developing a solution

When it comes to capital markets, the global community has developed a solution for dealing with the assets that banks are hesitant to hold, but which have strategic or other substantial value. During the financial crisis it has been customary for governments to pool all such ‘assets’ into a special purpose vehicle, thus lifting the burden off the shoulders of commercial banks and the private sector and pooling them together under strict supervision of regulators or some specifically designated governmental agency with the appropriate expertise.

A similar ‘pooling’ approach could be used regarding the energy assets that become less attractive to the world development community. In our opinion, the time has come to launch a discussion on establishing an international multilateral bank that will use the highest fiduciary standards, employed by the international community, and will rely on the expertise of top world experts to assist developing countries in identification, appraisal, financing and supervision of environmentally and socially acceptable fossil fuel-based energy projects.

Major oil and gas producing countries could be the founders of such international financial institution, mobilizing funds and applying their top knowledge and expertise for the common good. There is at least one existing and quite successful example of major fossil fuel producers pooling their funds to help the global community to tackle their development challenges.

In 1976 the Member States of OPEC have established the OPEC Fund for International Development. Recently the OPEC Fund has expanded its role in financing the energy sector with its Energy for the Poor Initiative and participation in the UN Sustainable for All Initiative.

Possible financial tools

We believe that launching such a Bank (we suggest naming it ‘International Bank for Sustainable Energy Future’ or IBSEF) would enable developing countries to develop reliable and cost-efficient power sources, while enabling just transition. The IBSEF would provide countries with so much needed financing and/or leveraging tools to financially back the fossil fuel-based facilities.

Those funds may be used for example, for developing environmentally conscious gas-powered generation, to help countries minimize natural-gas related emissions through development of low-carbon gases, carbon management solutions or deploying technologies at the existing fossil-fuel based facilities that could reduce their carbon impact.

At the same time, a specifically designed, transparent

governance structure that would include an independent board of environmental experts, would ensure that this financing is used efficiently, prudently and the best balance is achieved between the countries’ national priorities, their NDCs and the interests of the global community.

Key to a green tomorrow

The world’s road to a low-carbon future will not be easy and will be full of new challenges as we move forward. However, this journey cannot be undertaken without engaging oil and gas producers, as they hold one of the keys to the world’s green tomorrow. It is in our hands to ensure that during this journey the world uses its best minds and resources, and that no one along this road is left behind.

As Ibrahim Shihata, one of the founders of the OPEC Fund, noted:¹⁰ “The experience of the OPEC Fund shows ... that a modest, but well-structured step can, if pursued within careful limits envisaged for it, create, in time, the momentum needed for taking further steps towards the ultimate objective”. We believe that creation of the IBSEF could become such a modest step that would help create a much-needed building block towards the ultimate objective of a green, low-carbon world.



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10. *The OPEC Fund for International Development. The Formative Years. 1983.*