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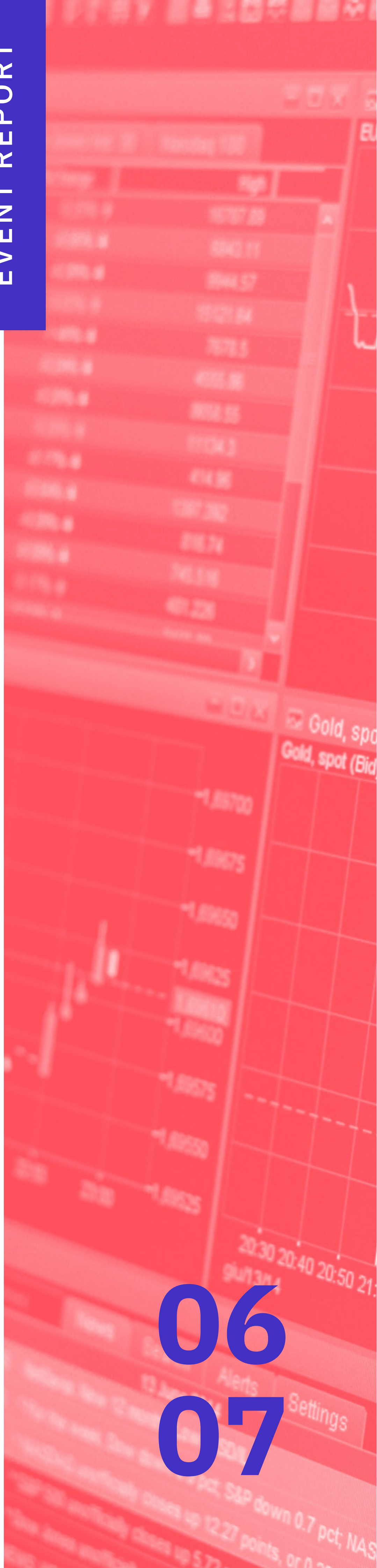
EVENT REPORT



Africa-Europe-Asia: catalysing green reform of the international financial system

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Introduction

Leaders gathered in June 2023 at the Paris Summit for a New Global Financing Pact to discuss how to pull together the estimated $2.4tn that is needed annually for low- and middle-income countries (LMICs) to adapt to the impact of climate change and cut carbon emissions. The talks came ahead of the Africa Climate Summit in Kenya in September and COP28 in Dubai, set to start in November.

On 6 July 2023, having had a couple of weeks to reflect on the outcomes of the Paris summit, envoys from Africa, Asia and Europe gathered in Brussels for a policy debate on catalysing green reform of the international financial system, organised by the Africa-Europe Foundation and Friends of Europe.

Key recommendations

- Actors should move away from a one-size-fits-all approach to development finance; they must take the different starting points of countries into account, particularly in Africa and Asia, and ensure adequate support for just transitions.
- International financial institutions (IFIs) must offer more loans to lower-income and vulnerable countries on a concessional basis and create a more enabling environment for the private sector to fill in investment gaps, including through foreign exchange guarantees and the revision of capital adequacy frameworks.
- The International Monetary Fund (IMF) should adopt a more egalitarian and democratic approach to its work, for example, by allocating special drawing rights based on needs and rules, not shares.
- The Loss and Damage Fund established at COP27 should be operationalised and funded through, for example, an international shipping emissions tax or even an oil pollution fund.
- Wealthier countries should explore the willingness of their citizens to pay a voluntary tax (for example, on electricity), whose proceeds feed into a global fund that contributes financing for climate change adaptation in hard-hit regions.
- The EU should reassess green barriers to trade that cannot reasonably bemet by partner regions in the near future. Instead, trade should be seen as a tool to support the green transition according to a timeline that is realistic for the respective partner country.
- The expansion of carbon markets across all three regions, and the sharing of best practices, is an opportunity to leverage natural resources and scale up financing for climate action.

It's not about the money for climate finance; it's about removing inequity in the system

Envoys from Africa and Asia expressed cautious optimism that momentum was building but warned that the way IFIs work remains a major barrier to green investment. High levels of expensive-to-service debt in LMICs and unequal access to capital were named as major culprits.

Positive steps taken in Paris included moves to potentially pause debt service payments for countries hit by climate shocks, progress on meeting past commitments on the reallocation of IMF special drawing rights and the announcement of country-level agreements, from debt relief for Zambia to a new energy investment package for Senegal.

However, no one present at the policy debate saw decisive progress on systemic change . "What was not present were any concrete solutions, especially on finance," one ambassador summed up. Representatives stressed the need to change structures and voting rights in multilateral development banks deemed to favour the 'Global North' over the 'Global South'.

Participants also identified good policy examples and innovative ideas. Envoys suggested filling the Loss and Damage Fund with an international shipping emissions tax or even an oil pollution fund. On debt, a good case of a relief measure, whereby Belgium committed to absolve Mozambique of 50% of a loan on the condition it be spent on climate-friendly projects, was cited.

Others pointed out that wealthy countries have yet to make good on the 14-year-old promise to provide $100bn a year to LMICs for climate financing and hoped to see the commitment fulfilled in 2023.

Review of the Paris Summit on New Global Financing Pact

While no one saw any breakthroughs from the gathering in France, several envoys praised the constructive atmosphere. "We thought that at least there was participation that turned out to listen," one African envoy said.

> *"We did make our voices heard [...] So the world's attention was brought to our vulnerabilities and hopefully, from the participation that we saw, they have listened.*

"Leaders across the Global North, they demonstrated the willingness to transform the governance of the international financial architecture," they continued.

> *" Now it remains to be seen what is translated into action.*

Participants hailed several positive, albeit small steps taken in Paris. For example, moves to potentially allow LMICs hit by climate shocks to pause debt service payments, progress on the question of special drawing rights at the IMF and a new energy investment package for Senegal, as well as a deal to restructure debt in Zambia. The commitment of summit participants to a clear monitoring framework and roadmap was also seen as a significant step in the right direction.

Unaddressed problems

The common thread identified by most speakers at the debate, however, was the issue of high debt levels in LMICs and the significant expense of keeping up with interest payments. Many argued that to tackle this, fundamental reform of the Bretton Woods Institutions was necessary.

"The debt problem has been on the table for many years in different forums. And it seems that we just touch superficially on the issue and that we don't go deep," one representative said. In a similar vein, a number of envoys raised the issue of unfair allocations of special drawing rights from the IMF.

Another representative described their current push for "fair, equitable and adequate access to the financial tools." Multilateral development banks "are largely perceived in the Global South as being eurocentric in their representation, even the voting rights," the envoy continued. "They have a lot of bureaucratic and procedural limitations that we all know about."

Moreover, it remains much easier (and cheaper) for wealthier countries in the Global North to borrow for climate-friendly projects. "The high cost of capital is very limiting to the Global South," the same representative continued.

An envoy from Europe also saw the need for change.

> *" It's not right, that it costs twice as much to access capital in Addis Ababa as it does in Berlin*

[...] Something that you need to address is this perception of country risk, not project risk, because a wind farm is as risky in Berlin as it is in Addis Ababa," the representative said.

Another problem highlighted by envoys was the lack of total delivery on climate pledges, like the one made by wealthier countries in 2009 to provide $100bn of climate finance to LMICs every year. They have yet to live it up to it entirely, as one envoy pointed out.

Another issue raised were new green 'protectionist' measures being implemented in Europe. "A lot of green barriers [...] are being erected,", which appear to go against free trade and make it harder for LMICs to do business.

Asian and African representatives furthermore levied criticisms against their European counterparts for often failing to work with them in the spirit of true partnership. One representative shared an example: they will regularly be given just a week to comment on important documents that their European partners had already been working on for months, begging the question of why legitimate co-creation is not more deeply embedded in these partnerships.

Several envoys from Asia also pointed out the importance of ensuring that transitions are seen as just in the eyes of their citizens. It is important to acknowledge that countries are coming from different starting points. For example, one envoy pointed to their country's high dependency on coal, arguing that structural reform takes time, especially if it is to be done in a socially responsible manner. If a country has a useful natural resource and a struggling population, there needs to be more support for a just transition.

Things to focus on now – ideas and potential solutions

A number of participants from all three regions identified the potential for global carbon markets, which would allow high polluting countries to 'offset' their emissions by paying for pollution-slashing projects in another one, as a key opportunity. It was noted that the idea had been brought up years ago but had somewhat fallen to the wayside in climate talks. Such schemes offer a promising way for poorer countries to fund climate-friendly investment projects, many participants felt.

The question of debt was the largest and also the most politically ambitious issue brought up by envoys, given the level of consensus needed among influential wealthier countries to really change IFIs.

"The debt that you're mentioning will continue to increase because we are not changing. And when we continue to have new regulations that are really imposing things on us [...] I don't know if we're going to move out of it. But the debt will continue over and over for the next generations."

In general, when it comes to granting loans to LMICs, such institutions need to be willing to offer them on a concessional basis. Given the relatively small carbon footprint of African and many Asian countries, and given the contributions that they make to fighting the climate crisis with carbon sinks like large forests, for example, it should not be so difficult to get one's hands on affordable finance.

One way to reduce borrowing costs for LMICs is for development institutions to offer foreign exchange guarantees to de-risk and reduce interest rates.

Various participants also cautioned against a one-size-fits-all approach to offering finance. It is important that international institutions take into account the different starting points of countries in Africa and Asia. In essence, many representatives were calling for more flexibility from international lenders towards LMICs.

> *“We need to have a very egalitarian or democratic approach in terms of discussing [these matters] with the IMF, with lots of flexibilities.”*

A concrete example of how to tackle debt was a deal mentioned between Mozambique and Belgium, whereby the latter would arrange to drop half of a specific bilateral debt on the condition that the money be spent on a specific environmental project. Both sides hope to finish negotiations on this before COP28, an envoy reported. At the same time, countries spoke to concerns over the growing conditionality of aid hampering development.

Various country representatives also emphasised the role that the private sector will need to play in filling the huge investment gaps and underlined the importance of using public money strategically to stimulate private investment – perhaps through public-private partnerships. Participants noted that it was positive that representatives of major international banks had been present in Paris.

In the shorter term, envoys expressed a desire to keep building momentum after Paris. One concrete matter brought up a few times was how to sufficiently fill up the Loss and Damage Fund for countries affected by the already unavoidable impact of climate change. It was discussed that this should be done under the coordination of the United Nations. Practical ideas for how to fill it floated by various participants included the introduction of an international shipping tax or an oil pollution fund.

Participants also brought up the idea of a voluntary tax on electricity, for example, in wealthier countries where many citizens are perhaps willing to contribute to climate finance for harder-hit areas. The point was also raised that while NATO countries have a set national target to allocate at least 2% of their GDP to defence spending, no such standard exists for climate-related spending, questioning where value is put in budgets.

A few countrizes were also keen to share good domestic policy examples. Rwanda, for example, put emphasis on scaling up proven local solutions, such as their ban on plastic bags from 2008. More recently, after decades of deforestation, Ethiopia has launched a transformative, multi-million tree-planting programme, raising the question of how we quantify green conservation efforts within climate finance allocations.

Looking forward

While nobody would dispute that there are major issues, several participants at the debate expressed a sense of optimism about the changing way the Global North and the Global South speak.

The debate concluded with the notion that times have changed. Today, there is more listening and willingness to act, however, measurable actions still speak louder than words. Whether we will see more of those in the near future remains to be seen.

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