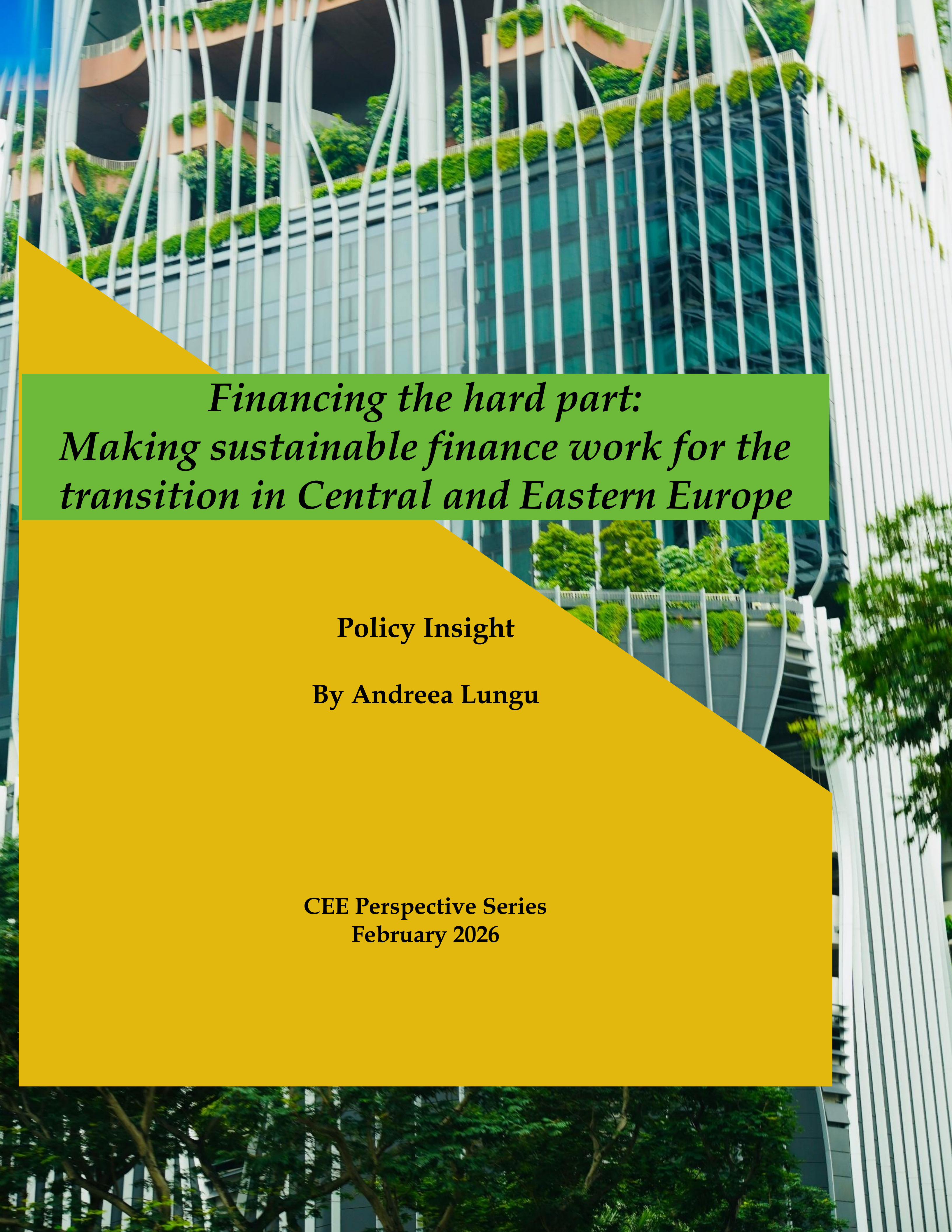

Financing the hard part: Making sustainable finance work for the transition in Central and Eastern Europe

Policy Insight

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Introduction

The EU's sustainable finance framework is entering a new phase with the proposed SFDR 2.0 reform, ongoing EU Taxonomy simplification and the phased rollout of CSRD/ESRS. For Central and Eastern Europe (CEE), where decarbonisation needs are high, but capital markets and data readiness remain constrained, the way these reforms interact will be decisive.

If transition finance tools fail to accommodate CEE's carbon-intensive starting point, the region risks being structurally sidelined from EU sustainable capital flows at precisely the moment when investment needs peak.

1. Why CEE starts the green transition from a structurally different position

CEE economies remain significantly more carbon-intensive than most Western EU Member States, with continued reliance on coal and lignite in power generation and heating. Legacy infrastructure, especially in district heating and building stock, increases both physical transition needs and investment costs

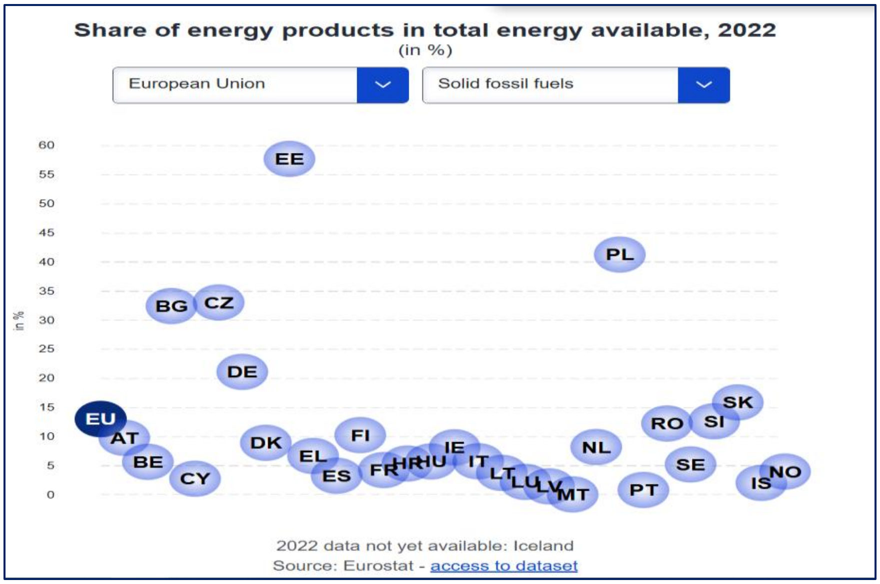

Figure 1: Share of solid fossil fuels in gross available energy, selected EU countries (2022). CEE economies display a structurally higher reliance on coal and lignite in their energy systems compared with most Western EU Member States. Source: Eurostat.

As solid fossil fuels are also widely used in district heating systems across several CEE countries, this structural dependence extends beyond power generation into residential and urban heating. By contrast, most Western EU Member States now derive the majority of their electricity from renewables and nuclear, highlighting the depth of the structural transition gap.

At the same time, income levels and purchasing power in many CEE countries remain below EU-average, constraining households, firms and governments' ability to absorb high upfront decarbonisation costs, especially in buildings renovation, heating-system replacement and industrial retrofitting, where payback periods are long and capital needs are front-loaded.

Financial system structures compound these challenges. CEE remains predominantly bank-based, with relatively shallow local capital markets and a smaller institutional investor base. Long-term project finance therefore depends heavily on banks, public investment and international financial institutions. This makes the usability and proportionality of EU sustainable finance rules particularly critical for CEE. Unlike larger

Western markets, regulatory complexity directly affects capital availability rather than merely compliance costs.

In such a setting, any regulatory friction in sustainable finance frameworks translates directly into reduced credit supply, rather than being absorbed by diversified capital market channels as in larger Western economies.

2. Why transition finance needs in CEE are quantitatively and qualitatively different

The 2024 EIB Investment Survey for the CESEE region shows that firms across Central and Eastern and South-Eastern Europe continue to rely heavily on internal funds to finance investment, with access to external and long-term financing remaining constrained, especially for smaller companies. While many firms are investing, or plan to invest, in energy efficiency and decarbonisation, high costs, tight financing conditions and persistent uncertainty are weighing on their investment decisions. Given the dominant role of SMEs in the region, this heavy dependence on own resources risks becoming a key bottleneck for scaling up the large-scale transition investments needed for the green transformation, unless access to long-term, transition-aligned finance improves.

On the financial sector side, persistent data gaps and methodological challenges in climate risk assessment continue to limit banks' ability to confidently classify and price transition-related lending. This makes the alignment between SFDR, the EU Taxonomy and CSRD not just a reporting issue, but a precondition for mobilising capital at scale.

3. Why SFDR 2.0 matters more for CEE than for most EU markets

The Commission's November 2025 SFDR reform proposal represents a major shift toward simplification and product clarity. The removal of entity-level disclosures, including Principal Adverse Impact statements, is particularly relevant for smaller CEE asset managers and advisers, for whom compliance costs were often disproportionate.

As illustrated in the figure below, SFDR 2.0 introduces a three-tier product classification system that fundamentally reshapes how sustainability and transition strategies can be structured in carbon-intensive economies such as those in Central and Eastern Europe.

SFDR 2.0 product classification and relevance for CEE

SFDR category	Regulatory purpose (EU Level)	Practical relevance for CEE
Article 7 - Transition	Finance the decarbonisation of high-emitting companies and assets through credible transition strategies and emissions-reduction pathways.	Core category for CEE. Enables financing of coal phase-out, industrial retrofits, district heating modernisation-fuel switching and building renovation that do not yet meet full Taxonomy thresholds.
Article 8 - ESG Basics	Apply ESG integration to to investment decisions without a dedicated sustainability objective.	Supporting role. Relevant for CEE. mainstream CEE portfolios where ESG risks are integrated but transition targets are not yet explicit.
Article 9 - Sustainable	Invest in activities with direct environmental or social objectives and strict exclusions.	Limited near-term coverage. Narrow pipeline of fully green assets in many CEE markets constrains immediate scalability.

Figure: SFDR 2.0 product categories and their relevance for financing the transition in Central and Eastern Europe. Source: European Commission, SFDR proposal (November 2025).

Most importantly for the region, the introduction of a dedicated Transition product category under Article 7 fundamentally changes how high-emission sectors can be financed. CEE decarbonisation depends heavily on upgrading existing assets that rarely qualify as "green" under current Article 9 or EU Taxonomy rules. The new Transition category allows financial products to explicitly target emissions reductions in carbon-intensive activities, using portfolio-level transition pathways or EU Climate Transition Benchmarks.

If the Transition category is defined too narrowly at Level 2, however, many of the very investments that matter most for CEE - industrial retrofits, district heating upgrades, fuel switching - could once again fall outside EU sustainable finance classifications.

For CEE markets, this creates a missing bridge between today's economic structure and future climate neutrality. Without such a category, many viable decarbonisation projects would remain misclassified or excluded from sustainable finance frameworks altogether, discouraging investment precisely where it is most needed. However, the real impact will depend on how Level 2 technical standards define thresholds, exclusions and transition metrics over the coming regulatory cycle.

4. Taxonomy and CSRD: Enablers of transition finance or new structural barriers?

The EU Taxonomy remains the backbone of sustainable finance classification, but its usability challenges are particularly visible in CEE. Early reporting shows that many companies still report zero aligned turnover while CapEx alignment is materially higher, reflecting investment in future compliance rather than immediate revenue transformation. This dynamic is especially pronounced in economies that are structurally earlier in the transition process.

At the same time, many transitional investments that are particularly relevant for CEE often face significant challenges in demonstrating alignment with strict technical screening and classification frameworks. While these investments can deliver substantial emissions reductions in practice, existing sustainable finance definitions and data requirements do not always fully capture their transitional value. As a result, without clearer recognition of credible transition pathways, parts of CEE's real economy risk facing reduced visibility or delayed access to sustainable finance, even where decarbonisation potential is high.

CSRD and ESRS are intended to provide the data backbone required for both SFDR and the Taxonomy. However, many CEE companies are first-time reporters with limited internal ESG capacity. Without targeted support, weak data quality could undermine investor confidence, slow product classification under SFDR 2.0 and ultimately restrict access to transition finance. In this context, CSRD implementation becomes not only a compliance exercise, but a strategic prerequisite for capital mobilisation across the region.

If implemented with proportionality and strong technical support, CSRD and ESRS could nonetheless become a foundational enabler of bankable transition pipelines across the CEE real economy

KEY TAKEAWAYS

TAKEAWAY #1

SFDR 2.0's Transition category is the single most important regulatory lever for making large-scale decarbonisation investable in CEE.

TAKEAWAY #2

Without workable Taxonomy and CSRD implementation, CEE risks facing a data-driven exclusion from sustainable finance rather than a mobilisation of capital.

TAKEAWAY #3

Absent targeted de-risking, supervisory coordination and corporate capacity-building, the EU sustainable finance framework could widen rather than close the CEE transition financing gap.

About the Author

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Andreea Lungu is a Brussels-based EU policy adviser specialising in sustainable finance, banking and pensions issues and long-term investment. With over seven years of experience across EU institutions, national administrations and European industry associations, she works at the intersection of financial regulation, climate policy and real-economy investment. Her work focuses on how EU sustainable finance frameworks shape capital flows, transition finance and decarbonisation pathways, with a particular interest in Central and Eastern Europe.

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