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EUROPEAN DEVELOPMENT FINANCE IN PERMA-CRISIS

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Outline

Acronyms

AFD	*Agence Française de Développement*
AfDB	African Development Bank
BAG	Business Advisory Group
CAF	Capital Adequacy Framework
CFA	Co-financing Framework Agreement
DFI	Development finance institution
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
ECDPM	European Centre for Development Policy Management
EDF	European Development Fund
EDFI	Association of European Development Finance Institutions
EFAD	European Financial Architecture for Development
EFP	European Financing Partners
EFSD+	European Fund for Sustainable Development Plus
EIB	European Investment Bank
ETTG	European Think Tanks Group
EU	European Union
EUBEC	EU Platform for Blending in External Cooperation
GEMs	Global Emerging Markets
GNI	Gross national income
GSSS bonds	Green, Social, Sustainability and Sustainability-linked bonds
ICCF	Interact Climate Change Facility
IDDRI	*Institut du Développement Durable et des Relations Internationales*
IDFC	International Development Finance Club
IDOS	German Institute of Development and Sustainability
IFC	International Finance Corporation
IFI	International financial institution
IID	International investment for development
IMF	International Monetary Fund
IPA III	Instrument for Pre-accession Assistance
JEFIC	Joint European Financiers for International Cooperation
JETP	Just Energy Transition Plan
KPI	Key performance indicator
LIC	Low-income country
MDB	Multilateral development bank
MFF	Multiannual Financial Framework
MIC	Middle-income country
MIGA	Multilateral Investment Guarantee Agency
MSME	Micro-, small and medium-size enterprise
NPBIs	European National Promotional Banks and Institutions
NDICI-GE	Neighbourhood, Development and International Cooperation Instrument – Global Europe
NRB	Czech National Development Bank
ODA	Official Development Assistance
ODI	Overseas Development Institute
PDB	Public development banks
PPF	Partnerships Platform for Funds
PRGT	Poverty Reduction and Growth Trust

RST	Resilience and Sustainability Trust
SCDI	State-contingent debt instrument
SDG	Sustainable development goal
SDI	Sustainable development investment
SDR	Special drawing right
T&C	Transferability and Convertibility
TCFD	Task Force on Climate-related Financial Disclosures
TDB	Trade and Development Bank
TEI	Team Europe initiative
TOSSD	Total Official Support for Sustainable Development
UNEP FI	United Nations Environment Programme Finance Initiative
WB	World Bank

Preface

San Bilal

Our world is in deep trouble. We are experiencing what IMF Managing Director Kristalina Georgieva described as the era of shocks, and the ECB President Christine Lagarde and others referred to as an age of perma-crisis. The compound shocks and permanent crises range from climate change, the COVID-19 pandemic, and the Russian war in Ukraine to the rising prices of energy, food and fertilisers, persistent inflationary pressures, rising debt burden and tightened monetary policy. While this crisis-ridden era confronts advanced economies with multiple challenges, they have drastic consequences for many developing countries, putting in grave jeopardy the 2030 Agenda for Sustainable Development. Yet, in the words of UN Secretary-General António Guterres, “in the face of these cascading crises, we are far from powerless. There is much we can do, and many concrete steps we can take to turn things around. […] Let’s come together, starting today, with ambition, resolve and solidarity, to rescue the Sustainable Development Goals [SDGs] before it is too late.”

This is precisely what the European Union (EU) has been doing: adopting ambitious agendas and plans for action, vigorously mobilising its policies and instruments to tackle the challenges of our times at home and abroad.

A strengthened European Financial Architecture for Development (EFAD), combined with reforms of the international financial system, provides the opportunity for the EU and its Member States, their financial institutions and development agencies to pursue more strategic approaches to development finance and sustainable investment aligned to European values and principles, goals and priorities, based on a ‘policy-first’ approach. The Team Europe approach and Working Better Together process allow the EU and its Member States to better coordinate their efforts, within the EU budget and beyond, to mobilise at-scale development resources for greater impact in a more (geo-)strategic and complementary way, including in poorer, more fragile and conflict-sensitive countries. The Global Gateway strategy should allow Europe to better project itself abroad, articulating a vision for quality infrastructure development anchored in European strategic objectives, including other geo-political actors. By pursing a reform agenda, European actors can help foster a more effective and impactful European and international development finance agenda, in line with developing countries' needs, priorities and ownership.

This e-book regroups brief insights from some key actors on concrete ways the EU, its member states and their (financial) institutions for development can best respond to the challenges of our times in a more strategic, developmentally sustainable, impactful and inclusive manner, in the context of the international and European financial architecture for sustainable development.

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Section I

Overview

Chapter 1

European development finance in the crisis-ridden era: Team Europe and the EFAD for a greener and more sustainable impact

San Bilal, Senior Executive and Associate Director, ECDPM

1. Rising uncertainty in a state of perma-crisis

1.1. Background

Our world is in deep trouble. We are experiencing what the Managing Director of the International Monetary Fund (IMF) Kristalina Georgieva described as the era of shocks, and the President of the European Central Bank (ECB) Christine Lagarde and others referred to as an age of **perma-crisis**. The compound shocks and permanent crises range from climate change, the COVID-19 pandemic, and the Russian war in Ukraine to the rising prices of energy, food and fertilisers, higher inflation, rising debt burden and tightened monetary policy. The prospects look bleak. Food crisis and energy shortage will further increase inequality, poverty and political instability. International tensions, rising protectionism and sanctions threaten to lead to a geopolitical fragmentation and de-globalisation process, marked by strategic autonomy, reshoring, friend-shoring, and more diversified sourcing, reshaping global value chains along geostrategic lines.

While the repercussions of the multiple crises are felt globally, their impact varies according to countries and regions. This crisis-ridden era confronts advanced economies with multiple challenges, but it has drastic consequences for many developing countries, particularly in Africa, where the IMF warns of a "dark period", putting in **grave jeopardy the 2030 Agenda for Sustainable Development (SDGs)**. A general trend emerges of a "two-track recovery" between advanced economies and developing countries, characterised by a "great finance divide", highlighting the increasing asymmetry in which the crises hit poorer countries and their limited capacity and support received to respond to them.

Yet, in the words of UN Secretary-General António Guterres, "in the face of these cascading crises, we are far from powerless. There is much we can do, and many concrete steps we can take to turn things around. […] Let's come together, starting today, with ambition, resolve and solidarity, to rescue the Sustainable Development Goals before it is too late."

2. The EU’s ambitious sustainable development framework

This is precisely what the European Union (EU) has been doing: adopting ambitious agendas and plans for action, vigorously mobilising its policies and instruments to tackle the challenges of our times at home and abroad. With the adoption of the €79.5 billion Neighbourhood, Development and International Cooperation Instrument – Global Europe (**NDICI-GE**) under the EU budget for the period 2021-2027, the EU can deploy strategically and flexibly this single unified development instrument to support developing countries more effectively. The establishment of the European Fund for Sustainable Development Plus (**EFSD+**) provides an open architecture for public development banks (**PDBs**) and development finance institutions (**DFIs**) to leverage public and private finance through **EU guarantees** and **blended finance**, to achieve more ambitious inclusive development and green impact.

The EU also fosters a common development finance approach, better coordinated. A strengthened European Financial Architecture for Development (**EFAD**) provides the opportunity for the EU, its Member States, and their financial institutions and development agencies to pursue more strategic approaches to development finance aligned to European principles, values, goals and priorities based on a **‘policy-first’ approach**. The **Team Europe** approach and Working Better Together process allow the EU and its Member States to better coordinate their efforts, within the EU budget and beyond, to mobilise at-scale development resources for greater impact in a more (geo-)strategic and complementary way, including in poorer, more fragile and conflict-sensitive countries. The external dimension of the **Green Deal** and the **Global Gateway** strategy should allow Europe to better project itself abroad, articulating a green vision for climate mitigation and adaptation, nature protection and biodiversity, addressing infrastructure development and broader development needs, anchored in European strategic objectives, combining development and geo-political ambitions. In doing so, the EU is also committed to inclusive approaches, supporting women and youth, and leaving no one behind.

3. Need to step up crisis responses with constrained means

However, the current state of play is not enough in the face of historical combined shocks, unprecedented uncertainties, and rising vulnerabilities. The international community, and Europe, must **rise to the challenge**, mobilise energies and resources, and deploy instruments in innovative ways at scale.

The EU means are limited. Increased domestic spending to address the socio-economic effects of the COVID-19 pandemic, the Russian war in Ukraine, the energy crisis and inflationary pressures do strain public budgets in Europe. On the international front, support for Ukraine is a military, economic, development and geostrategic priority for the EU, including in terms of European resources allocations, notably through the EU Recovery and Resilience Facility.

While the integrity of the EU budget is preserved, and resources will not be reallocated away from development objectives, including geographical allocations, this is not necessarily the case at the level of EU member states. Several donor countries are reducing their development budget or redirecting some of it to address the consequences of the Russian war in Ukraine and cover the costs of hosting refugees. Besides, even under the EU budget, resources are insufficient. In 2018, the European Commission proposed an NDICI-GE budget more than 10% higher than the adopted one. This was before the COVID-19 pandemic and the Russian aggression on Ukraine, not to mention the fast-rising climate change challenges. Hoping to tackle multiple crises of historical proportion with means lower than those foreseen in the absence of crises seems ludicrous. There can be no business as usual.

There is, therefore, a **need to move away from seeking only traditional development cooperation solutions** and simple calls for more aid, which, although desirable, may not be easy to achieve. Instead, it requires better channelling limited resources through catalytic approaches and operating in more agile and flexible manners through enhanced coordination, building better on existing mechanisms and adopting new approaches. It also entails identifying additional resources in one way or another.

Addressing systemic challenges through international monetary and financial approaches is part of it. **Mobilising development finance at scale**, in various formats, for more differentiated and targeted impacts should also be a priority. In practice, a more ambitious approach could entail, among other things, some of the following elements.

4. Broader development (finance) avenues

4.1. Address growing debt vulnerabilities and distress in a concerted manner

While a global **debt crisis** may be avoided, an increasing number of emerging and developing countries face increasingly acute **debt vulnerabilities** and possible distress. It is urgent to consider **systemic debt solutions**, including precautionary measures recently promoted by the IMF. The approach adopted for Zambia's debt restructuring is encouraging. Bringing traditional and emerging donors (read mainly China) together with private creditors is critical. The EU member states should collectively be more active in stimulating coordinated debt initiatives under the aegis of the IMF. They should also actively promote innovative solutions, such as **state-contingent debt instruments** (SCDIs), linking a sovereign's debt service payments to its capacity to pay, **legal tweaks and statutory options** to encourage private creditor participation, and **debt swaps** (e.g., debt-for-climate, debt-for-nature and debt-for-sustainability swaps). SCDIs provide for identifying, ex-ante, criteria and threshold conditions that could automatically trigger debt payment suspensions or restructuring. The G20 Common Framework for Debt Treatments could be strengthened and adjusted to promote the legal duty of private creditors to cooperate in good faith in sovereign-debt relief and restructuring. Debt-for-climate swaps could also be more broadly encouraged, building on the experience of a few developing countries such as Barbados and Seychelles and the bilateral initiatives by some EU member states such as France, Germany, Italy and Spain. They could also be linked to the issuance of Green, Social, Sustainability and Sustainability-linked bonds (**GSSS bonds**) to promote green, blue and sustainable investments in emerging and developing countries. The EU could collectively work out some of these options and others and pursue them through coordinated strategic engagement in the relevant forums, including the Paris Club, G20 and IMF.

4.2. Rechannel SDRs at scale, including through MDBs

To face the COVID-19 pandemic, the IMF issued the equivalent of US$650 billion of new special drawing rights (**SDRs**) in August 2020. Two-thirds of the new SDRs went to advanced economies, which have little or no need for fit, whereas 98 developing countries have used SDRs in some way; 30 nations, mainly developing countries, have used 90% or more of their SDRs allocation. African countries received a total of SDRs equivalent to US$33 billion only. The G7 and G20 countries committed to **reallocating US$100 billion** of their SDRs to countries in need.

The preferred channels are through the IMF: the well-established Poverty Reduction and Growth Trust (**PRGT**) concessional lending facility for poorer countries and the newly set up Resilience and Sustainability Trust (**RST**), which aims to channel SDRs to developing countries to help build resilience to external shock and address longer-term structural sustainability challenges of low and middle-income countries, including climate change and pandemic preparedness. Some member states have shown the way from the European side, such as France, Italy and Spain, which committed to reallocating 20% of their SDRs. French President Emmanuel Macron reportedly promised to bring France's rechannelled share to 30% to respond to the resulting crisis from the Russian war in Ukraine, encouraging other G20 leaders to do the same. Germany and Spain were among the first IMF members to effectively contribute to the RST. Total reallocation pledges to the RTS now amount to US$37 billion and could go up as high as US$55 billion. A few other EU member states have made smaller SDR-related pledges, but most have not made any commitment yet. Transparency is lacking in that respect. Yet, despite some declarations at the EU-Africa Summit, the EU has not collectively exhibited the leadership and commitment that one could expect from the world's biggest development actor. Besides, most current pledges have not yet been operationalised, leaving developing countries in need facing the crises without additional support from SDRs. Other funding contributions are also required for the subsidy account of the PRGT, to which only a few EU member states have contributed, together with leftovers from past European Development Funds (EDFs). The **EU could adopt concerted positions and collective commitments at the IMF towards the speedy rechannelling of SDRs towards countries most in need**. This could include **special commitments to Ukraine**. The President of the European Council, Charles Michel, is reportedly favourable to a possible EU member states' collective commitment to reallocating 10% of the SDRs specifically to Ukraine. But no public announcement by the Council has been made yet to that effect. If it does - and it should, commitments should be made towards Ukraine, which desperately needs support, and vulnerable economies, most notably in Africa.

The most innovative and potentially impactful way of **rechannelling SDRs** would be **through multilateral development banks (MDBs)**, the so-called prescribed holders. MDBs could set up hybrid capital instruments for that purpose, structured to preserve the required reserved asset and liquidity characteristics of SDRs, ensuring minimal risk to increase their lending capacity and leverage investments in a catalytic manner. The African Development Bank (AfDB) has set up such an instrument, cleared by the IMF, ready to receive SDRs directly rechannelled by some advanced economies. Others may follow suit. The AfDB claims it could reach a leverage ratio of 3 to 4, which means that a US$2.5 billion reallocation of SDRs could lead to up to US$10 billion in investments. This is the kind of innovative solution that resource-constrained advanced economies should look for to support more vulnerable countries.

The problem for EU member states is that the ECB interpretation of the rules prevents them from rechannelling SDRs to entities other than the IMF. That's where the EU should become more active to overcome the deadlock. The **EU could consider reviewing the ECB position and identify mechanisms that would ensure the SDRs' liquidity and reserved asset nature, in line with ECB's concerns, to be used by MDBs**. Indirect channels through the IMF could be carefully considered. These include RST support for local green bond issuance and support to MDBs, for instance for SDRs bond issuance, options that merit proper attention and design. Finally, some EU member states could **consider budgetary contributions equivalent to SDRs** for MDB-dedicated mechanisms, which could have similar leveraging effects on investment.

4.3. Strengthen and adapt MDBs to unleash their potential

More generally, the EU could also **adopt common positions** on proposals to better unleash the potential of **MDBs**. At the Washington DC gathering of Bretton Woods Institutions this Autumn, a new momentum seems to have emerged to **boost climate finance**, notably by the World Bank and the IMF (notably with the RST). The G20 Independent Review of Multilateral Development Banks' **Capital Adequacy Frameworks** made a range of very concrete recommendations to increase the lending capacity, leverage and impact of MDBs. **Recommendations** include: considering a prudent share of **callable capital** (i.e. contingent commitments by governments to MDBs, which could be converted - 'called'- into paid-in capital in case of potential default) in assessing MDBs' capital adequacy; reconsidering MDBs' approaches to **risk tolerance and appetite**; provide opportunities for **non-voting**

capital in the form of equity investments (paid-in capital) in MDBs and **hybrid instruments** for interested governments (e.g. donors) and private investors (e.g. institutional and philanthropist investors); support and scale up proven **risk transfer mechanisms** (e.g. guarantee and securitisation) to free up MDBs capital for more lending; and share disaggregated anonymised **statistics on credit performances** (from the Global Emerging Markets Risk Database - GEMs) to improve the accuracy of risk assessments (useful for other development banks, private investors and credit rating agencies) by private investors and credit rating agencies. A paid-in **capital increase** could also be considered for some MDBs.

MDBs should also better align their activities with the Paris Agreement and the SDGs, including by **adopting more transformative approaches beyond individual deals**. Dedicated **collaborative frameworks**, including between MDBs and national development banks, could be scaled up, building on the **Finance in Common initiatives**.

EU member states could identify together, in a Team Europe approach, priority consensus areas for reforms which they could collectively push for as shareholders through MDBs' boards.

4.4. Boosting green finance

Building on international commitments and mechanisms, **green finance**, including climate, nature protection and biodiversity, should be significantly boosted. The failure at the COP26 to reach the US$100 billion per annum climate finance commitment for developing countries illustrates the glaring financing gap and the need to adopt a renewed approach to development finance for climate change. While boosting finance for climate mitigation and the net zero-carbon transition is imperative, additional efforts should be made to **mobilise at-scale climate finance for adaptation, biodiversity, and nature protection**. Climate adaptation accounts for about 7% of global climate finance. Yet, developing countries, particularly poorer countries, face greater exposure to climate change and have a lower capacity to adapt to it. They should therefore benefit from greater support for adaptation and biodiversity and nature conversation. This means promoting **climate-resilient investments** through **public-private endeavours** and **risk mitigation** and adopting conducive macroeconomic and fiscal policies and regulations tailored for adaptation. It also means engaging more actively in **sub-sovereign climate adaptation operations** to reach out to rural areas affected by climate risks (from floods to droughts) and fast-growing urban centres exposed to climate changes.

The EU, its member states and financial institutions for development can play a leading role in that respect. Work on **sustainable finance taxonomy** should be systematically harnessed to development finance and adapted to more vulnerable contexts. The EU should encourage and actively support collaboration among financial institutions and relevant stakeholders on climate, nature and biodiversity. This includes relevant initiatives such as the United Nations Environment Programme Finance Initiative (**UNEP FI**), Task Force on Climate-related Financial Disclosures (**TCFD**), and the Adaptation & Resilience Investors Collaborative. European DFIs and PDBs could also cooperate on **more cooperative and standardised approaches to climate risk assessment**, including data collection and analysis, sharing of methodologies and best practices, and promoting transparency and harmonised reporting.

4.5. Actively combating illicit financial flows

While mobilising and reallocating resources to more vulnerable economies is essential to help them face multiple shocks and increased uncertainties, it is also key to support them in their efforts to mobilise domestic resources and retain legitimate revenues. In this respect, **fighting illicit financial flows** should be a priority not only for developing countries but also for advanced economies, as the main recipients of such illicit flows. The EU has made commitments in that sense. It should pursue active avenues, within the EU, the OECD and other relevant international fora, as well as with its partner countries, to better identify and effectively combat illicit financial flows.

5. Strengthening the EFAD

The European financial architecture for development has already been strengthened by a number of initiatives, including inter alia: the establishment of the **EFSD+**, the adoption of the **Team Europe** approach, the identification of Team Europe initiatives (**TEIs**), the launch of the **Global Gateway**, the programming exercise of the **NDICI-Global Europe**, the setting up of **EIB Global** - the new branch of the European Investment Bank (EIB) for its operations outside the EU, the formation of the Joint European Financiers for International Cooperation (**JEFIC**) - the "network of European bilateral banks and financial institutions which work with public sector partners in developing countries and emerging economies", currently comprising AECID (Spain), AFD (France), CDP (Italy) and KfW (Germany). Steps were also taken to further strengthen the cooperation and common approaches among and with the members of the Association of European DFIs (**EDFI**), the **EIB** and the European Bank for Reconstruction and Development (**EBRD**), and with other key stakeholders, including members of the Practitioners' Network for European Development Cooperation. The **governance** of the Global Gateway, EFSD+ and EIB Global, among others, are also meant to contribute to a better articulation of the EFAD. Efforts to promote a **collective EU response to multiple crises**, from the pandemic to the Russian war in Ukraine, have further stimulated cooperation among actors of the EFAD.

Yet, **strengthening the EFAD**, its (geo)strategic direction, articulation, approaches, connections, instruments, respective stakeholders and ultimately impact (inclusivity, gender-sensitivity, green and sustainability), **remains a work in progress**. The largest room of all is the room for improvement. A number of avenues should be considered.

5.1. Enhance the strategic coordination of a fragmented governance

The polycentric nature of the EFAD governance provides some flexibility and focus. But it is mainly articulated around key instruments, policies and initiatives. This results in a fragmented governance framework which **may lack some internal coherence and overall** strategic **direction if not well articulated by the EU, its member states and their institutions for development, and beyond**.

Coherence efforts towards strategic and operational coordination should be conducted at the level of the EU, by the European Commission, as well as between and within the EU member states and relevant institutions. These include, among others, articulating the coherence and synergies between the EFSD+ Strategic and Operational Boards, NDICI-Global Europe and Instrument for Pre-accession Assistance (IPA III) Committees, the governance of individual TEIs, the Global Gateway Board, the Council's respective committees and dedicated groups, the EIB Board and Board Advisory Group on EIB's Global Operations, the EDFI shareholders meetings, the Boards of relevant other MDBs and in particular the EBRD, and in partner country coordination mechanisms, to mention a few.

While some stakeholders understandingly complain about over-burdening layers of strategic and operational coordination, specific attention should be given to **enhancing the coordination of the overall strategic direction and operational implementation of the EFAD, including beyond the EU budget**.

5.2. Avoid overly EU-budget and EU-institutions-centric approaches

The **European Commission plays a central role** in the steering and effective implementation of the EFAD, **guided by the Council**. The adoption of new regulations (e.g., NDICI-GE, IPA III), instruments (e.g., EFSD+), new EU initiatives (e.g. European Green Deal, Global Gateway, REPowerEU), new approaches (e.g. Team Europe), proposed by the European Commission, and the programming process of NDICI-GE have given a strong impetus to **focus on the EU budget and mechanisms**.

Yet, to be truly effective, **the EFAD should also build on EU member states' own initiatives, coordination efforts, institutions, mechanisms and budgets**. These may, but do not necessarily need to be harnessed to the EU budget and initiatives. This is also the spirit of the Team Europe approach, not yet sufficiently embarrassed enough by some EU member states, which perhaps excessively rely on the initiatives of the European Commission. This may be an infant ailment, specific to the early stage of the Team Europe and EFAD setting up and implementation.

Going forward, EU member states and their (financial) institutions, as well as EIB Global and the EBRD, should not shy away from **branding their joint initiatives under the EFAD and Team Europe flags**. The **JEFIC** initiative among European PDBs is an important step in that direction. So are the numerous initiatives undertaken by EDFI, among its members and together with other European and non-European like-minded DFIs and PDBs, including the EIB and the EBRD. Initiatives such as the European Financing Partners (**EFP**) and the Interact Climate Change Facility (**ICCF**) should be boosted and replicated when relevant, and better highlighted under the EFAD in a Team Europe spirit, rather than kept as technical mechanisms mainly known by the financial insiders only.

The **direct partnership of EU donors with the EIB**, under the standardised Partnerships Platform for Funds (**PPF**), and the **EBRD multi-donor funds**, such as the recently approved EBRD-Ukraine Sustainable Growth Multi-Donor Account, **provide attractive frameworks for strengthening the Team Europe approach on financing for development beyond the EU budget**. These initiatives could be **boosted, expanded to other financial institutions and build upon** in innovative ways under the EFAD umbrella.

5.3. Promote more partnerships and wider collaboration

Strengthening the EFAD should require two types of endeavours: 1) continuing to build more partnerships and coordination among a wide range of European stakeholders, and 2) ensuring an open and transparent EFAD, not introverted on the EU, but also reaching out internationally and with partner countries.

5.3.1. Within Europe

EFAD partnerships and coordination within Europe should be pursued at several levels. First, **among European financial institutions for development (DFIs and PDBs)**, which is currently composed of four blocks: EDFI (for DFIs), JEFIC (for PDBs), EIB Global and the EBRD. These financial institutions could set up a joint forum, more structured than the current most ad hoc cooperation, where they could jointly address (geo)strategic considerations and operational priorities. Some smaller European financial institutions, also partly involved in international development, are currently left out of these frameworks and should be included in the EFAD. This is the case in particular of some European National Promotional Banks and Institutions (NPBIs), such as the Czech National Development Bank (NRB).

More broadly, greater synergies and complementarities should be identified **between European PDBs/DFIs operating outside the EU and European NPBIs engaged mainly within the EU**. These would help link EU internal dynamics and policies with external dimensions affecting sustainable development. A case in point is also around the green agenda and green finance in particular.

Greater engagement should also be sought with the European private sector and, in particular, European private investors. The setting up of the Global Gateway Business Advisory Group (**BAG**) is a potential major evolution in that direction, although the roles of European business, let alone **European private financiers**, are yet poorly defined and understood in this respect. Harnessing European institutional and philanthropic investors, as well as major commercial banks and financial institutions, including **private insurers**, could be a significant evolution for the EFAD. An **EFAD platform for European public-private financiers' collaboration** and strategic synergies on green and sustainable development could be established.

The EFAD could also contribute to **fostering greater synergies and complementarities between European public (financial) institutions with a commercial objective** (supporting European private actors, such as the **export credit agencies** and investment support and promotion institutions), **and those with a development mandate** (European **DFIs and PDBs**). Such complementarity could usefully serve to harness European business and private finance to SDGs and development finance objectives.

European public development actors should also enhance their cooperation. Building on past and existing collaboration platforms and groupings, such as the EU Platform for Blending in External Cooperation (EUBEC), the Practitioners' Network for European Development Cooperation, EDFI and JEFIC, an **EFAD platform for public development actors** could usefully regroup European donors, implementing agencies, DFIs and PDBs (including EIB Global and EBRD). This could serve both for strategic purposes and for fostering exchanges of knowledge and better practices, as well as stimulate innovative approaches and initiatives, including among sub-groups of development actors. In particular, it would be valuable to better align and synergise donors, development agencies, and DFIs/PDBs activities for:

- strategies and implementation of **blended finance** operations;
- **project preparation** and the development of a bankable **pipeline** of green and developmentally impactful projects;
- **technical assistance** and accompanying measures **combined with development finance**, including through **donors-DFIs/PDBs structures** such as the EBRD multi-donor funds and EIB PPF, and their equivalent at sub-group and national levels (possibly combining the efforts of several member states);
- **innovative approaches and instruments**, including **local currency financing** (e.g. fund and structures such as TCX and EIB local currency facility; guarantees such as EDFI Transferability and Convertibility Facility (T&C)), **policy-based financing** (grants and loans, policy support), **multi-stakeholder funds** (e.g. Dutch Fund for Climate and Development), etc.;
- **eco-system development**, policy and regulatory environment, and structural **transformative impact**
- **monitoring, evaluation and reporting** criteria and approaches;
- engagement in **poorer and more vulnerable economies**, and **fragile** and conflict-affected contexts (including on security and reputational risks);
- **gender, youth and leaving-no-one behind** approaches;
- **climate, biodiversity and nature protection approaches**, including climate risk assessment and management, green finance and **ecosystem support**, **local issuance** of green, social, sustainability and sustainability-linked (**GSSS**) **bonds;**

- approaches and initiatives responding to **rising uncertainty** and **emergency crisis response**, recovery endeavours and longer-term resilience and sustainability;
- fostering **local presence**, stakeholder engagement and networks.

5.3.2. Outside the EU

The Team Europe approach is meant to foster greater collaboration, synergies and coherence among EU actors, including in the context of the EFAD. But it should not become a closed EU shop. Some international and EU partner countries' stakeholders have challenged the Team Europe approach, informally referring to it as 'the EU to the exclusion of non-European' approach.

To avoid such misunderstanding, it is important that the EU collectively further **promotes a more inclusive approach towards like-minded and partner countries' stakeholders and institutions**. This is the case notably with international organisations, such as the United Nations institutions, MDBs, G7, G20 and other linked-minded collaborative initiatives, including global vertical funds (on climate, health, etc.).

In the context of the EFAD, the **European financial institutions could also foster better articulated, more structured and more transparent collaboration and partnerships with other non-EU DFIs and PDBs**, including with continental, regional and national ones (**MDBs**, RDBs and NDBs and equivalent). The EIB and EBRD could help anchor such worldwide MDBs' cooperative approaches, and work better with PDBs in developing countries, strengthening their governance, capacities and access to finance and engaging in joint operations, including on project origination. **European PDBs and DFIs, together with donors when needed, should more systematically engage with local PDBs/DFIs as the 'last-mile partners'**. Such local institutions can help prepare a continuous pipeline of projects, anchored on local knowledge and realities, attuned to local stakeholders' priorities and challenges. Even more importantly, by engaging and working in a more structured way with local PDBs/DFIs, European (financial) institutions can contribute to building and supporting local institutions' capacity and ecosystems through more transformative approaches through joint operations and interventions. They can also foster engagement with other local stakeholders, from local authorities to local communities, private actors and civil society. Support by European PDBs to local ones can take various forms, including knowledge sharing, technical assistance and capacity building, credit lines, joint operations and co-financing, equity participation in the capital of local PDBs (improving their governance and investment capacity) and public loans to enable increased government shareholding in their local PDB.

5.4. Encourage innovation, reactivity, diversity & harmonisation

The EFAD should encourage the **exchange of experiences and innovative practices** among European development (finance) actors. This can help replicate and scale up innovative approaches (as in the case of some of the proposals submitted to the EFSD and EFSD+). It can also promote a demonstration and learning effects for new approaches, from gender-sensitive approaches, as in the Gender Finance Collaborative and 2X Challenge, to climate adaptation finance, as in the Adaptation & Resilience Investors Collaborative and investment in fragile and conflict-affected environment as in the DFI Fragility Forum.

Innovation can also be stimulated by providing '**innovative funds**', to pilot new approaches and instruments with high potential but perceived as more risky. Some mechanisms can also be developed, such as **syndication** (joint financing), through structured entities - as in the case of the EFP and ICCF, and soon the JEFIC, or more ad hoc or opportunistic cooperation. **Securitisation** should also be considered by European DFIs and PDBs in the context of the EFAD, and with guarantees, if needed, to offload more mature operations from their balance sheet and match the risk appetite of private investors. Various forms of collaboration with private insurers could also be stimulated, to improve risk assessments and information and risk-bearing capacity.

As European DFIs and PDBs establish their own comparative expertise and approaches, they can not only encourage **peer-to-peer learning** but also help contribute to a more **effective division of labour and complementarity**.

Reactivity and adaptability could also be stimulated under the EFAD. This is particularly relevant in the new permanent multi-crisis context characterised by higher uncertainty. European development (finance) actors have to adjust their business models and modus operandi. A more cooperative approach of the EFAD may increase these adjustments and the overall resilience of the European development finance system, as experienced with the Team Europe approach initially triggered as a response to the COVID-19 pandemic. Given the constrained reactive capacity of the EFSD+, alternative structures such as the EIB's PPF and EBRD multi-donor funds can also be mobilised. Similar multi-PDB/DFI multi-donor funds could be set up to complement EU budget mechanisms, in line with EU priorities.

Last but not least, a strengthened EFAD can contribute to fostering harmonisation and standardisation of some procedures, frameworks, criteria, approaches, practices and mechanisms. The EU regulatory and policy frameworks, as well as NDICI-GE and EFSD+, provide ample opportunities to move towards more compatible, harmonised and common approaches. The European Commission, in coordination with the Council, has a central role to play in that end. Grouping of development actors, such as EDFI, which has an ambitious harmonisation agenda, JEFIC, and the Practitioners' Network for European Development Cooperation, as well as leading institutions, such as the EIB and EBRD, including as part of MDBs coordination efforts, can effectively contribute to better harmonisation while respecting the diversity of each actor.

Europe has the potential and capacity to unleash its developmental finance firepower to effectively pursue its agenda: significantly scale up development and climate finance, achieve greater, more inclusive and sustainable impact, and adopt a more (geo)strategic approach based on EU principles, values, interests and priorities. The articulation of the EFAD is a collective effort that should contribute to fostering greater coherence in the actions of the EU and its member states, building on its diversity and complementarity.

Section II

European financial institutions for development in action

Chapter 2

Adjustments needed in Team Europe and European financial architecture development (EFAD) efforts

Bruno Wenn, Outgoing Chair, Association of European Development Finance Institutions (EDFI)

We, at the Association of European Development Finance Institutions (EDFI) – having celebrated our 30th anniversary - are a good road model of 15 European development finance institutions (DFIs) working closely together based on following the lead as an effective and cost-effective mode of collaboration and based on harmonised standards and procedures. And we have a long history of working efficiently with the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), the International Finance Corporation (IFC) and other international, regional and bilateral development financial institutions. And we are looking forward to working with the new European DFIs being planned in some Member States of the European Union (EU).

Underlying the crucial role of the private sector in addressing the multiple crises and recalling the key role of the EDFI members in promoting the private sector in developing countries, especially in Africa, as well as in mobilising the much-needed private sector resources for a green, digital, and inclusive growth, European DFIs welcome the Team Europe approach and the strengthened European Financial Architecture for Development (EFAD). It is the right direction to increase the significance, relevance and impact of European development policy since the approach is meant to foster greater collaboration, synergies and coherence among EU actors. The multiple crises call for concerted and joined actions building on the diversity and complementarity of the many European actors in the European development policy. Today, strategic coordination and cooperation are needed more than ever to tackle the multiple crises. By bringing all relevant players and actors to one table, we have the great opportunity to strengthen the strategic role in coordination as well as enhance complementarity and coherence and, in doing so, efficiency and impact. Therefore, for us, transparency, open architecture, access to information and participation in the discussions are key.

This is still a process in the making, and the launch of the Global Gateway initiative a year ago has indeed marked an important milestone in terms of the EU asserting its geopolitical relevance and ambition. We now have much more clarity with respect to the articulation of Team Europe Initiatives and how they will contribute to Global Gateway. This is much welcome. We also welcome that DFIs and international financial institutions (IFIs) will be included in the Global Gateway governance (i.e., DFI Advisory Group) and this is of course equally reassuring.

Another dimension that remains still to be clarified is how we engage with the private sector. European DFIs' involvement in Global Gateway and EFAD is crucial in that respect, as we have expertise in working with private sector clients, we are the institutions designed for this purpose. We would ideally like to have an EFAD with a focus more towards the objective of engaging further and mobilising the private sector, both the European private sector and the local one.

Still, all these efforts on Team Europe and EFAD will require some significant adjustments:

1. We need to **focus much more on strategy** than technical issues in our coordination. The focus should be on setting the policy considering the different mandates, strengths, and complementarity of the various actors. For example, European DFIs play a key role in investing where the private sector is not ready to invest yet. Therefore, we would also like to ensure that in the policies the right balance is set between additionality and mobilisation expectations of the EU. Where DFI financing is most additional (e.g., in fragile contexts), mobilisation targets must be less ambitious than in sectors where private finance is already present and the DFIs act more as co-investors.
2. For the implementation, we need to **incentivise cooperation and working together**. What is still missing in our view is a governance body, a 'place' where all Team Europe national development banks, DFIs and IFIs can coordinate and agree together with EU Institutions and Member States on the implementation of Global Gateway, and related to this, the European Fund for Sustainable Development plus (EFSD+). EDFI has asked to be represented as an observer in the EFSD+ Strategic Board precisely for this reason, because we believe it would be a relevant body to (i) receive clear political steer from EU Institutions and Member States, and (ii) coordinate views and priorities across European finance institutions at a strategic level. For example, we should be able, as Team Europe, to issue clear statements and/or roadmaps on climate, Ukraine, and blended finance. We need a body that would allow this to happen. For now, the Team Europe Director Generals Meeting are very useful, but we would like there to see a much stronger focus on the strategy for the investment and infrastructure support programmes that will be needed for Global Gateway.
3. We need to be faster and more flexible in using the existing instruments to translate policies into concrete actions. This is especially true now in the midst of multiple crises. Today, the implementation of blended finance programmes remains at a small scale. The programmes are relatively costly to implement and require a long time. Likewise, within existing regulations, there are no incentives to create platforms for joint investments. For example, EDFI Management Company created in 2016 by EDFI members as a platform for joint actions and joint use of EU financial resources for market development is not yet able to get access to EU funding outside of EFSD+ directly as a pillar-assessed institution, although we are hopeful that it will be the case soon. Working with private sector investors require efficiency and flexibility, which are two qualities European DFIs are generally recognised for. This is the reason why we call for a successful roll-out of EFSD+, to consider relying as much as possible on the existing frameworks the DFIs have designed with their shareholders when investing in developing countries, such as those for impact measurement and E&S standards. We would like to see a review of the many financial and other regulations with a view to increase flexibility and speed as well as to reduce cost and time.
4. We need to focus on more harmonisation of standards. EDFI members are working towards developing further the Paris-alignment methodologies and are working towards compliance with the EU Taxonomy - but there is currently no common forum to design harmonised practices. DG INTPA is currently drafting a complex Results Management Framework with very granular indicators that lack practicality and links with existing DFI practice. We would like to see that EU harmonisation and standards are built on what we have already developed with our international and bilateral peers. We risk having different interpretations and different methodologies while the objective for all is Paris alignment.
5. We need to focus much more on policy dialogue and interventions with the aim to create the policy and regulatory environment for structural change and transformation. DFIs and private sector actors will need support from the EU and other donors in building the right business and investment environment as well as setting the right legal and regulatory conditions for sustainable and green investment projects. We believe mobilising private finance will also require that EU resources are dedicated much more to project origination and project preparation. And we need specific programmes to turn unbankable opportunities into bankable ones.

6. We need to scale up by using the guarantees in a much better way to mobilise private sector finance for climate and sustainable development. To be effective and attractive, these tools need to be flexible enough, but we observe that there is still a lot of complexity in structuring blended finance schemes (as well as guarantees) which is hindering the implementation, and the potential to scale those up. In short, we need to be faster, flexible and we need to work with harmonised standards that are practical, usable, and based on already existing international standards.
7. And finally, we need to enable our international network as leverage for European approaches. We are concerned that some of our international partners see the Team Europe Approach as a closed EU shop. But working together beyond Europe is key in terms of relevance and significance. For example, within the G7, the European Development Finance Institutions work very closely together with our peers in Japan, Canada, and the US to promote gender finance, green finance, and global infrastructure investments. In our coalition for micro-, small and medium-size enterprises' (MSME) financing in Africa, we cooperate with regional development finance institutions in Africa like the West African Development Bank (BOAD), African Development Bank (AfDB) and The Trade and Development Bank (TDB). And finally, with our international and bilateral peers, we are working on joint standards for impact measurement and reporting.

Chapter 3

Development finance: Tackling multiple crises while addressing resilience and global challenges

Lionel Rapaille, Director for Lending Operations in EU Neighbouring Countries, EIB

The world faces a cascade of shocks and crises: the pandemic, and now the Russian aggression against Ukraine, causing pain and devastation in the country, with multiple global consequences. Food and energy crisis, inflationary pressure, disruption of value chains. In addition to the climate crisis, all are growing more urgent by the day, and pose risks of delay in the ambitious agenda for the achievement of Sustainable Development Goals.

In parallel, the **means to address these challenges have eroded**, notably as governments and public entities had to tackle already previous local or global challenges and/or vulnerabilities. The rising indebtedness and debt servicing costs are expected to diminish the fiscal space of governments; financing conditions are tightening with an increase of interest rates by central banks.

Financing needs for development are enormous.

Estimates by the UN of the financing needs of the 2030 Agenda and Paris climate goals in developing countries point to an annual financing gap of USD 2.5 trillion, that no single actor, let alone development finance institutions, can tackle by themselves.

Ukraine has large external fiscal financing needs estimated at USD 42bn for 2023[1]; in addition, the cost of recovery and reconstruction has been estimated in a Rapid Damage and Needs Assessment[2] conducted by the government of Ukraine, the European Commission, the United Nations and World Bank at USD 411bn. As an order of magnitude, in recent years, the main multilateral financing institutions involved in the country (EBRD/EIB/IBRD) were committing altogether approximately EUR 3bn per year. A major global financial effort will be required to rebuild Ukraine and to support it on its European path in the medium to long term.

There is clearly a need for a concerted effort to scale up financing for development, and to make sure that all financial flows are aligned with climate and sustainability goals. We need to include the private sector and keep being innovative when developing new instruments.

[1] IMF Staff Report Ukraine– March 2023.

[2] Ukraine Rapid Damage and Needs Assessment – March 2023 - report jointly prepared by the Government of Ukraine, the European Commission, the United Nations and the World Bank, based on data as of February 2023.

Reactivity and adaptability to respond to multiple crises…

EIB Global – EIB's dedicated structure for activities outside the EU – is actively engaged to see how best it can respond to the impact of the multiple crises on EU partner countries, combining immediate response and longer-term impact and bringing lending, blending and advisory capacities to tackle the challenges in EIB countries of operation.

In 2022, a few days after the Russian invasion on 24th February, the Bank committed in coordination with the European Commission a first relief package for Ukraine of nearly EUR 700m fully made available in March. In July, EIB Board approved a second relief package of EUR 1.6bn. Whereas macro-financial assistance is essential, this package provides much-needed funding for priority recovery support to reconstruct transport networks (e.g. bridges, railway lines), to support municipalities and delivery of critical public services (district heating and electricity networks, reconstruction and refurbishment of buildings, shelters to enable children to go back to schools). This shows our strong solidarity with Ukraine, but we know more is needed. That is why we have just established the 'EU for Ukraine Initiative' to finance reconstruction and recovery. Thanks to support from the European Commission and member states, we will step up public and private sector investment for critical infrastructure in Ukraine. The initiative will also be accompanied by a large technical assistance and advisory package. The Bank is actively working on investments aiming at the recovery and reconstruction efforts of the country with the European Commission and, as the EU Bank, with a key role to support the EU accession process of Ukraine.

EIB support to Ukrainian people is also tangible outside of Ukraine with a EUR 4bn facility to help supporting needs of refugees in EU Member States.

This package shows the need for **EU financiers to be agile and reactive**, often **pushing the limits of what we thought was possible** in view of unprecedented circumstances.

To tackle the global consequences of the Russian war against Ukraine, the Bank intensified its activities to also support **(i) food security, (ii) energy security and (iii) connectivity/resilience of value chains** across all our regions of operation. If we take the case of food security: the EIB financed *for example* projects to improve the resilience of the food supply systems in countries such as Egypt and Tunisia, including infrastructure development such as the construction of silos for the storage of cereals; enhancing infrastructure for food production, harvesting, storage and logistics – introducing digital solutions. An important aspect in those cases is to tackle a **short-term shock while addressing at the same time the long-term resilience of the sector**.

…while addressing long-term challenges

Despite these acute crises, it is essential not to lose sight of the number one lasting challenge – **climate change**. Sub-optimal level of investment in climate action is the result of a number of market failures. Bilateral and multilateral development banks have a key role to play, in complementarity with banking and financial markets.

As one of the largest providers of climate finance, the EIB is committed to making climate the focus of at least half of its lending by 2025, mobilising EUR 1 trillion investments by end of the current decade.

We are also now implementing the **Adaptation Plan the EIB announced during COP26**, through which we are promoting faster and more systemic investment in climate adaptation worldwide. This means scaling up our support: the EIB will increase its adaptation finance **to reach 15% of its climate financing by 2025** and promote **climate-resilient investments** through risk mitigation. It also means engaging more actively in **sub-sovereign / local climate adaptation projects** to reach out notably to rural areas affected by climate risks (from floods to droughts) as well as fast-growing urban centres exposed to climate changes.

One of EIB's priorities in recent months was to develop a **holistic approach in developing economies to accelerate climate action alongside the pursuit of sustainable development goals**. The EIB's Just Transition work outside the EU will build on and **complement the Bank's ongoing efforts to increase synergies between climate action**, including adaptation and just resilience investments, **and broader social development**, with a focus on gender equality and women's economic empowerment, conflict and fragility, and migration and forced displacement.

A collective approach of development finance institutions

There is a need for a substantial level of reliable and affordable finance from multilateral and bilateral financing institutions to reverse the adverse effects of the pandemic and the consequences of the Russian war against Ukraine and to achieve climate and sustainability goals.

In view of the challenges, it is important to strengthen the partnership model. In particular, to leverage the different capacities and expertise of international partners. The Finance in Common Summit in Abidjan has shown financial institutions' dedication to combine their efforts to be at scale with those challenges. The synergies and transformational impact of the wide community of public development banks to deliver as a system play a central role to support the transitions through upstream policy and institutional support, the development of investment programs and joint project financing.

The EIB always adopts a **collaborative approach** and seeks partnerships whenever possible – not least because we can normally only finance up to 50% of the total investment cost. In terms of providing an overarching approach to such cooperation, we find a number of structures assembled by the European Commission to be most helpful in this regard.

As the EU bank, EIB is a **key participant in Team Europe Initiatives** which constitute more strategic and more coherent approaches to development finance aligned to European principles, values, goals and priorities based **on a 'policy-first' approach**. We are involved in a large majority of Team Europe Initiatives, in all regions outside of the EU. This process has provided a much-needed momentum to increase our common **impact** (to target priority policy objectives and avoid a scattered approach), **visibility**, and **effectiveness** (for EU institutions and partners not to duplicate efforts and leverage the expertise of each entity).

EIB Global is also working to strengthen its **operational cooperation** with Team Europe partners. We have experienced a **strong growth in co-financing** with other European institutions recently. Reinforcing the modalities of cooperation, notably through the existing Mutual Reliance Initiative between AFD, EIB and KfW and a new Framework Cooperation Agreement with EBRD, made an important contribution to this. The EIB also participates in joint platforms such as with the EDFI – European Financing Partners.

The EIB also established a direct partnership with EU Member States under the **standardised Partnerships Platform for Funds** – operating several regional Trust Funds (e.g. Mediterranean Region, Eastern Partnership, Economic Resilience). This enables us to operate with instruments providing high value added, notably advisory which plays a critical role, and flexibility to cope with the challenges currently faced.

Leveraging financing beyond development finance

To address the financing gap for climate, sustainability and development goals, in addition to the resources provided by development partners, **the issue of mobilisation of the private sector and domestic financial resources is strategic**.

Mobilising domestic financial resources through the local banking system and capital markets and channelling them into domestic sustainable investments will be crucial. This requires supporting countries to improve their business environments and to roll out financial products and tools that better mitigate risks. Development finance institutions need to complement domestic investments with grants and concessional finance. The EIB develops new products, such as green loans, de-risking instruments or layered equity funds. And we handhold clients embarking on a green transition, providing technical and financial expertise when needed.

For this, in addition to instruments, we also need a common **"language" that private sector actors understand**. The continuous efforts of the EU, its member states and financial institutions for development to develop a consistent, sustainable finance taxonomy to be attached to development finance will play an important role.

The combined support of multilateral and bilateral financing institutions with the private sector needs to be anchored more firmly in **national ownership and leadership through systematic dialogue with national partners**. We will only succeed in reaching our common goals if international cooperation and support go hand in hand with national priorities and development plans.

Last but not least, in this new permanent context of compounding crisis characterised by higher uncertainty, **reactivity and adaptability** are as essential as the scale of our collective responses. As evidenced during recent shocks, the flexibility of the instruments and institutional set-up allows us to maximise the response and development impact. In that respect, the ability to mobilise advisory support promptly to help get investment projects ready for financing is crucial.

Chapter 4

In times of crisis, development banks move even closer together

The goals of the European Financial Architecture for Development can only be achieved through closer cooperation

Christian Garve and **Dr. Jennifer Lenk**, KfW Development Bank/European Affairs,
Presidency of Joint European Financiers for International Cooperation (JEFIC)

A world in crisis/turmoil

The upheavals at the end of the 1990s, the fall of the Berlin Wall and the democratic processes in the Eastern European countries had nurtured hopes for a peaceful era. There was already a discourse of an "end of history" and that democratic systems would now prevail worldwide. Despite positive beginnings, this expectation has unfortunately not been fulfilled to date; Russia's war of aggression on Ukraine is a culmination of numerous crises that are again shaking today's world.

Contrary to hopes, the Arab Spring did not lead to democracy taking hold in the Islamic countries. In Syria, a cruel war has been raging for years, with no end in sight. In Africa, there seems to be no solution to the conflict in Sudan, and numerous crises are forcing more and more people to flee. Worldwide, around 90 million people are currently displaced or have fled. At the same time, there is no doubt that the climate is changing: weather extremes such as storms, drought and floods are increasing.

The multitude of crises is particularly affecting people in the countries of the Global South and is also presenting European development cooperation with new and diverse challenges: in a world that threatens to shatter into blocks again, development cooperation is helping to ensure that various actors continue to work cooperatively on global solutions. These efforts are to be strengthened through even more intensive cooperation in order to avoid backsliding, safeguard what has been achieved so far, leverage synergies between different institutions, increase impacts, and jointly reach more people.

Joining forces and cooperating closely

The fact that individual institutions cannot shoulder the multitude of challenges alone is being addressed by the various stakeholders in European development cooperation, who have for some time been discussing the efficiency and efficacy of a "European Financial Architecture for Development" (EFAD). As part of these efforts, the Joint European Financiers for International Cooperation (JEFIC) network was founded in June 2022, with AECID (Spain), AFD (France), CDP (Italy) and KfW (Germany) as founding members, followed by BGK from Poland in March 2023. The network remains open to new members in order to place European cooperation on an even broader foundation.

By joining forces and cooperating closely, JEFIC members put to best use their respective strengths and experience to further enhance the impact of their work in the partner countries, also and especially when it comes to acting in environments marked by crises and conflicts. The cooperation focuses on the public sector in developing countries and emerging market economies. In addition, JEFIC has set itself the task of involving the private sector and improving the local regulatory framework. Jointly, financing instruments are developed that make an engagement in developing countries attractive for private investors while at the same time supporting the capacity of local capital markets through sustainable cooperation with institutions and banks in the partner countries.

Based on the Co-financing Framework Agreement (CFA) signed on 17 March 2023, JEFIC partners can rely on each other's rules and procedures and delegate monitoring tasks, thus enabling harmonised and swift project implementation and avoiding time-consuming processes. This helps increase the volume of funds, allows funds from various European donor institutions to be released quickly, and thereby enhances efficiency in European development cooperation, thanks to the respective "lead financier" acting as a single contact point vis-à-vis the partners.

Members share their respective strengths and local networks within JEFIC, which allows for a maximum of synergies from their broad and diverse expertise. In doing so, they put to best use their specific experiences and contacts to benefit all stakeholders through close exchanges, thus providing access to a broad pool of European expertise and financial power.

Supporting sustainable transformation

JEFIC has a particular sensitivity to local structures and issues through different approaches. Despite the current crises, the network does not lose sight of the long-term transformation tasks. The members have committed themselves to the Paris climate protection goals and are consistently working on the implementation of the UN Sustainable Development Goals (SDGs).

JEFIC members are engaged worldwide and continue their work even under difficult conditions. In Africa, for example, the focus is on boosting the economy and supporting youth employment in particular, also to address the root causes of migration. Businesses and young self-employed people are supported to foster the creation of decent jobs.

One of the first projects under the new CFA aims to improve vocational education in Kenya. This involves the funding of various activities to digitise schools, starting with basic equipment, through the training and further education of teachers, to the provision of digital content. In a country with high youth unemployment, this is a valuable contribution to securing the livelihoods of the next generation and helps create job prospects for young people in their own country.

Overall, the JEFIC network provides a significant share of global financing for sustainable development, with a combined financing volume of more than €21 billion in 2022, and implements around one-third of the funds generated by the EU's blending and guarantee instruments. A local presence with more than 200 offices in 85 countries allows for very close cooperation and ensures that partners are there for people even in crisis regions.

Chapter 5

International development financing: A triple revival

Rémy Rioux, Chief Executive Officer - Agence Française de Développement (AFD); Chairman of the International Development Finance Club (IDFC); Chair of Finance in Common executive board, **Thomas Mélonio**, Executive Director of Innovation, Strategy, and Research and **Jean-David Naudet**, Advisor to the Executive Director of Innovation, Strategy, and Research

We have now entered the age of the consequences of climate change. This requires a re-examination of all international financing tools, and in particular the most operational of them, Official Development Assistance (ODA), in order to come up with proposals for the post-2025 period.

Official Development Assistance (ODA): a valuable global public policy

ODA is a well-established international tool: it reached record levels in 2021; it enjoys constant support from public opinion in the North, and it has proved to be a special tool in the management of international crises. Most importantly, ODA is one of the very few examples of global public policy built on a set of rules, norms and practices, with its own financing tool and a group of strong institutions to implement it.

Yet partly unsuited to the challenges of the future

Yet the adoption of the Sustainable Development Goals (SDGs) in 2015 has had the effect of both re-legitimising aid around a common international commitment and dissipating it in issues that exceed its ambition and means.

The capital requirements to finance the SDGs in developing countries would be 10 times the current ODA. But beyond the amounts, a North-South instrument of public investment transfers also appears to be insufficient by nature in the face of objectives that involve changes in development trajectories and not simply filling an investment gap.

Through their universal character, the SDGs break with a world divided into two blocs, which was the basis of ODA in the last century. The rise of emerging countries since the 2000s has created a continuum of global income distribution. Inequalities within countries now account for two-thirds of global inequalities, in a proportion that continues to grow.

ODA is a hybrid global public policy in the sense that it remains a voluntary and partly unilateral instrument on the part of the donor countries, and could be considered unsuitable for global public goods issues, calling rather for contractual or mandatory approaches, as is the case with the climate sphere.

Beyond ODA: three distinct changes

The response to the challenges of the future has sometimes been to broaden the scope of ODA. But broader aggregates, such as the Total Official Support for Sustainable Development (TOSSD) and climate finance, are struggling to build new 'global public policies', lacking precisely what makes ODA solid: precise accounting rules, burden- and good practice-sharing norms, specific determinants, legibility, support from public opinion.

International financing for development and climate challenges rather than an expansion of ODA calls for a triple revival.

- *Beyond a two-bloc world:* new geographies. Global poverty is increasingly concentrated in fragile countries, while ODA remains widely dispersed. And poverty mapping overlaps with climate vulnerability mapping. The opposition between developed/developing countries not only reflects the continuity of wealth distribution inaccurately, but also accounts less and less for the geography of greenhouse gas emissions. International financing for the development structure must be based on evolving, differentiated maps, according to the issues at stake, and should factor in environmental inequalities.
- *Beyond solidarity: new principles*. ODA has progressively integrated the local financing of global public goods. But managing the consequences of climate change raises a question of principle. It cannot be a voluntary action based on the principles of mutual interest and solidarity, which are those of ODA. It is also a question of international justice, based on responsibilities and vulnerabilities, and future financing for development must be based partly on these principles.
- *Beyond the financing of a gap: new coalitions*. The role of public climate finance is not just to fill a gap in resources. It is also a question of redirecting investments or other financial flows, particularly in countries that are already carbon emitters, to support credible country pathways. Future international standards for climate finance will not be the responsibility of States alone, but will involve multiple groups of similar players, such as the 'Finance in Common' initiative, which is working to bring together over 500 public development banks, international and national, around the SDGs.

Distinct, complementary policies and instruments

Beyond the existing divide between ODA and climate finance, a new reference framework could be made up of two major policies: an international investment for development (IID) policy focused on development and climate vulnerabilities together, and a sustainable development investment (SDI) policy, to mobilise as many players as possible—first and foremost the private sector—in order to accelerate the low-carbon transition throughout the world.

Shifting from ODA to <u>international investment for development (IID)</u> in the most vulnerable countries would involve:

- Concentrating the bulk of existing concessional resources in low-income and fragile countries to finance what no one is financing. This new policy would preserve and renew the achievements of the current ODA, while defining a framework open to new donors.
- Building an international climate insurance mechanism to manage the consequences of climate change in the context of the recent agreement around a loss and damage fund.

Increasing collective mobilisation for sustainable development investments (SDI), i.e. financing low-carbon transitions, would require the following:

- To explicitly and voluntarily allocate a portion of ODA budget resources to mobilising the largest possible number of players, primarily for risk reduction, risk sharing and co-investment with the private sector in support of the decarbonisation trajectories defined by countries.
- Expand, and multiply network coalitions of stakeholders with a threefold objective: mobilisation, transparency and the definition of credible standards and key performance indicators (KPIs) for the low-carbon transition.

COP27 marked a step forward in the recognition of the concept of 'loss and damage' arising from climate change, and it would be inconsistent for countries that are among the biggest historical emitters not to be involved in the effort to reduce or offset climate risks.

The recent agreement at COP27 to take into account 'loss and damage' due to climate change is still to be constructed, and constitutes a step in marking these different changes and inviting renewed contributors, beneficiaries and targets of international financing.

The two public policies of international investment for development and investment for sustainable development would make it possible to keep the best of ODA and reconcile ODA and climate finance, given the common imperative of combating climate change, in compliance with the SDGs.

The Summit announced on these issues by President Macron in June 2023 with G20 Indian Presidency follows the Bridgetown initiative led by Prime Minister Mottley and discussed in Washington could help move this crucial agenda forward.

Section III

European development finance reconsidered

Chapter 6

Building a shared European vision on the reforms of the international financial architecture for sustainable development

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As world leaders are packing their bags to travel to Washington for the Spring meetings of the World Bank (WB) and the International Monetary Fund, these discussions will offer the first opportunity of the year to collectively deliver on some of the propositions to reform the WB and the international financial architecture for sustainable development to make them fit for the poly-crises of the 21st century. The May G7 Summit in Japan, the June Summit for A New Financial Pact in Paris, the September Finance in Common Summit in Colombia, the SDG Summit in New York, the G20 Summit in India, the October World Bank and International Monetary Fund (IMF) annual meetings, and the COP28 in Dubai at the end of the year, are other opportunities to move the reform agenda forward.

Building a possible shared European vision on main priorities on the international development financial architecture is key for the European Union (EU) and its member states, given their political and economic weight in the international financial institutions (IFIs) and fora, and their responsibilities as key implementing actors in countries of operations.

The role of Europeans in reforming the international financial system for sustainable development

Multiple calls to reform the international financial system for sustainable development require the EU to establish a shared approach to the proposed changes and establish alliances with like-minded partners. This is of particular importance given the political and financial weight of Europeans at the global level and in IFIs in particular.

The EU and its member states collectively remain the largest international donor, providing over 40% of global Official Development Assistance (ODA) in 2021. EU member states also avail of a network of national development finance institutions working both with the public and private sectors for development. They own the European Investment Bank (EIB) and are a majority shareholder of the European Bank for Reconstruction and Development (EBRD), which are key and growing actors in terms of promoting EU external investment and priorities. Last but not least, EU member states are key shareholders of some of the major multilateral development banks. Collectively, they own around one-quarter of the World Bank's voting shares; and 4 to 5% more if we also include the UK.

Yet, the EU and its member states often do not operate as a collective actor, somewhat underplaying the policy agenda, adequacy and efficiency of their financing of and participation in such architecture. Europeans are thus challenged to demonstrate their added value and distinctive approach in a multipolar world where various development and financing models compete, particularly at a time when trust between North and South countries appears to have eroded. If well-coordinated along a clearer set of shared priorities, based on an open and constructive approach to Southern voices, Europeans could position themselves as some of the champions of this reform agenda and, when joining conscious and progressive alliances for change, restore some of this trust.

Insights from the reform process of the European financial architecture for sustainable development

In fostering shared views on the international financial architecture, the EU can draw on its past internal process of reforming the European financial architecture for development, which included objectives of rationalising the existing landscape, better integrating new challenges such as the fight against and adaptation to climate change, enhancing complementarities among a range of financial and development actors, and adapting various tools and institutions, including the EIB and EBRD.

Three areas particularly stood out:

I. *Adapting multilateral development banks operations to an evolving agend*a

With the adoption of the Green Deal and the emphasis on a policy-first approach, combined with the Paris Agreement and successive COPs, the EU and its member states have made increasing commitments to boost climate finance. This has led to further efforts to build on the potential of existing development finance institutions and public development banks to tackle both climate and development as intertwined and complementary goals (as opposed to substituting one for the other). This is the case, for instance, of the EIB, which became the EU Climate Bank and also set up its dedicated international branch in January 2022, EIB Global, with a view to doing more on international development while combining this ambition with climate action and environmental protection.

Challenges remain on the operationalisation of the dual ambition to tackle both development and climate objectives, just as there is a need to recognise that there are diverse paths to a just and green transition which do not always fit exactly with the European model, or at least expose some of its contradictions, a pushback point already mentioned by some countries in the South.

In this vein, the ongoing work of the EU high-level expert group on scaling up sustainable finance in low- and middle-income countries can contribute to establishing a clearer definition of what sustainable finance should look like, with a view to ensure that supporting transformation and impact at country-level is made a priority for the EU.

II. Better serving vulnerable and fragile environments by de-risking and mobilising the private sector through greater use of guarantees

A majority of operations by multilateral development banks (MDBs) are currently deployed in middle-income countries (MICs). The aversion of some of these banks and the European private sector to invest more in lower-income countries (LICs) may be considered justified by the perceived risks attached to more fragile economic and political environments. Further incentivising the use of guarantees is one option on the table to provide more and better access to finances to countries in need and their private sector.

The European Fund for Sustainable Development Plus (EFSD+), created by the EU in 2021 as part of the Neighbourhood, Development and International Cooperation Instrument (NDICI)– ‘Global Europe‘ includes a significant increase of finances made available for guarantees for the 2021-2027 period (up to €10 billion against €1.5 billion for the previous seven-year period). These instruments are designed to be used primarily for private sector mobilisation and job creation, in fragile contexts, especially on the African continent.
All EU entities have access to these funds, including the EIB, which also adds its own financial envelopes.

As the calls for greater de-risking of projects multiply, be it through an enhanced Multilateral Investment Guarantee Agency (MIGA) in the World Bank Group, through the implementation of Just Energy Transition Plans (JETPs), Europeans can also share lessons on their experimentation of such tools. The inclusion of the EFSD+ in the broader Global Europe instruments should also fuel discussions on the complementarity between instruments (be it grants, blending and guarantees) depending on the sector, region and type of projects.

III. Coordinating action: learnings from the Team Europe approach

The identified need for greater cohesion at the European level on international cooperation matters was already highlighted during the COVID-19 pandemic and led to the launch of the 'Team Europe approach'. The latter aims to gather European actors under one shared umbrella, with each providing some level of financing or expertise and sharing tasks and responsibilities that build on their respective strengths. This includes European member states' institutions working with the public sector but also those engaging more with the private sector, through the network of European Development Finance Institutions, for example. This approach translated numerous Team Europe initiatives, all with the potential to contribute to the overarching strategies, including the 2030 Agenda, the Global Gateway and the European Green Deal. While efforts have been made to map out various objectives and the expertise needed from various actors involved to seek greater complementarity, there still is a need for a clearer steer on the priorities that would unite Europeans and provide ground for stronger leadership on the international scene, including on where the reforms of MDBs should focus more and how.

Europeans can build on these past lessons to make the international financial architecture for sustainable development fitter to the 21st-century challenges. But more progress and a fundamental shift are needed to unleash its truly transformational potential and materialise a much-needed EU leadership in international fora.

The EU should speak with one voice beyond its borders

For Europeans to fully weigh in on the reforms by bringing their own ideas and joining progressive alliances with third states, a number of points remain unresolved at this stage and require further consideration.

Mobilising more finances

The magnitude of the challenges highlighted in the Capital Adequacy Framework (CAF) reform, MDB reforms and the Bridgetown agenda call for a quantum leap in the quality and volume of sustainable finance made available to countries in need. Yet, Europeans have given no sign of any new additional funding. ODA levels have already increased in some countries, although with rising criticism about the so-called 'inflated aid', while they are under threat in some others, including some big donors, with looming cuts rather than new injections that would help to collectively reach the 0.7% GNI on ODA target. The pledge of US$100 billion a year of Climate Finance has yet to be met, although research suggests that Europeans are among those that lead the way and have provided their fair share.

There is some level of interest in new forms of financing (with regards to taxation) along with reservations about their feasibility in the current political context. Special drawing rights (SDRs) re-channelling by richer countries brings some optimism: some European member states have already pledged to rechannel a total equivalent of € 28 billion through the IMF, among others, and there is room for additional commitments by Europeans.

However, more discussions are urgently needed with third parties to join the pledge and reach the US$ 100 billion reallocation target, starting with the US, whose pledge to reallocate some of its SDRs remains stuck in the US Congress. Mechanisms to rechannel SDRs beyond the IMF, and notably through MDBs - as currently made possible by the African Development Bank and Inter-American Development Bank - would also require lifting the blockage from the European Central Bank based on the interpretation of the EU Treaty.

Evolving MDBs business models to better respond to borrowers' needs

While the WB may already announce at the Spring meetings the availability of new finances, more discussions are needed to clarify how these funds should be used and ways in which the business models of these multilateral development banks need to evolve. Europeans call for a clearer division of labour between all institutions involved: between MDBs, between MDBs and the broader banking ecosystem (with PDBs and the private sector), as well as with state authorities.

Most importantly, European players support the idea that the reforms should help move away from a project-based approach to a portfolio one that fully takes into consideration the integrated nature of the challenges at hand and sets the right criteria for access to such financing (as opposed to increasing its cost because of new imperatives). An integrated approach would further support shifting existing finances away from negative impacts (such as fossil fuels).

Solving governance issues and reconciling tracks for better engagement beyond the EU

The absence of truly transformative decisions at the moment can partly be attributed to the standoff between some parties (from various ministries or different parts of an institution) opposing more sustainable development-oriented approaches to finance-oriented ones. Such divisions impede some member states from having a unified position, and this is mirrored at the EU institutions level between different directorates, and further in the governance bodies of MDBs where European voices are not necessarily unified. EU coordination between tracks and within boards is a key area where further progress is needed to join the dots and ensure greater political buy-in of various initiatives taken so far in a fragmented way. This should also play out in the context of the MDBs reform to ensure that they all move forward in a coherent manner, not just exchanging information but truly collaborating on the basis of their respective strengths and the mission set by their shareholders. In the European players' view, such coordination would also allow greater credibility in the discussions with credit rating agencies.

These governance issues also negatively impact discussions with EU partners. A change of narrative and stronger policy dialogue have been identified as needed to ensure that change happens at the country level where Europeans are also collectively often very present to implement their international development and cooperation work. Such changes would also contribute to making the voice of Europeans heard more strongly in international processes such as the G20 or the G7. Pressing on identified priorities and meeting the demands of borrowers will require a better understanding of where the EU collectively sits on some of the proposals on the table and who it can and wants to engage with, including China, which has been engaging only at the margins so far, if at all.

European collective leadership

The EU context illustrates that the type of reforms for the MDBs and international financial architecture for sustainable development on the table has, in fact, long been discussed in various forms and for a. But there is, this year, a conducive platform to address these burning issues and concretely deliver on a substantial reform agenda.

Europeans should be central to making it happen. Broad support already emerges on a number of issues and there will be numerous occasions to finetune them throughout the year. If an EU coalition of the willing can emerge from this process to concretely and urgently implement some of the proposed actions and join progressive coalitions with countries from the South, this would go a long way in the European attempt to restore trust and credibility with partners throughout the world.

Chapter 7

The EU's Global Gateway and the European Financial Architecture for Development

Jeroen Kwakkenbos, Deputy Head of EU Office and Senior Aid Policy and Development Finance Advisor, Oxfam

The European Union (EU) has adopted a new approach to foreign policy dubbed the "Global Gateway," supported by a new European Financial Architecture for Development (EFAD). These policies are a direct response to the state of perma-crises that the world finds itself in. It seeks to inject €180-300 billion over a period of six years into the EU's partner countries in the form of infrastructure projects, a green transition and digitalisation. This strategy seeks to mobilise resources from EU member states, multilateral development banks (MDBs), national development finance institutions (DFIs) and the private sector to reach its target of €30-50 billion a year.

The EU's main challenge is that the Multiannual Financial Framework (MFF) – the EU's budget - which dictates the limits on EU spending for a seven-year period, has already been concluded. All EU resources have been allocated. The same goes for the EU's main foreign policy financial instrument, the Neighbourhood, development and international cooperation instrument (NDICI) - Global Europe. This development instrument of roughly €14 billion per year has already seen its spending allocated to projects and programs - many of which would not qualify under the Global Gateway. The EU's main resource to leverage is private finance. The European Fund for Sustainable Development Plus (EFSD+) is an example of this, with its total cap of €10 billion over a seven-year EU budget period. This would mean an unrealistic leverage ratio as the instrument is supposed to primarily target the OECD's list of so-called 'Least Developed Countries'. This leaves EU member states, who are already under budgetary pressure and are unlikely to increase their development budgets in the coming year, and the MDBs, where the EU is not the only player, as the main source of finance for the Global Gateway.

While the green transition is critical in combating the climate crisis and additional finance must be found, we are concerned that the Global Gateway could draw resources away from other development interventions crucial for combating inequality, such as support for public services and poverty eradication programmes. Most of the EU's foreign policy instruments are development instruments, and those flows must retain their development characteristic and purpose. This money should not be redirected to geopolitical priorities. While much is made of leveraging resources from financial markets, these types of financial flows are not a given and come with significant development risks.

Through the Global Gateway and the EFAD, the EU may have set itself up for scoring an own goal, as the reputational risks of not delivering what was promised to our partners are significant. There are already alternatives to the Global Gateway where the EU and its member states could use geopolitical clout. This could free up significant financial resources for the EU's partner countries and comes with a minimal hit on the EU's purse strings. Rather than spending time frantically trying to raise funds that simply aren't there and double count already existing commitments, the European Commission could better spend its time on other, more effective, opportunities. Below are six ways to take the Global Gateway and EU development aid forward.

1. Pool all funding in the same pot

Europe and its member states can increase development resources by being more efficient by successfully implementing the aid and development effectiveness principles. In both Paris in 2005 and Busan in 2011, the global community gathered to declare "this is the way to do development" and then proceeded to implement the principles and recommendations with mixed results. Team Europe and the Global Gateway are opportunities to revitalise aid and development effectiveness by consolidating and harmonising the EU and member states' development resources. Reducing duplication of programmes and transaction costs and harmonising monitoring and evaluation would bring more resources to the table and increase their impact. While it would be good to see it in action, even if under the rubric of an EU branding activity, it will not provide anywhere near the resources required to achieve the sustainable development goals (SDGs). So, in short, while long overdue, it is not sufficient.

2. Live up to broken promised

The easiest way for the EU to increase its development resources is by making EU countries live up to their target to spend 0.7% of their gross national income (GNI) on official development assistance (ODA). If this target were taken seriously by the entire donor community, it would amount to significantly more than the promised €30-50 billion a year and contribute to achieving the objectives set out by the EU. However, this scenario is, sadly, incredibly unlikely. Aid budgets are stagnant, and very few countries have taken their commitment to the 0.7% ODA/GNI target seriously. Oxfam has estimated that in the 50 years since the target was initially developed, high-income countries have failed to deliver a total of US$5.7 trillion in aid. Worse, the future points to a reduction of aid rather than an increase and to EU countries spending more development money at home.

3. Be mindful of significant leverage

One of the key ways the EU plans to hit the €300 billion target is by using public money to leverage resources from financial markets and other public development banks. This will be done through its EFSD+ guarantee instrument. Experience under the previous EFSD instrument has shown that these kinds of projects are complex to negotiate, and, as the European Court of Auditors noted, its ability to mobilise additional investments was likely overestimated. Given that a significant amount promised is supposed to come from this leveraging of public money, which is an estimate yet to be realised, it is impossible to know if this target will be reached.

Alternatives that can raise significant revenues:

4. Cancel debt of partner countries

In 2022, the IMF warned that a quarter of emerging economies and two-thirds of low-income countries are in or near debt distress. In 2021, on average, low-income countries spent 27.5% of their budgets on debt repayments, double the proportion spent on education, four times that spent on health and nearly twelve times that spent on social protection. If the EU were to use its geopolitical clout to champion debt relief and debt cancellation, it could free up significant fiscal space for its partner countries. A first step would be to support the cancellation of all debt repayments for overindebted lower- and middle-income countries until the end of 2023.

5. Transfer Special Drawing Rights to poorer countries

The International Monetary Fund's (IMF) decision to issue an equivalent of US$650 billion in Special Drawing Rights (SDRs) to mitigate the economic impact of the Covid-19 pandemic was a momentous occasion in global solidarity. However, perversely, due to the IMF quota system, the majority of these SDRs went to rich countries that needed them least. Since then, there have been commitments by wealthy countries to transfer SDRs to low- and middle-income countries, but this has been hampered by arcane European Central Bank (ECB) rulings and self-imposed restrictions. There are ways for the Global Gateway to access these resources, circumventing the ECB's restrictions and transferring them to the Multilateral Development Banks and countries needing them the most, but so far, no action has been taken. This alone could free up billions of euros for partner countries. In addition, the EU could support a new issuance of SDRs, further increasing financial resources.

6. Tackle tax evasion and avoidance

Low-income countries lose billions to corporate tax avoidance and tax evasion stashed in tax havens every year. Countries on the African continent have had the highest net loss to profit-shifting from multinational companies. Other research has shown that the share of wealth hidden by rich elites in tax havens tends to be much higher for many low-income countries. Cracking down on tax havens and setting tougher rules to enforce tax transparency could unlock billions for development.

The EU's Global Gateway could be a game-changer. It could provide partner countries with the type of financial resources needed to support a green transition and scale up development projects. But to do so, the EU must deliver on its promises without undermining its already existing commitments. The EU already has means at its disposal to significantly increase its support to partner countries without having to resort to double counting and financial alchemy. If the Global Gateway amounts to a re-branding exercise for what the EU and its member states are already doing in partner countries, then it would amount to a wasted opportunity.

The EU has proven in the past to be a champion of supporting countries' systems and public services in its foreign policy. We expect it to continue doing so.

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