OPEN LETTER: A ‘NEW’ FINANCIAL PACT?

In November 2022 the French President Emmanuel Macron announced the organisation of a summit in 2023 together with international leaders to accelerate the process of International Financial Institutions (IFI) reform, as included in the Sharm El-Sheikh declaration, in order to push for a ‘new financial pact with the South’.

The gap between Northern and Southern countries has accelerated in recent years. Countries of the Global South are structurally vulnerable and do not have equal capacity to respond to the impacts of climate change, the COVID pandemic and violence and conflict. While countries of the Global North invested trillions in fossil fuel subsidies, vaccines and in green subsidies, countries of the Global South faced a debt crisis due to more frequent floods and droughts, the rise in interest rates in the EU and the US, higher cost of energy imports, and low vaccination rates. 93% of the most climate vulnerable countries are under debt distress, as are more than 60 countries in the world.

The 2023 Bridgetown Initiative, advanced by Barbados’ Prime Minister Mia Mottley and supported by various governments worldwide, seemed to provide important opportunities for a reformed international financial system as a female Global South leader was setting the agenda. However, the Initiative short-term list of proposals to change under the current financial structure fail to articulate a response to the multiple global crises so that social and environmental well-being for billions of people throughout the world are ensured for decades to come.

Our expectations for progressive change and an inclusive and democratic process are now far from what was initially anticipated. The few proposals from the Bridgetown Initiative have been watered down, (e.g. changes in the debt architecture) have been ignored. Only some Southern governments have been invited to attend the Paris Pact Summit, further perpetuating inequalities in the governance of the IMF and the World Bank, and the sharing of information for civil society organisations willing to engage has been slow, secretive and exclusive. This is clear evidence that the Summit does not aim at systematically reforming the international financial architecture, but rather tweak the current financial structures to scale up debt- and conditionality-creating finance.
The themes of the working groups fail to provide a focus on transformational reforms. Instead there is continued fixation on supposed solutions that have failed thus far, such as the acceleration of private finance and debt swaps.

Indus Consortium, Don’t Gas Africa, Alternative Law Collective, Policy Research Institute for Equitable Development, Ecumenical Institute for Labor Education and Research, Fundación Ambiente y Recursos Naturales, Don’t Gas Africa and Recourse propose some critical policy reforms for an IFI reform that respond to what organisations in the most vulnerable countries and communities have been striving to achieve for years.

**Reforming the international financial system: annual conditionality-free Special Drawing Rights (SDR) issuances, debt justice and international taxation**

Around one third of the world’s countries are right now under debt distress, and climate vulnerable countries are overrepresented in these. The Global Financial Safety Net, to which the IMF is central, is failing to properly respond to the climate and development crises. This is the case for climate extreme events which are pushing countries that were not responsible for the climate crisis into further debt. Loss and damage and adaptation finance need to be urgently scaled up, and this can only be well done by increasing grants. Long-term concessional finance and debt cancellation are necessary for the mid- and long-term impacts of climate change that can only be countered by adaptation policy.

The need for international finance will increase in the upcoming years for investments in adaptation and mitigation. The IMF should ensure new annual Special Drawing Rights (SDRs) issuance rather than rechanneling them. This would provide hard currency for countries to finance their imports related to climate policy or repay debt and alleviate pressures to accelerate harmful exports like fossil fuels.

Due to the over-representation of Global North countries on the IMF Board, these countries received two thirds of SDRs issued in 2021. The Resilience and Sustainability Trust (RST) was created for developed countries to rechannel their SDRs, transforming them in this way into debt- and conditionality-creating instruments, depriving these assets of their main benefit. In the case of Bangladesh, these policy conditionalities involve the reduction of energy subsidies without proper reshifting to renewables or accounting of distributional impacts. This has been the norm for the IMF in the last few years.

“There are legitimate doubts about whether there has been genuine financial reform in the
IMF under the COP framework, and whether the Fund is in fact fulfilling its obligations under the Paris Alignment. The reality is that the IMF has yet to develop an understanding of climate compatible finance. The RST mechanism remains tied to traditional policy frameworks, which have failed to solve the developmental crisis in the Global South, and now look set to prove themselves entirely inadequate for solving the global climate crisis” said Zain Moulvi from ALC.

Moreover, the IMF should coordinate efforts to guarantee debt cancellation for climate vulnerable countries to ensure more fiscal space for countries of the Global South. A correct assessment of the wrongdoings of the current international financial system would allow people to monitor and audit what has been the use of the debt their governments have undertaken to assess how legitimate it is for them to repay it. This should include reviewing the ‘preferred creditor status’ of IFIs.

In order to ensure an adequate new financial pact, countries of the Global North must ensure fast and effective debt restructurings including cancellation when needed, from bilateral, multilateral and private creditors through a UN-sponsored workout mechanism, as has been proposed by civil society.

**In Paris for Paris! Phase out of public finance to fossil fuels, explicitly excluding gas despite the EU taxonomy’s content**

The IPCC clearly states that global greenhouse gas emissions need to peak by 2025 and be cut in half by 2030 to keep the Paris Agreement’s goal of holding global average temperature rise to 1.5°C within reach. A “new financial pact” must be the opportunity to transform public finance to address the climate emergency as an absolute and urgent priority. The Paris Finance Pact must ensure that leaders commit to stop funding or directly and indirectly supporting fossil gas and related infrastructures across all their financing instruments as well as their technical assistance and policy advisory services.

“The Paris Pact should align countries to deliver on the Paris Agreement. This means working fast together to realign finance with a sustainable renewable future, to commit to rapidly scaling back support for fossil fuels from the global North, and to finance a sustainable renewable future in the global South, that leapfrogs gas lock-in, and focuses on energy security, energy access and sustainability” said Fiza Qureshi of Indus Consortium, Pakistan.

They must rule out support for all oil, coal and fossil gas, including co-firing of power stations, gas for hydrogen, the gasification of coal, the building of ports that facilitate the trade of liquefied natural
gas, carbon capture and storage that simply prolongs the use of fossil fuels and large harmful hydro projects.

There is no justification for mobilising capital to support climate adaptation and resilience, whilst also continuing to finance the root of the problem, i.e. fossil fuels. It is giving with one hand and taking away in gross handfuls with the other.

It is also disingenuous to believe that private capital will serve the laudable aims that seem to be embedded in the intent of new capital mobilisation. At Recourse we have seen the negative impacts for communities and ecosystems of intermediated finance to private enterprise time and time again.

**Example: Java 9&10 coal-fired power stations in Indonesia**

The 2,000 MW Java 9&10 coal project in Indonesia is currently still in construction (adding 2 new coal fired power stations to the existing 8 in the Suralaya complex in Banten province). This project is an example of how the World Bank’s private sector arm, the International Finance Corporation (IFC), can have huge climate impacts when making investments through financial intermediaries, which makes them harder to oversee and has allowed climate lending pledges to be worked around.

In 2019 the IFC took an equity stake in Hana Bank Indonesia, and signed it up to the Green Equity Approach to reduce coal exposure to zero or near zero by 2030. But in 2020 Hana Bank Indonesia provided loans to PT Indo Raya Tenaga to develop the Java 9&10 coal fired power stations. The Sub-project loans to Java 9&10 do not mature until 2035.

These two new coal fired power stations will add 10 million tonnes of CO2 per annum and 250 million tonnes over 25 years (equivalent to the annual emissions of Spain, or Thailand).

Recourse’s partners working in the area witness severe air and water pollution levels. Respiratory problems already account for over 30% of local disease, and this is according to the project’s own Environmental Impact Assessment.

The Paris PACT has an immense responsibility to ensure governments agree to change the course of history and to put themselves at the forefront of the just energy transition, that absolutely and unequivocally says no to any support for fossil fuels.

**Acceleration of international public finance to sustainable and local renewables**

International public finance for renewable energy investments is currently insufficient and not well enough targeted to meet the challenges of the energy transition. The Paris Pact Summit aims to address this challenge with additional capital channelled through public finance institutions, but without a clear direction on how such resources should be used in alignment with Paris agreement.
objectives and broader just transition concerns. Although limited in volume, public finance plays a crucial role in addressing these challenges. International finance institutions including the World Bank Group and the IMF play a catalytic role by helping create the fiscal and policy environment to accelerate the deployment of renewable energy sources at the country level. They also define the standard for private and public financial institutions in ensuring their investments are aligned with environmental and social standards. Further, these institutions set the narrative of what ‘clean energy’ means through their policy definitions that are largely based on the underpinning neoliberal extractivist model of development which allows climate injustice to persist.

Publicly backed finance for the energy sector should only be used to support the renewable energy transition and rule out finance for fossil fuel development. Likewise, public finance institutions must also refrain from supporting untested technologies, unsustainable and uneconomic solutions such as carbon-capture and storage (CCS), green hydrogen, large hydro, industrial biofuels, and nuclear power. It is crucial to ensure stronger human rights protections are in place especially in the mining sector, including for critical transition minerals, or land rights in the case of solar, wind, and geothermal energy production which are all expected to grow exponentially as demand for clean technology increases. Last but not least, public finance must focus on guaranteeing universal energy access especially for poor and vulnerable communities, including women, children, and indigenous peoples.

“A just energy transition cannot be achieved with mere technocratic and market-based solutions nor some technological fix. Any IFI reform must be anchored on supporting the transformation of developing economies that will allow them to create a path for national industrialisation and ensure a just and equitable transition to a renewable energy future,” said Rochelle Porras of Ecumenical Institute for Labor Education and Research (EILER), Philippines.

We ask for the Paris Summit for a New Global Financing Pact to reset the objective of the IFIs to prioritise:

- debt reduction, more grants-based finance and build resilience of countries in the Global South in the face of climate change; and
- holding global average temperature rise to 1.5°C within reach by accelerating the complete phase out of all fossil fuels and accelerating the transition to sustainable renewable energy economies.
- To enshrine the ‘do no harm’ principle in its working approach and avoid policy conditionalities that override countries’ agency over their development pathways
We recommend the following immediate responses from the World Bank and IMF:

1) For the World Bank and IMF main shareholders to acknowledge the need to provide more fiscal space for countries’ green and just transitions;

2) The World Bank to ensure publicly backed finance for the energy sector goes to truly sustainable renewable energy solutions, and rule out support for fossil fuel development including fossil gas, and untested technologies;

3) For the IMF to provide annual issuances of SDRs to low- and middle-income countries for mitigation, adaptation and loss and damage without damaging conditionalities;

4) For the IMF to develop an effective debt workout mechanism that ensures proper debt cancellation for countries to achieve green and just transitions;

5) Transparent and inclusive consultation process of the MDB Reform and finance mobilisation processes together with civil society and project-affected communities

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