“Sustainable finance: An imperative for the new normal”

Statement by
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On behalf of the Arab Monetary Fund (AMF), I would like to commend the Group of 24 (G-24) for convening this important meeting being an essential platform for developing countries to discuss ways and means to respond to and manage the evolving challenges we face. The G-24 has always championed multilateralism, and global governance which appears today more significant than ever. In the wake of the multidimensional and unprecedented crisis, we strongly believe in the merit of adopting coordinated and mutually agreed actions.

Sustainable development is profoundly multidimensional

Even before the outbreak of the COVID-19 pandemic, the global community was off-track to meet the Sustainable Development Goals (SDGs), as highlighted in the 2020 Financing for Sustainable Development Report. The pandemic we are facing today has much to teach us about an even more existential threat and has amplified the challenges of reaching the SDGs, while exposing the long-standing gaps and deficiencies in the international financial system, such as debt, global liquidity, and financial flows. These pressing challenges are being discussed in multiple fora, such as the G20, where Italy, currently holds the G20 Presidency, has organized the efforts under the theme of *People, Planet and Prosperity*. It has had a very specific focus on the role of all types of investors, including for instance institutional investors as part of the Sustainable Finance Working Group. These international commitments agreed by governments around the world, require nothing less than a paradigm shift in how economies and financial systems operate, and how they could create value for societies.

In fact, the 17 SDGs are interconnected and integrated, and have a long-term focus, aiming to ensure that any developments are sustainable for current and future generations. This makes the focus on Environmental Social and Governance (ESG) issues particularly important since reductions in poverty, for example, cannot be sustainably maintained if they come at the expense of environmentally destroying local areas or damaging the global climate. Addressing these pressing ESG challenges involves nothing less than a structural transformation that will put economies on a sustainable and inclusive path to meet the global ambition of achieving carbon neutrality by 2050 (Paris Agreement) and realizing 2030 Sustainable Development Goals (United nation). The financial sector is a pivotal component of this transition and has a profoundly important role to play in helping to achieve prosperity by mitigating sustainability-related risks, building resilience, and channeling the capital to sustainable uses that builds more resilient and inclusive societies and economies. *Sustainable finance shall be the standard, the new financial normal*.

Sustainable finance requires an integrated approach and effective coordination mechanism

The financial sector is exposed to a set of risks, from environmental and climate risks to those posed by social pressures, including contagious diseases and their socio-economic consequences such as the COVID-19 pandemic-related global crisis. In the 2020 World Economic Forum Global Risks Report, identified the top five risks in terms of likelihood were all environmental risks. In addition, the Bank for International Settlements (BIS) warns that, if not managed properly, climate-related risks could not only threaten the stability of financial institutions, but also lead to a systemic financial crisis.

Likewise, sustainable financial systems can contribute to achieving the goal of sustainable and inclusive economic development through promoting business innovation and strengthening economic, environmental, and socially responsible behavior of businesses. Businesses need access to capital in term of credit or equity to expand and grow. By setting the right incentives, the financial sector acts as a 'multiplier' of responsible business practices and sustainable economic development. Consequently, Sustainable Finance cannot be decoupled from the responsible business agenda as ultimately Sustainable Finance is a mean to responsible business.

In this regard and while the public sector's responsibilities include creating a regulatory and policy framework with clear rules and incentives for a successful transition of the economy and financial sector, the private sector also has a critical role to play in aligning capital flows with global targets and agendas in term of financing the transition to a sustainable economy and being resilient to the risks.

Building a sustainable financial system requires a comprehensive, systematic, and coordinated approach that governments, financial regulators, supervisors, and market players around the world are finding it challenging to adopt and implement. In this spirit, policymakers, development organizations and sector-specific experts, at both regional and global level, are currently discussing and assessing how sustainable finance providers are driving sustainable development, how they are aligned with the UN Sustainable Development Goals and the increasing interest in impact investing, and their future role in a world where inclusive and green growth will be paramount.

Key drivers for financial sector to support sustainability in the Arab region

The Arab region, as it is the case for the rest of the world, is vulnerable to climate change and there are pressing mitigation and adaptation needs related to issues such as water scarcity, rising sea levels, drought, and land desertification. Climate change is expected to have negative impact on the region's food, energy, and water security through its effect on vital sectors including, but not limited to, water, health, coastlines, tourism, and agriculture in a region where more than 50% of food is imported and most of its population is still rural and dependent on agriculture for its livelihood.

Translating the broad global and regional discussions into assets where financial sector can invest will come through change in supply and demand sides as well as in the maturity of market infrastructure. In fact, demand from investors can be expressed in changes in their long-term investment strategies through their own commitments to investing in companies with social impact and transparent governance. The expected changes either in the Arab region or globally need to be seen in this context, since if current local recipients of external investment do not adapt their strategies to ensure that they keep up with the requirements of external investors that may reduce demand for financing their assets by external investors.

One more driver of increased demand for long-term investment projects in the Arab region is created by government commitments for renewable energy, as well as broader SDG adaption plans. Another source of demand that is potentially important among Arab countries is the link between Shariah compliant investment and ESG factors. This is perhaps an underexplored field and one of the areas that requires intensifying the efforts on relevant products development and investment approaches that can achieve both goals at once.

On another hand, the supply of investable projects is enhanced where companies and governments develop projects or refocus their activities in ways that are attractive to investors seeking ESG friendly investments. There is clearly a strong feedback loop between demand and supply of ESG related projects, but globally each side is experiencing an important rate of growth. The demand for investable projects includes many examples, such as solar power as well as projects from governments who are developing green sovereign bonds. The supply of ESG related investments is already in progress for Arab institutional investors who can invest outside of the region given the size of global capital markets.

From required industry infrastructure standpoint, supporting market infrastructure, data and skills are needed to ensure that there is sufficient, clear, and transparent data to evaluate companies and skilled staff to both implement ESG issues in headline investment strategies and to evaluate specific investment opportunities.

To this end, substantial progress has been made in the last two decades towards implementing sustainable financial sector reforms across the Arab region, focusing on financial stability, inclusion, and digital transformation. This progress presents a potential vehicle for promoting sustainable finance in the region and can propel the region towards achieving the Sustainable Development Goals (SDGs) and mitigate climate change risks, particularly for unserved and / or underserved population. It presents a unique opportunity for the region to fully integrate environmental and social factors into their financial institutions' business models and core strategies.

Opportunities ahead and conclusion

While the financial sector faces many risks related to sustainability challenges, the transition to sustainable financial services also creates many opportunities for business and finance. For instance, in emerging markets alone, national commitments under the Paris Agreement would require more than USD 20 trillion between 2016–2030, in developing countries that represent almost 50% of global greenhouse gas (GHG) emissions[1], which includes investments in renewable energy, low-carbon cities, energy efficiency, and climate-smart agriculture (International Finance Corporation). As estimated by the Climate Policy Initiative, climate-related financial flows have increased in recent years, exceeding half a trillion US dollars in 2018, but still fall far short of global investment needs (Climate Policy Initiative).

Furthermore, given that large scale capital is needed to mitigate the effects of climate change and support solutions for climate adaptation, it is anticipated that public spending will not suffice to finance the climate friendly transformation. The financial industry is expected to play an instrumental role and the need for climate finance is more urgent now than ever before. It is therefore important to align the financial institutions, both banking, non-bank financial institutions and capital markets, with sustainable development, which will create new type of

[1] UNEP 2017a

challenges to central banks, and regulatory authorities that require actions by financial system actors at all levels.

In conclusion, there is a window of opportunity for every country to design regulatory framework and policies that promote sustainable financial services and build sustainable and inclusive economies that are resilient to environmental degradation, climate change, and social pressures. Today, many central banks worldwide, including in the Arab region recognize the importance of social and environmental related financial risks and consider them as part of their mandate. In fact, there are increasing efforts to incorporate environmental and social sustainability in financial sector policies, procedures, and practices, from green bonds to national sustainable finance plans and strategies.

Thank you!

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