The Climate and Debt Crises vs. Instruments of Private Finance

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Basic Rationale for Innovative Finance in Debt and Climate

- Financing Gap in the Global South/ Lack of access to finance/ capital markets – high risk of investment in the Global South

- Instruments can complement-Debt Restructuring- rooted in IMF DSA

- Instruments:
  - Debt for Climate/Nature Swaps
  - Thematic Bonds-Blue/Green/Sustainability
  - Blended Finance
  - Guarantees
  - Debt for Climate Pauses (not an instrument per se- but considered a tool for restructuring)

Innovative Instruments of Finance

Instrument	Definition	Specific Rationale/Goal	Examples
Debt Swaps	A debt swap is a financial instrument that provides conditional debt reduction in exchange for the debtor agreeing to invest the freed-up resources (usually in local currency) in specific areas, such as education, health, climate or the environment.	An offer of concession (lower interest rate – longer debt repayment etc) earmarking climate commitments. Key promise- some form of debt reduction.	Debt-for-climate swaps- Belize (2021), Ecuador (2023), Gabon (2023)
Green Bonds-ESG, Sustainability Bonds.	Works as a normal bond but Green/ ESG/ Sustainability encapsulates various environmentally positive themes and commitments- e.g using all or part of capital for ethical/environmental/sustainability projects	Means of filling the Finance Gap for Global South countries. Proceeds-end use for climate commitments	ESG bonds issued by Global South Countries: Indonesia 1.25bn USD (2018) , Egypt 750 million (2020), Chile 473 million euros (2022)

Impact of Innovative Instruments of Finance

Instrument	Impact	Examples	
Debt Swaps	a) **Inherent conditionality**. b) Expensive! c) Greenwashing d) No participation from affected e) Divert reform-expensive distraction	Ecuador (2023 Galapagos Swap)- repurchase of $656 mn of sovereign bonds out of a total of $1.68 bn.	-Marginal reduction- 0.8% of GDP -Failing sustainability-no evidence of improving debt sustainability indicator. -Hidden financial cost-interest rate of 11% on new 'blue bonds'-existing bonds were yielding only 5/4% . -Enriched intermediaries. -Strict conditionalities
Green Bonds	a) **Greenium" (lower borrowing cost) is unproven)** b) **Exacerbates debt vulnerability**. c) **High risk of greenwashing.** d) **Unequal**	Nigeria- first sovereign bond in 2017 (raised approx. $29.7 million). Second in 2019 (raised $41 million. The 7-year green bond issued in June 2019 had a coupon rate of **14.5%**, higher than the 13.48% on the first green bond issued in	**2017 vs. 2019** -2019 green bond had a **higher yield (high interest)** than a comparable non-green bond. This demonstrates that the green label no guarantee. **Sovereign credit risk remains the primary pricing factor.** **Internationally:** **Continued- punitive interest rates paid by**