

**Economic and Social Commission for Western Asia (ESCWA)**

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Water sector finance**Summary**

Confronted by severe water scarcity and climate change impacts, the Arab region faces significant challenges in fulfilling the water-related Sustainable Development Goals. Procuring sufficient financing for the water sector will be key to progress on this front. The Economic and Social Commission for Western Asia (ESCWA) is working towards enabling access to innovative finance tools. The main sources of finance for the water sector to date include national budgets, regional and international funds (including climate funds), and private sector investment. Data on national expenditures on water and sanitation are limited, but it is well known that the sector is heavily subsidized. There are several active regional funds and a desire for increased involvement by international climate funds and private investment. The recently launched Arab Initiative for Mobilizing Climate Finance for Water, led by a partnership between ESCWA, the Islamic Development Bank and the Green Climate Fund, is one example of the opportunities that exist to collaborate across the public and private sectors to facilitate access to finance in the water sector. Arab least developed countries and those in conflict and crisis are particularly disadvantaged with respect to accessing water finance. A lack of relevant data pertaining to water valuations and usage also impairs access to finance.

The present document provides an overview of ESCWA work on water finance. The Committee on Water Resources is invited to provide recommendations on areas of work that it would like to advance.

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Introduction

1. Water is critical for human and environmental health and, as such, the water sector requires significant investment to meet increasing demand and ensure the availability and sustainable management of water and sanitation for all, as called for by Sustainable Development Goal (SDG) 6. However, water investments can be costly. The Arab region is one of the most water-scarce regions worldwide, which increases the need for investments in water to meet growing demand. Water finance has been identified as one of four key accelerators to achieve SDG 6. The Arab region identified increasing finance for water as one of the key regional priorities resulting from the [Arab Regional Preparatory Meeting for the Midterm Comprehensive Review of the Water Action Decade](#) (Beirut, 18–19 May 2022).

2. To support member States in realizing SDG 6, the Economic and Social Commission for Western Asia (ESCWA) is working towards enabling access to innovative finance tools. The present document provides an overview of that work and recommendations on the way forward. The Committee on Water Resources is invited to make comments on its content and recommendations.

I. National water finance

3. The main sources of finance for the water sector in the Arab region include national budgets; Arab, regional and international funds; and private sector investment that is sometimes complemented by bilateral assistance packages. Data on national expenditures on water, sanitation and wastewater treatment is limited, but it is well known that the sector is heavily subsidized in many parts of the region.

4. Based on the [UN-Water Global Analysis and Assessment of Sanitation and Drinking-Water \(GLAAS\) 2022 Report](#), 61 per cent of water, sanitation and hygiene (WASH) funding globally comes from households, 29 per cent from Government, 7 per cent from repayable finance, and 3 per cent from external sources. The majority of Arab countries do not disclose disaggregated WASH expenditures. However, from a sample of nine Arab countries,¹ the composition of WASH funding in the region appears to differ from the rest of the world. Based on the 2021 GLAAS surveys of those nine Arab countries, 20 per cent of WASH funding comes from households, 69 per cent from Government, 5 per cent from repayable finance, and 6 per cent from external sources. Based on this data, the Arab region is twice as dependent on government funding for WASH than the rest of the world. The 2022 GLAAS report found that 76 per cent of WASH expenditures globally were for drinking water, 22 per cent for sanitation, and 2 per cent for hygiene. This is in line with the 2021 GLAAS survey results for six Arab countries,² where 71 per cent of WASH expenditures were for drinking water, 25 per cent for sanitation, and 3 per cent for hygiene.

5. A better understanding of expenditures in the sector can improve planning and budgeting at the sector and national levels. Some countries have already made such efforts and have been supported by the [social expenditure monitor](#) (SEM) tool developed by ESCWA to strengthen budgeting and fiscal policy reform in Arab States and improve the allocative efficiency of public expenditures. For example, [Tunisia](#) tracks its investment in water supply networks and reservoirs, water supply quality, wastewater treatment, wastewater management and sanitation, post-secondary training for staff, and other items in its national budget. However, these items are budgeted and managed across different ministries and programmes. This complicates the ability to develop integrated investment plans and comprehensively assess water-related expenditures, which in turn impedes efforts to track returns on investment and attract external finance. This can be particularly challenging for policymakers in a region where over 80 per cent of water withdraws are for agriculture³ and water use

¹ Comoros, Iraq, Jordan, Lebanon, Mauritania, State of Palestine, Sudan, Tunisia and Yemen.

² Iraq, Kuwait, Lebanon, Mauritania, State of Palestine and Tunisia.

³ [AQUASTAT](#).

efficiency remains low, and where sustaining rural livelihoods needs to be considered alongside allocating sufficient foreign currency reserves for food imports.

II. Regional water finance

6. There are several Arab and international financial institutions active in the region that support water projects, as well as dedicated green financial instruments and climate funds that have supported water projects in selected Arab countries. More opportunities exist if bankable project pipelines are prepared based on sound information and analysis. Funding for basin-level, aquifer-level and transboundary water projects could also be an opportunity to enhance water cooperation and water security in the region.

7. As at April 2023, 18 per cent of total loans from the Kuwait Fund were allocated to water and sewage, spread across 16 Arab countries. The Abu Dhabi Fund for Development has invested \$361 million in the water sector in Bahrain, Jordan and Morocco. Since 2021, the Saudi Fund for Development has signed \$1.8 billion in loan agreements for water sector projects in the Arab region. To date, 45.6 per cent of the Islamic Development Bank's total investments in the water, sanitation and urban sectors were focused on Arab countries. Moreover, in 2019, the Bank issued a green *sukuk*, an environment-friendly and Shariah-compliant financial instrument, raising over \$1 billion, with approximately 1 per cent focused on sustainable water and wastewater management projects. However, based on 2020 reporting, none of the green *sukuk*'s sustainable water and wastewater management finance was directed towards the Arab region.

8. Increasing regional understanding and building the technical capacity needed for valuating and costing water goods, services and investments can help countries mobilize finance for the water sector. Saudi Arabia has proposed to the Arab Ministerial Water Council the establishment of an Arab water economics centre hosted by Saudi Arabia to strengthen regional knowledge in that regard. The centre is expected to examine the social and economic dimensions of water and provide technical support to Arab member States. Research conducted by the centre and associated technical assistance could support the elaboration of regional or national water initiatives and the preparation of bankable water projects.

III. International water finance

9. While the Arab region is the most water-scarce region worldwide, it received just 18.1 per cent of total official development assistance (ODA) for the water and sanitation sector in 2021, equivalent to less than 0.01 per cent of the region's GDP. Egypt, Jordan, Morocco and Tunisia were the most successful in attracting ODA,⁴ but significant financial gaps remain. Arab countries need to commit to significant investments and tap into other innovative financial instruments and finance sources to achieve the water-related SDGs by 2030.

IV. Climate finance for the water sector

10. Within the framework of its activities under the Arab Centre for Climate Change Policies, ESCWA prepared a review of [climate finance needs and flows to the Arab region](#). As at June 2022, the articulated climate finance needs of Arab countries in the water sector were \$127.46 billion for adaptation activities. A mapping of these needs showed that eight of 18 Arab countries identified financing wastewater treatment as a need; seven countries specified a need for finance for desalination activities; six countries identified financing needs for water harvesting; and five countries sought climate finance for irrigation and environmental water systems. The findings also show that from 2010 to 2020, the energy sector received the largest share of climate finance flows to the Arab region (35 per cent), while the water supply and sanitation sector received only 14 per cent, despite water being a priority investment for Arab countries. The six Arab least developed countries (LDCs) received just 6.6 per cent of total climate finance flows to the region. There are significant financing

⁴ [Creditor Reporting System](#).

shortfalls in the Arab region, particularly with respect to financing water and adaptation projects, especially in Arab LDCs.

11. Climate finance in the region is also heavily skewed towards debt and non-concessional lending rather than grants. From 2010 to 2020, the Arab region received over seven times more loans than grants, totalling \$30 billion and \$4 billion, respectively. While LDCs had greater access to grants than other countries in the region, it is important to highlight that middle-income Arab countries face significant debt burdens that crowd out investments in water and climate adaptation.⁵ This includes high-income Gulf Cooperation Council (GCC) countries, where debt as a share of GDP increased from 10 to 41 per cent between 2008 and 2020, owing more recently to social spending to counter the effects of the COVID-19 pandemic.

12. To assist countries in better accessing water financing, projects need to be prepared for investment. The World Bank published a [discussion paper](#) in 2019 on preparing bankable projects for financing climate change adaptation in transboundary basins. The paper was discussed at a meeting convened by the secretariat of the United Nations Water Convention and highlights the challenges and opportunities that countries face when preparing transboundary basin projects. The paper helps countries sharing a river basin and river basin organizations to better understand the climate financing landscape and how to prepare bankable projects.

13. In February 2023, the Green Climate Fund (GCF) released its Water Security Sectoral Guide with its [Water Project Design Guidelines](#) for designing water-climate resilient projects. Its [accompanying document](#) details the application of the guidelines when designing integrated water resources management (IWRM), WASH, drought and flood management projects. The purpose of these guidelines is to assist GCF direct access entities and accredited entities in preparing well-developed water project proposals for GCF financing.

14. Several initiatives are being implemented across the Arab region to mobilize finance for water projects. In June 2022, ESCWA and the World Bank collaborated on a [climate finance workshop](#) as part of the [Mashreq Waters Knowledge Series](#). The workshop brought together senior officials from ministries of finance, water and agriculture, and representatives of international and regional organizations, to discuss financial and economic mechanisms and instruments for funding water and climate adaptation projects in the region. This included innovative approaches to financing, such as disaster-risk financing and insurance schemes, and the launch of green and blue bonds.

15. In September 2022, ESCWA hosted the [Arab Regional Forum on Climate Finance](#), which was one of five regional forums organized in partnership with the Egyptian Presidency of the 2022 United Nations Climate Change Conference (COP27) and the United Nations Climate Change High-level Champions, in preparation for COP27. Countries were invited to present priority climate adaptation and mitigation projects on funding for regional and international financial institutions and private banks. Fact sheets were prepared and posted online for each project. Of the 30 projects presented, 22 projects sought finance for adaptation; of those adaptation projects, 83 per cent were water projects proposed by Egypt, Iraq, Jordan, Oman and Tunisia, with the remainder focused on agriculture, land degradation and forestry projects. Selected projects were featured in a joint [Compendium of Climate-related Initiatives](#).

16. ESCWA also contributed the chapter on North Africa to the [State and Trends in Adaptation 2022 Report: Africa](#) issued by the Global Center on Adaptation. The chapter examines how green bonds can raise resources to finance new climate projects or refinance existing ones, such as in Egypt. It also explains how development funds are looking for ways to evaluate and classify projects as green or climate responsive projects, and that a common taxonomy and well-defined evaluation methodology can help project proponents to satisfy certain criteria for accessing climate finance, and also assist donors and creditors to classify the projects they fund based on a common set of criteria. Moreover, the chapter explores opportunities presented by debt swaps for

⁵ ESCWA, [Liquidity shortage and debt: Obstacles to recovery in the Arab region](#), 2021.

mobilizing finance for adaptation projects, including the [ESCWA Climate/SDGs Debt Swap and Donor Nexus Initiative](#).

V. Private engagement in the water sector

17. Historically, private sector engagement in the water sector has been low. This is due to a variety of factors such as barriers to entry, reflected in the degree of regulation and the large scale of investments typical to the water sector. Another factor believed to hinder private sector engagement in the water sector is its political sensitivity, rooted in human and ecological requirements, leading to considerable consumer interest and power. Furthermore, the water sector is considered a lower-return on investment industry,⁶ particularly where the opportunity for cost-recovery in the short term is limited. However, it is also considered a lower-risk industry, where long-term savings to public budgets can be secured by strategic water investment decisions and partnerships in the present. Governments may thus need to incentivize the private sector to engage in the water sector and provide their expertise, technology and financial resources to the same degree as other sectors. Attracting private sector engagement can also help accelerate innovation and modernization of the sector, and generate cost savings for the Government and build capacity to sustainably manage scarce water resources.

VI. Water finance in conflict- and crisis-affected countries

18. Conflict- and crisis-affected countries in the region particularly need water sector finance. Conflict can have profoundly negative consequences on water infrastructure and supplies. There is evidence of a steep decline in the availability of safe water and sanitation services in the Syrian Arab Republic since the start of the war.⁷ The Office of the High Commissioner for Human Rights (OHCHR) has also decried armed group attacks in Somalia on wells that were deliberately destroyed or poisoned.⁸ In the State of Palestine, occupied control of water resources has had a severely negative impact on agriculture in the West Bank, and limits Palestinian access to water for domestic use.⁹ Furthermore, Lebanon hosts the largest number of refugees per capita of any country globally, owing to conflict in neighbouring States, and is thus tasked with providing sufficient WASH services to displaced populations while also confronting a major domestic economic crisis.

19. The forthcoming ESCWA report entitled “Trends and impacts 7: Addressing climate security risks in the Arab region” calls for increased access to climate finance for Arab conflict-affected countries. The report discusses requesting that climate finance funds (Adaptation Fund, Green Climate Fund, Global Environmental Facility) include peacebuilding metrics and outcomes in project design. This may both motivate lending in regions impacted by climate security challenges and encourage climate security concerns to be mainstreamed in project design and implementation. The report also highlights the need for more research and pilot projects by international organizations, academics and practitioners on new ways to channel public investment flows in situations where the State is severely weakened by conflict. Reference is made to opportunities for the private sector to be involved in developing credit mechanisms that can de-risk investments in conflict and/or post-conflict countries.

VII. Data gaps in water finance

20. Financial markets need clear and transparent information to function effectively and efficiently and to reduce risk. Better data can improve the effectiveness of financial flows to the water sector. The collection and classification of water finance data can be improved by increasing the frequency and disaggregation of relevant data. This may include data disaggregating government expenditures on WASH, quantifying formally or

⁶ World Bank Group, [Achieving universal access to water and sanitation by 2030: the role of blended finance](#), 2016.

⁷ International Committee of the Red Cross, [Syria water crisis: Up to 40% less drinking water after 10 years of war](#), 2021.

⁸ OHCHR, [Somalia: Türk decries steep rise in civilian casualties amid surge in Al-Shabaab attacks](#), 2022.

⁹ ESCWA, [Palestine Under Occupation III: Mapping Israel’s Policies and Practices and their Economic Repercussions in the Occupied Palestinian Territory](#), 2021.

informally the value of water, and making available information on costs, prices and payments for water services provided by Governments and utilities at the national and subnational levels. Data and information inform the preparation of project pipelines and can lower barriers to entry for private sector engagement.

VIII. Ongoing and future water finance initiatives

A. Innovative water finance

21. The special drawing rights (SDRs) of the International Monetary Fund (IMF) could be used to supplement the financing of the water sector in the Arab region. SDRs are a global reserve asset in addition to the official reserves of IMF member States. An SDR is not a unit of account, but a tool to improve a country's liquidity. If a country is an IMF member, it has an SDR allocation proportional to its share in IMF. This allocation can then be traded with another country for a combination of United States dollars, Euros, Chinese renminbi, Japanese yen, and pound sterling. Historically, SDRs were used as a pure monetary policy tool; however, since the COVID-19 pandemic, SDR use has been broadened. The Arab region has approximately \$19.7 billion equivalent in SDRs allocations and is only utilizing 76 per cent of available allocations. Owing to lower interest rates on SDRs, currently at 3.575 per cent, it could be advantageous to use the allocations to refinance existing debt or invest in new water-related projects. ESCWA recently hosted a conference on the theme "[Special drawing rights and beyond: the future of development finance, fiscal spending and inequality in the Arab region](#)". ESCWA is actively exploring ways to expand the use of SDRs by member States to accelerate SDG achievement, including SDG 6.

22. ESCWA has also pioneered work on [climate/SDGs debt swaps](#) in the Arab region, which are structured as a multi-year arrangement between Governments and their creditors to allow for a portion or all of their debt payments (interest and/or principle) to be used instead to fund projects that advance national climate goals or SDGs. Sustainability bonds and green bonds have also been used in the region, including in Egypt and by the Islamic Development Bank, to fund water projects. Moreover, blue bonds have been issued by some international financial institutions, and as sovereign bonds by small island States, as a debt instrument dedicated to raising funds for marine and ocean-related projects, including wastewater treatment to avoid ocean pollution. The International Finance Corporation expanded the definition of [blue finance](#) to also include drinking water treatment, desalination and water management activities that reduce water consumption.

23. Several Arab countries have overcome water scarcity challenges with investments in desalination technology, repeatedly setting records for the size and efficiency of desalination plants. Nevertheless, efficiency can still be improved by updating plants and developing better technologies appropriate for local conditions. Engineers and physicists estimate that the theoretical efficiency limit of reverse osmosis desalination is close to 1.6 kWh per cubic meter of seawater.¹⁰ Meanwhile, the simple arithmetic mean for the Arab region is approximately 11.6 kWh per cubic meter of seawater. This translates into an average technological cost for the Arab region of between \$5.9 billion and \$9.3 billion annually, the latter including the social costs attributed to additional carbon dioxide emissions. This cost could be reduced by investing in more research and development.

24. Groundwater markets are not new to the Arab region. In Oman, there are weekly auctions for water allocations from their 1,000 years old Aflaj irrigation system. Similarly, cap-and-trade systems offer another market-based mechanism for valuating an environmental good. Cap-and-trade regimes have been successfully implemented for decades to limit carbon dioxide emissions in developed countries and have been applied more recently to the water sector. In such cases, the Government sets a limit (cap) stipulating the maximum amount of water that can be withdrawn; the cap is then split into allocations that are tradable. The state government of California, United States of America, successfully implemented a cap-and-trade system for groundwater in the Mojave Desert. The system decreased the total water withdrawal, increased water use efficiency, and increased property values. Australia also implemented a groundwater cap-and-trade system in several states, but with

¹⁰ Li Wang and others, [Derivation of the Theoretical Minimum Energy of Separation of Desalination Processes](#), 2020.

various degrees of success. This is in part because cap-and-trade systems are susceptible to various risks associated with institutional design, hydrology, political/social sensitivities, and economic variations. Drawing from experiences in applying cap-and-trade systems can help inform efforts to better manage groundwater or other water resources in the Arab region.

B. Modelling the financial viability of desalinated agriculture in the Arab region

25. The Arab region has widely implemented seawater desalination technology. It also has a substantial amount of saline groundwater. Several Arab countries have begun desalination-based agricultural projects. To complement these efforts, ESCWA is further exploring models to estimate the viability of desalination-based agriculture. Currently, the objective is to evaluate which crop in any given location is economically viable using desalinated water. This is premised on the theoretical efficiency limit of reverse osmosis desalination. This binding constraint can be used to forecast the financial viability of desalinated agriculture by crop for any given location. These forecasts, in turn, could be used by the public and private sectors to further optimize their desalination-based agricultural projects.

C. Valuing water in the Arab region

26. Efforts to address water scarcity through improved water management would benefit from a better understanding of the economic value of water. Using valuation techniques to make visible the many economic and social benefits arising from this limited resource would highlight the need for water preservation and more efficient use. ESCWA launched a discussion around the economic value of groundwater in its [Water Development Report 9](#), describing groundwater's contribution to key economic sectors, including industrial processes, mining, electricity and tourism. ESCWA will continue to engage in such work for the forthcoming Water Development Report 10.

27. One way to establish the macroeconomic valuation of water is by measuring its contributions to the agriculture sector. For example, in the Water Development Report 9, in the case of Yemen, data on groundwater withdrawn, groundwater use in agriculture, and agriculture's contribution to GDP was used to estimate groundwater's contribution to the national economy. However, these estimations do not take into account water's contributions to other diverse economic sectors. ESCWA is working on advancing new techniques that control for a wider array of variables, including other inputs to the agriculture sector.

28. ESCWA is also working to develop a microeconomic valuation methodology for water. It is possible to estimate the value of groundwater by calculating the difference in yields for the same crop in areas irrigated by groundwater versus rainfed areas.¹¹ The value of groundwater, in this case, is equivalent to the difference in gross margins between crops divided by the groundwater consumed to irrigate the irrigated crops. ESCWA is in the process of expanding upon this methodology by controlling for fertilizer and seed use. Groundwater valuations have been conducted in other parts of the world, but not widely in the Arab region. Given the region's unique characteristics, most notably water scarcity and hyper-aridity, it could greatly benefit from a more accurate valuation of its water.

29. Most studies on the economic value of groundwater focus on its productive or extractive (use) value, as described previously, in relation to the agriculture sector. Though more challenging to approximate, the in situ (non-use) value of leaving water untouched in the natural environment is also important to take into consideration. The non-consumptive value of water includes ecosystem support, cultural heritage, and soil erosion control, among other benefits.¹² Previous studies on the non-use values of groundwater have primarily used the contingent valuation methodology, which entails developing and deploying a survey to respondents

¹¹ José M. Martínez-Paz and Angel Perni, [Environmental cost of groundwater: a contingent valuation methodology](#), 2011.

¹² Ibid; E. Barbier and others, *Economic Valuation of Wetlands: A Guide for Policy Makers and Planners*, 1997; P. Koundouri and others, *Contribution of Non-Use Values to Inform the Management of Groundwater Systems: The Rokua Esker, Northern Finland*, 2013.

in a selected geographical area to determine their “willingness to pay” for the restoration and conservation of water resources. Member States are invited to express interest in pioneering similar studies in the Arab region.

D. Arab Initiative for Mobilizing Climate Finance for Water

30. At the 2023 Conference for the Midterm Comprehensive Review of Implementation of the United Nations Decade for Action on Water and Sanitation (2023 Water Conference), held in New York from 22 to 24 March 2023, ESCWA and the League of Arab States jointly announced the launch of the Arab Initiative for Mobilizing Climate Finance for Water (AIM Climate Finance for Water) in partnership with the Islamic Development Bank and GCF as a Water Action Agenda commitment. The Food and Agriculture Organization of the United Nations and the Government of Sweden have since joined as partners, as well as other collaborating institutions including the Arab Fund for Economic and Social Development (AFESD) and the Arab Center for the Study of Arid Zones and Drylands (ACSAD).

31. The initiative will prepare a climate finance brief on the water sector, organize a meeting and workshop for mobilizing access to adaptation finance for water projects, and provide tailored training and technical support for Arab States on ways to mobilize climate finance for water-related projects.

E. Middle East and North Africa Climate Week

32. The Government of Saudi Arabia will host the Middle East and North Africa Climate Week (MENA Climate Week) in Riyadh from 9 to 12 October 2023. The MENA Climate Week aims to build regional momentum in preparation for COP28, which will be hosted by the United Arab Emirates in Dubai. MENA Climate Week events and sessions are expected to examine climate finance needs in the region, including those related to the region’s articulated needs and priorities related to financing and investment in water projects.

F. ESCWA Water Development Report 10 on the Water Action Decade

33. In 2016, the United Nations General Assembly, including the 22 Arab member States, unanimously adopted the International Decade for Action on Water for Sustainable Development, 2018–2028. In 2022, ESCWA organized the Arab Regional Preparatory Meeting for the Midterm Comprehensive Review of the Water Action Decade with regional partners. This meeting submitted regional priorities and positions that informed the 2023 Water Conference, serving as the midterm comprehensive review of the decade.

34. The tenth issue of the ESCWA Water Development Report will review regional progress in achieving the objectives set out in the [Water Action Decade enabling resolution](#). In doing so, it will examine regional progress and gaps within the context of the United Nations SDG 6 Global Acceleration Framework. The Framework identifies five global SDG 6 accelerators, namely optimized finance, improved data and information, capacity development, innovation, and governance. A dedicated section of the report will address water finance in the Arab region.

IX. Recommendations

35. The Committee on Water Resources is invited to advise on further areas of work that it would like the ESCWA secretariat to pursue on water finance for improved water security, and provide suggestions on how to advance the implementation of current areas of work by ESCWA member States and the ESCWA secretariat. In this regard, the following recommendations are submitted for consideration by the Committee:

(a) Develop mechanisms for increasing the collection, classification and dissemination of data on financing water sector projects, including the quantity, quality and frequency of that data from international financial institutions, donors and national budgets;

(b) Participate in regional meetings and workshops on increasing finance for water sector projects and encourage the engagement of counterparts from ministries of finance, planning and water-related sectors in these events.

36. The Committee may also wish to discuss how the ESCWA secretariat can support member States through the following:

(a) Providing guidance on the types of water finance data that may be useful for the preparation of bankable water projects and improving access to finance, and ways to prepare and classify water-related projects to ensure that they are eligible for different funding lines;

(b) Convening events where member States, donors and financial institutions can gather to discuss financing guidelines, improving access, and expanding sources of finance for the water sector;

(c) Researching the non-consumptive value of water resources in the Arab region, particularly groundwater resources.
