Ninety First Sovereign Debt News Update: Macron's Global South Climate Summit: Stepping up on (Private) Climate Finance to Climate Vulnerable Countries

By:

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On June 22-23, 2023, the Summit for a New Global Financial Pact was held in Paris following the wishes of the President of the Republic Emmanuel Macron, shared during the COP27 in Egypt. During this Summit, the issues at stake were the repercussions of the multiple climate, energy, health and economic crises, particularly in the most vulnerable countries, as well as the financing needed to address these crises. Much of the discussion centred on the key requests of developing nations, framed through the Bridgetown Initiative led by Barbados Prime Minister Mia Mottley. In particular, the Summit had four major objectives namely:

- Restoring fiscal space to countries facing short-term difficulties, especially the most indebted countries;
- Promoting private sector development in low-income countries;
- Encouraging investment in green infrastructure for the energy transition in emerging and developing countries;
- Mobilising innovative financing for countries vulnerable to climate change.

Present at the Summit were nearly 40 heads of state and government, many from the Global South, and a similar number of ministers and high-level representatives. These leaders finalised a roadmap for the reform of the world's public finance institutions, including the World Bank, and of overseas aid and climate finance. A draft of the roadmap titled '*A green transition that leaves no one behind*' sets out a number of proposals for delivery at carefully choreographed points up to September 2024. It includes items for delivery at future meetings of the G20 summit, the World Bank and International Monetary Fund annual meetings in October, COP28 and other international meetings, up to the Summit for the Future to be held in September 2024.

On the face of it, it was expected that the Summit would be a show of global unity for international financial architecture reform. Instead, it showcased the wide chasm between what the global south needs and what the global north is willing to concede. Besides, while some of the outcomes presented by the French government claim to be based on an open and inclusive consultation process, the reality is that the process towards the Summit was chaotic and far from inclusive, with global south countries and civil society side-lined during the discussions of the working groups. In fact, the French government published a chair's summary of discussions, which patently ignored the criticisms and calls from several Global South leaders on the process and the lack of ambition from Global North countries.

The Summit ended without tangible results. Notably, as AfSDJN Eighty Eighth Sovereign Debt Update noted, the announcement of a restructuring deal for Zambia's external debt at the Paris gathering unfortunately excluded private creditors. The two-day gathering of world leaders and finance bosses ended without a major announcement. For example, to bring in more money, activists pushed for a tax on the fossil fuel industry, however, the proposal appeared to have little support from wealthy nations – especially China and the United

States. According to the French President, “if China and the US and several key European countries are not onboard, then you would put a tax in place that would not have any impact.” Under proposals for the tax, the money raised would be directed towards developing countries to help them deal with the challenges of climate change.

Consequently, the lack of results lowered the ambition of the extent of action needed to secure the levels and quality of public finance needed for development and climate action. There was no pact nor global commitments, nor anything really new in the summary shared by the French President on the final day. The hoped for "reform" was merely a repackaging of already existing proposals, some quite problematic. One striking example is the call for Multilateral Development Banks (MDBs) to 'step up' on climate mitigation and adaptation by mobilising more private climate finance. Despite being a plausible idea, such a strict and narrow focus on private climate finance solutions breeds several challenges. For instance, more private climate finance solutions increase the financialization of development and climate action instead of bringing about the much-needed qualitative change in how the multilateral financial architecture works and conceives development.

Notably, the mobilisation of private (i.e., commercial) finance can unlock further private investment in adaptation by facilitating access to finance for enterprises that want to invest in climate adaptation projects and that may be constrained from accessing the external finance needed. On the other hand, provision of such finance by banks, asset managers, asset owners or insurance companies is invariably linked to the ability to generate a financial return for the investor given the key impulse of (private) investment to select and support economic activities that will generate a financial return. In simpler terms, private sector enterprises will not build dams. But they will make a substantial investment only if doing so would yield better economic outcomes. Typically, private sector investment aims to generate predictable returns at sensible risk levels. As such, difficulties in evaluating the financial benefits from adaptation, as well as pricing the cost of inaction, make the mobilisation of private sources of capital less straightforward. This has led to the perception that there is no money to be made in climate adaptation given that adaptation projects may be perceived as riskier due to the uncertainty and complexity of climate impacts, and often result in public benefits rather than direct financial returns.

Furthermore, there exists an information asymmetries and knowledge gaps as far as climate investment is concerned. Investors may contend with limited access to information on climate impacts, future risks and likely adaptation outcomes. The impact of key approaches such as ecosystem-based adaptation has not been systematically measured; nor have the full range of potential environmental and social benefits been monetized and calculated. This makes it difficult to reliably calculate returns on investment and make informed investing decisions.

In addition, the investment horizon and size of adaptation projects may serve to discourage climate investors. Most adaptation projects are inherently long-term, taking 10-20 years to implement. It is hard to make the business case for potentially large upfront costs today set against relatively long payback times. Besides, adaptation projects often have relatively small ticket sizes (around $30-$50 million) which may not appeal to traditional investors.

Africa and Climate Finance

As Kenya prepares to host the forthcoming African Climate Action Summit in September 2023 along with the Africa Climate Week, climate finance will be a key discussion — finding a lasting solution for limited climate finance flows to the region that needs it most. Africa currently receives about $30 billion in annual climate finance flows, which is only 11 percent of what it needs annually. While evidence shows a relative year-to-year increase in global climate finance, unfortunately, the gulf between the needs to be urgently met (especially adaptation needs) and available resources keeps getting wider. However, the financial resources urgently needed for Africa’s low-carbon and climate-resilient development are not necessarily scarce. They are just unevenly distributed. Even when there is an adequate supply of climate finance, there is always a concern about the quality and form in which it is conditioned in. Meanwhile, faced with their own debt and political problems, donors have become less keen to provide pure grants, as such, Official Development Assistance (ODA) is becoming more loans than grants. At the same time, concessional ODA from Organization for Economic Cooperation and Development donors have continuously fallen over the years. Besides, most of the ODA coming to developing countries focuses on a limited number of countries, and about 70% of ODA goes to the social sector, with about 20-25%

going to the productive sector. In the meantime, compounded by the impacts of the Covid-19 pandemic and rising costs of food and fuel due to the Russia-Ukraine war, climate-vulnerable communities in Africa have limited fiscal space to adequately respond. This calls for these countries to seek more debt to respond to climate change impacts. However, the principle of climate justice would suggest that additional climate finance, for it to be effective, should not lead to an elevated debt burden on economies already severely impacted by climate change.

Therefore, in solving this menace, Africa, through its institutions, must creatively – but cautiously – engineer sustainable climate finance sources through frameworks that facilitate flows from where money is most abundant, and perhaps less needed, to where money is most needed but less abundant. Sustainable and innovative climate finance instruments hold promise for scaling up the supply of public and private capital for climate actions. With new instruments such as green bonds, sustainability-linked bonds, resilience bonds, green equity, debt-for-nature swaps, and carbon markets, having been used to finance projects, it is clear that diversity of instruments is beneficial for accessing untapped capital for climate investments.

Additionally, innovativeness in climate finance lends to the idea that blending development finance or public capital together with private capital can de-risk many of the sectors that hold high economic, social and environmental benefits for communities, but low commercial viability/financial returns. Blended finance – the strategic use of development finance to attract private finance – can contribute to building markets by enabling private investors to familiarise themselves with a new business model, region or type of investee. While adaptation continues to be an underdeveloped area for climate blended finance – representing only 14% of transactions- there has been an uptick in financing towards adaptation outcomes, indicating growing momentum around the sector. This, therefore, shows that blended finance for climate adaptation, particularly debt for nature swaps, will continue to gain momentum in 2023.

However, blended finance is no silver bullet. At a global uptake of only 14% in climate adaptation, it is clear that blended climate finance is ramping up but not mobilising much. 14% is a tiny amount when compared with an estimated annual Sustainable Development Goal (SDG) investment gap of $2.5 trillion per annum. Besides, blended climate finance is heavily concentrated in Middle Income Countries (MICs). Only $2.9billion (3.6%) of the private finance mobilised using blended finance flowed to Low Income Countries (LICs) between 2012 and 2015, crudely $728 million per annum. Furthermore, it is predominately going to banking and financial services, the energy sector and industry, with very little invested in social sectors. There are also challenges in aligning blended finance with development effectiveness principles, particularly the challenge of reporting of results and data on blended finance flows.

To address these challenges posed by blended climate finance, there is need to look firstly at how African countries and other stakeholders can generate better evidence to discuss how blended finance can be made more effective at country level. The goal is to ensure that African countries have the evidence and information needed to understand how blended climate finance can best be used to finance climate adaptation and mitigation as part of a coherent strategy that leaves no country behind. This means understanding country contexts and where blended finance can add real value, including the opportunity costs of using ODA for blending instead of traditional loans. African countries must be able to assess how and whether blending fits into their own national strategic plans, and should question whether it’s the best use of aid to strengthen their domestic economies and markets versus other catalytic uses of aid. Improving monitoring and evaluation systems, results frameworks and publicly available qualitative information on objectives and outcomes is needed to develop this evidence base – and a common space to discuss and agree what these systems and frameworks should look like.

Therefore, undertaking a reality check of the potential of blended finance to fund climate investment in the poorest countries – especially those in Africa – should be a priority. From a development effectiveness perspective, it is important that providers and African countries understand different climate finance resources such as blended finance in relation to one another to determine how they can be used to finance a development strategy. Questions such as what is the added value of blended finance as part of the climate financing toolbox, what are the potential risks, and where should it be targeted, are very crucial and should help guide these countries should they opt to take up blended finance.

Be that as it may, blended finance cannot make up for the absence of an enabling global policy environment. Rather, it can be part of an integrated approach to strengthen and support an enabling environment conducive to private investment – especially for vulnerable African countries. For instance, as emphasised by the African Sovereign Debt Justice Network, the World Bank and the IMF need to commence deliberations on a new comprehensive, fair and effective sovereign debt restructuring mechanism based in the United Nations that would be binding on all creditors, including private creditors. The two institutions also need to support the incorporation of natural disaster and pandemic clauses across sovereign debt instruments, including during restructurings, allowing countries to defer principal and interest payments in the event of the occurrence of natural disasters and pandemics. Therefore, to be effective and adequate, it is critical that there is an environment generally conducive to private sector climate investment in Africa if the continent is to attract private investment into adaptation and mitigation at the scale required. Climate finance providers need to exploit all opportunities for scaling up financing available for climate adaptation and mitigation, including from the private sector.

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