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Decarbonization and Growth: Economic and Sustainability Perspectives in the Western Balkans

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In this edition, we delved into the economic implications of decarbonization strategies, emphasizing their impact on Serbia and the Western Balkans. We explored the challenges of reducing greenhouse gas emissions but also the potential economic benefits.

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In your view, how might a science-based decarbonization approach enhance the economic growth and sustainability of the Western Balkans? Are there any exemplary case studies or best practices from other regions that might be effectively applied here?

Science-based decarbonization by nature does not aim to promote economic development, its task is to reduce greenhouse gas emissions into the atmosphere in accordance with the country's international and national obligations. Nevertheless, the introduction of such technologies, in many cases, has a positive economic effect.

To begin with, according to the majority of studies in recent years, the cost of renewable electricity is significantly lower than the cost of electricity from hydrocarbons. This becomes especially obvious considering the periodic spikes in oil and gas prices associated with political crises. IEA estimates that the EU would have spent 100 billion euros more on electricity without renewables in 2022. The outdated energy system of the Western Balkans requires modernization, and the most effective way, both from the point of view of economics and from the point of view of national security, is the introduction of solar, wind, and hydropower, coupled with increased market transparency and simplification of legislation. At the country's first stage of renewable energy development, the best effect in terms of ensuring a stable energy supply is given by pairing renewable sources with hydrocarbon capacities, which are gradually being replaced by energy storage capacities capable of supporting the uninterrupted operation of the grid. This is how, for example, the PRC's energy strategy is structured.

Secondly, many international funds and major investment companies have explicitly stated that they plan to prioritize financing low-carbon projects, and some have explicitly announced that they will divest from hydrocarbons and other projects harmful to the climate. This has led to a gradual increase in the so-called "greenium", i.e. the bond greenness premium, which has reached 7.2 bps on average across emerging markets at the end of 2022. The trend indicates that this indicator will increase, and borrowers can raise funds for green projects cheaper than non-green projects. By ignoring opportunities given by engaging in projects in renewable energy, electric transport, sustainable agriculture, construction, and low-carbon industry, the country loses access to a wide pool of investors who could otherwise willingly invest in it.

Thirdly, there are a huge number of technologies whose implementation is extremely cost-effective but simultaneously has unconditional positive climate effects. The so-called abatement curve, showing the cost of decarbonization - for economically viable technologies, this cost is negative - shows that almost two-thirds of technologies associated with emission reductions have a positive economic effect. These technologies include the increased use of electric transport and the construction of electrified railways, the development of public transport and micromobility, the modernisation of buildings, structures and street lighting in line with energy-saving principles, and many others.

Fourthly, by preserving outdated technologies, the country risks losing money on trade with states that introduce advanced climate legislation. In the case of the Western Balkans, the EU border carbon tax may cost them about 500 million Euros after implementation. Different regions in the world (including China) are testing emission trading systems akin to the one implemented by the EU, and we can safely assume that in 10-15 years' time, the climate footprint of the product will be one of the main characteristics influencing its competitiveness.

What potential implications do you foresee for the Western Balkans specifically based on the outcomes of COP28? Are there particular sectors or areas that might experience significant changes?

For the first time, participating countries, including oil-producing states, agreed to start "transitioning away" from hydrocarbons, which was unimaginable a few years ago. Although this statement does not mean an automatic ban on the use of fossil fuels, it clearly indicates a trend towards divestment and tougher conditions for those countries that ignore the energy transition. Much of the Western Balkan region, including Serbia, is critically dependent on coal-fired generation, which poses serious risks to the competitiveness of local products if additional restrictions are imposed in this area.

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Serbia, like other Western Balkan countries, has signed the Global Renewables and Energy Efficiency Pledge, committing to contribute to the tripling of global renewable energy production capacity by 2030, accelerate energy efficiency growth from 2% to 4% annually and make energy efficiency the number one priority in public policy development. This will require significant adjustments to the current Serbian energy policy, modernization of energy and transmission infrastructure, and significant efforts to attract foreign private capital.

The world's countries allocated another 3.5 billion dollars for the Green Climate Fund, which already has experience in projects in Serbia. The Fund can significantly help decarbonize projects in the country that require significant investments. Another opportunity of this kind is a 30 billion dollar UAE fund, Alterra, that was created at COP and is aimed at providing capital to green projects.

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Could you discuss the significance of certifications, standards, and taxonomies in advancing green practices? In what ways could these be utilised as effective tools to align the Western Balkan region's efforts with global green initiatives?

First, it is necessary to distinguish between national and international taxonomies, such as the Climate Bonds taxonomy, within which independent certification is available.

A national green taxonomy, whether developed and adopted in Serbia or the countries of the Western Balkans region, could become an essential element of climate policy and help the state and investors in many ways. The taxonomy itself is just a list of definitions to help determine which activities are compatible with the climate agenda and which are not.

IIt is created at the junction of climate science and national priorities and gives the state and market participants transparency about which activities the state considers a priority. In fact, the national taxonomy clearly defines which practices and activities are green and which only pretend to be so.

Based on the taxonomy, green bonds and green loans can be issued; it helps structure relatively new products such as green insurance and mortgages. The state can link certain support measures to activities corresponding to the taxonomy and encourage investment in them. The taxonomy also facilitates the collection of information about the real processes of green transformation taking place in the country and facilitates decision-making in this area.

An international taxonomy, for example, the Climate Bonds taxonomy, generally performs the same functions but imposes higher activity requirements. National taxonomy always combines climate science and national priorities, whereas international taxonomy is limited to science and does not consider the economic component of activity.

That is why only about 13% of green bonds in the world are certified according to Climate Bonds standards, but investors can be sure that these are the most high-quality projects presented on the market. They attract the widest pool of climate investors, which makes it possible to raise money in the market more cheaply.

From your perspective, what are the essential steps Western Balkans governments should undertake to seamlessly integrate green taxonomies and policies into their national strategies? What potential challenges might they need to navigate?

Developing local taxonomies could help decarbonize and build a green economy in the Western Balkans region. This can be done both at the level of individual countries and at the level of the entire region as a whole. We know that the region's countries intend to join the European Union in the coming decades and plan to use a similar document developed by the European Union (the EU Taxonomy) as a taxonomy. But I still think that developing a Balkan taxonomy could be useful for the period until the region's countries are admitted to the EU.

Firstly, it is unlikely that the region's countries will be admitted to the EU before the carbon border tax comes into full force, but it is necessary to adapt to it now.

A Balkans taxonomy, which is compatible with the EU taxonomy in the main criteria for emission intensity, could indicate the path that must be followed in order not to lose money under European restrictions. Subsequently, the existence of such a document would also ensure a smooth transition to the European taxonomy.

Secondly, the European taxonomy is based on European legislation: in order to comply with the taxonomy, it is necessary not only to meet the basic conditions for the intensity of emissions per unit of production but also to comply with the provisions of certain EU directives that are not yet in force in the Western Balkans. The creation of a European-compatible taxonomy of the Balkans could combine climate science with national priorities and legislation.

Finally, the creation of its own taxonomy would help improve the image of the countries of the region in the eyes of international investors and donors interested in developing a green economy around the world. Today, more than 40 countries have either already developed or are developing their own national taxonomies to attract the attention of the international community of climate investors and attract capital.

The regional taxonomy could be integrated into all documents related to the definition of the country's climate course and specify its goals. It is important to note that the taxonomy itself does not "punish" any kind of production. Unless the government specifically enacts any laws restricting investment in carbon-intensive sectors, taxonomy will not be an obstacle to continued investment even in coal-fired power plants. It will make it transparent to all market participants and residents of the country as a whole which types of activities harm the climate and the environment and are aimed at its preservation.

The only challenge that may arise when developing a taxonomy is the cost of developing it with the involvement of international consultants. This problem is being solved by attracting international donors willing to participate in such initiatives. For example, the taxonomies of Rwanda and Thailand published this year were developed with financial support from GIZ and IFC, respectively.

About our guest

Mikhail is an experienced specialist in green economics, international relations and project management. He has over ten years of experience in analyzing international political and economic processes, consulting, and project management in the field of green economy and finance. He participated in the development of green taxonomies for Russia, Singapore, Hong Kong and Rwanda. He led the development of Thailand's green taxonomy. Mikhail has authored more than one thousand materials and multimedia projects on international relations and green economy. He is a member of the Asian Forum on Global Governance. He speaks Russian, English, Chinese and Serbian. He is based in Serbia.

Climate Bonds Initiative is an international not-for-profit organisation working to mobilise global capital for climate action.