Key Messages

EMnet Working Group on
Business and Sustainability in Emerging Markets
2021

From promise to practice: mobilising private sector investment for an inclusive recovery

The Working Group on Business and Sustainability of the OECD Emerging Markets Network (EMnet) held a virtual meeting on 14 April 2021, to discuss private sector investment in sustainability across emerging markets. As fiscal space narrows due to the COVID-19 crisis, EMnet’s Policy Note on Sustainability identified the untapped potential of sustainable business to accelerate an inclusive recovery in emerging markets. Yet the crisis is likely to reduce appetite for sustainable investment with uncertain returns. With inequalities widening, there is an urgent need for co-ordination across stakeholders, to mobilise investment and support an inclusive recovery to ‘build back better’.

The Working Group featured OECD work on blended finance and impact investing and held focused regional discussions on investing in the social contract in Latin America; unlocking investment in Africa’s sustainable recovery; and inclusion to bridge the digital divide in Asia.

A sustainable and inclusive economic recovery will require significant investment from both the public and private sector across emerging markets, to ‘build back better’. When it comes to amounts mobilised from the private sector by official development finance interventions, over 2017-18, Latin America was the region benefiting the most (USD 9.5 bn), closely followed by Africa (USD 8.9 bn), Asia (USD 8.6 bn) and developing countries in Europe (USD 7.2 bn, of which Turkey accounted for 56%). Most private finance mobilised targeted middle-income countries, with Argentina, Turkey and Ukraine as the top three. Funding is also highly concentrated in specific sectors. In 2017-18, official development finance mobilised USD 12.1 billion of private resources towards the energy sector per year on average, followed by banking and financial services. Mobilisation in these sectors accounted for 55.5% of total mobilisation in 2017.

OECD initiatives on blended finance including the Blended Finance Principles seek to promote a Blended Finance 2.0 that can attract commercial investment, use a common framework and understanding of blending supporting cohesive action, and create consistent estimates of the market for blended finance as well as its effectiveness. Likewise the OECD UNDP Impact Standards for Financing Sustainable Development are designed to support donors in the deployment of resources through Development Finance Institutions and private asset managers, to maximise their positive contribution towards the Sustainable Development Goals (SDGs).

Across emerging markets, investment in the economic recovery can also promote the SDGs. For example, companies operating in emerging markets can implement inclusive practices throughout their own business and support greater inclusion through their business model, applying a ‘gender lens’ to these practices to ensure recovery efforts reach those sectors of society most affected by the crisis. EMnet aims to support through its proposed Handbook on Sustainability – see Next Steps below. In addition, building on the Impact Standards, the OECD will develop further guidance on (i) how to embed the Standards in development actors’ practice and (ii) what “compliance” to the Standards would mean through (iii) best practice examples. The guidance will build on pilots studies that show how the standards work in different contexts, including in different geographies (i.e. LDCs vs. middle-income countries), in different sectors (i.e. energy vs. healthcare) and for different investment types and sizes (i.e. SME investing vs. large infrastructure project). Organisations that are interested in taking part can contact the organising team.
In Latin America, while the region has seen GDP growth in 2021 (circa 4%), it will not be enough to recover pre-pandemic GDP levels. The pending long-term challenge is boosting productivity, which has been reducing year on year compared to the rest of the world. Up to 40% of the workforce, working informal jobs, had no safety net in the crisis and governments moved quickly to ensure that needs were covered. Yet social discontent is high and growing, in a context of increased public debt and reduced fiscal space. There is an urgent need to embrace megatrends such as digital transformation and green economy both as tools for recovery and to mitigate the impact and create resilience in the face of future crises.

In Asia a significant downturn in 2020 of -3.4% in ASEAN and -1.7% for emerging Asia has been followed by growth, though it has diverged greatly between countries in the region. The COVID-19 crisis has had a significant impact on employment in the region especially Philippines, Thailand and Malaysia. A move to reallocate resources towards digitally enabled initiatives across health, education and Industry 4.0 can help to support growth and resilience. However, digital access varies greatly across the region with strong variation in the level of internet usage depending on the level of education and income. It is critical to the inclusive impact of the digital transition for investments and policies to take account of this digital divide.

In Africa the GDP growth is expected to be around 4% over the next 5 years, but challenges remain as growth is uneven across countries and up to 40 million people could fall back into extreme poverty by 2021 in sub-Saharan Africa. The region has lower financial resources per capita than during the 2008 Global Financial Crisis and whereas average tax-to-GDP ratio increased between 2010 and 2014, it has since flatlined at around 16.5%. FDI inflows have increased fourfold but remain lower than other regions, and have seen a shift from extractives to services. Attracting private sector participation is critical to boost infrastructure investment financing. Currently the majority of Africa’s intermediary cities are located far from a high-speed terrestrial fibre-optic network. Closing the spatial gap in digital infrastructure will require private sector participation, as will investment in the region’s value chains and closing the skills gap.

**Private Sector Insights**

Across emerging markets the green transition and digital transformation present significant opportunities for private sector investment. Investment in these areas has the potential to contribute to the economic recovery whilst advancing the SDGs. In order for the private sector to seize this opportunity it is critical that companies engage with wider trends – from decarbonisation to digitalisation – and that governments use available policy levers to encourage this shift.

Companies can encourage an all of industry approach by integrating technology, green and inclusive practices across their value chain to multiply their impact. Progress on sustainable financing can also have a systemic impact, and sustainability is increasingly integrated in financing decisions.

Favourable policies will be key to overcoming challenges and determining the pace of change. Sustainable financing is encouraged by regulatory frameworks that provide a degree of security for investments while allowing for competition. Progress on taxonomies – particularly for social investment – can create a favourable enabling environment. A just green transition can be encouraged through support for job transition, and regulatory frameworks that ensure a level playing field and encourage an all of industry approach to responsible business conduct. Independent and adequately resourced regulatory agencies can raise standards, and speed up procedures. Investment in digital can be encouraged through ease of permitting, assessing the impact of fiscal policies on investment, and the potential of subsidies to encourage demand.

Legal certainty, rule of law and transparency will remain key to attracting responsible and sustainable investment. ESG criteria can reduce the risk perception of investments. Efforts to align ESG criteria across the public and private sector can promote collaboration and public-private investment, and incentivise progress where ESG criteria are promoted through public policies.
In Latin America participants noted the need to use available levers to urgently accelerate the green transition to face the climate crisis, such as decarbonisation and decentralisation. Likewise, digital transformation is a critical enabler that needs to be integrated across the energy sector. A number of countries in the region have embraced renewables (such as hydropower) but this should be accelerated – supporting job transition to growth sectors. A key challenge for the region is energy and digital inclusion. Vulnerable sectors of the population including women and youth, which were hardest hit by the crisis, stand to benefit from these efforts, such as through the integration of digital technologies in education. Participants see scope for public-private collaboration on a just transition that leaves no one behind.

Companies can lead from the front – integrating technologies, green, and inclusion in their business model – but it will require an all of industry approach and support from the public sector. A whole of value chain approach and multi-stakeholder efforts can help multiply this impact. For example, Tetra Pak’s partnership with suppliers in the region has allowed it to transition towards greater sustainability in its sourcing; while downstream partnerships with industry players and governments support waste recovery efforts.\(^1\)

Overall companies emphasised that legal certainty, rule of law and transparency will be key to attracting responsible and sustainable investment. Participants noted the potential of formalisation efforts across informal sectors. Regulatory frameworks that ensure a level playing field and encourage an all of industry approach to responsible business conduct are also necessary. Independent and adequately resourced regulatory agencies can raise standards, and speed up procedures (e.g. permits). Further, ESG criteria can reduce the risk perception of investments. Efforts to align these criteria across the public and private sector can promote collaboration and public-private investment, and incentivise progress where ESG criteria are promoted through public policies.

In Africa sustainable financing presents significant opportunities – the region is well-placed to benefit from investment in renewables and is resource-rich in key minerals – but also faces challenges. Local capital markets are currently underdeveloped and require FDI. This can create currency risk and increase financing costs to companies and projects. The large deal size needed to attract investment often disincentives countries form raising sustainable investment offshore. Local currency financing that strengthens local capital markets, and incentives for financing could help mitigate this. Progress on taxonomies – particularly for social investment – can support efforts by creating an enabling environment. Investment in a just transition that supports fossil-fuel dependent countries can be encouraged through transition financing.

Investment in digital, which has benefited from investment by international donors, can have a transformative effect, particularly when accompanied by an appropriate regulatory environment. Digital transformation can benefit a range of sectors across the continent from agriculture to construction, logistics and support productive transformation, in addition to services including e-government services. It can also have an outsize impact on jobs and contribute to greater stability in the region. Companies active in the digital space have invested in skills for their employees, supply chain and even customers, and there is an opportunity to expand the reach of digital to SMEs. Governments can encourage this through supportive policies, ease of permitting, by assessing the impact of fiscal policies on investment as well as the potential of subsidies to encourage demand. Governments can also invest in infrastructure assets, such as base stations, which could create future revenues through ownership, and create synergies between investment in other physical infrastructure (e.g. electricity and road) and the expansion of digital networks. Infrastructure providers currently offer this on an ad-hoc basis or as a service, but could be mandatory.

In Asia investment in digital, and in particular the financing of digital assets, remains specialised and it will take time for large financial institutions to adapt. In the interim, investment is driven by private equity and corporates. While the direction of travel towards digital transformation is clear, the fast pace of technology and risk of obsolescence means that financing is encouraged by regulatory frameworks that provide a degree of security for investments while allowing for competition. Multilaterals such as World Bank and ADB are supporting investment in digital across emerging Asia. There is scope for partnerships

\(^1\) https://www.3rinitiative.org/about
with the private sector, such as MUFG’s collaboration with the ADB to expand mobile coverage in rural Bangladesh.

Digitalisation across Asia (reflected in Euler Hermes research) has contributed to the region’s resilience to the COVID-19 crisis and can continue to enable resilience, for example through greater coordination of vaccination campaigns. This is a case where investing in digital inclusion is also an investment in economic resilience. Nonetheless, there are instances where investments in digital and sustainability are less aligned. For example, as investment in data centres is set to increase there is a need to account for their sustainability impact. There is progress in this area, as financial institutions increasingly take ESG criteria into consideration when financing. Governments can also provide incentives for companies to transition towards use of more sustainable components and sustainable infrastructure investments. However, the size of the infrastructure gap in Asia means there has to be a balance between these considerations and reliance on existing infrastructure as governments focus on closing the digital gap.

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