

Mixed messages: IMF loans and the green transition in Argentina and Pakistan



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Mixed messages: IMF loans and the green transition in Argentina and Pakistan

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Introduction

Over the past few years, the International Monetary Fund (IMF) has presented itself as a climate champion through its flagship research publications, staff policy papers, public-facing factsheets, and speeches. In doing so, it has consistently highlighted the need to discourage fossil fuel subsidies and, in 2021, recognized that many countries could face transition risks from stranded fossil fuel-based assets if the world commits to greenhouse gas reductions in line with international agreements.

The objective of this report is to present policy recommendations to shape IMF conditionality so that it can be consistent with a low greenhouse gas economic future. To this end, the report assesses the organization's progress towards its emerging climate champion role by focusing on two significant countries currently participating in IMF programs: Argentina and Pakistan. It considers two key questions in relation to these cases. First, to what extent are the IMF programs consistent with enabling these countries to transition away from dependence on fossil fuels? This question relates to whether IMF conditionality directly or implicitly compels reliance on fossil fuels for domestic energy needs and as a source of foreign exchange, as well as the extent to which IMF recommendations interact with climate adaptation objectives as set out in Nationally Determined Contributions under the Paris Agreement. Second, are such efforts aligned with a just transition that safeguards the rights and needs of the poorest in society? This question relates to longstanding debates over whether the IMF mandates premature and excessive fiscal consolidation that fails to fulfil its own mandate vis-à-vis growth, jobs, stability, and debt reduction.

This report finds that IMF lending programs affect borrower countries' capacity to facilitate a green transition and just recovery above all via fiscal policy. In Argentina, energy subsidy reductions were consistent

with a transition away from dependence on fossil fuels, but the encouragement of private sector energy investment to limit reliance on energy imports and generate export earnings was not. The rights and needs of the poorest were safeguarded to some degree, as they were protected from energy subsidy reductions, and the envisaged domestic fossil fuel production may offer reprieve from high energy prices. In Pakistan, removal of tax breaks on renewable energy technologies represented a fundamental threat to the country's green transition. And while energy price increases and subsidy reductions could aid decarbonization, they were not politically or socially palatable, despite attempts to buffer the poorest households with an expansion of social support schemes.

Ultimately, the IMF's lending programs provided mixed messages in relation to green transition and just recovery goals. Energy subsidy reductions were the IMF's prime policy advice, coupled with suggestions for for redistributive measures — both policies can help bring about a just green transition. However, at the same time, encouragement of investments in fossil fuel extraction in Argentina and the removal of tax incentives for investments in renewable energy can hamper this goal. Further, IMF programs lacked a serious consideration of climate-related objectives, despite clear relevance to the IMF's package of reforms and in terms of the risks to livelihoods and the economy associated with climate change.

IMF lending, fiscal policy, and the green transition

Since the onset of the Covid-19 pandemic, the IMF has reasserted its role as the world's leading financial firefighter. It scaled up financial support to countries in need, revamped its lending instruments, and boosted global liquidity (Stubbs et al. 2021), providing an unprecedented number of loans with relatively few strings attached in acknowledgement of the scale and depth of

the pandemic-related economic crisis. The IMF also became a strong public advocate of a green transition, positioning itself at the forefront of policy debates on climate change in the run-up to the 26th UN Climate Change Conference of the Parties (COP26). It has identified mitigating and adapting to climate change as critical to macroeconomic stability, and—to this end—recently began rolling out policy measures to underpin country efforts. Up until now, these attempts primarily pertain to IMF activities in the areas of economic surveillance and technical assistance (Kentikelenis and Stubbs 2021a, 2021b; Sward et al. 2021).

What is the experience of IMF borrowers in attempting to simultaneously stabilize their economies and pursue a green transition? Low- and middle-income countries like Argentina and Pakistan commonly face major and overlapping policy dilemmas: macroeconomic and social challenges mount against a backdrop of growing climate risks. These and other nations resort to the IMF when they are facing serious economic trouble, like being unable to service external debt repayments or pay for essential imports. In exchange for IMF financial assistance, governments must agree to implement a range of policy reforms. These far-ranging policies—collectively known as conditionality—cover issues like balancing the government budget, improving debt sustainability, replenishing foreign exchange reserves, privatizing state-owned enterprises, and deregulating economic activities. The introduction of these reforms is phased throughout the duration of a lending program, often lasting between one and four years, with successful implementation

unlocking access to subsequent loan payments (see Appendix 1 for the types of conditions included in IMF programs). From the perspective of low- and middle-income country publics, IMF conditionality is often viewed as an illegitimate imposition because financial resources are made contingent on ideological and politicized goals of advanced Western shareholders (Bretton Woods Project 2022), and because it frequently deepens pre-existing economic problems (Ban 2016; Tamale 2021), resulting in a series of negative human rights implications (Munevar 2020; Stubbs and Kentikelenis 2018; UNGA 2019).

IMF conditionality affects all aspects of borrowing countries' economies, above all via fiscal policy. 'Fiscal consolidation' or 'austerity'—shorthand for the mix of public spending cuts and revenue increases forming the staple response to past crises—has been the default policy recommendation attached to IMF loans (Babb and Kentikelenis 2021; Ortiz and Cummins 2019; Ortiz and Stubbs 2022). In relation to a green transition, this can mean cuts in subsidies to industries, including in domestic coal production and fossil fuel extraction for export. But it can also mean a reduction in fiscal space that would enable public investment—the prerequisite to transition away from unsustainable greenhouse gas emissions and fulfil commitments made in Nationally Determined Contributions. Evidence from IMF (2022f) fiscal projections for 2023—presented in Figure 1—already shows the organization is recommending austerity in 54 low- and middle-income countries. These fiscal responses make a green transformation and just transition unlikely.

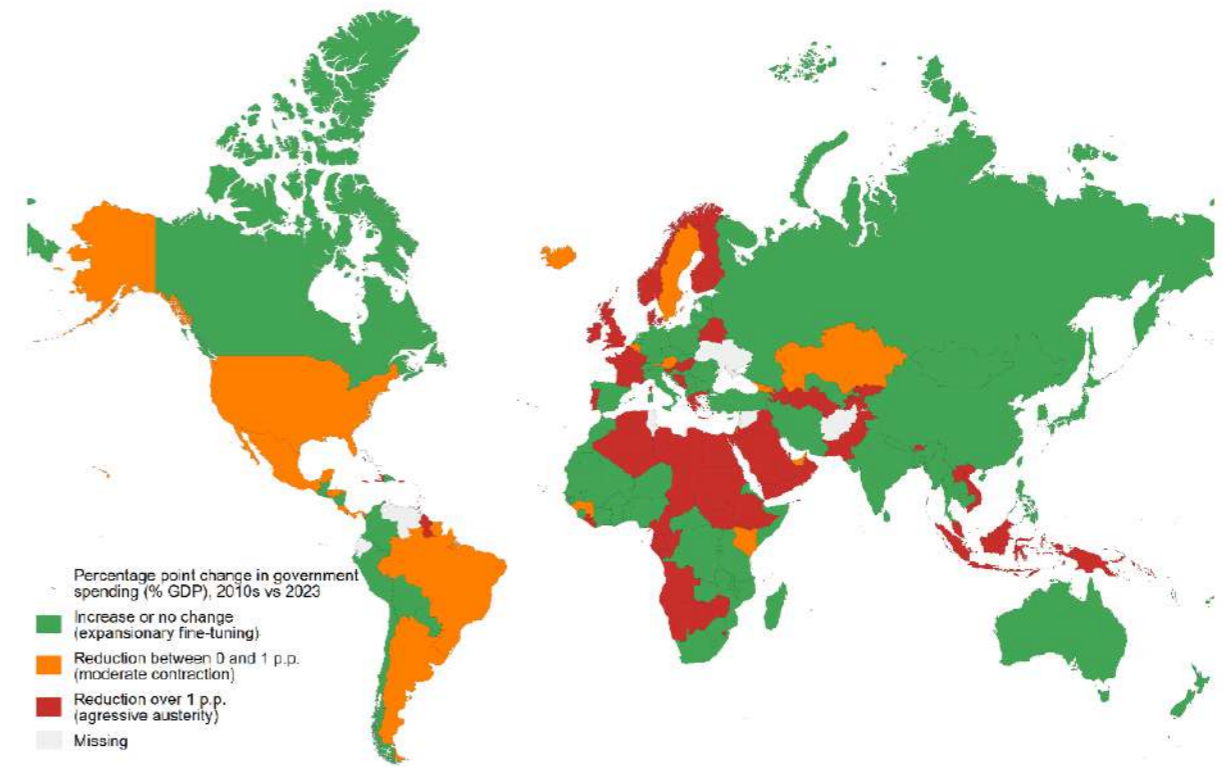


Figure 1. Government expenditure changes as a share of GDP, 2010s vs 2023

This dire fiscal outlook, combined with the scaled-up IMF involvement in low- and middle-income countries through its lending programs, begs important questions about the future of climate change adaptation and mitigation. As noted above, the IMF has a key role to play in facilitating the green transition, and its role as the world's lender of last resort provides the organization with unique power over its borrowers' policy choices. The view from the IMF's top seems to hold promise. As IMF Managing Director Kristalina Georgieva noted, "we embrace the transition to the new climate economy—one that is low carbon and climate resilient, that helps fight the causes of climate change and adapt to its consequences" (Georgieva 2021). This recognition of the central importance of a green transition builds on developments within the IMF prior to the pandemic. Over the last few years, IMF leadership positioned the organization as a champion of meeting Sustainable Development Goals, evidenced by initiatives to promote environmental sustainability, enhance engagement in social

spending, and cultivate resilient regulatory and institutional frameworks (IMF 2018c, 2019d, 2019b; Kentikelenis, Stubbs, and Reinsberg 2022).

These large-scale ambitions have implications for the IMF's lending operations. Indeed, the organization's own 2018 review of program design identified gaps in conditionality related to climate change issues (IMF 2019a). But how green transition objectives can be embedded in conditionality remains unaddressed. In practice, the key policy that has been promoted in recent lending programs has sought to alter energy consumption patterns, rather than the behaviour of private investors. Most commonly, this has taken the form of policy reforms requiring the removal of energy subsidies provided by a government to households and/or businesses. From the perspective of the IMF, this type of policy has two key benefits: it reduces government expenditure, thereby contributing to alleviating budgetary problems; and it

prompts the population and corporations to reduce fuel consumption and use cleaner energy sources, thereby limiting greenhouse gas emissions (Parry, Black, and Vernon 2021).

These types of policies represent steps in the direction of a green transition, but they are far from comprehensive. What is missing from this approach is a fuller appreciation of different types of macroeconomic risks posed by climate change, and a streamlined approach towards aiding countries to address them. This would relate to the three key ‘macro-critical’ risks stemming from climate change: physical risks linked to the macroeconomic and fiscal impact of natural hazards, transition risks linked to the emergence of ‘stranded assets’ (i.e., assets that lose their market value due to decarbonization efforts), and spillover transition risks that capture the macroeconomic impact of climate policies in the Global North on countries in the Global South (e.g., the introduction of carbon taxes at the border for imported goods whose price does not capture their associated carbon emissions) (Gallagher, Gao, et al. 2021; Gallagher, Ramos, et al. 2021; Ramos et al. 2021; Volz et al. 2021; Volz and Ahmed 2020).

Engaging with these types of risks would not only entail more comprehensive analyses and recommendations by the IMF (currently done in a somewhat haphazard fashion for individual countries), but also considering the borrowing countries’ own priorities. These are described in the Nationally Determined Contributions documents that are drafted by countries in compliance with the Paris Agreement to set out their targets and policies on climate change adaptation and mitigation. Already, other international financial institutions have embarked on a process of becoming ‘Paris-aligned’ in their lending portfolios, especially vis-a-vis project lending—such as that undertaken by the Asian Development Bank, Inter-American Development Bank, and World

Bank. While the IMF does not provide that kind of investment financing, its lending operations nonetheless have a direct impact on the environment and countries’ ability to fulfil their Nationally Determined Contributions. Climate change also has profound implications for the ability of the IMF to meet its own mandate of ensuring macroeconomic stability.

A just transition in the context of economic adjustment?

The high-level interest in positioning the IMF as a champion in the fight against climate change intersects with the organization’s narrative on combatting income inequality and avoiding a ‘divergent recovery’ from the pandemic (Gopinath 2021), where some countries steam ahead and others fall further behind. To achieve this, new perspectives on economic management were introduced to supplement the traditional focus on fiscal and macroeconomic targets: from increasing taxes on wealthier individuals and corporations to scaling up social investments in health, education, infrastructure, and basic services (Sandbu 2021). While these are important steps, they point to the extensive efforts that are still necessary to ensure the IMF lives up to its own ambitions on facilitating a just transition.

In this context, tensions may occur between the green transition objectives (i.e., primarily meeting the terms of the Paris Agreement) and a just recovery in terms of reducing inequalities and strengthening social protection systems. The starkest example of such tensions is the case of energy subsidies. The IMF has long advocated for the removal of such subsidies because they do not expose consumers and businesses to the true cost of carbon, thereby leading to excessive use, and because they have adverse distributional implications, as richer households and corporations benefit more from them. However, while it is true that the bulk of these subsidies tend to benefit

middle-class or wealthy individuals, they still have the potential to make a real impact on the lives of the poor, who commonly spend a high proportion of their income on energy (IMF 2020b).

To address these issues, the IMF advises governments to couple the removal of energy subsidies with well-targeted social assistance programs to cater to the needs of those most adversely affected. At first encounter, this approach appears to carry obvious economic benefits, as it simultaneously reduces public subsidies to polluting industries and redistributes some of these savings to those in need. However, two problems may emerge. First, appropriately identifying the groups to be targeted by social assistance programs entails difficult and expensive administrative procedures. Comparative experience suggests that bureaucratic attempts at targeting tend to lead to the exclusion of many credible potential beneficiaries due to excessively stringent eligibility criteria or administrative hurdles (Mkandawire 2005). Second, the removal of energy subsidies can generate domestic resistance from carbon-intensive energy-producing firms, workers, and regions, which hampers the ability of governments to implement green transition policies (IMF 2019c). For example, in Ecuador successive governments attempted to remove fuel subsidies following IMF guidance, only to reverse course following widespread protests (Kueffner 2021; Valencia 2019). Opinion surveys also suggest that poorer households are less likely to favour protecting the environment over boosting economic growth. This is because they are more likely to experience losses in income as they tend to rely on employment in carbon-intensive sectors like manufacturing, transportation, and energy, and are also more likely to be hurt by higher energy prices, as they spend a relatively larger share of their income on energy-intensive goods, such as electricity and heating (IMF 2020b). These arguments are not to defend the use of energy subsidies, but to point to

potential short-run trade-offs between climate policies and inequality reduction. Consequently, a narrow green transition focus of IMF programs that is not sensitive to concerns about inequality and social cohesion can be short-sighted: it fails to adequately factor in political economy considerations by alienating potential supporters, disproportionately hurting the poor and contributing to political upheavals. To complicate matters further, these trade-offs are nested within a matrix of unpalatable economic policy decisions that countries requiring IMF assistance are facing given their macroeconomic problems, which necessitate recourse to the IMF in the first place. These decisions commonly entail sharp reductions in public spending, as discussed above, and extensive so-called structural reforms, which typically have adverse effects on inequality and the environment (Forster et al. 2019; Shandra, Shircliff, and London 2011).

What does recent experience suggest?

To what extent are IMF programs consistent with enabling countries to transition away from dependence on fossil fuels? Are such efforts aligned with a just transition that safeguards the rights and needs of the poorest in society? To generate fine-grained evidence on these questions, we analysed ongoing IMF programs in two countries: Argentina and Pakistan. Both countries are among the top 30 for global greenhouse gas emissions and therefore represent critically important cases in the array of different IMF lending programs. They are important not only as tests for whether the IMF is fulfilling its rhetoric on climate, but also have complex trade-offs relating to reform of their energy sectors and adequate protection of the needs of the most vulnerable groups in society. Moreover, as shown in Figure 1 above, Argentina is slated for a moderate contraction in expenditures in the medium-term, while Pakistan will experience aggressive austerity. In short, these cases illuminate current practices in

IMF lending and its implications for a green recovery and just transition.

Argentina entered into a 30-month \$44 billion IMF program in March 2022 to replenish foreign exchange reserves, control inflation, reduce the budget deficit, and improve long-term growth (IMF 2022a). The country had been in the midst of a full-blown economic and social crisis since 2018, exacerbated by the Covid-19 pandemic and the war in Ukraine. An unsustainable public debt burden and current account deficit had drained the country of foreign exchange reserves, and a collapse of investor confidence meant there was little access to new loans. Inflation had reached over 50% year-on-year, fuelled by the Central Bank printing money to support the budget deficit as well as global commodity price rises, placing a massive burden on the poorest households. Most significantly, the new IMF loan meant Argentina could avoid defaulting on debt repayments of \$19 billion in 2022 owed to the IMF itself as a result of a previous lending program in 2018.

Argentina's IMF program affects three key arenas in relation to the country's climate change efforts: energy subsidy reforms, energy investment, and climate risk and green transition. First, energy subsidy reforms are mandated in IMF conditions related to fiscal consolidation that would see a gradual decline in the primary budget deficit from 3.0% of GDP in 2021 to 0.9% by 2024. To reach these targets, the program calls for reducing the energy subsidy bill by 0.6% in 2022, with further reductions scheduled for subsequent years. These reforms can support climate objectives by raising the price of fossil fuels to the end-user, thereby encouraging more efficient usage of energy and incentivizing a shift to renewable sources like solar. However, the IMF discussed energy subsidies only in relation to immediate fiscal risks, thereby overlooking opportunities to foster a green transition in the long-term—for example, by reorienting savings from fossil fuel

subsidies towards green transformation. While the removal of energy subsidies can place a disproportionate burden on poorer households, these are being phased out in a progressive way: eliminated for the top 10% of urban residential users and for large commercial users; pegged so that prices reflect 40% of average wage growth for poor households; and pegged so that prices reflect 80% of average wage growth for other residential users. That subsidies are pinned to wage increases rather than energy prices means they should remain affordable even as energy prices soar, thereby hinting at the IMF's constructive role at designing effective approaches in phasing out energy subsidies.

Second, Argentina's IMF program encourages the development of a strategic tradeable sector in energy in order to replenish foreign exchange reserves and ensure long-term debt sustainability. To this end, the IMF endorses promoting private investment in exploration, production, and transportation of energy from the shale oil and gas reserves of Vaca Muerta, a large untapped region in Northern Patagonia. This would allow the country to become an exporter of natural gas and reduce its reliance on expensive energy imports. But such incentives for fossil fuel expansion contradict the IMF's advertised climate orientation that centres on aiding countries phasing out of fossil fuel usage. Furthermore, the IMF missed opportunities to consider large-scale government investment in renewable energy production and supply-side subsidies to encourage private investment in wind and solar. Whether or not the provision of incentives for the exploitation of Vaca Muerta represents a just transition is a complex question. On the one hand, where consumer energy subsidies are being cut at the behest of fiscal expediency, it could be viewed as inequitable to advocate incentives for wealthy private investors through producer subsidies, tax breaks, and other guarantees. On the other hand, Vaca Muerta represents the potential to reduce domestic energy

costs throughout the country, including for poorer households. Vaca Muerta can also offer a crucial source of foreign exchange that would enable the country to avoid painful IMF austerity programs in the medium-term. Third, the IMF considered physical risks linked to climate change, such as climate-induced commodity export shocks impacting production and exports but provided only negligible coverage of such risks. The organization also failed to identify any risks linked to the green transition. For example, there was no consideration of the global spillover transition risks linked to the government's economic dependence on Vaca Muerta energy reserves and on highly-pollutive agroindustry. As an increasing number of countries commit to decarbonization, trade partners may impose carbon border taxes, impacting the earnings from such exports. There was also no recognition of national-level transition risks linked to asset stranding in the fossil fuel sector if the country chooses to move towards an energy matrix dominated by renewables.

Turning to Pakistan, the IMF resumed its 39-month \$6 billion lending program in March 2020 (approved in July 2019, but interrupted due to the pandemic), and completed the latest round of reviews and updates to conditionality in February 2022. The resurrected program seeks to reduce the fiscal deficit, control inflation, replenish foreign reserves, and improve the financial viability of the energy sector (IMF 2021c, 2022e). It responded to urgent balance of payments issues that arose due to a surge in the value of imports linked to higher commodity prices, which depleted Pakistan's foreign exchange reserves.

Pakistan's IMF program impacts three important facets of the country's climate change efforts: tax reforms, energy sector reforms, and climate risk and green transition. First, tax reforms were predicated upon a series of IMF conditions to achieve a fiscal consolidation of 2% of GDP for the 2022 fiscal

year. As a result of the removal of various goods from tax zero-rating, discounted tax rates, and other tax exemptions, a 12% increase in sales tax was implemented for imported electric vehicles and a 20% tax was introduced on solar panels, wind turbines, and other renewable energy technologies. While the government has since announced a reversal on solar panel taxation, it has not done so for other renewable technologies. These reforms represent a fundamental threat to Pakistan transitioning away from fossil fuel dependence and achieving its climate commitments. By effectively increasing the price of renewable energy, the IMF-mandated tax reforms disincentivize investor uptake, including from existing fossil fuel-based producers, self-generating agriculturalists, and industrial consumers, who may instead opt for existing fossil fuel-based arrangements. The tax reforms also fail to safeguard the rights and needs of the poorest in society. Major beneficiaries of the growth in solar and wind energy in Pakistan have been poorer subsistence farming communities that remain without grid access. By thrusting higher costs onto these communities—which are also the most impacted by climate change—the tax reforms undermine the achievement of a socially just low-carbon transition.

Second, Pakistan's program contains conditions to reduce the fiscal deficit through energy subsidy and pricing reforms as part of a more comprehensive energy sector restructuring. Two reforms are co-occurring that raise costs to the end-user but reduce government expenditures: energy price reform, which seeks to bring electricity and gas prices in line with cost recovery along prescribed formulas and procedures; and energy subsidy reform, which seeks to target subsidies to a smaller group of consumers on a more progressive tariff structure. These energy sector reforms could support climate objectives by raising the price of fossil fuels to the end-user, thereby providing more incentive to invest in energy efficient production capacity

or shift to off-grid renewable sources like solar. However, more ambitious reforms to the energy sector are overlooked because the IMF's recommendations are guided by short-term fiscal expediency, rather than considering climate concerns that will impact macroeconomic fundamentals in the long run. For instance, cheaper renewable energy could allow for a financially viable long-term solution to addressing the sector's recurrent deficiencies. Similar to Argentina's experience, the IMF recognized that vulnerable populations will be most adversely affected by energy price hikes in Pakistan, since it constitutes a larger proportion of their spending, and called for the expansion and better targeting of social support schemes to compensate such households. However, recent social conflict over food and energy prices imply that this package of measures is neither politically palatable nor sufficiently compensatory for a just transition.

Third, Pakistan's IMF program contained negligible coverage of physical or transition risks, as was the case in Argentina. The IMF identified climate change as a risk to the program, but the analysis was too vague to be of substantive use. Higher frequency and severity of natural disasters is simply flagged as a potential cause of severe economic damage. Outside of the risk assessment, the IMF described the recent history of extensive damage that climate-related disasters have dealt to the Pakistan economy, and the country's position as one of the world's largest emitters on an absolute basis. But these descriptions were self-contained and

did not consider trade-offs involved between the program and climate adaptation and mitigation objectives.

For instance, the IMF advised Pakistan to accelerate efforts to meet greenhouse gas reduction commitments by reforming energy prices, subsidies, and taxes. Not only does this fail to recognize how fiscal constraints prescribed by the program impede efforts to invest in new infrastructure and incentives for adaptation and mitigation efforts, but it also retrofits austerity measures as climate policy. In addition, the IMF did not consider risks linked to the banking sector from changes in carbon-intensive asset values or include any climate-related stress tests in its debt sustainability analysis, despite being well within its remit. As a result, the IMF failed to quantify the macroeconomic benefits of environmentally sound policy measures.

The path towards a just green transition and the role of the IMF

Whither IMF conditionality? As the organization tries to increase its role in efforts to combat climate change, it currently sits at a critical juncture: will it reform its conditionality to help facilitate country efforts to meet the goals of the Paris Agreement, or will it continue to promote policies that have been shown to have adverse effects on climate goals? We weave together the different strands of research, policy analysis, and the evidence presented here to develop a set of recommendations on how to ensure that IMF lending is more consistent with a low greenhouse gas economic future.

Target audience	Recommendation	Action item
IMF	IMF leadership should adopt a 'do no harm' approach and commit to ensuring that lending programs do not impede countries' efforts to meet their Nationally Determined Contributions under the Paris Climate Agreement.	Shift from the incomplete and ad hoc incorporation of climate concerns in IMF programs toward more systematic treatment.
	All IMF assessments should systematically analyse the trade-offs of short-term (1 to 3 years) macroeconomic needs against long-term (10 to 30 years) macroeconomic needs and climate adaptation and mitigation needs, to ensure that the economic and social benefits of environmentally sound policy measures are quantified.	Develop templates and operational guidelines on how to provide ex ante assessments of physical, domestic transition, and global spillover transition risks in IMF programs—including the risks posed by the IMF's own programs, and especially in relation to fiscal consolidation and support for fossil fuel exports.
	The IMF should generate an evidence base on how its programs are fulfilling or impeding commitments to green transition and just recovery.	Conduct regular ex-post impact assessments of IMF program impact on the green transition, and communicate to IMF staff best practices and areas for policy improvements.
	The IMF should ensure representatives from environmental ministries are privy to program discussions with domestic counterparts in finance ministries and central banks.	Develop a protocol that encourages staff to work across ministries to ensure macro-critical issues are considered in light of domestic environmental commitments.
	The IMF should ensure policies that directly impact energy and climate are firmly embedded within national dialogue on just transition pathways with reference to Nationally Determined Contributions, and are politically and socially acceptable.	Consider alternatives to eliminating consumer energy subsidies, such as reducing fossil fuel producer subsidies while using savings to expand investment incentives for renewable energy. If no other options exist, energy tariff increases should occur in a progressive way by reducing subsidies more at the top of the income distribution than at the bottom and should be accompanied by the expansion of social assistance (see Argentina case).
Civil society	Civil society should prioritize clear transmission of priorities to IMF officials both through national dialogue channels and via direct communication with IMF mission staff, and invest in a knowledge-exchange infrastructure that can be drawn on if/when IMF programs are being negotiated.	Initiate informal contacts with the IMF resident representatives and/or mission chiefs.
	Civil society should link up to global efforts at the G20 level (especially the 'Governing Climate' policy stream), in order to foreground how green transition issues interact with the international financial architecture.	Engage with C-20 and T-20 (the G-20's advisory network) on feeding civil society priorities into the preparatory policy work of subsequent summits and communiqués.

Appendix 1. Types of IMF conditionality

Quantitative Performance Criteria	Quantifiable binding macroeconomic targets, such as monetary and credit aggregates, international reserves, fiscal balances, and external borrowing. These are typically monitored at quarterly intervals and compose the majority of conditionality. These must be met—or otherwise require waivers—for the IMF Executive Board to conclude a review. These targets specify policy ends rather than means, and governments can—in theory—pursue a range of alternative policies to meet them.
Indicative Benchmarks / Targets	Quantifiable non-binding macroeconomic targets, such as monetary and credit aggregates, international reserves, fiscal balances, and external borrowing. These are typically monitored at quarterly intervals and are intended to supplement quantitative performance criteria for assessing progress on program goals. Sometimes these targets are set because of data uncertainty about economic trends (e.g., for the later months of a program) and, as uncertainty is reduced, are converted into quantitative performance criteria.
Prior Actions	Microeconomic binding reforms that alter the underlying structure of an economy and/or specify the policy 'means' toward meeting macroeconomic targets and other objectives. These must be undertaken before the IMF Executive Board approves new financing or concludes a review.
Structural Benchmarks	Microeconomic non-binding reforms that alter the underlying structure of an economy and/or specify the policy 'means' toward meeting macroeconomic targets and other objectives. These are intended as markers for assessing broader progress on program goals.

CASE STUDY 1

ARGENTINA

This case is part of a comparative study analysing the extent to which recent IMF loan agreements can support a green transition and just recovery. Argentina was selected to illuminate the complex interplay of acute macroeconomic challenges and climate-related risks. The country has a long history of IMF involvement (22 programs since 1956), features in the top 30 for global greenhouse gas emissions, and faces significant national-level and global spillover transition risks as society shifts toward a low-carbon and more climate-friendly future. The current program is among the largest ever committed by the IMF (\$44 billion), thus representing an important case for examining whether the IMF is fulfilling its rhetoric on addressing climate-related issues. It has also been subject to intense controversy, since it is ostensibly aimed at providing Argentina with enough credit to make debt repayments owed to the IMF from a previous loan in 2018. Furthermore, the program endorses fossil fuel exploration and extraction, but does not sufficiently consider significant global spillover and national-level transition risks linked to the government's economic dependence on extractive sectors.

Economic Context

Argentina is an upper-middle income country with a \$480.6 billion economy—ranking 19th in the G20 group of largest economies—and its income per capita is \$10,496 (World Bank

2022a). Before the Covid-19 pandemic hit, the country was already in the midst of a full-blown economic and social crisis. Inflation had reached over 50% year-on-year, the economy was contracting, the public debt burden had become unsustainable, and the country was running out of foreign exchange reserves—with little access to new loans since international investors lacked confidence that the country could repay its debt (World Bank 2021b). Following the breakout of Covid, the economy experienced its largest contraction ever recorded, shrinking 9.9% in 2020.

Social conditions were also sharply deteriorating. Poverty had kept increasing since 2017, real wages had fallen by over 20% between 2017 and 2019, and unemployment levels were nearing 10% even before the pandemic (IMF 2022a). The pandemic exacerbated these issues: labour informality increased, real incomes fell across the entire distribution, poverty incidence remained high, and more than 20,000 firms were forced to close during 2020, with unemployment peaking at 13% in mid-2020 (IMF 2022a; World Bank 2021b). In addition, social discontent at the mismanagement of the economy by Mauricio Macri's centre-right government, which had been in power since 2015, resulted in Alberto Fernández's centre-left administration being voted into office in late 2019 in the country's general elections.

Table 1. Key economic indicators for Argentina

	2019	2020	Estimates	Projections
			2021	2022
Economic growth / Real gross domestic product growth (%)	-2.0	-9.9	10.3	3.6
Balance of payments: Current account balance (% of GDP)	-0.8	0.9	1.3	0.5
Public debt (% of GDP)	98.5	106.4	89.1	84.6
Primary budget balance (% of GDP)	-0.4	-6.4	-3.0	-2.5
Inflation (% of consumer price index, period average)	n/a	42.0	48.4	47.6

Sources: World Bank (2022a) and IMF (2022a).

To address the inherited economic crisis and impact of the pandemic, the new government that took office in December 2019 introduced a stimulus package in 2020 worth 3.7% of GDP. This was channelled through existing social protection programs, a new emergency family income scheme targeted at informal workers, and the new 'Program for Work and Production' scheme to help pay workers' salaries (IMF 2022a). The government also restructured \$82 billion in debt held by the private sector, estimated to provide \$33 billion in relief over the coming decade through maturity extensions and lower interest rates (IMF 2022a). In 2021, the government made efforts to boost revenues by levying a one-off solidarity tax applied to individuals with a net worth over \$2.4 million, which yielded 0.5% of GDP earmarked for health, education, social projects, and energy production (IMF 2022a). Economic activity recovered, growing 10.3% in 2021 and also bringing the economy 5% above its pre-pandemic size. The primary budget balance also improved—from a 6.4% to 3.0% deficit—as a result of unwinding Covid-19 spending measures and the increased revenues from the solidarity tax.

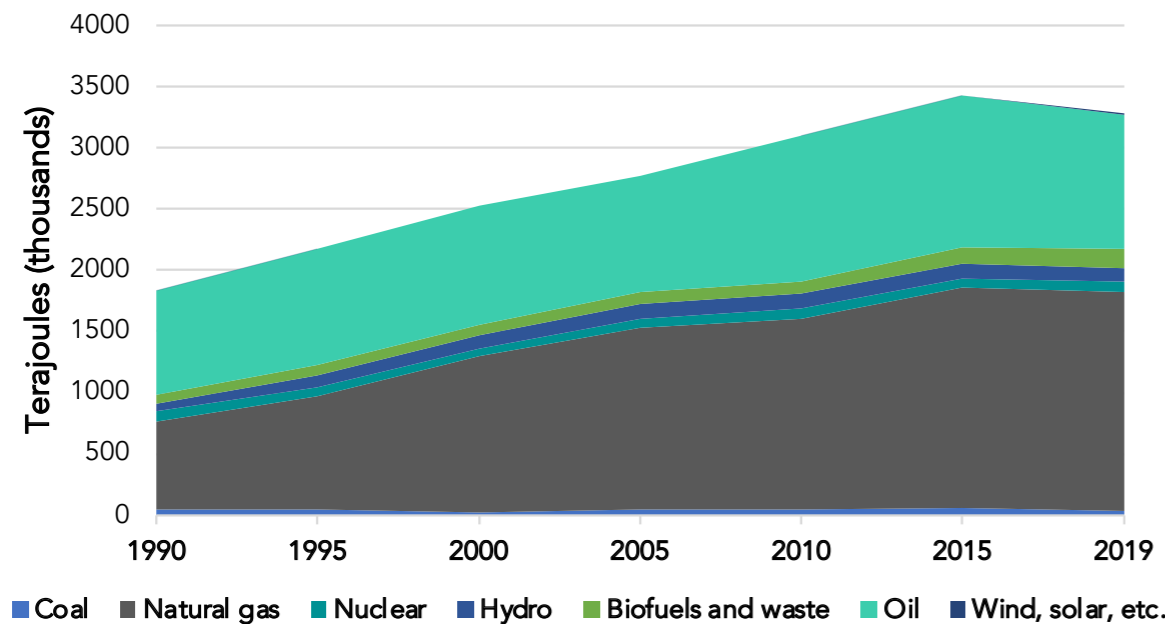
Despite improvements on some economic indicators, the Argentine economy remains in turmoil. Inflation is still over 50%, fuelled by multiple factors including the Central Bank printing money to support the budget deficit (since the country remains locked out of international lending markets), a revival in domestic economic activity, depreciation of the peso, negative real interest rates, and higher global manufacturing and

commodity prices which have been further exacerbated by the war in Ukraine (IMF 2022a). The impact of these price rises on poor households is disproportionately high, given the larger share of their incomes spent on food and energy. Foreign exchange reserves were also perilously low, covering less than ten days of merchandise imports in early-2022 (World Bank 2022a). Without IMF intervention, reserves would have been insufficient to make debt repayments of \$19 billion owed to the IMF itself in 2022 as a result of a previous lending program in 2018 (The Financial Times Editorial Board 2022) (described in detail later on). Nonetheless, because the country is a major exporter of meat and grain, global commodity price rises present an opportunity for foreign reserve accumulation, although this potential boon is currently being offset by higher oil and gas imports, as Argentina remains a net importer of energy (World Bank 2022a).

Climate Mitigation

Argentina's 45 million inhabitants contribute 0.8% of global greenhouse emissions. Of the country's emissions, 47% was from the energy sector, 33% from agriculture, 7% from land-use change and forestry, 7% from industrial processes, and 6% from waste (World Resources Institute 2021). Figure 1 shows that the country's energy mix is dominated by fossil fuels, at 88%, of which 54% is from natural gas, 33% from oil, and 1% from coal (IEA 2022a). The use of oil and gas has decreased only slightly since its peak in 2015, while coal usage has declined considerably—halving in absolute terms (but from a low base).

Figure 1. Total energy supply in Argentina, by source



Non-fossil fuel energy sources include 5% from bioenergy and 3% each from hydropower and nuclear. While only 0.6% of Argentina's energy needs are currently being met by wind and solar, this renewable energy source has witnessed a ten-fold increase in absolute terms between 2015 and 2019. Indeed, several public policies—foremost of which is Plan Renovar—have sought to boost utility-scale investments in solar and wind energy (Costantini and Di Paola 2019). By 2021, these were feeding 12.5% of the power grid (IEA 2022a), a significant gain from 1.8% in 2015 (Marcacci 2019). Argentina also achieved universal electricity access in 2017 (World Bank 2020), catalysed by a rural electrification project—Project for Renewable Energy in Rural Markets—that connected the remaining 2% of the national population lacking access to modern energy to the grid (World Bank 2015).

Argentina has the second largest reserve of shale gas and the fourth largest reserve of shale oil worldwide, although remains a net importer of energy (IEA 2022a). In a bid to achieve self-sufficiency, Argentina's Secretariat of Energy aims to double gas and oil extraction by 2024, with the goal of exporting 50% of its crude oil and 38% of gas (Fundación Ambiente y Recursos

Naturales 2019). Despite pledges by the government to also engage in renewable energy projects, heavily subsidised natural gas exploration increased since the Covid-19 pandemic in the untapped deposits of Vaca Muerta in Northern Patagonia, whereas many renewable energy projects that started prior to the pandemic have been kept on hold (Climate Transparency 2021).

Nonetheless, the government declared a climate emergency in July 2019, and passed a Climate Change Law five months later (Government of Argentina 2019). The law institutionalised government responsibilities related to climate change and established budgets for mitigation and adaptation policies. In December 2020, Argentina submitted its Second Nationally Determined Contribution (NDC), committing to the goal of not exceeding the net emission of 359 million tons of carbon dioxide equivalent in 2030 (Government of Argentina 2020), which is a 10% reduction from current levels. The proposed goal is to be fully funded from the country's own resources. The NDC was then updated in October 2021 to an emissions ceiling of 349 million tons of carbon dioxide equivalent by 2030 (Government of Argentina 2021). The NDC

pledges to carry out an energy transition by promoting energy efficiency and renewable energies, viewing natural gas as a transition fuel during this period. Critics contend that the NDC goal is not adequately reflected in concrete actions and sectoral plans, such as phasing out exploration and extraction of fossil fuels, eliminating fossil fuel subsidies, and addressing dependency on meat production and export (Climate Action Tracker 2021).

Climate Adaptation

Argentina ranks 85th of 182 countries in the ND-GAIN index, which measures exposure, sensitivity, and ability to adapt to the impact of climate change (Notre Dame Global Adaptation Initiative 2021). Despite a highly diverse topography and climate, Argentina will see overall increases in temperatures due to climate change, negatively impacting animal health, agriculture, water resources, and biodiversity. Droughts and floods will also occur with greater frequency and intensity. Argentina experienced droughts in 2006, 2009, 2011, and most recently in 2018, the latter of which alone caused \$4 billion in economic losses (Masters 2018). Furthermore, with one-third of Argentinians living in flood-prone areas, flooding is expected to cause \$700 million in damages every year (World Bank 2021a). Such risks are especially high in the greater Buenos Aires area where rapid urbanization and increasing rainfall have degraded natural drainage networks and diminished the capacity of the soil to absorb flood waters. As a leading global food producer, Argentina also faces macroeconomic risks linked to climate change. The economy is highly dependent on large-scale livestock and agricultural industries, with meat and grain exports accounting for 55% of export revenues (World Bank 2021a). Climate related natural hazards could disrupt this key source of foreign exchange reserves.

Argentina also faces significant global 'spillover transition risks' (Gallagher, Ramos, et al. 2021; Volz et al. 2021), where policy

decisions on the green transition in other countries may affect its economic fortunes. In particular, the Vaca Muerta energy reserves are an integral component of the country's development plans, touted by the government as the solution to Argentina's energy and economic woes (Di Paola 2020). Not only would it provide the country with a substantial source of foreign exchange reserves to repay external debts, it would also reduce pressure on the balance of payments since imports of energy would no longer be needed in the winter months (when current levels of natural gas production are typically insufficient to supply the country). However, as an increasing number of countries commit to decarbonization, potential trade partners may impose carbon border taxes, impacting the potential earnings from such exports and—by extension—the availability of resources for a range of domestic adaptation policies. Furthermore, if gas is genuinely going to be a transition fuel—as described in the NDC—and not a permanent solution, then there are likely to be significant national-level transition risks linked to asset stranding as the country moves towards an energy matrix dominated by renewables.

The poorest segments of the population are those most vulnerable to climate change, and have the least resources in which to adapt to such risks. Argentina experienced declines in its poverty headcount from 2002 up until 2017, reaching 10% of the population living in poverty (based on the upper middle-income poverty rate of \$5.50 per day), but since worsened year-on-year to 18.2% of the population live in poverty by 2021 (World Bank 2022a), coinciding with the economic crisis of 2018-19. This reversal was compounded by the pandemic. In response, the government expanded social protection programs and increased producer and consumer energy subsidies. It set the domestic oil price at a minimum of \$45 per barrel for 2020 despite international oil prices remaining lower at the time, justifying the intervention on the basis of protecting jobs and rescuing the energy sector in the context

of Covid-19 (Climate Action Tracker 2021). The government also capped electricity and gas tariffs to 2019 levels (Climate Action Tracker 2021). In this context, energy subsidies act as a form of social protection. Nonetheless, Argentina is currently (still) developing a National Adaptation Plan, which will present policies for climate change adaptation, integrate them into the existing institutional architecture, and assess and reduce vulnerability to the adverse effects of climate change.

Relationship with the IMF

Argentina has participated in 22 IMF programs since joining the Fund in 1956, most of which have ended in failure and an even larger economic crisis (The Financial Times Editorial Board 2022). The country was a prolonged user of the IMF's resources up to the mid-2000s. But following the Argentine great depression of 1998-2002 and financial crisis of 2001-02, many observers seriously questioned the role played by the IMF over the preceding decade, during which it had been almost continuously engaged in the country through five successive programs (IEO 2004). As a result, the Argentine government—led by a centre-left Peronist coalition—chose to shun the IMF for over a decade.

A new centre-right Argentine government then ended the hiatus by participating in a 36-month IMF program commencing June 2018 to obtain access to \$57 billion, representing the IMF's largest ever program. Mauricio Macri's pro-investor government borrowed heavily from 2016-18 in foreign-denominated currency from private creditors. When the lending boom came to an end, the Argentine peso collapsed, resulting in rapid inflation, recession, and a debt crisis. In this context, the aim of the program was to restore business confidence by reducing the balance of payments and fiscal balance, and by bringing down inflation (IMF 2018a). To this end, the program called for fiscal consolidation measures, including budget cuts at federal and provincial

levels, reductions in the wage bill through hiring freezes and layoffs, pension reform, subsidy elimination on gas and electricity, cuts in education and other public works, and reduced transfers to public enterprises (Romero, Ellmers, and Brunswijck 2018). But it went off-track in August 2019 after the economy further deteriorated, the finance minister resigned, and the government announced plans to introduce capital controls, with only four out of the twelve scheduled program reviews completed (IMF 2021a). The IMF had failed to require any debt restructuring before issuing the loan or insist on the use of capital controls, so funds had simply left the country in the form of debt repayments and capital flight, in effect bailing out private lenders (Banco Central de la República Argentina 2020; Jubilee Debt Campaign 2020). By the IMF's own admission, the program did not deliver on its objectives and adversely impacted vulnerable populations (IMF 2021a).

In March 2022, the IMF approved a 30-month program for Argentina, unlocking access to \$44 billion over the course of ten reviews, \$9.7 billion of which was immediately disbursed. This current program contains four key objectives: 1) reduce the budget deficit via expenditure cuts on energy subsidies and reorient spending toward essential infrastructure and more targeted social protection; 2) reduce inflation by—inter alia—eliminating 'deficit monetization' (i.e., printing money to finance the budget deficit) and increasing interest rates; 3) strengthen the balance of payments and rebuild Central Bank foreign reserves through policies that support trade surpluses and help regain access to international lending markets; and 4) improve long-term growth prospects with reforms to increase domestic savings, improve the effectiveness of public investment, and encourage the development of strategic tradeable sectors (IMF 2022a).

Advocates of the IMF deal expect that the program will contribute to a more stable environment for development because

the new loan will allow Argentina to avert an imminent debt default on an upcoming repayment of \$2.8 billion owed to the IMF itself from the previous loan in 2018, while setting up the policy and institutional architecture to strengthen long-term debt sustainability (Elliot and Stott 2022; World Bank 2022a). The Argentine Senate was also optimistic for the country's prospects under the program, voting on 18 March 2022 to confirm the agreement. This vote is required by Argentinean law in a process that is not typical of IMF programs in other countries or in previous programs in Argentina, as the law itself was passed after the 2018 program (Raszewski 2020). As lawmakers debated the program, thousands of protestors marched

in opposition, describing the program as "a colonization agreement, which can only bring more crisis, more adjustment, more poverty" (Lo Bianco and Sigal 2022). Civil society representatives called on legislators to vote against the new program given the painful cuts the country experienced under the 2018 program and those before it (Bretton Woods Project 2022). And a collective action lawsuit filed in March alleges the 2018 loan violated the Argentine constitution and breached human rights laws; they therefore contend the IMF debt is illegitimate and should be cancelled—which would obviate the need for a new loan since most of the \$44 billion is being used to repay the 2018 agreement.

Box 1. Timeline of IMF engagement in Argentina since 2005

- June 2018: IMF approves Standby Arrangement loan for \$50 billion over 36 months
- October 2018: IMF augments Standby Arrangement loan by an additional \$7 billion
- August 2019: Program suspended due to deteriorating economy and introduction of capital controls.
- March 2022: IMF approves Extended Fund Facility loan for \$44 billion over 30 months.

As the program currently stands, the IMF Executive Board approved the first review in June, giving Argentina access to the next \$4 billion loan tranche. According to the IMF press release, all quantitative targets for the first quarter of 2022 were met, and adequate progress was made on structural reforms, most of which are scheduled for implementation later in the year (IMF 2022b). The annual objectives established at approval of the program—including commitments related to the primary fiscal deficit, monetary financing, and foreign reserve accumulation—also remain unchanged.

Impact of the IMF Program

To what extent is the IMF program consistent with enabling Argentina to transition away from dependence on fossil fuels? Are such efforts aligned with a just transition that safeguards the rights and needs of the

poorest in society? We examine these questions based on analysis of the loan documentation (IMF 2022a), focusing on key conditions and recommendations since the program began in March 2022.

Energy subsidy reforms

Several conditions related to the reduction of the fiscal deficit have the potential to impact the country's climate change efforts. The IMF calls for a fiscal consolidation strategy that would see a gradual decline in the primary budget deficit from 3.0% of GDP in 2021, falling to 2.5% in 2022 (see Table 1), 1.9% in 2023, and 0.9% by 2024, for a total reduction on the deficit of 2.1% of GDP during the course of the program. These targets will be achieved primarily by reducing expenditures on demand-side—or consumer—energy subsidies (supply-side—or producer—subsidies are described in the next sub-section). In 2022 alone, the program

envisages a 0.6% of GDP reduction in the energy subsidy bill, with further reductions scheduled for subsequent years. These objectives are underpinned by a series of conditions, including quarterly performance criteria on the federal government primary budget deficit, a structural benchmark to modify the current budget law to be in line with the 2022 primary fiscal deficit target, and a structural benchmark to call a public hearing on a proposal to update wholesale energy tariffs.

Reforms to energy subsidies hold important implications both in terms of the shift away from dependence on fossil fuels and the extent to which this shift is consistent with a just transition. In 2021, energy tariffs reflected 37% of the full cost of electricity and 44% for gas, and were among the lowest in Latin America, while subsidies amounted to 2.3% of GDP in 2021 (IMF 2022a; Parry, Black, and Vernon 2021). Reducing the subsidies can support climate objectives by raising the price of fossil fuels to the end-user, thereby encouraging less and more efficient usage of energy, and providing an incentive to shift to cheaper renewable sources, like solar. However, it is clear the IMF's advice is not motivated by these concerns, as energy subsidies are discussed in the loan documentation only in relation to immediate fiscal risks. For this reason, several opportunities to foster a green transition in the long-term are overlooked. For instance, projections show that if an amount equivalent to all energy subsidies (both demand- and supply-side) were dedicated toward a green transformation of the energy sector, Argentina would have an 100% renewable energy matrix by 2045 (Fundación Ambiente y Recursos Naturales 2021).

Because energy constitutes a larger proportion of poorer households' spending, energy subsidy reductions can place a disproportionate burden on them. Yet, according to the IMF, subsidies will be reduced in a way that protects the poor—a

claim that does hold up to scrutiny (thus far). First, the increase in energy tariffs will occur in a progressive way by reducing subsidies much more at the top of the income distribution than at the bottom, and has already been approved by the government. Specifically, the introduction of a new tariff segmentation scheme will eliminate energy subsidies only to the top 10% of urban residential users, who are typically those with the greatest capacity to pay. For other residential users, increases in wholesale electricity and gas prices—as determined by reductions in energy subsidies—will be anchored on ensuring that tariffs rise by 80% of average wage growth, except for poor households already receiving a subsidized tariff ('tarifa social'), where the increase will be only 40% of average wage growth. That the tariffs are pegged to wage increases rather than energy prices is important, as it means that it should remain affordable for most households even as energy prices soar due to the war in Ukraine—although subsequent modifications to the proposed reforms cannot be ruled out if the IMF considers the changing context to be fiscally unsustainable. For large commercial users, there will be no subsidies, so wholesale energy prices will reflect full cost recovery; while for other users—such as smaller commercial users—energy tariff increases will be decided upon in the public hearing.

Second, the IMF envisages that the reduction in subsidies will release resources in the budget to scale-up spending on social assistance programs, including the universal social protection allowance (Asignación Universal para Protección Social), food stamps (Tarjeta Alimentar), and scholarship program (Progresar). This objective is supported by indicative benchmarks that set a floor on quarterly federal government spending on social assistance programs, and a structural benchmark to provide a comprehensive evaluation of social support programs to identify options for policy improvements. While the projections in the loan documentation do indeed show that

social assistance spending would more than double as measured in Argentine pesos (from 1,723 billion in 2021 to 3,991 billion in 2024), when considered as a proportion of GDP spending would actually fall from 3.7% in 2021 to 2.9% in 2024—a reflection both of optimistic economic growth projections and high inflation. On the balance of evidence, it may be more accurate to suggest that spending on the social assistance programs will be maintained during the program rather than expanded.

Energy investment

An objective of the IMF program is to ensure long-term debt sustainability by improving the effectiveness of public investment and encouraging the development of strategic tradeable sectors as a source of foreign exchange, explicitly including energy. To this end, there is a structural benchmark requiring the government to develop a medium-term plan to improve the efficiency of the energy matrix. At first, the goal appears at odds with the fiscal consolidation strategy described above, which envisages reductions in expenditures rather than stepping it up to allow for greater public investment. However, public investment spending in Argentina has been consistently lower than relevant comparators, averaging 2.6% of GDP since 1990 compared to 5.7% in Latin America and 6.4% in other middle-income countries (IMF 2022a). The IMF thus anticipates infrastructure spending to increase from 1.4% of GDP in 2021 to an average annual spend of 2.2% over the course of the program.

An increase in infrastructure spending could represent a boon for the renewable energy sector, which will require major investment to foster a green transition. Indeed, Argentina has huge potential for renewable energy generation through solar power and wind, given its topography and climate (Marcacci 2019; World Bank 2021a). However, the loan documentation gives only brief consideration of potential investments in renewables. A single paragraph notes

that “further efforts are needed to start addressing the challenges from climate change”, and endorses three of Argentina's environmental policies: preparation of a new Electro-Mobility Law to incentivize the production and use of renewable energy-powered vehicles; establishment of a new regulatory framework to support investment in the hydrogen sector; and implementation of a Green Productive Development Plan to promote environmental adaptation and energy efficiency by firms (which is a separate medium-term plan from that described in the structural benchmark). There was a missed opportunity to consider large-scale investment in renewable energy production, as well as providing supply-side subsidies. Already from 2016 to 2019, the government awarded contracts for renewable energy capacity that attracted nearly \$7.5 billion in new investment and created more than 11,000 jobs, and has made wind and solar the country's cheapest unsubsidized sources of energy (World Bank 2021a).

Instead, the IMF focuses its efforts on endorsing fossil fuel investment. They recommend “investment and exports on a number of key strategic sectors, including hydrocarbons [oil and gas], mining, agro-industry, automotive, and knowledge economy.” Describing sustainability and efficiency of the energy sector, they note how “efforts are needed to improve the efficiency of the energy sector and tap Argentina's vast energy potential to reduce reliance on more expensive energy imports and transition to a cleaner energy matrix.” In this context, the ‘cleaner energy matrix’ refers to natural gas, which is described as a transition fuel in Argentina's NDC but is a huge drain on the country's balance of payments—further exacerbated by the war in Ukraine. Further, the IMF approvingly cited the Hydrocarbons Law that was being considered in Congress at the time, which—amongst other goals—aims at promoting private investment in exploration, production, and transportation of energy from the shale oil and gas reserves of Vaca Muerta. Such incentives for fossil

fuel expansion clearly contradict the IMF's advertised climate 'champion' role.

To what extent does the provision of incentives for the exploitation of Vaca Muerta represent a just transition? On the one hand, in a context where demand-side subsidies are being cut at the behest of fiscal expediency, it could be viewed as inequitable to advocate incentives for big private investors, which include producer subsidies, tax breaks and guarantees, and greater freedom around foreign currency obtained through exports. Indeed, supply-side subsidies already comprise over 0.6% of the national budget for 2022 (Fundación Ambiente y Recursos Naturales 2021); and among recipient companies of the Plan Gas incentive scheme to expand energy production are TotalEnergies, Wintershall Dea, and Pan American Energy. On the other hand, Vaca Muerta represents the potential to reduce domestic energy costs throughout the country, including for poorer households, as it would avoid the need to import additional gas at global prices, which are currently high due to the war in Ukraine. In addition, Vaca Muerta represents a crucial source of foreign exchange that would enable the country to avoid painful IMF-mandated fiscal consolidation in the more distant future. The prospect of sacrificing the attainment of global environmental goals to obtain immediate tangible social benefits may well sound appealing to a population that has faced the harsh consequences of being perpetually stuck in a sovereign debt trap, some of which dates back to odious loans made to the military dictatorship of the 1970s (Cibils 2015; Jubilee Debt Campaign 2020).

Climate risk and green transition

Beyond what has already been mentioned above, the broader program documentation contained only negligible coverage of climate risks and the green transition. The program's risk assessment matrix recognized a 'medium' relative likelihood—of probability between 10% and 30%—of a climate-

induced commodity export shock impacting production and exports, noting that climate shocks had become increasingly frequent and more severe. The event was classified as 'high impact' if realized, as declines in exports from drought-induced lower agricultural output would lead to foreign exchange outflows and pressures to devalue the peso. This is a prudent assessment: the end of the 2016-18 lending boom that resulted in rapid inflation, recession, and a debt crisis leading to IMF intervention may have initially been triggered by investor concerns over the drought reducing agricultural exports, before becoming a self-fulfilling prophecy (Jubilee Debt Campaign 2020). In addition, the IMF called for improvements in the public investment project selection process, setting a structural benchmark for the government to establish clear criteria for inclusion in the 2023 budget. These criteria will be informed by a recently completed IMF technical assistance mission to benchmark government practices against a Public Investment Management Assessment (IMF 2018b), which included a new climate module to ensure climate objectives were incorporated (Kentikelenis and Stubbs 2021b).

However, the IMF did not consider the significant global spillover transition risks linked to the government's economic dependence on Vaca Muerta energy reserves and on highly-pollutive extractive sectors such as agroindustry more broadly. As an increasing number of countries commit to decarbonization, potential trade partners may impose carbon border taxes, impacting the potential earnings from such exports. There was also no recognition of risks linked to asset stranding if the country decides to genuinely commit to a renewable energy mix. History shows that once investment has occurred in fossil fuel infrastructure of the type envisaged in Vaca Muerta, it becomes entrenched for decades in order to 'spread the overheads': it often makes economic—but not environmental—sense to offset the high overhead costs of extraction equipment and transport infrastructure such as a pipeline

by operating until the oil and gas deposits are completely exhausted. Reversal may also be problematic where legal guarantees have been made to private investors to allow for long-term extraction. Finally, the IMF failed to identify balance of payments risks linked to the rapid influx of renewable energy technology imports that will be required in order to fulfil NDC commitments.

Conclusion

In this latest chapter of Argentina's encounters with the IMF, the energy sector is the backbone of how the country is envisaged to overcome economic problems. For the IMF, this sector represents low-hanging fruit in helping Argentina achieve macroeconomic stability: reductions in energy subsidies will help reduce the budget deficit, while increases in domestic energy production can limit reliance on expensive energy imports and generate export earnings that will improve the country's balance of payments position. Overall, the IMF's logic is compelling through a short-term economic lens, but comes up short when adopting a longer term economic view that factors in the global decarbonization drive and Argentina's own climate commitments, codified in its NDC.

In relation to green transition goals, the IMF program is at best incoherent. On the one hand, the proposed energy subsidy reforms are consistent with a transition away from dependence on fossil fuels. On the other, the encouragement of private sector energy investment is not consistent with a

transition away from dependence on fossil fuels. This incoherence could be a reflection of weaknesses in the IMF's framework for assessing environmental risks, which it has recognized is in need of improvement (IMF 2021b), or a lack of sufficient candidness—perhaps at the borrower's request—about the trade-offs inherent therein. Yet, despite such divergent effects in environmental terms, these policies might have some beneficial effects in terms of safeguarding the rights and needs of poorest: they are protected from energy subsidy reductions, and domestic fossil fuel production might offer them reprieve from high energy prices. Ultimately, Argentina's case teaches us that climate, adjustment, social welfare, and debt are inextricably linked. Large stocks of foreign debt mean that the country needs foreign exchange to repay it, otherwise debt sustainability is threatened, which puts the country in a downwards socioeconomic spiral. Energy production is a key way of generating this foreign exchange. So, unless debt swaps for climate action or other forms of fundamental debt relief are firmly on the table, exploiting domestic energy resources is likely to remain the most appealing path, even if it is to the detriment of climate objectives (Fundación Ambiente y Recursos Naturales 2022). Indeed, it is worth reiterating that the current IMF program is ostensibly designed to repay debt from the previous program. As Sergio Chodos—Argentine representative at the IMF—pointed out, "the only balance of payments problem [Argentina] has is with the IMF" (Laudonia 2021).

CASE STUDY 2 PAKISTAN

This case is part of a comparative study analysing the extent to which recent IMF loan agreements can support a green transition and just recovery. Pakistan was selected to illuminate the complex interplay of acute macroeconomic challenges and climate-related risks. The country has a long history of IMF involvement (22 programs since 1950), features in the top 30 for global greenhouse gas emissions, and is among the most vulnerable to the impacts of climate change. The current program involves a significant transfer of IMF resources (\$6 billion), representing an important case study for examining whether the IMF is fulfilling its rhetoric on addressing climate-related issues. The program has also been subject to intense controversy since it resumed in 2021, and is currently being renegotiated for 2022. Pakistan civil society advocates have already voiced concerns over how the program has insufficiently navigated complex trade-offs relating to energy sector reform, tax policy, and adequate protection of the needs of the most vulnerable in society.

Economic Context

Pakistan is a lower-middle income country with a sizeable \$345.5 billion economy, equating to income per capita of \$1,534

(World Bank 2022a). Between 2015 and 2018, Pakistan achieved consistent economic growth rates of around 4-6% (World Bank 2021c). The Covid-19 pandemic and accompanying containment measures led to a collapse in economic activity, with the economy estimated to have shrunk by 1.0% in the 2019/20 fiscal year (World Bank 2022b). Half the working population saw either job or income losses, with workers in the informal sector facing the strongest contraction in employment (World Bank 2021b).

To revive the economy, the Imran Khan-led government introduced a stimulus package worth 2.9% of GDP, which entailed increasing public health spending, expanding the Benazir Income Support Program, introducing subsidies to reduce food and oil prices to ensure essential items remained affordable, and providing relief on electricity and tax bills (IMF 2020a). The State Bank of Pakistan also lowered its policy rate—thereby allowing banks to lower their interest rates—and expanded refinancing schemes to support lending (IMF 2021c). These measures contributed to a rapid recovery, with the economy growing by 5.6% in the 2021 fiscal year (World Bank 2022b).

Table 1. Key economic indicators for Pakistan

	2018/19	2019/20	2020/21	Estimates
				2021/22
Economic growth / Real gross domestic product growth (%)	3.1	-1.0	5.6	4.3
Balance of payments: Current account balance (% of GDP)	-4.2	-1.5	-0.6	-4.4
Foreign exchange reserves (months of imports)	1.7	2.4	2.7	3.2
Public debt (% of GDP)	85.3	87.6	83.6	82.0
Primary budget balance (% of GDP)	-3.6	-1.8	-0.6	0.0 (-2.0*)
Inflation (% of consumer price index, period average)	6.8	10.7	8.9	9.4

Sources: World Bank (2022b) and IMF (2022e). Notes: * Projection prior to implementation of a supplementary budget is in parenthesis. Fiscal year runs from 1 July to 30 June.

These positive-seeming headline figures on economic growth belie the severe economic—and political—crisis that Pakistan is currently facing. As economic activity rebounded following the acute phase of the pandemic, the economy began to experience high levels of inflation (Khan, Nazar, and Janssen 2021), reaching a year-on-year rise in the consumer price index of 12.7% in March 2022 (World Bank 2022b). Global rising food and energy prices have diminished the purchasing power of households, disproportionately affecting poorer households that spend a larger share of their budget on these items. This fuelled public anger, directed at Imran Khan for the perceived economic mismanagement of the country, and generated momentum for his ousting in a no-confidence vote in April, with Shehbaz Sharif replacing him as prime minister.

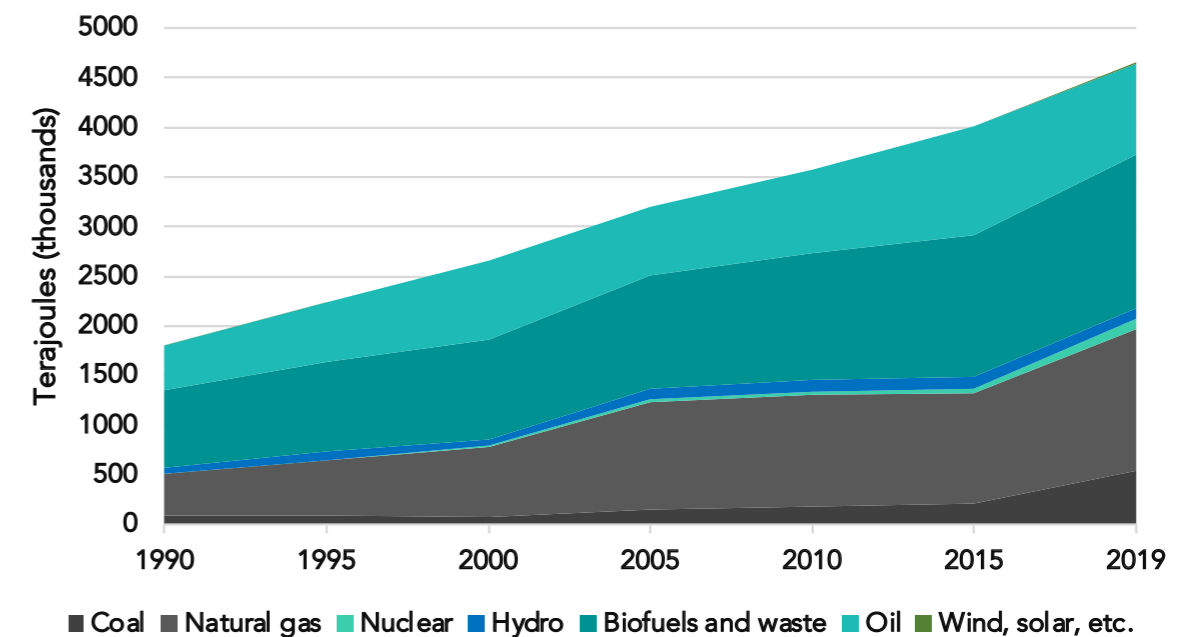
Urgent balance of payments issues—a sign of an impending financing crisis that compels countries to turn to the IMF for financial support—also arose from the Covid-19 pandemic because of sharp declines in exports, as well as a temporary loss of market access from outflows of non-resident holdings of domestic treasuries (IMF 2020a). Initially, Pakistan was able to meet these external financing needs under an emergency IMF loan (not a typical IMF program requiring the implementation of policy reforms) and fresh resources from the World Bank and the Asian Development Bank. However, higher global commodity prices have now contributed to a surge in the cost of imports (but without a commensurate increase in the value of exports), which has depleted Pakistan's foreign exchange reserves—for a time covering less than two months of imports and prompting fears that the country may default on its foreign debt (Rachman, Bokhari, and Parkin 2022). These factors have also resulted in a fall in the value of the Pakistan Rupee by 20% over the

past year, reinforcing domestic inflationary pressures (World Bank 2022b).

Climate Mitigation

Pakistan has developed a series of institutional arrangements to mitigate global greenhouse gas emissions, including the Climate Change Act of 2017, the Alternative and Renewable Energy Policy of 2019, and the National Electric Vehicle Policy of 2019 (Government of Pakistan 2017, 2019b, 2019a). The government also announced a moratorium on new coal-fired power generation at the December 2020 Climate Ambition Summit. These policies culminated in the country's highly ambitious Nationally Determined Contributions (NDC), in compliance with the reporting requirements of the Paris Agreement (Government of Pakistan 2021). The NDC targets an overall 50% reduction of its projected emissions by 2030, of which 15% will be funded from the country's own resources and an additional 35% subject to international financial support. To reach this target, Pakistan committed to generate 60% of all energy produced in the country from renewable resources by 2030, ensure that 30% of all new two- and three-wheeler as well as heavy vehicles sold in the country are electric by 2030, issued the moratorium on new coal power plants from 2020, and planned to completely ban imported coal. To put these ambitions in context, Pakistan—a population of 225 million—contributes 0.9% of global greenhouse gas emissions. These emissions are dominated by the energy sector at 46% and agriculture at 44%, followed by land-use change and forestry (6%), industrial processes (2%), and waste (2%) (World Resources Institute 2021). As shown in Figure 1, approximately 62% of Pakistan's energy needs are currently being met by fossil fuels, primarily from natural gas (30.6%) and oil (19.7%) (IEA 2022b). The contribution of coal to the energy mix has also grown since 2015, reaching 11.7% in 2019.

Figure 1. Total energy supply in Pakistan, by source



Outside of fossil fuels, hydropower is the main source of energy in the country. Within Pakistan's legal and regulatory context (e.g., Government of Pakistan 2019b), it is not considered renewable—although at present the Government of Pakistan is including hydropower to claim progress on the renewables target in the NDC. Historically, Pakistan's experience with hydropower has been neither green nor just, having resulted in severe social dislocation, extensive greenhouse gas emissions, disruption of regional hydrological patterns, as well as causing inter-provincial disputes due to the drying up of river delta in lower riparian provinces (Abbas and Hussain 2021). Hydropower is also vulnerable to climate change because it is directly affected by changing patterns in rainfall and temperatures. This includes the greater frequency and intensity of heat waves and droughts currently being experienced by Pakistan (described in the next section), which will leave less water available to generate power.

In terms of renewable energy, solar entered the mix from 2015, driven by the coming online of large-scale solar power parks of

independent power producers, as well as by small-scale solar uptake in the residential sector and farming communities. With regard to the latter, solar photovoltaic (PV) installations are a cost-effective solution for remote rural regions that are off the power grid, where they can be used for powering tube wells, water purification systems, and water pumps for irrigation. Approximately \$2 billion worth of solar PVs has been imported in the country since 2014 (Government of Pakistan 2019b). Yet, despite the growth of off-grid solutions, more than 40 million people still remain without access to electricity (IEA 2022b).

Nearly one-third of Pakistan's energy resources are imported, primarily in the form of oil, coal, and liquefied natural gas (Asian Development Bank 2019). This depletes foreign exchange reserves, as well as exposing the country to inflationary pressures due to international fossil fuel price shocks. In the 2017-18 fiscal year alone, the value of energy imports increased by 32% (from \$10.9 billion to \$14.4 billion), with three-quarters of this increase due to higher energy prices and only one-quarter due to increased volumes (Asian Development

Bank 2019). Further energy price increases—such as those currently experienced in the world energy market—represent a major economic risk in the future, as these price shocks move down the supply chain and translate into higher costs of living and of conducting business. The increase in energy prices is also expected to be highly socially regressive, hurting poorer households and small businesses the most (ILO 2022).

Climate Adaptation

Pakistan faces significant physical risks from climate change, ranking 151st of 182 countries in the ND-GAIN index in terms of its exposure, sensitivity, and ability to adapt to the impact of climate change (Notre Dame Global Adaptation Initiative 2021). The country is already experiencing a greater frequency and intensity of large-scale flooding, especially along the Indus River where the majority of the population resides. Floods have cost the economy an estimated \$1.7 billion annually since 2010, and damages are projected to increase to \$5.8 billion per year by 2030 (World Bank and Asian Development Bank 2021). This predicted risk is currently coming to pass, with ongoing floods since June 2022 resulting in a humanitarian crisis that has left over a thousand people dead, a million people homeless, and caused \$30 billion in economic damages (Associated Press in Islamabad 2022). Climate change is also increasing the incidence of severe droughts in Pakistan, disproportionately affecting the livelihoods of the 38.6% of the workforce in the agricultural sector, most of whom are poorer subsistence farmers (World Bank and Asian Development Bank 2021). Furthermore, heat waves—such as the one experienced in April of this year—will increase in frequency and intensity due to climate change, resulting in deaths from heatstroke and related illnesses, reduced crop-yield and desertification, critical water shortages, floods from rapidly melting glaciers, and economically debilitating power cuts due to increased use of air conditioning (Aftab 2022; Ellis-Petersen and Baloch 2022). Because the poor are more exposed to climate risks and have fewer resources with

which to adapt, they are more vulnerable to climate change (Anjum 2022). And while poverty rates have fallen dramatically in the country over the past decade—in 2007, 44% of Pakistan’s population lived below the national poverty line, declining to 22% by 2018 (World Bank 2020)—the collapse in economic activity in response to the Covid-19 pandemic reversed some progress. Contractions in employment as a result of widespread lockdowns to control the spread of Covid-19 in its first wave resulted in an additional 5.8 million people falling below the national poverty line and at least 40% of households suffering from moderate to severe food insecurity (Nazar et al. 2022; World Bank 2021c). The Pakistan government adopted a more localised approach to lockdowns in subsequent Covid-19 waves and increased spending on the national cash transfer program—the Benazir Income Support Program—by 80% in order to reach more households.

The expansion of social safety nets helped to alleviate the adverse effects of the pandemic on poverty incidence in Pakistan (World Bank 2022a), but even with this expanded scale and scope will not be sufficient vis-à-vis the actions required to ensure the readiness of local communities to a prolonged climate emergency. In recognition of these realities, Pakistan has already embarked on efforts to reduce the country’s vulnerability to climate impact, including the Ten Billion Tree Tsunami Program, the Ecosystem Restoration Fund, and the Recharge Pakistan initiative, as well as implementing the aforementioned Alternative and Renewable Energy Policy, National Electric Vehicle Policy, and coal moratorium. The country’s NDC also outlines actions to improve the resilience of communities—such as climate smart agriculture, water management, and afforestation projects—and commits to integrating these adaptation measures through the development of a National Adaptation Plan by 2023, which will establish a framework for guiding the mainstreaming of climate change concerns into national

sectoral policies and programs (Government of Pakistan 2021).

Relationship with the IMF

Since joining the IMF in 1950, Pakistan has been a regular recipient of IMF loans, participating in 22 programs in total, its first a 12-month program commencing December 1958. In recent years, the country’s record of IMF program performance has been mixed. For example, Pakistan participated in a 23-month IMF program commencing November 2008 to obtain access to a \$7.6 billion loan. The program aimed to restore economic stability and confidence by reducing the fiscal deficit and tightening monetary policy; and to ensure social stability and adequate support for the poor (IMF 2008). But in 2010 the government failed to fulfil conditions on implementing a value added tax, reigning in the general budget deficit, and reducing government borrowing from the central bank, resulting in a suspension of the program (IMF 2010a). Against a backdrop of massive flooding, the IMF then approved the disbursement of \$451 million under an emergency IMF loan in September 2010 to enable the government to provide urgently needed food, shelter, and health services (IMF 2010b). Following a two-year hiatus from IMF lending the

government entered into a 36-month program for \$6.7 billion in September 2013 that aimed to address economic instabilities and enact structural policies that would bolster market confidence, as falling capital inflows had led to a large reduction in foreign exchange reserves (IMF 2013). The program was successfully completed and the entire loan was drawn.

In July 2019, the IMF approved a 39-month program for Pakistan, unlocking access to \$6 billion over the course of eight reviews. The aim of the program was to tackle, in the IMF’s words, “macroeconomic imbalances” including large fiscal deficits, loose monetary policy, and defence of an overvalued exchange rate (IMF 2019e). Even in these early stages, the program was not without controversy, as market and wholesale merchants went on strike across the country over steps to boost tax revenues (Hassan 2019). These protests failed to stall the program, and its first review was completed on schedule in December 2019. The program remained on-track until March 2020, at which point the government deviated from it to develop a policy response to the unfolding Covid-19 pandemic, which was in part funded by a separate emergency IMF loan of \$1.4 billion in April 2020 (IMF 2020a).

Box 1. Timeline of IMF engagement in Pakistan since 2005

- November 2008: IMF approves Standby Arrangement loan for \$7.6 billion over 23 months.
- July 2010: Program suspended due to failure to implement conditions and never resumes.
- September 2010: IMF approves an immediately disbursing Emergency Natural Disaster Assistance loan for \$451 million.
- September 2013: IMF approves Extended Fund Facility loan for \$6.7 billion over 36 months.
- September 2016: Program completed.
- July 2019: IMF approves Extended Fund Facility loan for \$6 billion over 39 months.
- March 2020: Program suspended due to deviations in policy objectives linked to Covid-19 pandemic.
- April 2020: IMF approves an immediately disbursing Rapid Financing Instrument loan for \$1.4 billion.
- March 2021: Program resumes.
- February 2022: Program suspended due to failure to implement conditions.
- June 2022: Program resumption imminent.

After lengthy deliberations between the IMF and domestic officials, the program resumed following the completion of the second-through-fifth review in March 2021, which gave the government access to \$0.5 billion. The delay was in large part due to the government resisting IMF recommendations to increase electricity prices and impose additional taxes, given the widespread unpopularity of these measures among the population. The program was also given a new focus to reflect pandemic-related challenges. It now contained five key objectives: 1) achieving fiscal discipline over the medium-term, while mobilizing revenues and controlling spending to make space for more infrastructure and social spending; 2) fostering disinflation through monetary policies; 3) preserving the market-determined exchange rate and continuing to replenish foreign exchange reserves; 4) restoring the financial viability of the energy sector; and 5) advancing structural reforms, including in state-owned enterprise governance (IMF 2021c).

There were further delays before the completion of the sixth review in February 2022, linked to apprehension by the Khan government over General Sales Tax reforms and the removal of fuel subsidies, which were eventually enacted, enabling the release of the next \$1 billion tranche under the program (described in detail in the next section). Completion of the seventh review—which commenced March 2022—has also been delayed over the reversal of expenditure cuts incorporated in a supplementary finance bill that was adopted at the IMF's behest (IMF 2022d). Khan reintroduced a \$1.5 billion subsidy on fuel and electricity to reduce inflationary pressures, and the new Sharif-led government was initially reluctant to remove them for risk of stoking public anger with Pakistanis struggling with the increasing cost of living. IMF staff view the subsidies as fiscally unsustainable and will not resume the program until the subsidies are abolished (IMF 2022c). In June 2022, the government finally surrendered to IMF demands by

removing fuel subsidies, resulting in a 29% hike in fuel prices (Press Trust of India 2022).

Impact of the IMF Program

To what extent is the IMF program consistent with enabling Pakistan to transition away from dependence on fossil fuels? Are such efforts aligned with a just transition that safeguards the rights and needs of the poorest in society? We examine these questions based on analysis of the loan documentation (IMF 2021c, 2022e), focusing on key conditions and recommendations since the program resumed in March 2021.

Tax reforms

Pakistan's progress on achieving its climate commitments will be affected by several conditions aimed at reducing the fiscal deficit. In the second-through-fifth program review in March 2021, the IMF called for a cumulative fiscal consolidation of 3.3% of GDP by the 2023 fiscal year, to be achieved by increasing revenues through taxes and no quantitative changes on expenditures, which would instead undergo reprioritization toward health and social spending. The government's 2022 budget, approved in June 2021, departed from these objectives on taxation. In the program's sixth review (concluded February 2022), the IMF called for a cumulative fiscal consolidation of 2% of GDP in order to achieve an underlying primary balance of 0% of GDP for the 2022 fiscal year (see Table 1) through revenue mobilisation. This objective was underpinned by quarterly performance criteria on the government primary budget deficit, indicative targets on tax revenues collected by the Federal Board of Revenue, and a prior action requiring the National Assembly to adopt a supplementary finance bill, which the President signed into law on 15 January 2022.

Tax reforms incorporated in the IMF-backed supplementary budget represent a fundamental threat to Pakistan transitioning away from fossil fuel dependence and achieving their climate commitments. They also contradict the IMF's own climate

strategy, which states that "adaptation and resilience building to climate change ... require substantial investments, which can complicate fiscal management and impair debt sustainability ..., [such as] significant changes to tax regimes" (IMF 2021b). The budget reformed the General Sales Tax by removing various goods from tax zero-rating, discounted tax rates, and other forms of tax exemptions, instead shifting to the standard sales tax rate. As a result, a 12% increase in sales tax was implemented for imported electric vehicles, and a 20% tax was introduced on solar panels, wind turbines, and other renewable energy technologies (Moulvi 2022). While the government has since announced a reversal on solar panel taxation, it has not done so for other renewable technologies.

The tax on electric vehicles undermines mitigation efforts in Pakistan's NDC and elaborated upon in the National Electric Vehicles Policy to reach sales penetration of 30% for several vehicle classes by 2030. When a tax break scheme came into effect in July 2021 to incentivise the development of a fledgling import market for electric vehicles (Mukhtar 2021), the government was unequivocal on how integral such breaks would be to the successful implementation of the policy: "The initial years of EV [electric vehicle] penetration in Pakistan are not possible without governmental support as EVs still cost much higher than [fossil fuel-based] counterparts" (Government of Pakistan 2019a:vii). The government also appealed to the fact that "governments around the world give subsidies, incentives and tax breaks for EV adoption" and that this short-term cost "pays for itself with the savings in fuel import bill, reduction in emission related expenses, usage of idle electricity capacity and income from charging revenues" (Government of Pakistan 2019b:vii). In this light, the IMF-mandated tax reforms appear short-sighted and raises questions around the propensity of the organization to prioritize short-term fiscal sustainability—typically up to three years—

over a long-term future that can be both fiscally and environmentally sustainable.

Similarly, by effectively increasing the price of renewables, the 20% tax on renewable energy technologies disincentivizes investor uptake, including from existing fossil fuel-based producers, self-generating agriculturalists, and industrial consumers, who may instead opt for existing fossil fuel-based arrangements. Indeed, the tax hikes extend to inverters, batteries, and other installation equipment, significantly raising upfront capital expenditure for renewable projects and increasing energy generation costs (Moulvi 2022). The government has since announced their intention to reverse solar panel taxation, but not related technology (Ali 2022). Yet, the frequent oscillation between imposing and withdrawing such taxes also renders long-term planning difficult, eroding investor confidence and fomenting uncertainty in the market regarding the profitability of the technology. This undermines the country's emerging solar and wind energy market and threatens the goal of generating 60% of energy from renewable resources by 2030. Integral to achieving this target is the displacement of entrenched fossil fuels through the integration of renewables into off-grid solutions, private contracts, and rural energy services (Government of Pakistan 2019b), but this is less likely to occur given the changes to the incentive structure by the IMF-mandated budget.

The tax reforms also fail to safeguard the rights and needs of the poorest in society. Thus far, major beneficiaries of the growth in solar and wind energy since 2015 have been poorer subsistence farming communities that remain without grid access. These typically remote and sparsely populated rural villages constitute one of the most vulnerable populations in Pakistan. By thrusting higher costs onto these communities—which are also likely to be the most impacted by climate change—the tax reform will jeopardise the goal of achieving a

socially just transition to a low-carbon future. It may also deprive these communities of any access to electricity and thereby undermine achievement of the internationally agreed-upon Sustainable Development Goal Target 7.1 of universal access to affordable, reliable, and modern energy services by 2030, since extending the grid to them is unlikely to be economically feasible—the government plans to extend access on-grid from 77% to 97% by 2030, with 3% of the population still requiring access off-grid (IMF 2022e)—and they may be priced out of solar and wind energy solutions.

Energy sector reforms

Another key pillar in the IMF's plan to reduce the fiscal deficit is through energy subsidy and pricing reforms, which is part of a comprehensive energy sector restructuring through the Circular Debt Management Plan. The energy sector suffers from long-standing deficiencies related to circular debt—a complex form of public debt accruing due to unpaid government subsidies to distribution companies, who in turn cannot pay independent power producers, thereby affecting the entire power and gas chain. To address this issue, the IMF set a series of energy sector conditions in the second-through-fifth and sixth reviews. In effect, two reforms are occurring conjointly that have raised costs to the end-user but reduced government expenditures: energy price reform, which seeks to bring electricity and gas prices in line with cost recovery along prescribed formulas and procedures in the amended National Electric Power Regulatory Authority Act and the Oil and Gas Regulatory Authority Act; and energy subsidy reform, which seeks to target energy subsidies to a smaller group of consumers on a more progressive tariff structure.

On the surface, these energy sector reforms could support climate objectives by raising the price of fossil fuels to the end-user, thereby reducing demand and offering greater incentives to invest in energy efficient production capacity or to

shift to off-grid renewable sources such as solar PV. Yet, while a dozen or so pages of the loan documentation are dedicated to energy sector reforms, Pakistan's NDC commitments are never mentioned, despite the sector's centrality to them. If the country's mitigation pledges are to be achieved, then a wholesale reordering of the energy sector toward renewables will be required. Against this backdrop, IMF advice risks further entrenching fossil fuel architecture, by restructuring it into a more economically efficient—but still environmentally destructive—form. As with the tax reforms, more ambitious reforms to the energy sector are overlooked because the IMF's recommendations are guided by short-term fiscal expediency, rather than considering climate concerns that will impact macroeconomic fundamentals in the long run. Indeed, the potential for cheaper renewable energy could allow for a financially viable long-term solution to addressing the sector's recurrent deficiencies.

The recent turmoil in Pakistan over increasing food and energy prices attests to the fact that these reforms are not politically palatable, especially among vulnerable populations. Fuel and power price hikes burden poorer households the most because such goods constitute a large proportion of their spending—and energy prices in Pakistan were already three times higher relative to other countries in the MENAP (Middle East, North Africa, Afghanistan, and Pakistan) region. Pakistan's energy subsidy amounts to only 0.5% of GDP compared to over 3.5% in MENAP (Parry, Black, and Vernon 2021). Recognizing this issue, the IMF calls for such households to be compensated through the expansion and better targeting of social support schemes like the Benazir Income Support Program, supported in the IMF program by quarterly indicative benchmarks that set a cumulative floor on targeted cash transfers spending. As yet, it is unclear whether a time-sensitive rollout of the Benazir Income Support Program will be possible, although steps to facilitate the

enrolment of beneficiaries and improve its targeting (i.e., to ensure it is reaching the poorest households and not higher-income groups) were incorporated in a structural benchmark to update the National Socio-Economic Registry.

Climate risk and green transition

If the IMF program is to facilitate green transition and just recovery priorities, it will need to consider the physical risks of climate change and transition risks associated with a low-carbon future. But despite IMF claims of “embrace[ing] the transition to the new climate economy—one that is low carbon and climate resilient, that helps fight the causes of climate change and adapt to its consequences” (Georgieva 2021), the program contained no conditions explicitly relating to climate change and the green transition, and the broader program documentation contained negligible coverage of physical or transition risks. In the second-through-fifth review, the section devoted to energy sector policies referred to the reduction of greenhouse gas emissions once in describing “a range of ongoing reforms [that] seek to gradually reduce commercial and technical losses, power generation costs, and greenhouse gas emissions; improve governance; and introduce competition”, and noted that the Circular Debt Management Plan would incorporate savings from the coming-on-stream of cheaper renewable energy production (IMF 2021c). In a subsequent section on structural policies, the IMF noted that discussions were held around implementing policy related to the sale of electric vehicles “with the aim to reduce Pakistan's greenhouse gas emissions and fuel import bill, and promote industrial growth and job creation through new investments and the introduction of new technologies” (IMF 2021c). No further details were provided on this discussion, although it appears that the IMF did not prioritize reductions in greenhouse gas emissions given the ensuing reversal of tax breaks on electric vehicles in the supplementary budget adopted as a prior action for completion of the sixth review.

The sixth program review fleetingly recommended “a modern electricity policy that [...] tackles the poor and expensive generation mix, including a wider use of renewables” in relation to the Circular Debt Management Plan. It also contained a paragraph describing the extent to which Pakistan is affected by climate change, as “among the 10 countries worldwide with the largest damages from climate-related disasters since 2000 [...], hav[ing] caused an estimated US\$22 billion in material damages, left more than 55 million people affected and 11 thousand killed” (IMF 2022e). In the same paragraph, the IMF noted that the country is “in the group of 20 largest emitters worldwide on an absolute basis” (IMF 2022e). However, the IMF did not draw any links between Pakistan's climate vulnerabilities and high emissions on the one hand, and its own lending program on the other (for instance, by considering the trade-offs involved between the program and climate adaptation and mitigation objectives).

While there was engagement elsewhere with how climate change risks may impact the program in a risk assessment matrix, the analysis was too vague to be of substantive use. Higher frequency and severity of natural disasters is simply flagged as a potential cause of severe economic damage. Some reference to the economic costs of previous instances of environmental disasters, such as the 2010 flooding or recent droughts, could have provided much-needed context to the risk analysis in terms of estimating the potential financial needs.

In addition, there is another area within the IMF's remit that did not factor in climate considerations: risks to the banking sector from changes in carbon-intensive asset values. There is high potential for asset stranding given the country's ambitious NDC mitigation commitments and the energy sector's centrality to it. For instance, while the IMF advised the State Bank of Pakistan to unwind the mandatory target on banks

to double to 5% the share of their lending portfolio to the housing and construction sectors (out of concerns for financial stability and efficiency), it missed an opportunity to consider equivalent measures to incentivize green investment (or disincentives for emission-intensive lending), which may be justified on the basis of financial stability and efficiency if transition risks are taken into account. The IMF does plan to extend support to countries for such costing through surveillance and technical assistance activities, but it is unclear how (or if) this will be incorporated into lending programs (IMF 2021b; Kentikelenis and Stubbs 2021a, 2021b). Furthermore, the debt sustainability analysis did not include any climate-related stress tests, even though the IMF is capable of delivering them (e.g., IMF 2021d), thereby failing to quantify benefits of environmental policy measures vis-à-vis the country's debt profile. There was also no coverage of the potential trade-off between Pakistan's policies to increase electric vehicles and solar PVs—which at present need to be imported because there are no domestic producers—and the depletion of foreign exchange reserves. A concerted examination of such an issue could have brought out the need to invest in or incentivize domestic renewable production.

The sixth review also contained some alarming contradictions. IMF staff commended the national electric vehicle policy, despite removing the tax breaks contained within it. Staff also recommended prioritization of what they called “no-regret measures” (IMF 2022e)—measures that simultaneously deliver on the objectives of economic growth, development, and climate change—such as enhancing early warning systems for communities living in flood- and drought-prone areas. And staff advised authorities to “accelerate efforts to meet their international GHG reduction commitments...[by] reforming energy prices, subsidies, and taxes” (IMF 2022e). Not only

do these comments fail to recognize how fiscal constraints prescribed by the program impede efforts to invest in new infrastructure and incentives for adaptation and mitigation efforts, but they also retrofit these fiscal consolidation measures as climate policy.

Conclusion

The IMF program lacks a serious consideration of Pakistan's climate-related objectives, despite its clear relevance in relation to the tax and energy sector reforms, and in terms of the physical risks to livelihoods and transition risks to the economy presented by climate change. While the fiscal consolidation plan did demonstrate some sensitivity to the potential impact on the poorest segments of the population by counterbalancing measures with targeted social safety net approaches, these fall short of the ambitions set out by Pakistan in its NDC as well as by the IMF's leadership on fostering a green and just transition. Indeed, the IMF gave little-to-no weight to the existing climate-related commitments that Pakistan has made, at least as reflected in the program objectives and related documentation.

Our analysis shows that IMF reforms tend to be short-sighted and reactive to recent economic crises. Moving forward, the IMF will need to extend its vision much further into the future, as avoiding balance of payments issues in 20 years time may stem from actions taken today. In this light, it is well within the IMF's remit to consider structural reforms that are better suited to new climate realities. In the Pakistan context, for instance, this means considering how to shift toward an economic model that is less reliant on the Indus Basin Irrigation System, which will struggle to support water-thirsty crops, and that considers how communities will be able to make a living outside of flood-prone areas, which they will need to relocate from. These now represent core macroeconomic and social risks that could plausibly benefit from IMF analysis.

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