

THE DEBT-FOSSIL FUEL TRAP

Why debt is a barrier to fossil fuel phase-out and what we can do about it



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Written by Tess Woolfenden, Debt Justice

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About Debt Justice

(formerly Jubilee Debt Campaign)

We are a campaigning organisation working with others to end unjust debt and the poverty and inequality it perpetuates, in the UK and across the world.

debtjustice.org.uk • info@debtjustice.org.uk

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Debt Justice, Oxford House, Derbyshire Street,
London, E2 6HG, United Kingdom

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Introduction

This briefing explores the links between debt and fossil fuel production in global south countries, and presents a number of solutions for addressing high debt burdens as a contribution towards efforts for a fossil fuel phase-out.

It provides evidence of a **debt-fossil fuel production trap** whereby countries rely on fossil fuel revenues to repay debt, and anticipated revenues from fossil fuels are often overinflated and require huge investments to reach expected returns, leading to further debt, eroding long-term development prospects, and causing devastating environmental and human harms.

Thus, not only do many fossil fuel developments in global south countries cause human and environmental harm, they also do not make economic sense and leave many countries financially worse off, further indebted and even more reliant on fossil fuel exploitation than they were before.

Global south governments will not be able to phase out fossil fuel production unless we address harmful debt levels and vulnerabilities and inequalities embedded within the existing debt and financial systems.

In order to remove debt as a significant barrier to fossil fuel phase-out and the transition to clean energy, wealthy governments and institutions must:

1. **Implement ambitious debt cancellation for all countries that need it, across all creditors, free from economic conditions.** This includes key jurisdictions introducing legislative reform so private creditors are no longer able to block debt relief negotiations.

2. **Debts accrued from fossil fuel projects should be recognised as illegitimate and cancelled.**
3. **Significantly scale up grant-based, new and additional public climate finance** as a form of reparations in light of the climate and ecological debt owed by the global north to the global south.
4. **Bilateral and multilateral finance should be aligned with a 1.5 degree warming scenario and fair shares calculations, and not be used to finance fossil fuels.** Multilateral and international financial institutions should set deadlines for shifting finance out of fossil fuels and into sustainable, climate measures for adaptation, mitigation and to address Loss and Damage.

This paper intends to introduce the topics and provide a number of existing examples to demonstrate how the dynamics between fossil fuel exploitation and debt play out for many global south countries, drawing on the brilliant work that already exists from grassroots groups, organisations and researchers. We recognise that there is a wealth of further information already available on many areas presented in this briefing, and that there is further research that could be done including on specific country experiences as well as on the dynamics between debt and fossil fuel exploitation.

Setting the context

This section briefly sets out some context which is important to account for when exploring the links between debt and fossil fuel exploitation.

Climate debt

Wealthy polluters have taken up more than their fair share of atmospheric space. Some argue that because of this, global south countries should still be allowed to exploit their fossil fuels while wealthy polluters reduce their emissions.^{1,2,3} However, many climate justice groups in the global south argue that this will contribute to further climate breakdown and sovereign financial risks, and instead call on wealthy polluters to provide structural and financial reparations in recognition of a climate debt (alongside historical, financial, ecological, political, cultural and social debt) for the damage they have caused. This would include the provision and achievement of climate finance obligations and debt cancellation, as well as ecological restoration, phasing out fossil fuels (which includes stopping investments in fossil fuels abroad), ending extractivism, and shifting to decarbonised modes of production, distribution and consumption.⁴

The case for phasing out fossil fuels

The harms of fossil fuels are well documented. We know that the overuse of fossil fuels from industrialisation to the present day by global north corporations, governments and elites is largely responsible for the climate crisis^{5,6} which is most acutely felt by marginalised communities⁷ and global south countries.⁸ Furthermore, right through every fossil fuel supply chain there are countless examples of human and environmental harm. For example,

burning coal, oil and natural gas has been shown to create seven million premature deaths worldwide because of the harmful health impacts.⁹ Thousands of people have been displaced from their land, often by force, coercion or the contamination of farmland or drinking water as a result of fossil fuel projects.¹⁰ Meanwhile, vast swathes of land have been cleared to make way for fossil fuel projects, destroying critical wildlife habitats and polluting the local area¹¹ causing untold harm for communities that live in those areas.

The case for phasing out fossil fuels is clear, and has been well made in recent decades by activists, grassroots groups and organisations calling for not only the phase out fossil fuels, but a fair and just transition to clean, renewable energy¹² and green, sustainable and resilient economies. Yet the struggle continues as governments, corporations and institutions continue to invest in and enable fossil fuel projects, prioritising the profits of fossil fuel companies and extractive development models over the rights, health, cultures, and wellbeing of people and the energetic and ecological boundaries of the planet.

This paper does not intend to explore the need for a fossil fuel phase-out, or indeed how we should go about it in a just and fair way (many other brilliant groups have done this already). Rather, this paper aims to make clear the ways in which debt in global south countries is a key factor preventing the phase-out of fossil fuels, and to detail the ways in which this can be overcome.

Context: the colonially-rooted 'commodity dependency trap'

Global south country reliance on fossil fuels sits in a wider context of commodity export dependency dating back to colonialism. Under European colonial rule, many countries' economies were transformed to focus on the export of raw materials such as fossil fuels, metals and cash crops to feed industrial growth taking place across Europe.^{13,14} A lack of resources (many of which were, and continue to be, plundered by former colonial powers)¹⁵ and the inequalities etched into global trade, tax and financial systems have meant that for many global south countries, it has been nearly impossible to diversify economies away from commodity exporting and dependency.

Furthermore, global north powers, especially global north dominated institutions like the International Monetary Fund (IMF) and World Bank, have actively encouraged and enforced the continued reliance on commodity exporting in global south countries through, for instance, direct funding or conditions attached to loans pushing a policy prescription based on extractive development models that see natural resources, including fossil fuels, as a key opportunity for economic growth and development.¹⁶ A promise that not only fails to materialise, but also causes significant environmental and human harm. The United Nations Conference on Trade and Development (UNCTAD) have outlined that balanced economic strategies are more suitable than export-led development to achieve economic sustainability,¹⁷ a message echoed by many civil society organisations.¹⁸

Reliance on commodity exporting means vulnerable economies are susceptible to shocks such as volatility in the price of goods on the global market. It is associated with lower levels of income than countries with diversified economies¹⁹ and typically creates less highly skilled, long-term or well paid jobs than other sectors.²⁰

Countries dependent on commodity exporting often lack sustainable means to uphold the needs of citizens, including financing the transition away from fossil fuels, and must rely on borrowing from domestic and external creditors to keep afloat.

As such, countries dependent on commodity exporting often lack sustainable means to fully uphold the needs of citizens,²¹ including financing the transition away from fossil fuels, and many must rely on borrowing from domestic and external creditors to keep afloat.²² Meanwhile, wealthy governments, institutions and corporations – particularly in the global north – benefit greatly from these policy approaches, through cheap access to the resources of global south countries for example, and the opportunity to make large profits through access to global south country industries.²³

This history of exploitation, plunder, extraction and inequality is an important backdrop for understanding global south country relationships to fossil fuel exploitation, continuous cycles of indebtedness, elevated climatic risks, and fragile economic and development prospects.

The links between debt and fossil fuels

1. High debt burdens limit the resources available to transition to clean energy

High debt levels drain resources

Global south countries have been facing increasingly high debt over recent years, with external debt payments increasing by 150% between 2011 and 2023, reaching their highest levels in 25 years.²⁴

Debt Justice calculates that there are 54 countries in debt crisis,²⁵ many of which have been forced to reduce public spending during the pandemic to keep up with payments.²⁶ The situation could get much worse as interest rates rise, markets destabilise and the war in Ukraine pushes up food and energy prices.²⁷

Global south countries are currently spending **five times more** on repaying debt than they are on addressing the impacts of the climate crisis.

High levels of indebtedness mean that countries lack the resources to invest in the needs of populations, including pandemic recovery, public services and transitioning to clean energy.²⁸ Global south countries are currently spending five times more on repaying debt than they are on addressing the impacts of the climate crisis.²⁹

Existing processes for debt relief have failed

When the COVID-19 pandemic hit and the debt crisis reached new peaks, the G20 reacted by establishing a new process, called the Common Framework, to assist global south countries with their debt levels by providing a way for them to negotiate debt relief with their external bilateral and private creditors.³⁰ However, three years later just four countries have applied, with only Chad reaching an agreement with all its creditors (which didn't actually provide any debt relief,³¹ see more below) and Zambia only reaching an in principle agreement with its bilateral creditors (as of July 2023). The Common Framework has a number of issues preventing it from being effective. Many middle-income countries in debt crisis are not eligible to apply, for example, but one of the main issues is that it has nothing to compel private creditors to participate. As per the rules of the Common Framework, a debt restructuring can only go ahead if a borrowing government is able to reach a comparable agreement with both bilateral and commercial creditors, meaning that the refusal of private creditors to play ball can derail the whole process.

A significant proportion of global south debt is owed to commercial creditors,³² often at much higher interest rates than other lenders which they argue is to cover the risks of lending to global south countries, potentially making them huge profits if repaid in full.³³ Furthermore, if a borrowing government is unable to pay and defaults on its loans, there is currently nothing stopping private lenders taking governments to court to demand a full repayment. Many court cases would take place in the UK or New York as virtually all international debt contracts are governed by New York or English law.³⁴ For example, Sri Lanka is currently being sued in New York by Hamilton Reserve Bank Ltd for full payment of a bond Hamilton has bought on the secondary market.³⁵

Understanding External Public Debt

Governments borrow for a variety of reasons, for example to pay for the costs of unexpected events like pandemics, to smooth economic shocks, to fund investment or current public spending, or to plug the finance gap created by inequalities in the financial system such as capital flight or undelivered climate finance promises. In some cases there is a lack of adequate accountability or transparency to the public. Many countries have to finance their regular expenditures like health care through borrowing. In the 2010s there was a large increase in lending. Low interest rates in the western world following the 2008 financial crisis led financiers to seek to lend to global south governments who they charge higher interest rates for loans, and thus potentially make high profits. Meanwhile, global south governments continue to be encouraged to take on more debt to fund their development efforts by key institutions like the World Bank and IMF. Economic shocks such as falls in commodity prices, climate extreme events and the Covid pandemic cut government revenues and so increase the frequency and seriousness of debt crises. Between 2013 and 2023, the number of global south countries the IMF says are unable to pay their debts or are at high risk of doing so has increased from 17 to 37, while the number at low risk has fallen from 21 to just 7.

Countries can borrow from three types of lenders:

- Foreign governments (bilateral creditors)
- The IMF, the World Bank and other multilateral creditors
- Private actors such as banks and hedge funds.

This paper refers to 'external sovereign debt', which is debt owed by governments to creditors outside their country. Governments can also take on domestic debt by borrowing from lenders in their own country, usually domestic banks.

A lack of good quality climate finance is exacerbating the debt crisis

In 2009, global north governments committed to providing \$100 billion in climate finance every year to global south countries by 2020, but continuously failed to meet this commitment.³⁶ In 2015, they then recommitted to contributing \$100 billion a year every year between 2020-2025 to global south countries.³⁷ Not only is this commitment woefully inadequate – according to the most recent Needs Determination Report from the Standing Committee on Finance, global south

countries will require at least US\$5.8-5.9 trillion cumulatively to reach their individual NDC commitments for adaptation and mitigation by 2030³⁸ – it has also yet to be reached.³⁹ Without adequate climate finance, many global south countries are forced to find resources for adaptation, mitigation and addressing Loss and Damage elsewhere, including taking on more debt. Loans often come with high interest rates because of the climate vulnerability global south countries face,⁴⁰ creating the opportunity for large profits for creditors if they are repaid in full.

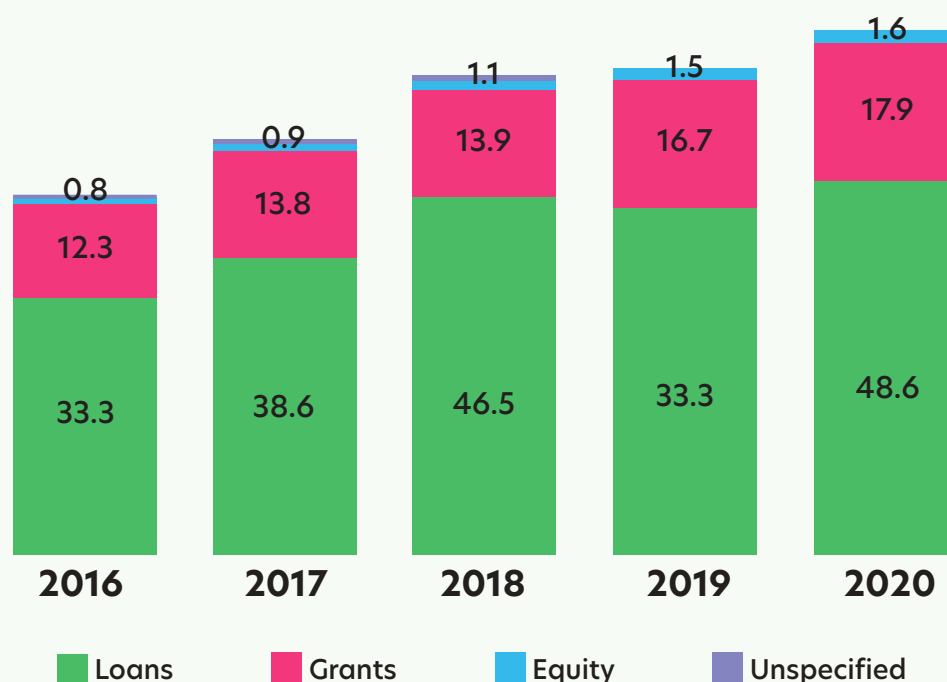


This is especially the case for countries that are experiencing Loss and Damage. In the absence of any adequate finance for addressing Loss and Damage, many countries are being forced to borrow to cover the costs of reconstruction and recovery. In Dominica for example, debt as a percentage of GDP rose from 68% to 78% after Hurricane Maria hit the island in 2017. Many others have been forced to borrow after climate extreme events, such as the Bahamas which took on a \$100 million loan from the Inter-American Development Bank to fund the recovery from Hurricane Dorian,⁴¹ or Mozambique which was given a \$118.2 million loan from the IMF to fund the recovery from cyclone Idai.⁴² The financial assistance offered to Pakistan after the devastating floods that hit the country in 2022 was not only woefully inadequate (reaching \$10 billion so far while the total damage is estimated at over \$40 billion⁴³), but will mostly come in the form of loans.⁴⁴

Without adequate finance for adaptation and to address Loss and Damage, it is estimated that over the next ten years Sub-Saharan African countries will have to take on an additional **\$996 billion in debt** – a 50% increase on current debt levels as a percentage of GDP.⁴⁵

The little climate finance that is provided largely comes in the form of loans – 71% is provided as loans, with only 26% provided as grants (and 3% as equity) according to the latest OECD figures.⁴⁶ This once again adds to debt levels and unfairly forces the costs of the climate crisis onto countries who have done the least to create it.^{47,48}

Instrument split of public climate finance in 2016-2020 (USD billion)



Note: The sum of instruments may not add up to totals due to rounding.

Source: Based on Biennial Reports to the UNFCCC, OECD DAC and complementary reporting to the OECD.

High debt levels prevent countries from accessing finance for renewable energy

Given the lack of good quality, adequate finance for climate action, many global south countries currently rely on borrowing from financial markets in order to transition to renewable energy. However, when debt levels are high, countries are no longer able to borrow from international markets, and thus lose access to this as a financing option. This is not to suggest that countries should have to rely on borrowing from financial markets to

finance their transition (which is often a very expensive way to borrow),⁴⁹ but to highlight that under existing financing options for global south countries, high debt levels can be a major blocker for accessing the finance required to transition away from fossil fuels.

For example, in 2021 the Argentinian government began cancelling contracts under its RenovAR plan – a renewable energy program designed to scale-up private renewable energy⁵⁰ – after the 2018 debt crisis meant that the country was no longer able to obtain the necessary financing to develop the project.⁵¹

2. Debt traps countries in fossil fuel production

The need for foreign exchange to repay debt

Many global south countries are looking to their natural resources, including fossil fuels, to generate the revenue they need to respond to multiple crises and repay debt.^{52,53,54} Research by the New Climate Institute found that out of 76 lower-income countries, about half have proven fossil fuel reserves and are planning to, or already are, expanding fossil fuel extraction.⁵⁵

Ecuador

Ecuador is currently at risk of a public debt crisis, diverting about 10% of government revenue to repay its debt,⁵⁶ rising to 15% in the mid-2020s.⁵⁷ President Guillermo Lasso has based the country's pandemic recovery plans on doubling its oil production by 2025, including to generate revenues to pay back its foreign creditors.⁵⁸ Indigenous and environmental groups in Ecuador have fiercely opposed the proposals.⁵⁹

Debt contracts can lock countries into fossil fuel production

Some loan contracts, such as resource backed loans (RBLs), keep countries locked in fossil fuel production. RBLs refer to loan contracts where "repayment is either made directly in natural resources (in kind) such as oil or minerals, or from a resource-related future income stream; or repayment is guaranteed by a resource-related income stream, or where a natural resource asset serves as collateral."⁶⁰

These arrangements tend to be hidden from public view, absent from international debt statistics and not reported on nationally. They also present significant risks to borrowing governments who may find themselves unable to meet debt repayments should the value of commodities fall.⁶¹

It is not just debt contracts that can lock countries into fossil fuels. Investor State Dispute Settlements (ISDS) are procedural mechanisms that are often included in international agreements such as trade and investment deals. They allow investors to sue the host state if it takes any action that undermines or adversely affects the value of their investment.^{74,75} According to Global Justice Now, this can mean corporations

Suriname

Suriname defaulted on its debt in late 2020, and in 2021 started negotiations with its bilateral and private creditors to reduce its debt down to a sustainable level. It did this outside the G20 Common Framework process as Suriname is not eligible to apply.⁶⁸ A deal was made with Paris Club creditors in June 2022,⁶⁹ and a deal with private creditors was recently made almost a year later in May 2023.⁷⁰

The resulting deal cuts Suriname's principal payments to external commercial creditors from \$675 million to \$650 million, and reduces the interest rate from 9%+ to 7.95%.⁷¹ However, this deal is heavily skewed in favour of private creditors who will still be making millions in profit from this deal.⁷² Despite this, private external creditors will still be compensated for their so-called losses by receiving potentially millions from Suriname's oil revenues. Creditors will get the right to 30% of Suriname's oil revenue until 2050, up to a maximum of \$689 million after Suriname has received the first \$100 million in royalties.⁷³ Once again, this deal keeps Suriname trapped in oil exploitation whilst being incentivised to maximise oil revenues.

Chad

In 2013, the commodity trading and mining company Glencore lent \$2 billion to the government of Chad. In return, Glencore took on ownership of a stake of the state-run oil company – Société des Hydrocarbures du Tchad. A crash in the price of oil in 2014 meant Chad had to restructure its loan with Glencore twice, but despite this, the country remained in debt distress.⁶²

In early 2021 Chad applied to the G20 Common Framework for debt relief. Glencore delayed negotiations throughout 2021 and 2022, while continuing to be paid in full. In late 2022, the G20 announced that Chad would not be getting any debt cancellation through the scheme because bilateral creditors and Glencore (which holds about one third of Chad's external debt via the oil backed loan)⁶³ agreed that high oil prices had boosted Chad's revenues enough to enable it to keep up its repayments, even though there is no guarantee that oil prices will stay high.⁶⁴ Even World Bank President David Malpass expressed concerns about this, stating "The agreement reached by the creditors provides no immediate debt reduction. As a result, the debt service burden of Chad remains heavy and is crowding out priority expenditures on food, health, education and climate."⁶⁵ Chad continues to repay the oil-backed loan to Glencore, keeping the country trapped in the harmful industry while also incentivising the maximisation of oil revenues.⁶⁶ In 2023 in a document reviewing Chad's progress under the Extended Credit Facility Arrangement, the IMF stated that "Additional oil revenue will... help rebuild buffers and reduce domestic arrears and external debt."⁶⁷

suings countries "for doing almost anything they don't like – environmental protection, regulating finance, renationalising public services, anti-smoking policies,"⁷⁶ and of course, phasing out fossil fuels.⁷⁷ As a result of ISDS, governments have already been forced to pay out \$100 billion to corporations in the coal, oil, gas, electricity and mining industries in response to climate and/or environmental measures they have put in place.⁷⁸ Research by the Global Policy Development Centre at Boston University shows that 33 countries could face significant financial losses via ISDS if they decide to cancel oil and gas projects. Some of the countries that could face the greatest losses could include Mozambique (\$7-31 billion), Guyana (\$5-21 billion), Kazakhstan (\$6-18 billion) and Indonesia (\$3-4 billion).⁷⁹ Costs such as these could push countries further into debt if they are already facing fiscal deficits.

3. Global north governments and institutions continue to encourage and enforce fossil fuel projects in global south countries

Continued fossil fuel financing

Despite various commitments over recent years to stop investing in fossil fuels in global south countries by multilateral and bilateral lenders,⁸⁰ many continue to finance fossil fuel projects, often through loans, adding to debt burdens and keeping countries locked in fossil fuel production.⁸¹

Many grassroots groups and civil society organisations refer to debt incurred from the projects as illegitimate, outlining the harm that these projects have caused to people and the environment, and thus demand that they should not be repaid.⁸²

This continued investment in fossil fuels also presents a huge opportunity cost, crowding out much needed finance for clean energy sources.

Multilateral Development Banks

Multilateral Development Banks provided on average \$3.3 billion a year in direct financing to fossil fuel projects from 2020 to 2022.⁸³ The actual amount is likely to be greater if one were to calculate indirect sources of financing going towards fossil fuels, for example through budget support, financial intermediaries, technical assistance and trade finance provided by these institutions.

The World Bank

Of the MDBs, the World Bank has been highlighted as one of the greatest multilateral contributors to fossil fuels since 2015.⁸⁴ Research estimates that between 1947 and 2020, nearly 20% (\$237 billion) of the \$1.2 trillion dispersed by the main institutions for loan making and development finance within the World Bank went to fossil fuel projects, provided as loans, grants, equity or guarantees.⁸⁵ Between 2020 and 2022 the World Bank provided \$1.3 billion a year on average in fossil fuel finance, with at least 67% of this for fossil gas.⁸⁶ This is despite the institution making claims that it stopped investing in upstream oil and gas in 2019.⁸⁷

Asian Development Bank (ADB)

The ADB has also been providing finance to the Asian region for fossil fuel projects, largely in the form of loans. From 2009-2019, the ADB provided \$42.5 billion for fossil fuel projects via loans, grants and technical assistance. In 2008 for example, the ADB provided a \$450 million loan for the Tata Mundra Ultra Mega Coal Plant in Gujarat, India (pictured below), which has resulted in significant harm for local communities, livelihoods and the environment.⁸⁸



Mundra Programme for Social Action India CC: BY-2.0

The ADB is also rolling out plans to support countries to transition to cleaner energy under its “Energy Transition Mechanism”. Part of this programme includes providing loans to Asian countries to decommission coal fired power plants, many of which have caused significant harm to communities’ health, livelihoods and environments.^{89,90} While this is necessary and welcome, it is important to note that many of these power plants were initially financed through loans which governments and their state owned enterprises have had to repay. Providing new loans for their decommissioning has created a double burden of debt which should not have to be shouldered by countries and communities which have done the least to create the climate crisis.

USA, China and Japan

A 2021 study by Chen *et al* found that the USA, China and Japan were the biggest bilateral funders of fossil fuel finance to global south countries between 2000-2018, and that their investments in fossil fuel projects far outweighed the funding deployed for renewable technologies. They estimate that the financing for fossil fuels from these three countries alone will lock in 24 gigatonnes of CO₂ emissions by 2060.⁹¹

The IMF and World Bank conditions enforce an extractive development model

IMF surveillance and loan agreements and World Bank projects in many cases actively encourage or enforce fossil fuel extraction, despite presenting themselves as climate champions in many contexts.⁹² This sits in a wider context of IMF and World Bank conditionality where in order for global south countries to get an IMF or World Bank loan, they must often put in place a series of economic reforms based on austerity, privatisation and market liberalisation which, in theory, will enable countries to economically grow, pay down debt and allocate more resources to development.⁹³

This model has been in place since the 1980s debt crisis, and has neither helped reduce debt levels in the long run nor supported sustained inclusive economic growth for most countries.⁹⁴ Furthermore, in most cases, poverty levels and inequality have increased exponentially as a result, harming the most marginalised in society.^{95,96,97} Yet the IMF and World Bank, with the backing of their majority global north shareholders, continue to push

this approach,⁹⁸ including continuing to encourage and enforce fossil fuel exploitation and thus exacerbate the climate crisis as a means of economic growth.

Research by the Bretton Woods Project and Action Aid found that between 2015 and 2021 (after the Paris Agreement was signed), the IMF endorsed or directly supported the expansion of fossil fuel infrastructure in 55% of member countries.⁹⁹ Between 2014 and 2018, World Bank financing for the energy transition included incentives specifically targeting the new oil and gas initiatives in Indonesia, Mozambique and Pakistan.¹⁰⁰

As well as directly encouraging or enforcing fossil fuel exploitation, IMF and World Bank conditions can also undermine efforts to phase out fossil fuels and transition to clean energy in other ways. For example, the economic policies enforced as a part of loan contracts have been shown to reduce the fiscal space countries have,¹⁰⁶ reducing their ability to invest in the energy transition¹⁰⁷ as is currently happening in Ecuador.¹⁰⁸ Conditions can also force countries to adopt punishing fiscal measures that could hamper the country’s renewable energy markets.



Uganda

As a means of meeting the needs of the population during Covid-19, the Ugandan government took on a number of loans from the IMF and World Bank, including a \$1 billion loan from the IMF in 2021. According to civil society groups, the conditions of the loan stipulated that the government should take a “hands-off approach to the country’s development and to place greater priority on the oil and gas sector” as a way of strengthening the country’s collection of revenues and repaying debts.¹⁰¹ In an effort to fast-track oil and gas extraction, the Ugandan government has allocated some of the resources made available by the loan towards the construction of the East Africa Crude Oil Pipeline (EACOP), intended to transport oil from Uganda to Tanzania and enable the start of oil exportation in 2025. The construction will require 5,300 hectares of land, displacing thousands of households across the two countries (many of whom have been inadequately compensated or re-settled), and causing significant harm to wetlands and farmland across the region from anticipated oil spills, despite claims to the contrary by those involved in the project.¹⁰² Civil society groups WOMIN and SEATINI have highlighted how women will be most impacted as caregivers, and because of their reliance on the environment for daily life. Over 260 organisations from nearly 50 countries have called on banks to refuse to finance the construction of the pipeline¹⁰³ including the global campaign ‘Stop EACOP’.¹⁰⁴

Recent research by Recourse has shown that the IMF is pushing climate harmful policy conditions attached to its loans in Uganda. The report highlights how, as a part of the country’s IMF Programme, the IMF implicitly encourages further reliance upon fossil fuels as a means to balance the country’s budget and current account, and that investment in oil infrastructure has been ring fenced while there were only limited attempts at considering climate issues.¹⁰⁵

Pakistan

The IMF has recently forced a series of tax reforms on Pakistan as part of its programme under the Extended Finance Facility which are likely to significantly undermine “Pakistan’s nascent renewables energy market, threatening the country’s ability to meet its environmental goals and international climate obligations.”^{109,110} This includes a 20% tax on solar and wind, and a 12% increase in sales tax for imported electric vehicles, which have been heavily criticised by the Alliance for Climate Justice and Clean Energy, a civil society alliance working for a just energy transition away from dirty fossil-fuels and towards clean and renewable sources in Pakistan.¹¹¹

This can be for a variety of reasons. For example, potential impacts of commodity price and demand volatility (which many global south countries are disproportionately exposed to because of their colonial legacy of commodity dependency)¹¹⁴ are not always fully accounted for when projecting growth in revenues from fossil fuel production. We might also expect to see reduced demand for fossil fuels as countries transition to cleaner energy in line with the Paris Agreement.^{115,116} Governments may also require a significant amount of investment to be able to scale up their fossil fuel production, impacting projections and adding to debt levels rather than reducing them¹¹⁷ whilst also using up already scarce public finance. Finally, fossil fuel project contracts are often structured in a way which means that investors and project developers recover their investments first, while government revenues accrue later, meaning it is government revenues that will be most impacted by delays, cost overruns and if/when global demand for fossil fuels declines.¹¹⁸

4. Fossil fuel projects lead to increasing debt levels

Overprojected returns can lead to increased debt

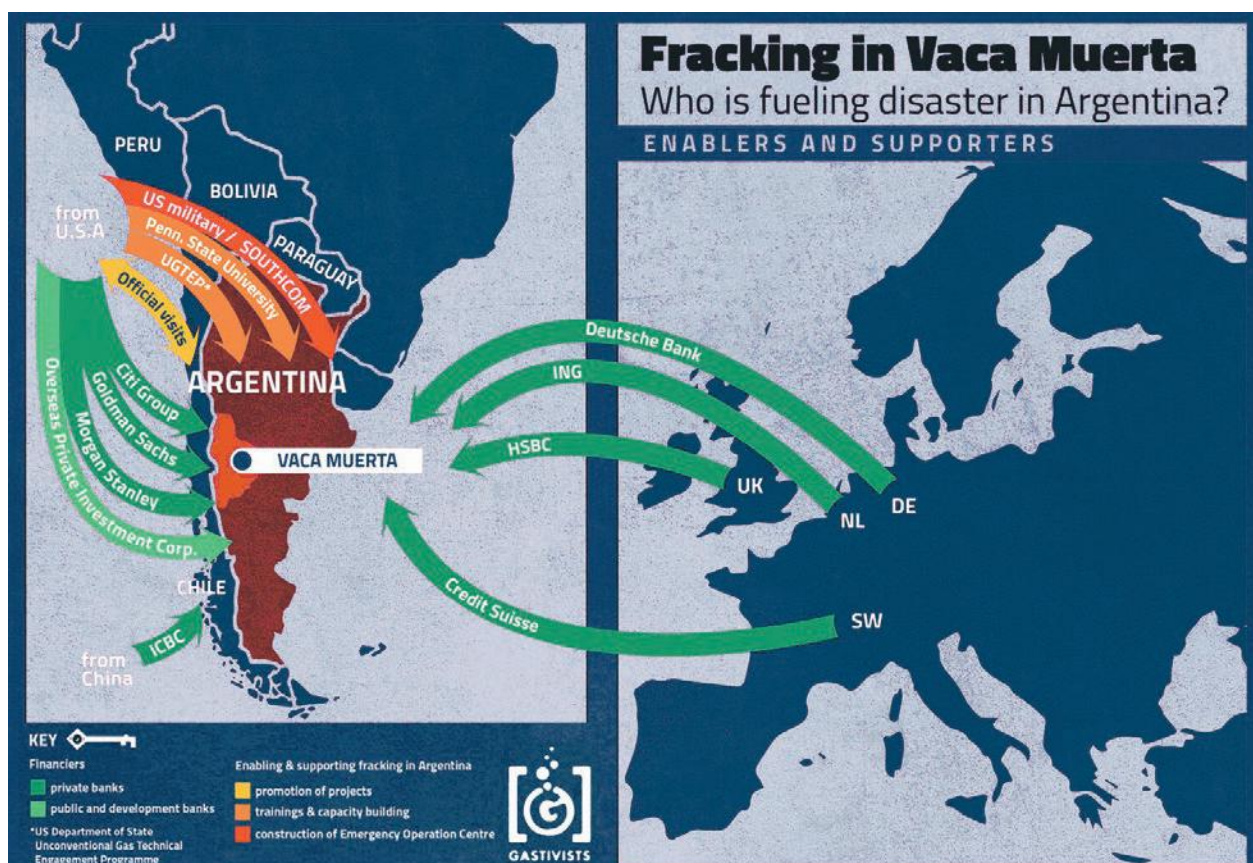
Not only do the IMF and World Bank continue to promote fossil fuel projects, they also overestimate anticipated revenue benefits of such projects which historically have not materialised, leaving countries at risk of further debt whilst remaining locked in climate harmful activities.¹¹² Research by the Natural Resource Governance Institute shows that growth following oil discoveries have systematically underperformed against IMF predictions.¹¹³

Overestimations of fossil fuel project returns can also encourage irresponsible borrowing and lending, as creditors and borrowing countries rely on returns from fossil fuel projects to make debt repayments. This has been the case in Mozambique where three large loans from London-based banks (all of which were taken without proper parliamentary scrutiny, breaking the Mozambique constitution) were based on the prospect of using revenues from LNG projects to meet repayments¹¹⁹ (see case study at the end of this briefing). The government of Uganda has also reportedly been taking on more loans from external creditors banking on using expected oil revenues to meet repayments.¹²⁰

Argentina

The IMF and Argentinian government are pushing the development of fracking in the Vaca Muerta oil and gas field in Northern Patagonia as a way to solve the country's debt crisis and wider economic problems.^{121,122,123} They propose that foreign currency could be saved by supplying oil and gas domestically while additional foreign currency can be generated through oil and gas exports.¹²⁴ The former economy minister Martin Guzman suggested that exports could hit \$15 billion by 2027, part of which would be used to pay down the country's debt^{125,126} which has been at unsustainable levels since mass lending to the government from 2016-2018 (partly to pay mass profits to vulture funds as a hangover of the 2001 economic crisis and partly to support the country in addressing its economic and debt crisis, including a \$57.1 billion loan from the IMF – the largest loan provided in IMF history¹²⁷ – which has largely failed to get debt down to a sustainable level).¹²⁸

Those supporting fracking in the Vaca Muerta oil and gas field include banking institutions, export credit agencies (like UK Export Finance, the investment arm of the UK government)¹²⁹ and private banking institutions (such as HSBC).^{130,131} Many Argentinian groups are campaigning against these activities, highlighting the potential damage to both communities and the environment (such as increasing carbon emissions, the health and ecosystems implications of potential oil and gas spills¹³² and displacement due to contamination which is already taking place¹³³), including Indigenous groups who filed a lawsuit against the plans in 2018.¹³⁴ Others have also highlighted that the proposed benefits are likely not to materialise given the risks of relying on fossil fuel revenues and given the huge amount of investment required to scale up extraction in the next few years which will require taking on more debt from external creditors.¹³⁵ The country's strategy to reduce down debt may end up adding to debt levels without generating adequate revenue to repay.^{136,137,138,139}



Ghana

This case is based on research conducted by ARIA. Please contact them directly for more information – leigh.elston@aria.info or sarah.evans@aria.info.

In 2007, significant oil and offshore gas reserves were discovered in Ghana.¹⁴⁰ Since 2010, Ghana has received at least \$2.8 billion in direct project finance from Development Finance Institutions such as the World Bank, UK Export Finance, and the African Development Bank, as well as investments from commercial entities such as Helios Investment Partners, for upstream and downstream fossil fuel projects.

Some of the contracts with investors are underpinned by 'take-or-pay' terms which commit Ghana to purchase gas and other fossil fuel supplies at a set price and volume irrespective of Ghana's actual needs. These were agreed in the context of protracted electricity shortages in the country between 2012-2016¹⁴¹ (partly due to a lower gas supply from the West African Pipeline than anticipated – contractually expected to deliver 123 million standard cubic feet of gas per day¹⁴² which has never been achieved.)¹⁴³ In some cases these were backed by World Bank guarantees.¹⁴⁴

These contracts were widely criticised by civil society at the time. For example, in the case of the gas supply agreement between the Ghanaian government and private corporations developing the Sankofa offshore fields, the Africa Centre for Energy Policy said that "the deal is fraught with badly negotiated terms" and that "the Government has...over-exposed the country to too much risk due the decision to buy all the gas produced by the contractor."¹⁴⁵

The result has been a significant oversupply of fossil fuel energy supplies for Ghana at huge cost to the country. In 2019, Ghana's Finance Minister stated in the Mid-Year Fiscal Policy Review of the 2019 Budget Statement and Economic Policy that:

On average, less than 40 percent of the contracted take-or-pay capacity is actually used, meaning that we are basically throwing away money by paying for the remaining 60 percent of excess capacity which we do not actually consume. In monetary terms, what this means is that we are paying over half a billion U.S. dollars or over GH¢2.5 billion annually for power generation capacity that we do not need.¹⁴⁶

It has been estimated that Ghana is paying \$1.2 billion annually for excess fossil fuel energy supply that it does not use.¹⁴⁷ This has significantly contributed to Ghana's high debt levels – the country's payments this year alone would stand at \$3 billion had it not defaulted on some of its repayments to external creditors.¹⁴⁸ Ghana is currently seeking debt relief under the G20's Common Framework and has just reached a deal for a new programme with the IMF which includes a new set of economic conditions aimed at "restoring macroeconomic stability and debt sustainability while protecting the vulnerable, preserving financial stability, and laying the foundation for strong and inclusive recovery."¹⁴⁹ Furthermore, because of the nature of some of the contracts, Ghana is having to reinject or flare much of the excess gas it has had to purchase¹⁵⁰ with significant environmental risks.¹⁵¹

Despite the significant financial and environmental damages caused through the development of fossil fuels projects in Ghana, and the significant oversupply of gas, there are now plans underway to develop a new LNG import terminal in Ghana which will be supplied by Shell.¹⁵² This development is supported, once again, by Development Finance Institutions.

Mozambique

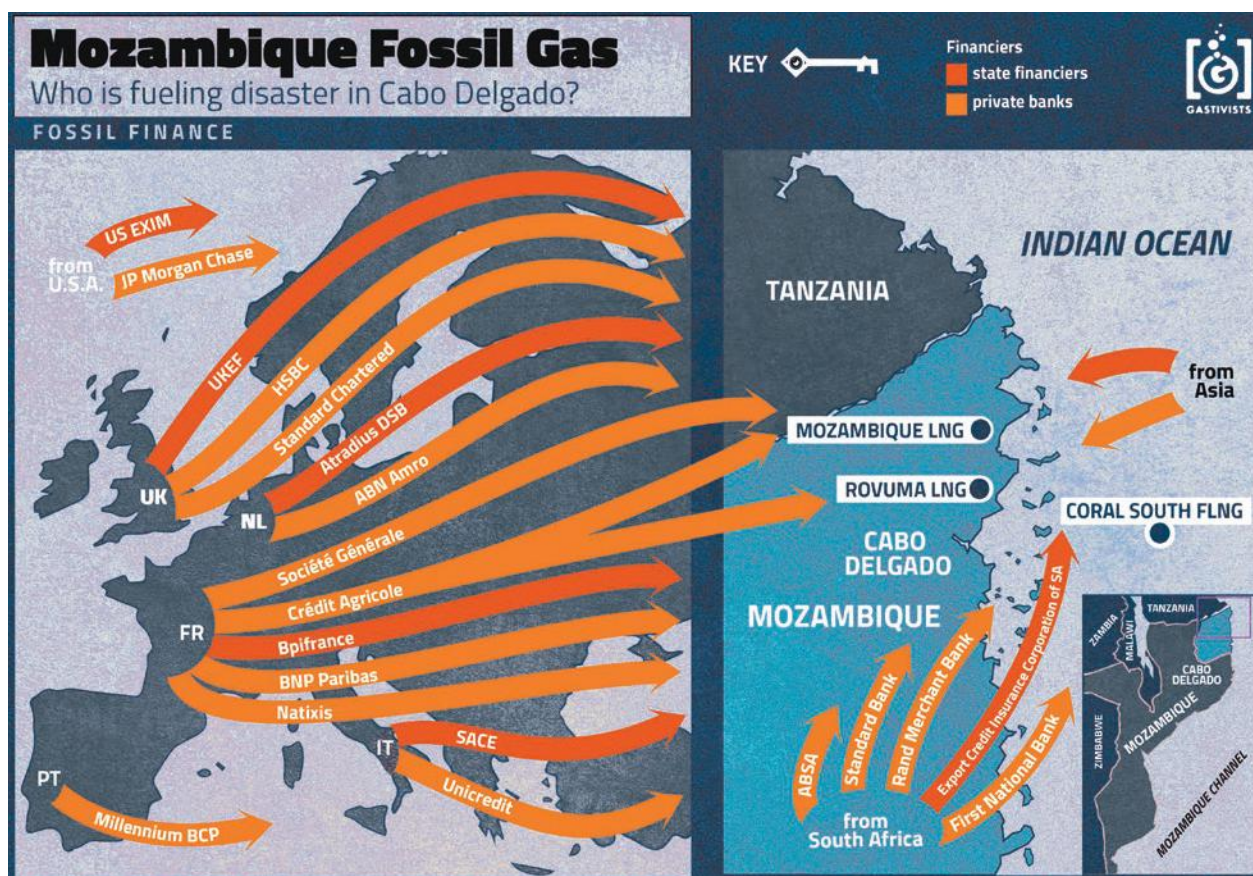
Discovery of natural gas reserves

In 2010, large natural gas reserves were discovered in Mozambique. Following this, the government gave the go ahead for a number of Liquefied Natural Gas (LNG) projects to begin, actively encouraged by the IMF as a part of a loan program.¹⁵³

One of the projects given the green light includes the Rovuma Basin Area 1 Mozambique development plan (Mozambique LNG) in the Cabo Delgado Province which is being developed by the world's seventh largest oil and gas company, Total. Total has secured around \$15 billion in investments for the project so far (out of the \$24 billion required) from commercial and public entities, including the African Development Bank, UK Export Finance, HSBC and Standard Chartered (both banks registered in the UK.)¹⁵⁴ The Mozambique government has also guaranteed \$2.25 billion of the state-owned ENH's (Mozambique's state-owned oil company) equity share.¹⁵⁵

The anticipated revenues were huge - up to half a trillion dollars over the LNG project's life span,¹⁵⁶ enough to predict Mozambique transitioning to a middle-income country, and to have the resources to significantly scale up public investment, economically develop and pay down debt according to E3G.¹⁵⁷ *Petroleum Review* magazine said that the projects could "catapult the country from being one of the poorest African nations to one of the richest."¹⁵⁸

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Revenues fail to materialise

However, these anticipated benefits for Mozambique have not materialised. In 2016, the IMF projected 39% GDP growth in the country in 2021,¹⁵⁹ however actual economic growth for that year was estimated at 2.2%¹⁶⁰ with the people of Mozambique now poorer than they were 10 years ago.¹⁶¹ This pattern of failed predictions has continued. In 2019 the IMF predicted Mozambique's economy would be 37% larger by 2023, based on gas exports in 2022 and 2023. In reality in the absence of major exports it was just 13% larger. But rather than change its tune, the IMF just moves its predictions into the future – now expecting annual growth rates of 15% in 2027 and 2028.¹⁶²

Predictions for future revenues from LNG assumed that the price of gas on international markets would increase steadily over time, while in reality, LNG prices are likely to fluctuate. Delays resulting from Covid-19, regional insecurity (see below), the global transition away from fossil fuels¹⁶³ and contract structures which mean most revenue goes to investing companies,¹⁶⁴ all pose series of challenges to the future prospects for Mozambique's LNG projects.¹⁶⁵ Recent government analysis now suggests that revenues will not exceed \$500 million before 2030 and will peak at \$3.2 billion in 2040.¹⁶⁶

It is important to note that the LNG projects in the Cabo Delgado province have been impacted by instability pre-dating the projects' commencement. Since well before 2016, instability had been brewing in the area related to several complex and overlapping grievances. These have been fuelled and exacerbated by LNG development, leading to a full-blown militarised insurgency in recent years that has resulted in thousands of deaths and nearly a million displaced people.¹⁶⁷ In 2021, Total paused its project and declared force majeure due to the conflict around the project site that continues until today. When, if, and on what terms this LNG project will resume remains in flux.^{168,169}

The links with debt

In 2013 and 2014, three loans were given to state owned enterprises in Mozambique by London-based branches of Credit Suisse and VTB totalling \$2 billion. While the loans were not a direct outcome of the gas discoveries, it seems Mozambique officials involved were enabled to take out the loans with the prospect of being able to use revenues from the LNG projects to meet repayments.¹⁷⁰

The loans were guaranteed by the then Finance Minister Manuel Chang without the proper approval of Mozambique parliament, making the loans illegal in the country. Two of the loans were not made public until 2016. When they were revealed, the country was plunged into debt and economic crisis and aid flows from the IMF and donor countries dried up. This has cost the people of Mozambique at least \$10 billion in total, and has pushed over two million people into poverty.¹⁷¹

Despite the loans being deemed illegal and not benefiting the people of Mozambique, the government has been repaying some of the loans. In 2018, they reached an agreement with creditors to restructure one of the loans (Ematum)¹⁷² to make repayments more sustainable. However, the terms of the restructuring were deeply unjust, and left the people of Mozambique paying between \$1.7 and \$2.2 billion for a \$760 million loan which they have not benefited from.¹⁷³ Furthermore, as a part of the agreement, creditors will receive 5% of yearly revenues the country generates from LNG projects up to \$500 million¹⁷⁴ keeping the country locked in LNG production, while also undermining gas advocates' claims that LNG will have a wider positive developmental impact in the country.

continued...

Moreover, there is a chance that the LNG projects may add to the country's debt burden given the billions of dollars of guarantees issued by the government to enable its state-owned oil company to participate in the LNG projects. As highlighted by Open Oil, the potential returns for ENH are uncertain,¹⁷⁵ and if they do not materialise, the government of Mozambique could be exposed to significant contingent liabilities as a result of the guarantees it has provided for LNG development. For example, in the World Bank's 'Mozambique Economic Update 2021', it highlights how the economic impacts of the Covid-19 pandemic have created financial vulnerabilities for LNG projects in the country, stating that:

worsening financial conditions posed by the crisis will make it impossible for ENH to pay its carry (money it borrows from venture partners) from the Coral South FLNG without a cross-subsidy from the Rovuma LNG... In a scenario where the Rovuma LNG project does not move ahead..., ENH would end up with unpaid debt from the Coral South FLNG when the project reaches the end of its economic life (in 2047).¹⁷⁶

However, in contrast to this, in a 2022 document, the World Bank states that:

External debt assessment would not be significantly affected if the LNG projects do not resume, although future growth potential would be compromised. This is because the contracts between the national hydrocarbon company - Empresa Nacional de Hidrocarbonetos (ENH) - and its partners would only make the state liable for the ENH share in a small amount of debt disbursed so far.¹⁷⁷

Without having seen the contracts, it is difficult to know which assessment will be correct, however it seems possible if gas revenues don't materialise, the Mozambique state could inherit a significant debt from ENH.

Resistance

There has been strong resistance against the construction of gas facilities in Cabo Delgado,¹⁷⁸ which has contributed to the militarisation of the region to protect facilities (under the guise of protecting people.)^{179,180} There has also been the displacement of nearly one million people,¹⁸¹ the destruction of villages and 2,000 people have died.¹⁸² Furthermore, the broken promises of increased prosperity combined with rising inequality and human rights violations, have increased tension between local groups, exacerbating militia violence in the region.¹⁸³ Local communities have also been highlighting the environmental damages of the projects.¹⁸⁴

Despite this, the IMF and World Bank still continue to see the LNG projects as critical for the country's debt sustainability.¹⁸⁵ In the most recent Debt Sustainability Analysis for Mozambique, the IMF said that the country's debt is "assessed as sustainable in a forward-looking perspective because a significant share of projected borrowing reflects the state's participation in sizable LNG projects, which will be repaid directly from future gas revenues."¹⁸⁶ The World Bank has also recently said it is open to supporting the further development of the country's natural gas resources.¹⁸⁷

Solutions

In order to remove high debt burdens as a significant barrier to fossil fuel phase-out and the transition to clean energy, wealthy governments and institutions must:

- 1. Implement ambitious debt cancellation for all countries that need it, across all creditors, free from economic conditions. This will free up resources at a national level to address multiple crises, and mean global south countries are not reliant on revenues from fossil fuels to repay debt.**

Existing debt relief initiatives implemented by the G20 have so far failed and are not providing the level of debt relief required for many global south countries. In the short run, existing debt relief initiatives must be strengthened and extended to all countries that need it, and all creditors (bilateral, multilateral and private) must participate. As nearly all global south country loans from external private creditors are given under English and New York law,¹⁸⁸ the UK and US can play a leading role in strengthening debt relief processes by introducing legislation that would compel private sector participation in debt relief negotiations, a process that is already underway in New York.¹⁸⁹

In the longrun, an independent multilateral debt workout mechanism under the UN should be introduced to serve as a framework to restructure and cancel debt for any country that needs it, across all creditors, to a level compatible with sustainable development and the ability to address the climate crisis.¹⁹⁰

Debt cancellation should be provided free from economic conditions so that governments and citizens have fiscal and decision making space to determine where freed up resources can best be allocated, including in the transition to clean energy.

Resources freed up through debt cancellation should not be counted as climate finance or towards any global climate finance goals, because these resources are not new and additional.

- 2. Debts accrued from fossil fuel projects should be recognised as illegitimate and cancelled** so countries are not forced to make repayments for activities that have caused harm to citizens or locked countries in climate harmful activities.
- 3. Significantly scale up grant-based, new and additional public climate finance,** as a form of reparations in light of the climate and ecological debt owed by the global north to the global south. This will allow global south countries to implement adaptation and mitigation measures, including decommissioning fossil fuel projects, and to address Loss and Damage without having to go into more debt.
- 4. Bilateral and multilateral finance should be aligned with a 1.5 degree warming scenario and fair shares calculations, and not be used to finance fossil fuels.** Multilateral and international financial institutions should set deadlines for shifting finance out of fossil fuels and into sustainable, climate measures for adaptation, mitigation and to address Loss and Damage.

A starting point would be for multilateral and financial institutions to join the Glasgow Statement, a joint commitment launched at COP26 in 2021 to end new direct international public finance for fossil fuels by the end of 2022 and instead prioritise public finance for clean energy.¹⁹¹

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Debt Justice is a campaigning organisation working with others to end unjust debt and the poverty and inequality it perpetuates, in the UK and across the world.

Keep in touch

📧 debtjustice.org.uk ✉ info@debtjustice.org.uk
🐦 @debtjustice 📘 Debt Justice

Debt Justice, Oxford House, Derbyshire Street
London, E2 6HG, United Kingdom

Debt Justice is a company limited by guarantee no. 3201959
and a registered charity no. 1055675. Registered office:
Oxford House, Derbyshire Street, London E2 6HG.

