

Policy Brief

Leveraging National Development Banks To Enhance Financing For Climate-Smart Urban Infrastructure

Directed to Ministers of Finance, Environment/Climate Change, Infrastructure, Urban Development of National Governments

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KEY TAKEAWAYS

- While National Development Banks (NDBs) are well positioned to scale up financing for climate-smart urban infrastructure, only a small minority finance local governments or green infrastructure.
- This research evaluated the demand (cities) and supply (NDBs) side barriers of climate-smart urban infrastructure financing to identify actionable opportunities to scale up NDB financing for climate-smart urban infrastructure. Twelve maturity dimensions were identified across NDBs' strategic, financial, operational, and business parameters, representing areas of opportunities and specific actions that can be taken to capture them.
- Overcoming barriers faced by cities and NDBs also requires close collaboration between stakeholders, including national governments and DFIs. Each key stakeholder identified can play a role individually and collaboratively in bridging the gap in financing green urban infrastructure.

Investments in climate adaptation and mitigation measures in cities' infrastructure will determine the resilience and wellbeing of all communities for years to come. Inaction on climate change in cities will lead to increased inequality both within and among countries. Climate change can have significant financial implications that can create a threat to the stability of the financial system, by disrupting business operations and increasing unexpected expenditures. Up to US\$ 4 trillion worth of assets are at risk from climate change in cities worldwide.¹

At the same time, infrastructure needs are most acute in cities, and even more so in developing countries and smaller cities. Infrastructure financing needs are estimated at US\$ 4.1-4.3 trillion per year from 2015 to 2030.² Making infrastructure low-emissions and climate-resilient will require additional costs of US\$ 0.4-1.1 trillion per year.² However, climate-resilient infrastructure is estimated to have a favourable benefit-cost, with the World Bank estimating that investing US\$ 1 trillion in the incremental cost of making infrastructure more resilient in developing countries would generate US\$ 4.2 trillion in benefits.³

To close the investment gap in climate-smart urban infrastructure, National Development Banks (NDBs) have the potential to play a stronger role. Sitting at the nexus of public policy and the financial system, NDBs are well positioned to scale up financing for green urban infrastructure. Based on their strong local knowledge and proximity to cities, they are the ideal intermediaries to channel funds for climate-smart urban infrastructure and provide technical assistance and project preparation support for local governments.

This analysis from the Cities Climate Finance Leadership Alliance (Alliance) aims to provide a conceptual framework that looks at the essential dimensions that must be in place to enhance the role of NDBs in financing climate-smart urban infrastructure. The research builds on the main conclusions from the Alliance's Policy Brief on "Enhancing the Role of National Development Banks in Supporting Climate-Smart Urban Infrastructure".⁴

This latest research has focused on:

- **Cities as the demand side of green⁵ urban infrastructure financing.** The analysis is based on interviews with six municipalities to develop key insights on the challenges in accessing finance for green urban infrastructure projects, particularly from national development banks. The research and analysis on common barriers and key enablers for cities is presented.
- **The supply side of green urban infrastructure financing, and specifically the role of NDBs.** The research focuses on the barriers and opportunities that NDBs face in financing green urban infrastructure. Based on the interviews with ten NDBs globally, the study develops a "maturity" model of the key attributes required by an NDB to

1 CDP, <https://www.cdp.net/en/climate>

2 Cities Climate Finance Leadership Alliance (Alliance). "The State of Cities Climate Finance 2015." Alliance, 2015, [ccfla.wpengine.com/wp-content/uploads/2015/12/CCFLA-State-of-City-Climate-Finance-2015.pdf](https://www.ccfcla.org/wp-content/uploads/2015/12/CCFLA-State-of-City-Climate-Finance-2015.pdf).

3 Global Commission on Adaptation. "Urban Resilience Infrastructure: an Imperative in a Climate Uncertain World." The Rockefeller Foundation, 20 Sept. 2019, www.rockefellerfoundation.org/blog/urban-resilience-infrastructure-imperative-climate-uncertain-world/.

4 Cities Climate Finance Leadership Alliance (Alliance). Enhancing the Role of National Development Banks in Supporting Climate-Smart Urban Infrastructure. Alliance, 2020. https://www.climatepolicyinitiative.org/wp-content/uploads/2020/08/Enhancing_the_Role_of_National_Development_Banks_in_Supporting_Climate_Smart_Urban_Infrastructure.pdf

5 There is no widely accepted definition of "green infrastructure", but for the purpose of this memo, we refer to all low carbon, climate resilient infrastructure.

successfully support green urban infrastructure finance.

NDBs can play a central role in enhancing the support for municipalities throughout the climate-smart infrastructure lifecycle from concept, design and scoping to pre-feasibility, feasibility and implementation stage. However, only 4% of Public Development Banks are specifically mandated to finance local governments, and even fewer NDBs have a green infrastructure-focused mandate.

The Role of National Ministers

National ministers have areas of responsibility that are pertinent to the relationship between NDBs and cities with respect to financing climate-smart urban infrastructure.

- Minister of Finance: ensure the NDB has the mandate and financial base to operate effectively in support of climate-smart urban infrastructure. As key stakeholders with a unique capacity to unlock climate action, Finance Ministers are encouraged to adhere to the Helsinki Principles (established by the Coalition of Finance Ministers for Climate Action), designed to align national climate objectives with fiscal policy and planning, exchange expertise and work towards common climate goals.
- Minister of Environment/Climate Change: ensure the NDB is aligned with and part of the country's Nationally Determined Contributions (NDCs) under the Paris Accord.
- Minister of Infrastructure: ensure that NDB financing is part of the national vision for infrastructure development.
- Minister of Urban Development: ensure that NDB financing is part of the vision for urban development.

Barriers and Opportunities for NDBs to Provide Financing to Cities for Green Urban Infrastructure

In most countries, NDBs have a responsibility to finance the transition towards a low-carbon, climate-resilient economy to improve the health and well-being of their citizens, and enhance their ability to achieve their development mandate. NDBs are a critical development financing arm of the national government and can be leveraged to advance the national and international climate goals and commitments as well as contribute to the achievement of the Sustainable Development Goals (SDGs).

The research and interviews with NDBs and municipalities identified a number of barriers to NDBs providing climate-smart urban infrastructure financing to cities, but also identified opportunities. These barriers were identified at the policy, legal and regulatory frameworks level, institutional level and financial level.

Table 1: Barriers for NDBs Financing Climate-Smart Urban Infrastructure

Policy, Legal and Regulatory Barriers	Institutional Barriers	Financial Barriers
<ul style="list-style-type: none"> Legal structure can limit the flexibility and ability of the NDB to take higher risks Unspecific / broad mandate can hinder the NDB's focus and prioritization of climate-smart infrastructure projects Fragmented policies and lack of coordination at the national and sub-national level can interrupt project design and implementation 	<ul style="list-style-type: none"> Lack of resources and sectoral expertise in climate infrastructure financing to identify and structure projects Lack of bankable projects pipeline or capacity to support municipalities with designing, developing and implementing climate-smart infrastructure projects Weak internal capacity to support municipalities through TA or PPF 	<ul style="list-style-type: none"> Insufficient capitalization can impede on ability to finance green infrastructure projects with upfront capital requirements Lack of access to international funds and dedicated resource mobilization to match needs of green infrastructure projects with financing Weak fiscal capacity Limited access innovative capital or de-risk instruments to finance climate-smart urban infrastructure projects.

While there are many potential barriers, there are also opportunities for NDBs to provide climate-smart urban infrastructure financing to cities.

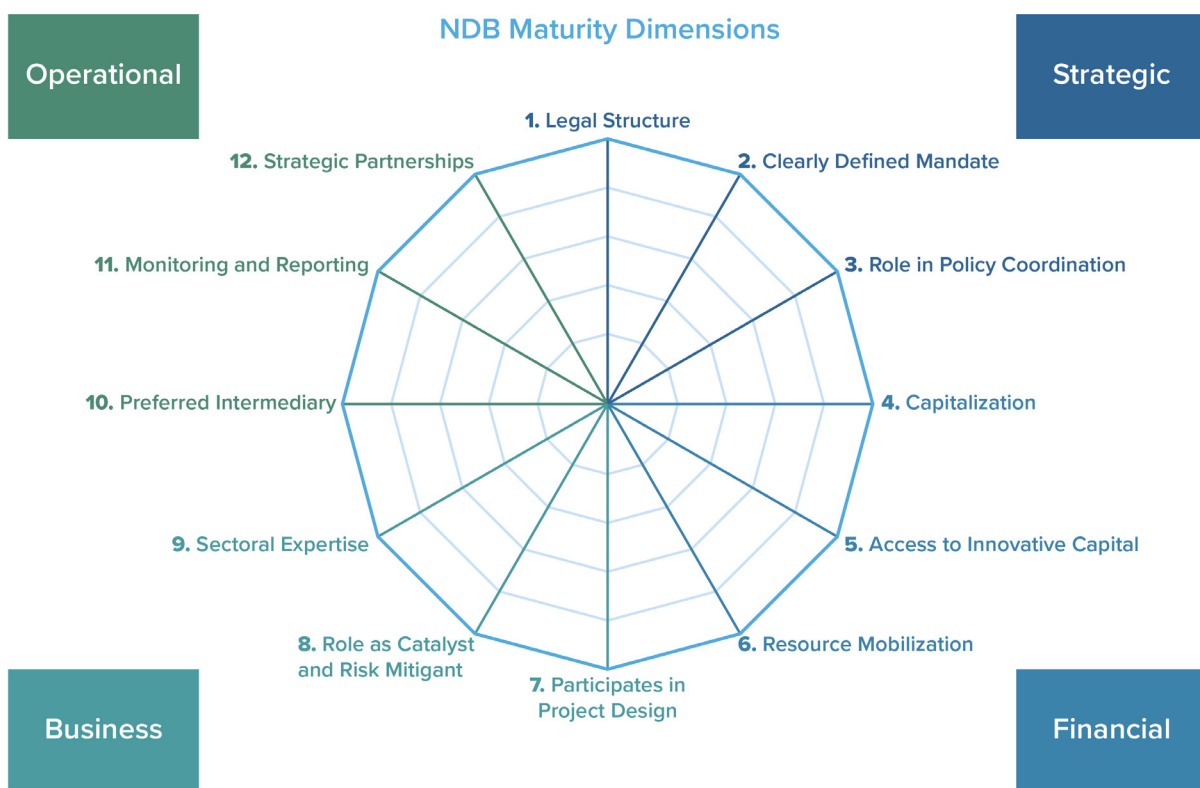
Figure 1: Enablers for NDBs Financing Climate-Smart Urban Infrastructure

Enablers	Bankable Infrastructure Projects Pipeline Platforms	NDBs are creating platforms to pool bankable infrastructure projects to attract private sector investments.
	Capacity Building	NDBs are helping local governments in capacity building to enhance their access to diverse sources of finance.
	Dedicated Fund	NDBs have funds dedicated to sustainable infrastructure projects which helps NDBs prioritize the resources for this sector.
	Resource Mobilization	NDBs have a dedicated unit or staff that mobilize resources from donors to the specific needs of local governments and infrastructure projects (PPF & TA).
	International Climate Funds' Accreditation	Climate fund accreditation enhances the capacity of NDBs to support green infrastructure projects.
	Green / Sustainable Bonds	NDBs that issue green bonds can support green urban infrastructure projects.

The NDB Maturity Model for Financing Climate-Smart Urban Infrastructure

NDBs that finance infrastructure have different capacities and may face different constraints based on their size, structure and local financing needs. Nevertheless, common themes have emerged in the challenges and opportunities NDBs globally face at the strategic, financial, business and operational level. Twelve dimensions have been identified and developed to define – in normative terms – what constitutes a mature NDB’s ability to finance climate-smart urban infrastructure.

Figure 2: The NDB Maturity Model



About the NDB Maturity Model Dimensions and Parameters:

Based on the 12 main dimensions explored, each of these dimensions is presented in a positive value statement intended to define what “mature” means for each area. Each dimension is scored out of 5, based on our assessment, with 5 being a fully fledged NDB capable of optimizing climate-smart urban infrastructure financing.

It is not enough to be very strong in one area or parameter. One stronger area does not necessarily offset a weaker area. The most mature NDBs are those that find a balance between all four parameters. For a strong and mature NDB, the harmony or balance among the four common parameters, and the four key dimensions within each parameter, is as important (if not more important) than the absolute “scores” of individual dimensions or parameters.

The NDB maturity scale is intended to create a standard and consistent measure of comparison for NDBs financing green urban infrastructure.

The below table summarizes the twelve dimensions of the NDB Maturity Model, which evolved from the barriers and enablers NDBs face in financing climate-smart urban infrastructure. These dimensions provide evidence-based analysis to develop the recommendations for several key stakeholder groups.

Table 2: Summary of the NDB Maturity Model Dimensions

Parameters	Dimensions
Strategic	<ol style="list-style-type: none"> 1. The Bank’s legal structure is established in an Act or specific legislation 2. The Bank has a clearly defined mandate to support green infrastructure as well as local governments. 3. The Bank has a strategic policy role with a seat at the policy table, plays a convening role in developing a green urban infrastructure strategy, coordinates among ministries, provides policy recommendations and supports in the operationalization of the project.
Financial	<ol style="list-style-type: none"> 4. The Bank’s size of equity is sufficient to support climate smart urban infrastructure deals. 5. The Bank has access to innovative capital sources to fund a range of green infrastructure projects. 6. The Bank has a devoted resource mobilization unit to access blended finance or grant funds from international DFIs.
Business	<ol style="list-style-type: none"> 7. The Bank participates in project design for green urban infrastructure at the national level or at the origination phase. 8. The Bank acts as a catalyst and de-risking instrument to facilitate bankable infrastructure projects using various forms of guarantees, project preparation facilities and technical assistance to support municipalities. 9. The Bank has the sectoral expertise of climate smart urban infrastructure financing.
Operational	<ol style="list-style-type: none"> 10. The Bank is the preferred intermediary for international climate funds. 11. The Bank sets indicators to monitor and report on green urban infrastructure transactions. 12. The Bank has strategic partnerships with diverse sources of finance to channel funds to green infrastructure projects.

Recommendations

It is recommended that Ministers:

1. **Reassess the legal structure** of NDBs with an infrastructure mandate to allow for the flexibility to take higher risks and provide longer tenors which are necessary for financing climate-smart urban infrastructure.
2. **Assign NDBs and cities a clear role in national climate goals**, including Nationally Determined Contributions, and in the national infrastructure strategy.

Case Study: PT Sarana Multi Infrastruktur (Persero) is Leveraged by the Indonesian Government to Help Achieve SDGs and Climate Goals

Municipal capacity limitations, low-risk appetite of investors, high transactional costs, and financing gaps for urban infrastructure projects act as major barriers to the implementation of climate-smart infrastructure projects. To address these barriers, Indonesia's PT SMI and the Indonesian Ministry of Finance created SDG Indonesia One.

SDG Indonesia One is an integrated project funding platform which combines public and private funds through a blended financing scheme to develop, finance, and implement SDG oriented Indonesian infrastructure projects.

The platform promotes four primary services to attain these goals: Development Facilities, De-Risking Facilities, Financing Facilities, and an Equity Fund. These services consolidate and standardize technical assistance and risk mitigation, improves the consistency of Indonesia's climate-smart infrastructure project pipeline, ensures steady and varied funding, and ultimately increases the implementation of bankable SDG compliant projects.

SDG Indonesia One reduces transactional costs between DFIs, commercial entities, municipalities, and higher levels of government by merging stakeholder interests into a singular forum, enabling a multitude of project and financing opportunities for stakeholders. SDG Indonesia One is an important step by Indonesia to address its climate-smart infrastructure needs.

3. **Review and update the mandate** of NDBs that finance infrastructure and urban development, to include a climate focus.
4. **Review the legal and regulatory frameworks** to overcome barriers for municipalities in executing climate-smart urban infrastructure projects. This may include revisions to laws on financial responsibility that may limit a municipality's budget debt limit which hinders its ability to finance large infrastructure projects. Consider fiscal decentralization on the authority to collect taxes, to empower municipal revenue stream to finance projects. Also review enabling frameworks for implementing agencies that can undertake sustainable climate investment at scale such as development corporations.
5. **Ensure the NDBs are well capitalized**, have the political support and sufficient resources to leverage their role to finance and operationalize climate-smart urban infrastructure that are aligned with national goals.
6. **Recognize the importance of National Development Banks as critical public policy instruments** by inviting them to the **policy table** to contribute to policy recommendations, participate in project design and support in financing, implementing and monitoring climate-smart urban infrastructure. **Encourage dialogue** with NDBs among different ministries. The Ministerial responsibility:
 - **Finance:** NDB mandate and financial base.
 - **Environment/Energy:** NDB alignment with NDCs and encourage the formulation and implementation of NDCs at the local government level through City Climate Action Plans.

- **Infrastructure/Transport:** NDB's part of the national vision for infrastructure.
- **Urban development:** NDB's part of the vision for urban development.

The full knowledge product 'Leveraging National Development Banks To Enhance Financing for Climate-Smart Urban Infrastructure' includes further case studies and examples of how NDBs are implementing the recommendations listed above.

Access the knowledge product on the [Alliance website](#).

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ABOUT THE CITIES CLIMATE FINANCE LEADERSHIP ALLIANCE

The Cities Climate Finance Leadership Alliance (the Alliance) is a coalition of leaders committed to deploying finance for city level climate action at scale by 2030. It is the multi-level and multi-stakeholder coalition aimed at closing the investment gap for urban subnational climate projects and infrastructure worldwide. Climate Policy Initiative (CPI) serves as Secretariat for the Alliance. Funding for the Alliance's activities is jointly made available through two German government ministries: The Federal Ministry for Economic Cooperation and Development (BMZ) and the Federal Ministry for the Environment, Nature Conservation, and Nuclear Safety (BMU).

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