

GREENING IMF LENDING:

Elusive prospects, mixed evidence



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● Executive Summary

The IMF's growing engagement with climate issues represents a major development in the field of global economic governance, and its new Resilience and Sustainability Facility (RSF) is a significant innovation in multilateral climate finance. By recognizing the macro-critical nature of climate risks and integrating climate considerations into its lending activities, the IMF has taken steps towards addressing the intertwined challenges of revenue mobilization, debt sustainability, and climate change.

Are these developments revealing a new, greener *modus operandi* of the IMF? This review highlights several key challenges and areas for improvement in its approach:

Austerity Policies and Fiscal Space: The IMF's traditional emphasis on fiscal consolidation may undermine countries' ability to invest in climate change adaptation and mitigation. Austerity measures can limit public financing for green policies and hinder the implementation of green industrial policies. Countries like Kenya and Senegal under fiscal consolidation pathways of 5.7% of GDP between 2021-2025 and 3.7% of GDP end-2022-2025 respectively need to decide between cuts to politically-sensitive areas of public spending (e.g., education and health) versus policies that only have a pay-off in the medium- to long-run.

Debt Sustainability Analyses (DSAs): While the IMF has started incorporating climate issues into its DSAs, there are limitations in the methodology and assumptions used. The IMF should consider a wider range of physical and transition risk scenarios in its modelling efforts and ensure that DSAs accurately reflect the economic consequences of climate change.

Conditionality and Policy Advice: The conditions attached to IMF lending programs, including those under the RSF, should be carefully designed to support countries' green transition objectives. IMF policy advice should go beyond market-based approaches and carbon pricing to allow policy space for green industrial policies and comprehensive social protection measures, thereby contributing to a just green transition. Such explicit links to private finance form a novelty for IMF lending programs, which are generally focused on macroeconomic policies, rather than involved in microeconomic decisions of firms.

Energy Subsidy Reform: The IMF emphasizes removing energy subsidies as a key step toward a green transition, aiming to reduce fiscal deficits and align prices with carbon costs. In many countries, subsidies form a de

facto social policy, and their removal without appropriate and adequate social infrastructures in place can adversely affect vulnerable groups and exacerbate inequalities. The IMF should reconsider the nature, timing and pacing of its advice on energy subsidy removal to minimize such adverse social costs. Domestic resource mobilisation is essential for financing green transformation policies, provided it is pursued through progressive means rather than regressive policies like carbon taxes.

Social Impact: IMF-mandated austerity measures can disproportionately affect vulnerable social groups, exacerbating inequalities and undermining social protection policies. The IMF should prioritize policies that promote inclusive and sustainable development, taking into account the social impact of its lending programs.

● Introduction

The International Monetary Fund (IMF)—the central actor in global economic governance and the world’s lender of last resort to countries in economic crisis—has in recent years positioned itself at the forefront of policy debates over climate change and the green transition. As early as 2015, then-Managing Director Christine Lagarde (2015) explained that climate issues are “macro-critical”—that is, impacting the economy as a whole and, therefore, within the Fund’s remit. Eight years later, in the 2023 IMF-World Bank Annual Meetings in Marrakech, these issues were dominating the agenda, with current Managing Director Kristalina Georgieva reiterating that “climate risks affect macroeconomic and financial stability [... and] we are a financial institution, so we put money where our mouth is” (World Bank 2023b).

To transform these high-level pronouncements into concrete organisational action, the IMF has made several strides. At the broadest level, the organisation introduced its Climate Strategy in 2021, where it committed to scale up its engagement with macro-critical climate issues, primarily by expanding its analytical capabilities on these issues and incorporating climate considerations into its regular multilateral and bilateral economic surveillance (IMF 2021b). In the same year, the Comprehensive Surveillance Review committed to expand analyses on climate issues in line with the goals set out in the Paris Agreement, as well as to recruit additional staff with climate-relevant economic expertise (IMF 2021a). The IMF also developed a new lending facility—the Resilience and Sustainability Facility (RSF)—that is intended to provide financial support primarily to climate-vulnerable countries that face steep adaptation and mitigation challenges (see Box 1). The RSF has a lending capacity of SDR 10.4 billion (after excluding commitments of SDR 6.3 made to date) and has already approved 18 programs. The IMF’s closer engagement with the economic dimensions of climate change is a positive development, and the introduction of such considerations into its lending activities is welcome, as it holds the promise of helping borrowers pre-empt large scale economic dislocations from environmental risks.

Box 1: The Resilience and Sustainability Facility and the road to the green transition

Established in 2022, the RSF represents the IMF’s most significant foray into incorporating climate considerations (as well as pandemic preparedness) into lending operations. As of end-2023, IMF member states have pledged \$42.8bn, of which SDR 16.7bn are usable loan resources that this facility can

lend out. Approximately two thirds of IMF members are eligible for borrowing. What makes these funds distinct from other IMF lending facilities is that they are intended to support policy reforms that reduce macroeconomic risks due to climate change over the long term, with corresponding long maturities and grace periods. To signal commitment to reform, RSF loan recipients need to simultaneously have in place a conditionality-carrying IMF program, as well as sustainable debt burdens. In addition, the RSF loan also carries conditionality that borrowers must implement before any disbursements are made. In the two years of its operation, 18 programs have already been approved (until March 2024), a sign of the urgency of securing low-cost finance to support green transition objectives.

But a core challenge remains: countries that resort to the IMF for financial support are facing policy problems limiting their policy space. This is particularly true for those countries undergoing balance-of-payments problems, that need to request financial support from the IMF through its lending programs. Is the reform path designed by Fund staff and national authorities—and subsequently included in lending agreements—going to put these countries on a solid trajectory to simultaneously deal with economic turmoil as well as climate change? This is important to address, because problems stemming from climate change can become balance-of-payments issues in the medium- or long-run (for example, through export shocks due to global decarbonization efforts, through additional debt to deal with damage from climate change, or through developing countries' currency liquidity premia). This situation can potentially lead to entrenching financial subordination of decarbonizing developing countries, whereby their policy space for green transition policies is constrained due to the need to implement “export-friendly policies and to adhere to investors' taste for profit and security by creating an investor-friendly climate” (Löscher and Kaltenbrunner 2023). Most notably, climate change generates physical and transition risks, as well as spill-over risks from decarbonisation policies of trading partners, like the EU's Carbon Border Adjustment Mechanism (Gallagher et al. 2023), thereby—sooner or later—requiring engagement by the IMF.

The IMF sought to address these issues indirectly in recent high-profile publications. The October 2023 Fiscal Monitor examined the relationship between fiscal policy and the green transition, and—based on simulations—argued that the introduction of comprehensive climate policy packages is

likely to increase public debts and deficits, particularly in the short run but also persisting into the medium term (IMF 2023a). This means that many developing countries “would be unable to afford a large redistribution of carbon revenues or meet their public investment needs” (IMF 2023a, 13). In addition, the Global Financial Stability Report, published at the same time, delivers a similar message: given the limited capacity to ramp-up public investment, developing countries should introduce financial policies that would mobilise private capital, including by public-private risk sharing, blended capital and other innovative financial instruments (IMF 2023b). Yet, neither of these reports dealt directly with the IMF’s own practices in its lending programs, which—as past research has shown—can depart markedly from promises made through organisational rhetoric (Kentikelenis and Stubbs 2023a). Further, they both underplay the transformative potential of green industrial policies, seen as out of fiscal reach for most developing countries.

This report tackles these issues in light of recent IMF lending. First, we discuss the links between debt and climate risks, examining the ongoing debt problems in the Global South as well as the IMF’s toolkit for approaching such questions. We next turn to the promise and practice of the IMF’s new RSF facility and present evidence from the conditions attached to these loans. Subsequently, we examine how the IMF’s broader policy advice impacts countries’ green transition trajectories, with special emphasis on the experience of Kenya and Senegal. The report concludes by outlining a path forward for the organisation’s engagement with climate issues.

Debt, climate risks, and the measurement of economic consequences

The IMF’s growing engagement with climate issues takes place against a backdrop of deepening debt problems in developing countries. This is important because of the many transmission channels between climate risk and debt. First, climate change has a range of follow-on implications for fiscal sustainability, financial sector stability, and overall macroeconomic health, which in turn affect debt sustainability (Volz and Ahmed 2020). Second, countries with high degrees of climate vulnerability also have to pay risk premiums on their sovereign debt, which inevitably increases their overall debt burden (Kling et al. 2021). Indicatively, V20 countries—a group of climate-vulnerable countries—faced average real interest rates of 9% in the mid-2010s, compared to 6% for G20 members, the group of 20 richest economies in the world (Volz and Ahmed 2020, 20). Further, high levels of debt service also hamper the introduction of green transition policies, as public funds get directed to paying off external debt rather than financing climate change adaptation or mitigation projects (Ramos et al. 2022). Debt problems also prompt countries into development trajectories that are

antithetical to green transition objectives: civil society has pointed to “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” (Woolfenden 2023).

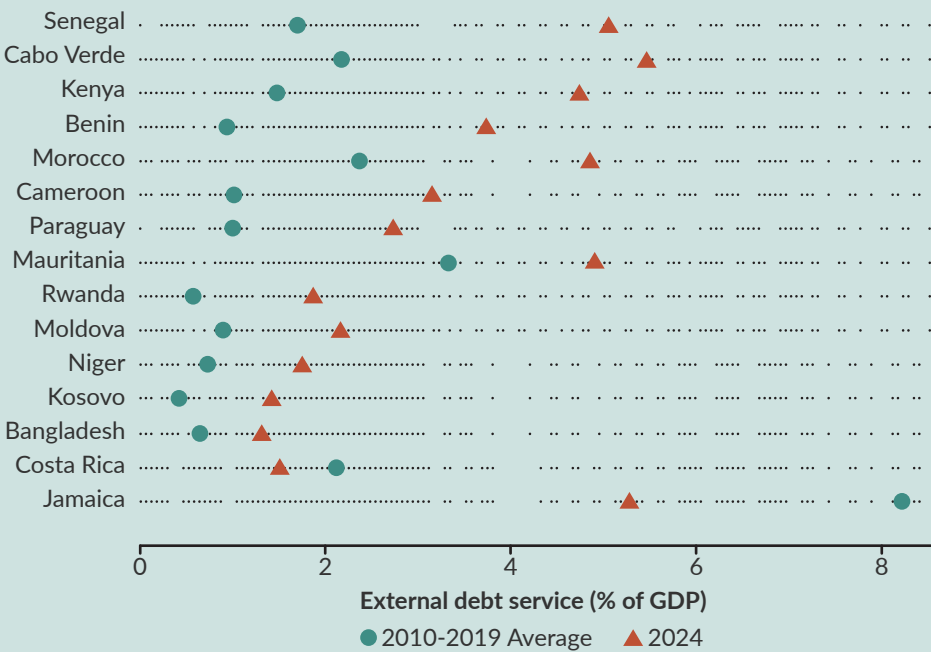
In other words, there is a deep and reciprocal relationship between climate change and debt, whereby climate risks contribute to debt problems, and debt problems make dealing with climate risks even more difficult in resource constrained environments (ActionAid International 2023). Against this backdrop, how policymakers approach debt problems matters. The IMF’s main approach towards debt issues is the Debt Sustainability Framework (a joint enterprise with the World Bank), which classifies the debt vulnerabilities of countries and—when appropriate—calls for debt restructurings. Of the 69 low-income countries included in this framework, 11 are already in external debt distress (World Bank 2024). A shallow reading of this data would suggest that debt problems are mostly limited and not systemically important, as low-income countries have relatively small economies that pose no major risks for global financial stability. However, such a reading would miss the fact that many more countries are at moderate or high risks of debt distress. Moreover, in order to prevent greater debt problems, countries are adjusting their public finances to primarily ensuring debt sustainability and market confidence, rather than investing in climate change mitigation or adaptation policies. The World Bank estimates that in servicing their external debt, developing countries spent \$443.5bn in 2022 alone (World Bank 2023a).

A closer look at debt service statistics of the first 17 RSF loan recipients reveals the scale of the problem. Figure 1 shows the average of external debt service (as a share of GDP and excluding debt to the IMF) over the decade preceding the pandemic (blue dot) and compares it to its level in 2024; the countries are ordered by the magnitude of difference (excluding Barbados and Seychelles due to data unavailability). All countries excluding Costa Rica and Jamaica have witnessed increases, often sizable ones. Senegal, Cabo Verde, Kenya, and Benin stand out for having the steepest rises in debt service, while rising external debt is a smaller problem for Niger, Kosovo, and Bangladesh.

Helping countries deal with such debt problems is a core function of the IMF, and—to this end—the organisation employs Debt Sustainability Analyses (DSAs) to shape its activities in this area. The methodology for these analyses depends on the income classification of the evaluated country: one methodology applies to low-income countries, while another to the remaining so-called ‘market access’ countries. These evaluations are

important because if the IMF considers a country's debt unsustainable, it must stop lending to it and propose debt restructuring. Yet, such negative assessments are uncommon (Rehbein 2023). A pre-pandemic review at the IMF showed that highly debt-vulnerable countries generally did not pursue restructurings, even though the latter were associated with a greater probability of the IMF's lending being successful (IMF 2019).

Figure 1. External debt service in RSF program recipients



Source: Authors, using data from the October 2023 World Economic Outlook report.

In light of the climate crisis, the IMF has started incorporating climate issues within DSAs. For example, the recently updated framework for market access countries ('Sovereign Risk and Debt Sustainability Framework') has introduced a two-part climate change module. The first component examines the impact of adaptation investments, and the other focuses on mitigation policies. Based on the scenarios pursued in these modules, the outcome is projections for debt-to-GDP and gross financing needs-to-GDP ratios, which—in turn—illustrate debt-related risks from green transition policies (IMF 2021g). Pursuing these analyses is mandatory for requests under the RSF, thus foregrounding the centrality of this debt toolkit in the IMF's engagement with climate issues.

The analyses and assumptions included in DSAs remain the subject of sustained debate. In relation to climate issues, a recent analysis pointed out the limited consideration of different physical or transition risk scenarios into

the IMF's modelling efforts (Maldonado and Gallagher 2022). This matters because once different risks are considered, and the introduction of baseline or greener transition policies modelled, then the findings on government financing needs and public debt can vary considerably. Beyond the inclusion of climate issues, debt sustainability analyses are not an exact science, but an exercise that entails a high degree of subjective judgement by IMF staff (Hagan 2023), and also one that is heavily politicised due to its momentous implications for opening up a path for debt restructuring (Wheatley 2023).

The climate module within DSAs is not the only set of analytical modules that the IMF has put forth. In recent years, the IMF introduced the Debt–Investment–Growth and Natural Disasters (DIGNAD) toolkit, which examines the economic implications of physical risks. In relation to debt, this toolkit enables assessing debt vulnerabilities in scenarios of both the aftermath of a natural disaster and of the introduction of “ex-ante policies, such as building adaptation infrastructure, increasing fiscal buffers, or improving public investment efficiency” (IMF 2024c).

The build-up of growing debt vulnerabilities, combined with inadequate analytical toolkits, pose major challenges for crafting development policies and pre-empting debt crises. Indeed, the forthcoming review of the DSA framework for low-income countries is expected to grapple with how to expand the remit of analysis and make this instrument fit for purpose, in light of the economic challenges posed by climate change (Fresnillo 2024). In following this path, however, the IMF is not alone: in recent years, the World Bank has assumed an ever greater role in analysing how countries can integrate the fight against climate change with the pursuit of developmental objectives. This track-record is summarised in Box 1, and represents a momentous development because it has supplanted many of the IMF's own analytical frameworks. As discussed below, many of the IMF's climate-related measures are drawn directly from the World Bank's Country Climate and Development Reports.

Box 2: The proliferation of climate change analyses by international financial institutions

When the IMF and the World Bank both sought to participate in global efforts to combat climate change in the mid-2010s, one of their key innovations was to introduce a joint analytical toolkit for countries: the Climate Change Policy Assessment (CCPA). Between 2017 and 2020, six such evaluations were conducted for small island developing states, conducted for six small island states on a pilot basis between 2017- 2020. Given high demand for such a product, the IMF planned to continue and scale up CCPAs to expand the coverage of countries beyond small states.

Despite early optimism for the prospects of such cooperation, World Bank leadership decided to pause their engagement with the IMF on the CCPA. This was a source of concern within the IMF, as staffers considered this a duplication of work that the IMF was already performing and a step back for enhancing coordination between the two institutions (Kentikelenis, Stubbs, and Reinsberg 2022). The World Bank launched its own climate-related evaluations through the Country Climate and Development Reports (CCDR) in 2021. In response, the IMF developed the Climate Macroeconomic Assessment Program (CMAP) with a focus on its comparative advantage in macro-fiscal analysis, public financial management and tax policies. Two pilots were conducted between 2021-2022. After the review of the pilots, the IMF concluded that the Fund would provide streamlined CMAP in exceptional cases while expanding targeted capacity development, in order to avoid duplication of the work. The IMF now draws on the World Bank's CCDRs to inform the analyses and policies included in recent loan agreements, while using more targeted toolkits such as the Climate Public Investment Management Assessment (IMF 2024b) and the Climate Policy Diagnostics.

Even so, the IMF's RSF has been the pioneering development in global climate finance, as it provides financing to climate-vulnerable countries on advantageous terms. For example, unlike the new Just Energy Transition Partnerships (JETPs) that offer funds by consortia of Global North countries on a mix of concessional and market terms and have been criticized for overly promoting creditor priorities (Bradlow and Kentikelenis 2024), the RSF is a truly multilateral alternative for financing green transition objectives. Consequently, closely tracking its practices and performance allows us to monitor whether the IMF is indeed helping to augment the policy space of Global South countries to finance green transition policies, or whether it is simply repackaging market-oriented policies in a new guise—we turn to this question next.

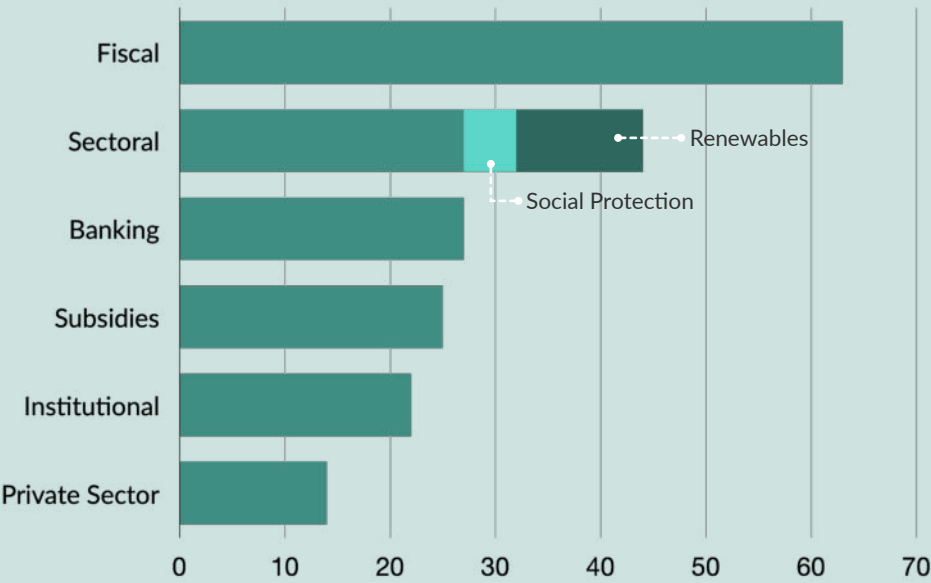
The promise and practice of Resilience and Sustainability Facility loans

Between 2022 and March 2024, 18 countries have had such loans approved, totalling SDR 6.3bn of committed resources. This is higher than the pre-pandemic average of lending under the Poverty Reduction and Growth Trust, that averaged SDR 1.2bn per annum over 2000-2019 (IMF 2022a), although RSF financing has only partially overlapping criteria with this Trust. Codifying the early experience with RSF lending, the IMF issued an operational guidance note for staff in late 2023, where the organisation clarifies that RSF conditionality—known as Reform Measures (RMs)—should focus on “reforms that lead to permanent institutional changes, such as by involving legislative

changes” and should have a catalytic effect that would facilitate private investment and even “help attract private investors” (IMF 2023e). Such explicit links to private finance—including through consultations between IMF staff and investors “to identify reform measures that can reduce barriers to climate finance” and “to reduce the risk of such investments” (IMF 2023e)—form a novelty for IMF lending programs, which are generally focused on macroeconomic policies, rather than involved in microeconomic decisions of firms.¹ The rationale, according to the IMF, is that through such mobilisation of private finance can adequate amounts be raised for climate change adaptation and mitigation, as most climate objectives “are not attainable without the mobilization of significant private finance” (IMF 2023e, 24). However, recent scholarship has criticised this approach for limiting the possibility of green developmental states emerging, instead relying on states to assume the risks of private investment (Gabor 2021).

To investigate the actual content of the IMF’s RSF programs, we collected all RMs specified in the first 17 agreements—yielding a total of 195 conditions—and then classified them in mutually exclusive policy areas. As Figure 2 shows, nearly a third of RMs targeted fiscal policy: these reforms were almost always related either to Public Financial Management or Public Investment Management measures related to climate policy. For example, Benin and Rwanda committed to implement ‘climate budget tagging’ to ensure climate is embedded into domestic budgetary decision-making, while Mauritania committed to incorporate climate considerations in all aspects of its public investments.

Figure 2. External debt service in RSF program recipients



Source: Authors

¹ However, the IMF’s Guidance Note also specifies that the IMF “cannot seek to mobilize climate financing by development banks or investors on behalf of the member, nor act as a financial advisor, and it cannot be involved in the management or oversight nor vouch for the bona fides or success of any climate finance vehicle or fund, or any climate project. The Fund focus is to provide policy advice to support an enabling environment for productive investments” (IMF 2023e, 30)

Turning to sectoral policies, this is a varied set of measures aiming at altering policy in economic sectors of relevance to the IMF borrower. For example, Benin, Morocco, and Barbados had to implement reforms to water use, Benin and Seychelles on revamping building codes, and Kosovo and Paraguay on electricity markets. Importantly, about a quarter of sectoral reform measures directly targeted renewable energy. Paraguay implemented reforms to enhance use of electric vehicles and incentivize recycling, Kosovo made steps to increase use of wind and solar power in its energy matrix, and Jamaica introduced new fiscal incentives for investment in renewables. Finally, five of the 44 sectoral measures directly related to social protection issues, and four of those sought to institute or reform social registries, a measure related to the introduction of compensation measures for the energy subsidy removals (discussed at length below).

Banking issues, taxation and subsidy measures, and institutional reforms all accounted for approximately 12-14% of RSF conditions. In these instances, countries are required to implement policies like incorporating climate issues into bank stress testing, the removal of energy subsidies, and the introduction of various legal frameworks to embed consideration of climate risks into different policies. Finally, RSF agreements also include measures pertaining to private sector investments into green transition policies (7% of total conditions). These were primarily of two types. First, they related to country efforts at mobilizing climate finance, as was the case in Cabo Verde and the Seychelles. Second, several Reform Measures sought to revamp domestic frameworks on public-private partnerships in order to include climate requirements, as was the case in Bangladesh, Jamaica and Cabo Verde.

While this is early evidence on how RSF agreements incorporate climate into the IMF's activities, these reforms form only part of the broader apparatus of conditionality included in IMF programs. Borrowing countries still need to implement a range of additional reforms attached to their parallel conditionality-carrying IMF programs. The organisation provides this financial support through a variety of lending instruments, ranging from the short-term Stand-By Agreements that are usually heavy on fiscal consolidation measures but generally only last 12-18 months, to longer term facilities—like the Extended Credit Facility (ECF) or the Extended Fund Facility (EFF)—that have more leeway for including a holistic policy design that is sensitive to climate issues. The latter programs, similar to the RSF, have medium- to long-term horizons, and it is thus no surprise that 12 of the 18 countries with RSF loans have parallel lending agreements under the ECF and/or the EFF. It is through an analysis of these broader non-RSF conditions that we can generate a more complete understanding of how the IMF's overall policy advice has evolved and we turn to this issue next, with special reference to the experiences of Kenya and Senegal.

Fiscal consolidation, market-based approaches to the green transition, and their limits

There is a fundamental tension in IMF lending: the organisation's programs demand that borrowers introduce far-ranging fiscal consolidation measures—commonly known as 'austerity'—with the hope of improving their macroeconomic positions, yet these are the policies that constrain countries' ability to introduce green transition policies. This occurs through several pathways. First, and most obviously, austerity measures limit available public financing for climate change adaptation and mitigation. Public funds to support a range of green policies—like phasing out coal, incentivizing a switch to cleaner energy sources, scaling up production of renewable energy sources, or providing green subsidies—are likely unavailable for countries introducing extensive budget cuts, and that need to decide between cuts to politically-sensitive areas of public spending (e.g., education and health) versus policies that only have a pay-off in the medium- to long-run.

Second, austerity measures are also likely to stunt the introduction of any green industrial policies. Such policies include incentives for research and development and tax relief for green investments by the private sector and require active state policies to appropriately and effectively channel green investments. Absent such investments, countries run the risk of relying primarily on private finance to pursue a green transformation (discussed below) or on the financing available through multilateral institutions and donors.

Finally, austerity also has more insidious effects on the likelihood of the green transition. A long-established strand of academic scholarship has shown that the economic performance of countries implementing IMF programs tends to suffer (Dreher 2006; Vreeland 2003). The reasons for this are many and go beyond the observation that countries that resort to IMF programs are generally already going through crisis before resorting to the organisation's lending. Ineffective or overambitious IMF-designed policies, inappropriate pacing of reforms, and poor analytical frameworks (for example, in estimating the fiscal multipliers that inform the design of austerity measures) can all contribute to deepening and prolonging pre-existing economic troubles.

Depressed economic activity has climate-damaging follow-on implications. Households find it unaffordable to shift to greener consumption patterns, with low-income ones being particularly hard-pressed. Private firms struggle to invest in green technologies and adaptation measures, thereby increasing their vulnerability to climate shocks and forestalling reductions in their emissions. And the public sector is further starved of revenue sources. In line

with the goals set out in the Paris Agreement and the Nationally Determined Contributions that spell out countries' climate plans, domestic resource mobilisation is essential for financing green transformation policies, provided it is pursued through progressive means rather than regressive policies like carbon taxes. But austerity-induced economic downturns further reduce tax revenues.

More broadly, the effects of austerity are differentially distributed. In particular, low-income households—that are least responsible for climate damage and are already vulnerable to climate risks—are the most at risk of experiencing further deteriorations in income and living conditions. Pakistan's recent experience provides a case in point. While implementing IMF and World Bank programs, the country removed energy subsidies (a policy covered in detail in the subsequent section), while not having in place comprehensive social protection policies. This meant that vulnerable groups were hit both by the removal of subsidies and by the follow-on increases in the costs of everyday goods (Recourse 2023). This evidence strengthens a long-standing concern that IMF-mandated austerity adversely affects vulnerable social groups—including women, children, and those informally employed or unemployed—and widens inequalities (Donald and Lusiani 2017; Lang 2021; Saalbrink and Amerasinghe 2021).

What has been the austerity track-record of IMF lending to Kenya and Senegal? In both countries, the IMF required the introduction of extensive budget cuts through its EFF/ECF agreements, which form the backbone of the economic adjustment programs applicable in the countries. Kenya's program mandates an increase in the primary fiscal balance by a staggering 5.7 percentage points: from a deficit of 4.0% of GDP to a 1.7% surplus by the 2024-2025 fiscal year. Senegal is also mandated to implement steep cuts to the primary budget deficit: from 4.4% of GDP at end-2022 to 0.7% by 2025. In advocating for such measures, the IMF's advice disregards the urgent financing needs for climate adaptation and mitigation that Senegal's NDC estimates requiring \$13 billion in financing by 2030.

These austerity policies can be at odds with the goals of the RSF programs, which call for scaled up financing for adaptation projects. To be sure, these adverse effects are not destiny: it is possible that the ECF/EFF reforms live up to their promise of improving revenue mobilization and spending efficiency, thereby improving fiscal space for green transition policies and reducing debt vulnerabilities. It is too soon to tell whether this will actually materialize, but evidence of the past track record of IMF programs vis-à-vis social spending leaves little ground for optimism. Despite earlier long-standing pronouncements by the IMF that its programs were designed in ways that would increase rather than limit public social expenditures, this—for the most part—failed to materialize in IMF borrowers (Kentikelenis and Stubbs 2023a).

Beyond fiscal policy, IMF programs also target a broader set of policies that seek to alter countries' economic policy profiles and the relative role of the state versus the market in shaping development policies. For example, the IMF has a long track record of promoting carbon pricing as a key policy to underpin climate change adaptation and mitigation, as was the case in Kenya's recent RSF agreement. Such policies can indeed be powerful tools in the fight against climate change, but they can only be one part of a broader approach towards the green transition. As the IMF's own research has shown, implementing green transition policies in the Global South also entails increasing low-carbon manufacturing capabilities domestically (Prasad et al. 2022) and providing public support for research and development (Bettarelli et al. 2023). These are forms of green industrial policy that are neglected in the context of the IMF's advice.

At the same time, other policies included in IMF agreements may be in direct contradiction to implementing climate change adaptation and mitigation policies. Senegal's program provides a case in point. Since the country's discovery of oil and gas, the IMF has foregrounded in its analyses how the exploitation of these natural resources is likely to affect public finances and debt sustainability. In contrast, the loan agreement fails to meaningfully consider the perverse climate implications of fossil fuel extraction. While the organisation briefly acknowledges the inherent tradeoffs vis-a-vis environmental protection, ultimately the IMF solely focuses on the short-term economic implications of fossil fuel production. Detailed analyses of how global attempts at decarbonization might affect export earnings are notably absent, and the risks to damage for the livelihoods of coastal communities are not considered.

Subsidies and social spending: tools for a just green transition?

In the IMF's view, removing energy subsidies forms a key plank of the proposed path towards the green transition (de Mooij, Keen, and Parry 2012). This is because such a reduction purportedly has doubly positive effects: it reduces the fiscal deficit by removing a drain on the public budget, and it reduces energy consumption by ensuring that prices reflect the true cost of carbon. While the economic logic of subsidy removal might be compelling and—as we documented above—these policies are commonly included in IMF loan conditionality, such measures have clear social and political implications. Indeed, recent political turmoil in Ecuador and Sri Lanka is linked directly to government decisions to remove subsidies.

Discussion of subsidies needs to distinguish between two types of intended recipients. First, subsidies can be directed to firms to support their productive activities and protect them from high energy prices. As a sort of industrial policy, this approach can have beneficial effects on economic

activity, even if it does not expose firms to the true price of carbon. But there is no guarantee that this in-kind support to producers will even be reinvested into productive, development-enhancing activities—they may just end up accumulating profits. Consequently, policymakers face two simultaneous challenges: how to phase out energy subsidies to producers while also ensuring that the additional costs are not passed on to consumers (here, taxation of past hyper profits in the form of windfall taxes can help raise public revenues to compensate consumers for higher prices); and how to ensure that any new industrial policies are ‘green,’ thus not hampering domestic or global efforts to combat climate change.

Second, energy subsidies can be directed to consumers, which is a *de facto* social policy in many Global South countries where other forms of redistribution and social provision are severely constrained. However, a common problem is that these subsidies are often not targeted, thus favouring those with higher incomes more in absolute terms and contributing to widened inequalities. Even so, individuals with lower incomes still benefit substantially from these policies, as fuel expenditure tends to be a high proportion of their overall spending and these subsidies may be the only type of support they receive from the government. Thus, even though fuel subsidies do not expose individuals to the true cost of carbon, they also help maintain social peace and provide substantial support to the low-income individuals.

The IMF’s approach to fuel subsidies is their wholesale elimination and replacement by targeted social assistance measures. In Kenya, all fuel subsidies were eliminated in March 2023 in order to fulfil a condition to “publicly announce and constitute a taskforce to oversee the progressive elimination of the fuel subsidy” (IMF 2023a, 116) and to meet a structural condition requiring the submission of a supplementary budget consistent with programmed deficit and revenue targets; and cost-based upward adjustments to electricity prices were effective April 2023 and occurred in response to a structural condition to “submit to the cabinet sub-committee on KPLC an action plan to restore KPLC’s medium-term profitability and fully cover any financing gaps (IMF 2023a, 115). The program purports to protect vulnerable groups in a set of non-binding quarterly indicative benchmarks on priority social expenditures. However, these floors only preserve current spending levels once accounting for inflation (Kentikelenis and Stubbs 2023b)—and represent a decline as a share of GDP from 3.6% in the 2020-21 fiscal year to 3.2% in 2023-24 (IMF 2024d, 9)—rather than increasing it in a time of heightened need, as reflected by rising poverty rates and joblessness since the pandemic onset and the drought.

In Senegal, the aforementioned fiscal consolidation is to be driven primarily

by a phasing out of untargeted energy subsidies—via reductions to gasoline and diesel subsidies under the ECF-EFF and via increases to electricity tariffs under the RSF—from 4% of GDP in 2022 to 1% of GDP in 2024, and to completely eliminate them by 2025. To facilitate this process, the IMF set structural conditions under the ECF-EFF requiring the government to establish by November 2023 an independent committee with the mandate to determine and publish final consumption fuel prices based on a revised pricing formula; and to revise the current pricing formula for petroleum products to ensure that prices at the pump reflect developments international markets by December 2023. The IMF also included a condition under the RSF stipulating that the government adopt by June 2024 an electricity tariff adjustment plan that would see it gradually eliminated. According to the IMF “generated savings will be redirected to strengthening social welfare policies and, especially, increasing investment expenditures” (IMF 2023f, 54). To this end, the program includes a structural benchmark requiring a scaling up the social safety net system's coverage from 500,000 to one million households by June 2024. While the IMF also includes as a quarterly indicative benchmark a floor on social expenditures as a share of total government spending, this is set at 40% throughout the program thus far (i.e., up to December 2024), so does not clearly represent an increase, especially as government spending—the denominator—is being cut.

Such policies are regularly included in IMF loans, and the same is true of recent RSF agreements, as discussed earlier. While the policy rationale is compelling, its realisation is marred with difficulties. The most pressing concern relates to the pacing of subsidy removal. The IMF’s policy advice tends to promote the simultaneous removal of subsidies and investment in social assistance policies, using part of the savings generated from the elimination of subsidies. For example, Benin’s December 2023 IMF loan calls for establishing “a compensatory mechanism to limit the effect of fuel subsidy reform on vulnerable groups using the Social Registry” (IMF 2024a, 51). However, building up such compensatory mechanisms takes time, and often key populations that would benefit from compensation struggle to access these policies (e.g., due to bureaucratic hurdles, complex eligibility criteria, or inadequate information). In other words, if low-income households are to be adequately sheltered from the effects of energy subsidy removal, the appropriate infrastructures and social programs need to be in place earlier in order to ensure that no blows to incomes and livelihoods are incurred. Yet, within the context of IMF programs, this is not always the case. On the more promising side, Moldova’s loan agreement explicitly foresees support for consumers related to energy price increases (IMF 2023d). The challenge for the organization is to more systematically include appropriately phased measures in its lending programs.

In short, energy subsidy removal can be an important tool to combat excessive fuel consumption. However, unless it is appropriately designed and targeted it can lead to extensive hardship among the population, which simultaneously erodes the social basis of support for green transition policies and undermines the principles of a just energy transition.

Policy recommendations

IMF Board

- For the RST interim and full review:
 - Ensuring more coherence between climate-related objectives of RST programs and the concurrent UCT programs.
 - Change in the qualification criteria to allow for more access to rechannelled SDRs in the current world macro context.
- Review of the IMF's Climate Change Strategy to come up with a more coherent approach to climate policy, including an expert panel.
- The IMF needs a framework to ensure conditionality and surveillance recommendations are aligned with 1.5C pathways, ensuring the necessary fiscal space. The RST should not work in isolation and ignore the impact of the IMF's traditional operations.
- IMF must abide by UNFCCC and human rights frameworks.
- The review and subsequent update of Debt Sustainability Analyses should consider how to meaningfully include climate financing needs into the debt sustainability framework.
- The IMF Board must consider emergency measures given the debt crisis, including debt cancellation to ease the fiscal burden on countries budgets for them to be able to respond to the climate crisis.

IMF staff and management

- Draft a guidance note around energy subsidies, to ensure Staff are hold accountable to the impact of its recommendations and its alignment with just transition guidelines.
- Transparency around climate diagnostic tools that feed into the design of arrangements under the Resilience and Sustainability Trust.
- Wider engagement with civil society organisations at a bilateral and multilateral level.
- The transition, social and environmental risks of exacerbating reliance on fossil fuel exports must be properly addressed.

IMF mission engaging with the Senegalese government

- Integrate climate considerations into political reforms and supporting efforts to adapt to climate change with adequate financing.
- Strengthen institutional capacities of the state for effective implementation of economic and climate reforms.
- Encourage transparency and good governance in the management of natural resources, particularly in the exploitation of new oil and gas fields.
- Promote political and social stability to foster an investment-friendly environment.

IMF mission engaging with the Kenyan government

- Properly assess the impacts of fiscal consolidation in development pathways aligned with 1.5C.
- Assess the impacts of energy generation privatisation in balance of payment stability.
- Support the Kenyan government in reducing its debt burden through progressive policies that address the Paris Agreement.

For Global South governments

- Governments should develop long-term climate policy development strategies that can demonstrate the positive case for frontloading public investments in mitigation and adaptation.

● Case Study I:
KENYA

● Background

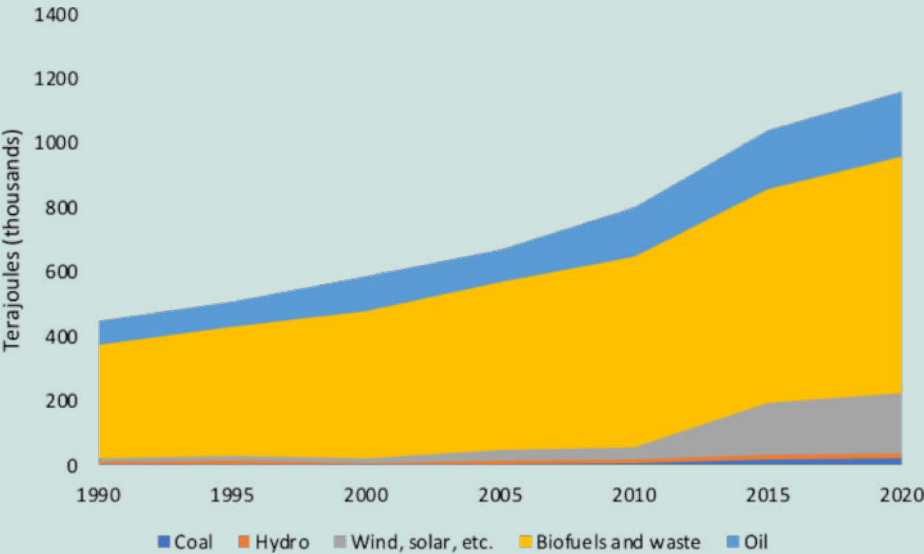
Kenya is a lower-middle income country of 54 million people and an estimated \$113 billion economy, with an income per capita of \$2099 (World Bank 2023h). The country grapples with significant developmental challenges, including high levels of economic inequality and poverty, governance issues, and climate vulnerabilities stemming from its reliance on rainfed agriculture. Kenya achieved sustained economic growth in recent years, averaging 5.7%, between 2015 and 2019, one of the fastest growing economies in Sub-Saharan Africa (World Bank 2020). The country suffered a mild economic downturn of only 0.3% in the face of the COVID-19 pandemic, followed by a 7.6% rebound. Since 2022, the economy has experienced stable growth of circa 5% per year and is projected to maintain this performance in the next few years, although this is subject to uncertainty given Kenya's exposure as a net fuel, wheat, and fertiliser importer to the global price impacts of the war in Ukraine (World Bank 2023g).

While Kenya's economic growth remains strong, the country's public finances are cause for concern. Kenya's public debt surged from 40% of GDP in 2012 to 73% by end-2023 in order to fund mega-infrastructure projects (e.g., the Mombasa-Nairobi Standard Gauge Railway), respond to the COVID-19 pandemic, and navigate climate change-induced droughts, with debt service consuming about 55% of government revenues (IMF 2021e, 2024d). This increase in debt is underpinned by steep growth in high-interest foreign commercial loans (Okoa Uchumi Campaign 2020). Indeed, Kenya recently offered a 10.4% interest rate on new governments bonds in order to avoid a default—compared to the 6.9% bonds they were replacing (Savage and Jones 2024). The government's increasing debt burden prompted protests on social media to dissuade the IMF from approving a loan, with critics alleging loans were misappropriated by corrupt officials and that citizens stand to bear the brunt via higher taxes (Mwaura 2021).

In terms of climate mitigation, Kenya published its Updated Nationally Determined Contribution (NDC) in 2020, pledging to cut emissions by 32% by 2030 relative to the business-as-usual scenario and committing to domestically fund \$3.7 billion of the estimated \$17.7 billion in costs (Government of Kenya 2020). Kenya emitted 72.6 million tonnes of CO₂ equivalent in 2020 (the most recently available data), representing 0.15% of global greenhouse gas emissions (World Resources Institute 2024a). At 1.35 CO₂ equivalent per person, the country is one of the lowest emitters per capita in the world (174th of 198 countries). Agriculture is the leading source of emissions, at 66%, primarily from enteric fermentation and inefficient

animal waste management, followed by energy at 25%. In terms of the country’s energy mix, Figure 1 shows that it is dominated non-fossil fuel sources, including 63% from biofuels and waste, 16% from wind and solar, and 1% from hydro. However, use of biomass for domestic heating and cooking has resulted in substantial deforestation and land degradation (World Bank 2021). Fossil fuel sources accounted for only 19% of the energy supply, primarily oil. In terms of electricity, 90% is generated from clean sources, including geothermal (48%), hydro (22%), and wind (12%); and the country aims to reach 100% from renewable sources by 2030 (World Bank 2023d).

Figure 3. Total energy supply in Kenya, by source



Source: International Energy Agency (IEA 2024a).

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With regard to climate adaptation, Kenya pledged to domestically fund \$4.4 billion of the estimated \$43.9 billion in costs (Government of Kenya 2020). The country is highly vulnerable in terms of its exposure, sensitivity, and ability to adapt to the impact of climate change, ranked 150th of 185 countries in the ND-GAIN index (Notre Dame Global Adaptation Initiative 2023). Communities have suffered significant losses in agriculture due to increases in temperature, more erratic rainfall, and more frequent and extreme climate events such as storms, floods, and droughts, disproportionately affecting the livelihoods of the rural poor (World Bank 2021). As the economy is highly dependent on rainfed agriculture, macroeconomic stability is also at risk. For example, the tea sector is one of Kenya's top foreign currency earners (along with tourism and remittances), and employs about three million people (Bhalla 2021), but areas with optimal and medium tea-growing conditions are expected to shrink by 25% and 40% respectively by 2050 due to climate change (Jayasinghe and Kumar 2020). Kenya's climate vulnerability is also demonstrated by the most recent multi-season drought of 2020-23, which reduced agricultural output, elevated food price inflation, and slowed down poverty reduction, as well as placing a drag on government fiscal resources (World Bank 2023g). Previously, the 2008-11 drought cost Kenya US\$12.1 billion, including US\$0.8 billion from the destruction of physical assets and US\$11.3 billion from losses across all sectors of the economy (IMF 2024d).

Relationship with the IMF

Kenya has participated in five IMF lending programs since 2010. In January 2011, the country signed on to a 36-month loan for \$509 million aimed at boosting international reserves while adopting gradual fiscal consolidation (IMF 2011), for which all six program reviews were completed and the entire amount was drawn. Then, in February 2015, the government requested precautionary access to \$688 million across a 12-month program with two program reviews to protect against shocks in global financial markets and security- and weather-related risks (IMF 2015a). All reviews were completed and no credit was drawn. The government entered into a follow-up 24-month program in March 2016 for \$1.5 billion, again to guard against external risks that might lead to a balance of payments need (IMF 2016). The program went off-track after one of four scheduled reviews: conditions on

the primary deficit were missed due to drought and election-related expenditures; and monetary policy effectiveness declined because of the introduction by parliament of interest rate controls (IMF 2018).

Against the backdrop of the unfolding Covid-19 pandemic, the IMF disbursed \$739 million under a non-conditionality emergency loan in May 2020 to support the fiscal response and a pandemic-induced balance of payments gap (IMF 2020a). The IMF then approved a 38-month lending program with conditionality in April 2021, unlocking access to \$2.3 billion over the course of seven reviews. The ongoing program aims to continue supporting the government’s COVID-19 response as well as reduce debt vulnerabilities via multi-year fiscal consolidation, strengthening governance, and enhancing the monetary and financial sector framework (IMF 2021e). The first review of the program was completed in June 2021 and the second in December 2021, both without major delay (IMF 2021d, 2021c). More significant interruptions occurred in the third review, completed July 2022, due to—inter alia—a condition on the supplementary budget containing tax measures for 0.4 percentage points of GDP, including income tax changes, excise rate increases, and VAT exemption removals—some of which parliament elected to amend or remove (e.g., those related to VAT on fertilisers and export services) (IMF 2022c). Following completion of the fourth review in December 2022, the loan was augmented to meet additional fiscal needs and support foreign exchange reserves (IMF 2022b).

Box 2. Timeline of IMF engagement in Kenya since 2010	
JANUARY 2011	IMF approves Extended Credit Facility loan for \$509 million over 36 months.
FEBRUARY 2015	IMF approves combined Standby Arrangement and Standby Credit Facility for \$688 million over 12 months.
MARCH 2016	IMF approves combined Standby Arrangement and Standby Credit Facility for \$1.5 billion over 24 months.
MAY 2020	IMF approves immediately disbursing Rapid Credit Facility for \$739 million.
APRIL 2021	IMF approves combined Extended Credit Facility and Extended Fund Facility (ECF-EFF) for \$2.3 billion over 38 months and disburses \$308 million.
JUNE 2021	IMF completes first review of ECF-EFF and disburses \$407 million.

JULY 2022	IMF completes second review of ECF-EFF and disburses \$236 million.
DECEMBER 2022	IMF completes third review of ECF-EFF, augments loan by \$216 million, and disburses \$447 million.
JULY 2023	IMF approves a concurrent Resilience and Sustainability Facility (RSF) loan for \$551 million over 20 months; IMF completes fifth review of ECF-EFF, augments loan by \$316 million, and disburses \$415 million.
JANUARY 2024	IMF completes first review of RSF and disburses \$60 million; IMF completes sixth review of ECF-EFF, augments loan by \$311 million, and disburses \$625 million.

In July 2023, the IMF subsequently approved a parallel 20-month Resilience and Sustainability Facility (RSF) loan for \$551 million, disbursed over four reviews and operating on the same review schedule as the pre-existing program—which at the same time concluded its fifth review and was extended 10 months, augmented again, and had two additional reviews scheduled (IMF 2023c). The RSF aims to incorporate climate risks into fiscal planning and the investment framework, reduce emissions through carbon pricing, enhance existing frameworks to mobilise climate finance, and strengthen disaster risk reduction and management. Finally, in January 2024, Kenya completed first review under the RSF and the sixth review of the program approved in April 2021, the latter of which included a further loan augmentation (IMF 2024d).

IMF Program Conditions and Recommendations

To what extent are the IMF programs—both RSF and ECF-EFF—consistent with enabling Kenya to circumvent dependence on fossil fuels and achieve climate policy objectives included in its NDCs? Is the program aligned with a just transition that safeguards the rights and needs of the most vulnerable members of society amidst a global climate emergency? We examine these questions based on analysis of the loan documentation, focusing on key conditions and recommendations since the RSF program began in July 2023 (IMF 2023c, 2024d).

Climate risk and green transition

The IMF recognizes that despite Kenya’s modest contribution to global greenhouse gas emissions, its economy is highly vulnerable to climate change shocks. In recognition of these challenges, the RSF contains 9 conditions pertaining to four reform priorities: incorporating climate risks into planning and investment framework; mobilising climate-revenue and strengthening efficiency; enhancing effectiveness of existing frameworks to support climate finance; and strengthening disaster risk reduction and management. As shown in Table 1, specific conditions include using climate change scenarios in fiscal risk analysis, adopting climate-informed investment selection criteria, implementing climate budget tagging, introducing carbon taxes, providing green fiscal incentives in land and water management, regulating electricity markets to promote energy efficiency, developing a green finance taxonomy, issuing guidelines for financial institutions on reporting climate-related risks, and adoption of a framework to enable dissemination of a digital early warning system platform.

Table 1. Resilience and Sustainability Facility conditions

Condition	Climate reform area
1: Cabinet to adopt the National Framework for Climate Services to enable dissemination of a digital early warning system platform for a multi-sector climate-related information to most vulnerable counties, including ASAL and coastal regions.	Disaster risk management
2: National Treasury to conduct long-term fiscal sustainability analysis under different climate change scenarios and publish the results in the Fiscal Risk Statement starting in FY 2024/25.	Fiscal planning and investment

Condition	Climate reform area
3: Subject to Parliamentary approval, National Treasury to implement carbon pricing in line with IMF recommendations to better reflect the externalities of fossil fuel consumption and to achieve emissions reduction targets in line with the updated NDC.	Climate revenue
4: CBK to develop a draft green finance taxonomy adapted to Kenya's updated NDC and circulate the draft for stakeholder consultation	Climate finance
5: National Treasury to (i) develop a standardised climate change and disaster risk methodology to be integrated in project appraisal, (ii) include climate considerations in project selection criteria and (iii) reflect the use of the analysis in project concept notes, feasibility studies, and the publication of the project selection criteria.	Fiscal planning and investment
6: National Treasury to adopt priority fiscal incentives in agriculture, water, and land management sectors, as listed in the draft National Green Fiscal Incentive Policy Framework.	Climate revenue
7: Cabinet to approve net metering regulation, electricity market, bulk supply, and open access regulations, including rates determination methodology to promote energy efficiency, electricity wheeling, and distributed renewable power generation in the residential, commercial, and industrial sectors, including Special Economic Zones and Industrial Parks.	Climate revenue
8: National Treasury to implement a prototype of climate budget tagging in key climate sensitive sectors, develop guidelines (applied to all sectors) in the FY2024/25 MTEF circular for budget preparation with a clear definition of climate-related expenditure and publish the results.	Fiscal planning and investment
9: CBK to (i) adopt a green finance taxonomy adapted to Kenya's updated NDC and reflecting stakeholders' comments, (ii) issue guidelines for the implementation of climate related disclosures for the banking sector in line with international best practices, and (iii) introduce time-bound targets for the implementation of climate disclosure requirements.	Climate finance

As is encouraged in the RSF operational guidance note (IMF 2023e), the selection of these reforms was informed by climate expertise from the IMF’s Monetary and Capital Markets Department and by two separate technical assistance missions carried out by the IMF’s Fiscal Affairs Department in May 2023: one implemented the Climate Policy Diagnostics (CPD) module to identify critical climate policy and institutional gaps; and the other completed a Climate Public Investment Management Assessment (C-PIMA), which involves an assessment of public investment management for climate-aware infrastructure. This support is aligned with the IMF’s operational The IMF

states that these reforms aim to complement the World Bank's Development Policy Operation loan for \$1 billion approved in May 2023, which focuses on agricultural policies to promote green and inclusive growth (World Bank 2023f), and was itself informed by what were at the time unpublished analyses conducted for the World Bank's (2023c) Kenya Country Climate and Development Report. It is also clear that the conditions reflect national climate-related strategies, as evident most explicitly in conditions #3, #4, and #9 (see Table 1), which refer explicitly to Kenya's NDC. While the ECF-EFF program contained no conditions that directly addressed climate-related challenges, several have indirect implications for a green and just transition, described further below.

Beyond what has been mentioned above, climate concerns are firmly embedded in the IMF program documentation. The apex of this treatment is the 10-page Annex III in the RSF program approval documentation showcasing climate-related challenges grouped under nine headings: climate-related natural hazards, impact, and vulnerabilities; legal, institutional and policy framework for climate change in Kenya; Kenya's National [sic] Determined Contribution; climate finance policy framework; macro-fiscal implications of climate change policies; cost of climate mitigation and adaptation investment; financing needs; RSF support and related reforms; and collaboration with multilateral partners. Within the annex, the IMF provides detailed climate context, including a record of historical damages of natural disasters in Kenya from 1900-2023 in terms of event counts, fatalities, number affected, and total damages. The IMF also recognizes key risks to the economy from climate change, such as production losses in the agricultural sector—which provides 80% employment of the rural workforce, comprises over 50% of GDP, and constitutes the largest share in the country's exports—and vulnerabilities in electricity generation, as 35% of it is generated from climate-vulnerable hydropower. The IMF also notes that climate-induced natural disasters place pressure on the balance-of-payments through output losses and the destruction of capital, imports for reconstruction spending, and terms-of-trade shocks stemming from price pressures in agriculture and energy (including the need to increase food imports when crops fail). Presentation of these risks is bolstered by statistical estimates: "Total cost [of climate change] is estimated at 2–2.4% of GDP per year in Kenya: while droughts are estimated to cost about 8% of GDP every five years, the cost of floods is estimated at 5.5% of GDP every seven years" (IMF 2023c, 68). Another highlight of the annex is coverage of the legal, institutional, and policy framework for climate change in Kenya, where the IMF charts Kenya's institutional milieu to demonstrate risk of fragmentation due to parallel institutional frameworks that are not well integrated. The IMF reflects that "regulatory fragmentation and inadequate coordination mechanisms prevent private sector investment in climate adaptation and

mitigation”(IMF 2023c, 73), naming funds and agencies where weaknesses are identified.

Outside of Annex III, climate spending is incorporated into macro-fiscal assumptions made under the program. First, assumptions underlying the baseline scenario of the debt sustainability analyses include an estimate of the government’s climate-related public investment at 2.6% of GDP and forecast additional climate investment of 0.25% of GDP per year. The potential for natural disaster shocks is also incorporated in debt sustainability analyses where it is simulated as a tailored stress test—even if results of its illustrative scenario are concerning, showing “very limited scope for meeting additional financing needs without jeopardising debt sustainability if faced with a large climate-related disaster” (IMF 2023c, 21). The IMF interprets these results as “underscoring the importance of existing mitigation and adaptation strategies to curb and cushion climate risks, [and] putting in place the necessary regulatory framework to tap private sector solutions and enable access to concessional green financing” (IMF 2023c, 2), as well as “highlight[ing] the need to expedite institutional reforms and capacity building to improve public investment efficiency” (IMF 2023c, 19).

Second, the IMF performs Debt, Investment, Growth, and Natural Disasters (DIGNAD) model simulations calibrated to the Kenyan economy to demonstrate the macro-fiscal benefits and pitfalls of investing in adaptation measures, thereby functioning as an opportunity to quantify benefits and drawbacks of policy measures vis-à-vis the environment. They model three scenarios: no policy change; some adaptation investment along with moderate improvements in mobilising climate finance and increasing public investment efficiency; and robust adaptation investment along with significant improvements in mobilising climate finance and increasing public investment efficiency. Based on the simulation output, the IMF concludes that “investing an additional 1.5% of GDP in adaptation infrastructure ... could save Kenya nearly 3% of GDP in output loss when disaster hits. While [this investment] would result in higher public debt in the three years preceding the shock, it would stabilise at 75.1% of GDP by the end of the 5-year post-shock recovery, significantly below the level in the baseline (80.8% of GDP), ... and would contribute to a declining debt trajectory over the long run” (IMF 2023c, 79).

Finally, the IMF addresses earlier criticisms of siloing climate concerns rather than integrating them throughout its various analyses and documentation (Kentikelenis and Stubbs 2021b, 2021a). For example, in its statements on the near-term economic outlook, the IMF flags climate-related shocks as a sizable downside risk; and climate events feature in the Risk Assessment Matrix as both a potential external and domestic shocks. The documentation

for the RSF's first review also includes coverage on gender equity and climate change, showing how women will be disproportionately vulnerable due to their restricted access to capital and ownership over resources and in turn calling for gender-balanced climate policies. Overall, both the conditions included in the program and underlying discussions were skewed toward adaptation rather than mitigation measures, which is appropriate given Kenya's vulnerability to the impact of climate change and modest contributions to global greenhouse gas emissions. However, several program measures may inhibit achievement of a green and just transition, described below.

Fiscal policy

Condition #6 of the RSF requires Kenya to implement measures listed in its draft National Green Fiscal Incentive Policy Framework. The draft policy incentivizes low-carbon, climate resilience, and environmentally sustainable private sector green investment, via—inter alia—carbon pricing, tax exemptions and subsidies for climate-friendly activities, and the development of a green investment bank and credit guarantee schemes to enhance access to finance (Government of Kenya 2022). These policies hold the promise of encouraging more efficient usage of energy and incentivizing a shift to renewable sources like wind and solar. Notable, too, is that the draft policy explicitly calls for increased “government spending [to] directly target the delivery of environmental outcomes that the private sector might otherwise ignore”, such as adaptation measures related to disaster risk reduction and management activities and the restoration of degraded lands (Government of Kenya 2022, 9). Whether the policy is in toto progressive or regressive remains to be seen and will not be fully known until details of some of its key elements of its revenue mobilisation measures—like the carbon tax—are fully fleshed out. The government reported in the first review of the RSF that implementation of carbon pricing in line with IMF recommendations—also included as condition #3—could take longer than originally envisaged. Nonetheless, it is clear already that the inclusion of plans for public investment in adaptation and financing incentives for renewable energy markets is a shift from the IMF's economic surveillance activities in other countries, where policy advice vis-à-vis climate mitigation centred around carbon taxes (Stubbs and Kentikelenis 2023b).

Despite recognizing that increased public spending on climate adaptation and mitigation can improve the Kenya's debt profile, the IMF has nonetheless been calling for an extensive multi-year fiscal consolidation since the ECF-EFF program began in April 2021. The program initially called for a decline in the primary balance from a deficit of 4.0% of GDP to a 0.2% surplus by mid-2024 (IMF 2021e), buttressed throughout the program by conditions

requiring a procession of program-consistent supplementary budgets and adherence to quarterly performance criteria on the primary budget balance. By the most recent review, the IMF is calling for a 1.7% surplus by the 2024-2025 fiscal year, totalling a staggering 5.7 percentage point increase to the primary fiscal balance over the course of the program (IMF 2024d). Notable in its absence was any explicit consideration of the trade-offs involved of such fiscal consolidation measures in achieving climate objectives. The ECF-EFF program also appears to be at cross-purposes with the RSF program: while the IMF notes lack of funding for adaptation projects when describing climate finances, it fails to recognize that the very fiscal austerity they endorse may undermine the ability of the government to fund such projects.

Tax policy was viewed as a core area for reform in the fiscal consolidation strategy, supported by quarterly targets for tax revenues. To reach these targets, the country commenced a process of broadening the tax base by eliminating value-added tax exemptions via the 2023 Finance Act, which—among several policies—increased the VAT rate on fuel products from 8% to 16%. While such a policy may be a potential boon for fostering a green transition, without appropriate compensatory mechanisms for the affected population (assessed further below), they are unlikely to be just. IMF analyses elsewhere show that poorer households are more likely to be hurt by higher fuel prices since a larger share of their income is spent on energy-intensive goods like transport, electricity, and heating (IMF 2020c). Nor are these measures gender-responsive. Women, especially, bear the brunt of rising fuel prices due to gender differences in consumption expenditures. Since women typically harbour responsibility for managing the household, they tend to spend a larger share of their income on household needs such as transport, cooking, and related costs (Strub 2023). Domestic civil society also raised concerns over the regressive implications of other planned tax measures, such as removing several VAT exemption measures to the agricultural sector (Okoa Uchumi Campaign 2023), such as pest control products and animal feed (The East African 2023).

On the expenditure side, the government revised domestic fuel and energy prices to ensure fiscal consolidation consistent with the program objectives. All fuel subsidies were eliminated in March 2023 in order to fulfil a condition to “publicly announce and constitute a taskforce to oversee the progressive elimination of the fuel subsidy” (IMF 2023c, 116) and to meet a structural condition requiring the submission of a supplementary budget consistent with programmed deficit and revenue targets. Cost-based upward adjustments to electricity prices were effective April 2023 and occurred in response to a structural condition to “submit to the cabinet sub-committee on KPLC an action plan to restore KPLC’s medium-term profitability and fully cover any financing gaps (IMF 2023c, 115).

The IMF itself recognizes that this piling up of expenditure measures contributed to higher inflation—which is still exceeding the 7.5% upper limit of the target band—thereby compounding the misery for vulnerable households at a time when cost of living is already elevated due to the 2020–23 drought and war in Ukraine affecting food prices. Despite the IMF acknowledging the high—and increasing—cost of living and “potential implementation challenges of planned reforms from renewed social discontent” (IMF 2024d, 32), there is only limited engagement with social protection in the loan documentation. The program purports to protect vulnerable groups in a set of non-binding quarterly indicative benchmarks on priority social expenditures. However, these floors only preserve current spending levels once accounting for inflation (Kentikelenis and Stubbs 2023b)—and represent a decline as a share of GDP from 3.6% in the 2020–21 fiscal year to 3.2% in 2023–24 (IMF 2024d, 9)—rather than increasing it in a time of heightened need, as reflected by rising poverty rates and joblessness since the pandemic onset and the drought. Platitudes are made with regard to using carbon pricing revenues to “compensate vulnerable groups and offset the costs of higher energy prices” (IMF 2023c, 23) and controlling the government wage bill to “free much-needed resources for priority social and development spending” (IMF 2021c, 110), but these statements are devoid of substantive analytical rigour, such as an assessment of the distributional impact of the aforementioned fiscal policies or even an account of what form such compensatory social protection will take and an estimate of its costs. However, it is worth noting that more in-depth analyses of the effect of fiscal consolidation on low-income households were provided in the World Bank’s Development Policy Operation loan to Kenya for \$1 billion approved in May 2023 (World Bank 2023e), which informed the IMF’s program.

Privatisation and climate finance

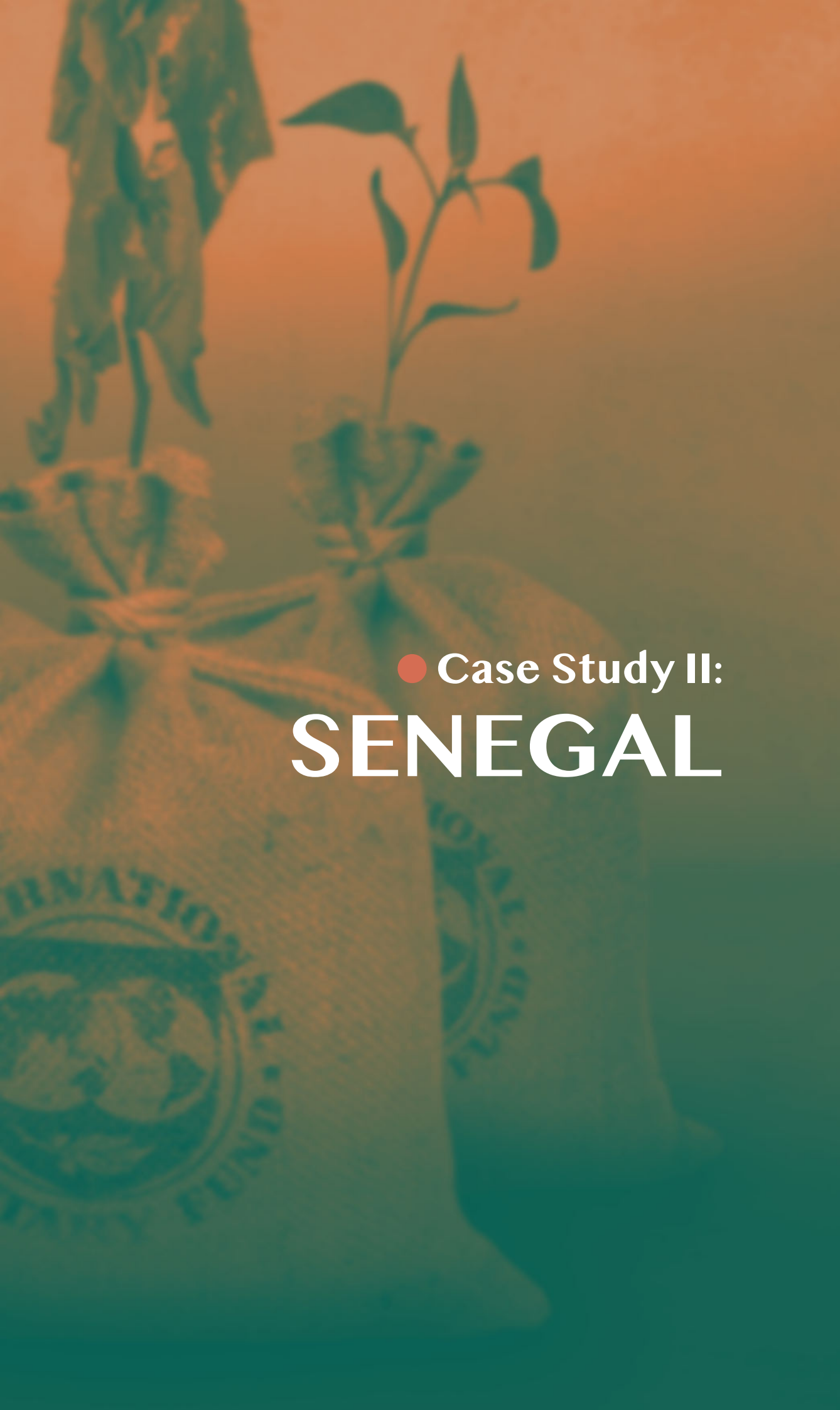
Condition #7 of the RSF calls for the Kenyan government to approve net metering regulation, electricity market, bulk supply, and open access regulations on the basis that these will provide a signal to private investors to invest in certain sectors, such as electric vehicles and renewable energy. These regulations pave the way for private sector generation companies to transmit electricity to their customers via bilateral power purchase agreements in deals that bypass the partly state-owned enterprise Kenya Power and Lighting Company (KPLC), which operates most of the electricity transmission and distribution system. Under the ECF-EFF, the IMF also set a condition requiring the transfer of KPLC’s power transmission lines to Kenya Electricity Transmission Company, that KPLC enter into a commercial contract with Renewable Energy Corporation for future Rural Electrification Schemes maintenance costs, and for the establishment of a new governance

structure that gives private shareholders better representation by end-December 2024.

There are concerns from civil society that the climate crisis is being used as a pretext to open up Kenya's energy provision to the private sector and that the unbundling and restructuring of KPLC is an initial step towards its full privatisation—where the underlying motive for these measures is based more on the IMF's ideological predisposition for market-driven approaches over active government intervention than for their green credentials. Supporters of private sector provision, including the IMF, claim that this benefits consumers and green transition objectives, as market competition should lead to lower prices, improved energy efficiency, greater innovation, and better access. But this neglects the underwhelming experience of several countries with the role of private companies in the energy transition, where typically the opposite has occurred: consumers face higher prices due to oligopolistic concentration in the energy sector, and low-income and rural areas are neglected as private companies prioritise profits over development considerations (Prasad et al. 2022; Prinsloo 2019). Reversal of privatisation can also be problematic where legal guarantees have been made to private investors to allow for long-term service provision, rendering more ambitious green industrial policies unfeasible. Industrial policies developed by the government in consultation with the relevant stakeholders may offer a more sustainable and equitable path forward—for instance, the Colombian Ministry of Environment and Sustainable Development is working on a *comunidades energéticas locales* project to enhance community participation in energy projects and share in its revenues (Stubbs and Kentikelenis 2023b).

In terms of climate financing for adaptation and mitigation measures, the IMF expects the RSF loan to substitute costlier domestic financing options, thereby improving public debt dynamics, and to catalyse further private financing. Kenya requires an estimated annual climate financing of about 6% of GDP, or \$62 billion by 2030, to achieve its updated Nationally Determined Contribution (Government of Kenya 2020). According to IMF analysis, only about one-third of Kenya's annual financing gap is being filled annually. Given this underwhelming track record, it may be unrealistic to place heavy weight on the private sector stepping into the gap. Indeed, as the IMF recognizes, current private sector commitments are falling far short of projected requirements and “almost 100% of foreign private climate-related investment financed mitigation activities, mostly renewable energy projects. No private investment was channelled towards adaptation efforts” (IMF 2023c, 75). In short, the private sector seems to have no appetite for adaptation measures, perhaps because outlets for profitability are limited in a lower-middle income context. To ameliorate the issue, the IMF highlights

“causes for market failure potentially holding back private adaptation investment ... that would need to be addressed with appropriate government interventions” (IMF 2023c, 75): a mismatch between the design of financing products offered by the market and the form of financing needed, such as micro-credits for small farmers and households to finance adaptation investment needs); a higher risk premia for investing in adaptation; and a lack of private sector borrowing capacity due to lack of secure income or collateral. Such advice foresees a role for the state purely as an enabler for the private sector, whereas—again—more active forms of government intervention are overlooked.



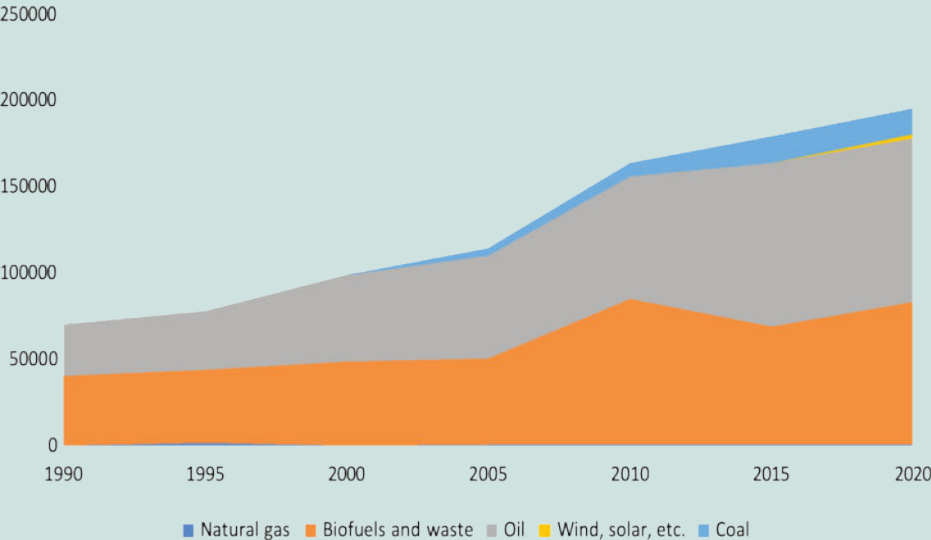
● Case Study II:

SENEGAL

Background

Senegal is a lower-middle income country of 17 million people and an estimated \$27 billion economy, with an income per capita of \$1,599 (World Bank 2023h). Although economic growth averaged 6% between 2015 and 2019, the COVID-19 pandemic and the war in Ukraine caused major terms-of-trade shocks, resulting in a widening current account deficit and persistently high budget deficits and debt levels (World Bank 2023g). GDP growth decelerated to 1.3% in 2020 before rebounding to 6.5% in 2021 and then slowing down to circa 4% since. In the meantime, public debt had reached 75% of GDP by 2022 and the primary deficit was 3.9% of GDP. The economic situation was further exacerbated by political instability in neighbouring countries and social unrest linked to the 2024 presidential elections, which resulted in business closures and deterred domestic and foreign investment. Domestic political turmoil came to a head following President Macky Sall’s unilateral decision to indefinitely postpone the election, though he ultimately settled for a delayed date of March 24 following weeks of political turmoil and violent protest (Rich 2024). Opposition candidate Bassirou Diomaye Faye subsequently won the presidential vote, pledging—inter alia—to weed out corruption, prioritise economic sovereignty, and renegotiate mining and hydrocarbon contacts (Shamim 2024). Rising food and energy prices and trade disruption also contributed to an average inflation of 9.6% in 2022, which the government responded to by increasing fuel and electricity subsidies and raising public sector wages (IMF 2023h). However, the economic outlook is brighter for the near-term future: the commencement of oil and fossil fuel gas production and its exportation (described below) is projected to ramp-up GDP growth to 8.8% in 2024 and to narrow the current account deficit (World Bank 2023g).

Figure 4: Total energy supply in Senegal, by source



Source: International Energy Agency (2024b).

Senegal pledged in its Nationally Determined Contribution (NDC) to reduce emissions by 29% by 2030 compared to the business-as-usual scenario, subject to the support of the international community with funding and technological transfer, at an estimated cost of \$8.7 billion (Government of Senegal 2020). To put these ambitions in context, Senegal emitted 34.7 million tonnes of CO₂ equivalent in 2020 (the most recently available data), representing 0.07% of global greenhouse gas emissions and placing per capita emissions—2.07 CO₂ equivalent per person—at 153rd out of 198 countries (World Resources Institute 2024b). By sector, agriculture comprises the greatest proportion of emissions (38%), driven primarily by enteric fermentation from livestock and savanna burning, followed by energy (24%), industrial processes (13%), land-use change and forestry (13%), and waste (12%). In terms of the country's energy matrix, Figure 2 shows that oil, at 49% and biofuels, at 42% compose the bulk of energy supply in 2020. Coal and wind and solar entered the energy mix in the early-2000s and now make-up 8% and 1% respectively, while natural gas constitutes less than 1%. However, the country made significant oil and gas discoveries off its coastline between 2014-16, extraction of which is expected not only to increase their emissions proportion in the energy matrix, but will also see the energy sector grow to account for more than 63% of the country's greenhouse gas emission by 2030 (Government of Senegal 2020). Two fields will begin production in 2024: the Sangomar deepwater oil field located approximately 100 kilometres south of Dakar and operated by Australia's Woodside Energy; and the Greater Tortue Ahmeyim offshore liquefied fossil fuel gas project on the maritime border of Senegal and Mauritania, both countries of which signed an arrangement with a BP-Kosmos partnership to operate it (Lemmerich 2024). A third gas field, Yakaar-Teranga, could produce as early as 2026. Initially owned by a BP-Kosmos partnership, BP exited development of the field in November 2023 following disagreement with the government on the use of gas, which BP wanted to export but Senegal wanted to use for the domestic market. Currently Kosmos owns 90% of the field, but Senegalese state-owned enterprise PETROSEN aims to acquire the majority stake in it (Diop, Diene, and Shafaie 2023).

Under the G7's Just Energy Transition Partnership (JETP), Senegal gained €2.5 billion in funding, mostly in the form of loans, and also committed to increase its share of renewable energy in installed capacity to 40% of its electricity mix by 2030 (Government of Senegal and International Partners Group 2023). Senegal was characterised a decade ago by production capacity that was well below national demand, resulting in frequent load shedding that cost the economy up to 2 percentage points of GDP growth annually, and relied on imports of liquid fuels such as diesel, where price fluctuations made economic planning unpredictable and drained public finances (Sy 2023). In response, the government implemented the 2013 Senegal Emerging Plan, which entailed increasing its renewable energy capacity by commissioning four solar photovoltaic power stations—namely Senergy (30MW), Ten Merina (30MW),

Kahone Solaire SA (35MW), and Kael Solaire SA (25MW)—and a large-scale wind farm, the Taïba Ndiaye project (158 MW). By 2021, photovoltaic solar energy and wind power accounted for 24% of electricity generation (Sy 2023). In September 2023 the West African Development Bank then approved a €23 million loan to construct the Niakhar (30 MW) solar power plant (Takoulev 2023). The government also plans to put in place infrastructure to use domestic gas for electricity generation under its 2018 gas-to-power strategy, deploying fossil fuel gas resources as a “transitional energy” source (Government of Senegal and International Partners Group 2023).

On the climate adaptation front, Senegal needs \$4.3 billion to fund its NDC commitments (Government of Senegal 2020). The country is highly vulnerable in terms of its exposure, sensitivity, and ability to adapt to the impact of climate change, ranked 137th of 185 countries in the ND-GAIN index (Notre Dame Global Adaptation Initiative 2023). Rising sea levels place the coastal population and infrastructure—where approximately 70% of the country resides and is the location of 90% of industrial production—at risk from flooding and erosion (USAID 2023). Climate change will also impact the agricultural sector, which accounts for 75% of the workforce and 18% of GDP (IMF 2023g; World Bank 2023g); as agricultural production is primarily subsistence-based and rainfed, poorer smallholder farmers are expected to suffer most from the impacts of climate change (GIZ 2022). In addition, Senegal’s fishing industry, which employs about 15% of the labour force and contributes over 10% of the value of exports, is already severely impacted by overfishing, pollution, and climate change. These issues will be compounded with the commencement of oil and gas production, which will harm marine and coastal ecosystems (Greenpeace Africa 2018; Lemmerich 2024).

Relationship with the IMF

Senegal has entered into two IMF lending programs and received one rapidly dispersing loan since 2010. However, prior to the COVID-19 crisis, Senegal had not received a loan from the IMF since 2010. Instead, between 2010 and 2020, the country participated in a series of Policy Support Instrument and Policy Coordination Instrument programs—one-to-five year programs where the IMF offers advice, monitoring, and endorsement of their policies, but no access to credit (IMF 2015b, 2023i). The IMF then approved a disbursement of \$442 million under a non-conditionality emergency loan in April 2020 to provide the government with fiscal space to mitigate the impact of the COVID-19 pandemic on the economy (IMF 2020b). Subsequently, the country entered into an 18-month loan for \$650 million in June 2021 aimed at supporting the COVID-19 recovery and creating jobs (IMF 2021h), for which all three program reviews were completed and the entire amount was drawn.

Box 2. Timeline of IMF engagement in Senegal since 2010	
DECEMBER 2010	IMF approves 36-month Policy Support Instrument program.
JUNE 2015	IMF approves 36-month Policy Support Instrument program.
JANUARY 2020	IMF approves 36-month Policy Coordination Instrument program.
APRIL 2020	IMF approves immediately disbursing combined Rapid Credit Facility and Rapid Financing Instrument for \$442 million.
JUNE 2021	IMF approves combined Standby Arrangement and Standby Credit Facility for \$650 million over 18 months.
JUNE 2023	IMF approves combined Extended Credit Facility and Extended Fund Facility (ECF-EFF) for \$1.51 billion over 36 months and disburses \$216 million; and approves a concurrent Resilience and Sustainability Facility (RSF) loan for \$324 million over 36 months.
DECEMBER 2023	IMF completes first review of RSF and disburses \$64 million; IMF completes first review of ECF-EFF and disburses \$215 million.

In June 2023, the IMF approved a combined 36-month program under the Extended Credit Facility and Extended Fund Facility (ECF-EFF), unlocking access to \$1.51 billion over the course of six semi-annual reviews, \$216 million of which was immediately disbursed. At the same time, the IMF approved a parallel 36-month Resilience and Sustainability Facility (RSF) loan for \$324 million, operating on the same review schedule. The stated aims of the ECF-EFF are to reduce debt vulnerability through fiscal consolidation (primarily via revenue mobilisation and phasing out energy subsidies), to strengthen public sector governance, and to foster a more inclusive and private-sector led growth trajectory (IMF 2023g). The aim of the RSF is to support efforts to tackle climate change mitigation objectives, accelerate climate change adaptation, and integrate climate change considerations into the budget process (IMF 2023g).

IMF Program Conditions and Recommendations

To what extent are the IMF programs—both RSF and ECF-EFF—consistent with enabling Senegal to circumvent dependence on fossil fuels and achieve climate policy objectives included in its NDCs? Is the program aligned with a just transition that safeguards the rights and needs of the most vulnerable members of society amidst a global climate emergency? We examine these questions based on analysis of the loan documentation, focusing on key conditions and recommendations since the programs began in June 2023 (IMF 2023g, 2023f).

Climate risk and green transition

If IMF programs are to facilitate green transition and just recovery priorities, they will need to consider the physical risks of climate change and transition risks associated with a low-carbon future. As shown in Table 2, the RSF program contains 10 conditions grouped into three pillars. The first pillar seeks to support climate change mitigation goals by adopting an implementation plan for greener public transport and phasing out untargeted subsidies in the electricity sector. The second pillar aims to accelerate adaptation to climate change via adopting a country development strategy consistent with its NDCs, submitting urban planning laws that mitigate coastal erosion and urban flooding, disseminating climate risk data to relevant committees, and strengthening the institution in charge of implementing water management. The third pillar looks to integrate climate change considerations into the budget process by integrating climate considerations into public investment management, assessing disaster-related fiscal risks for the 2025 budget law, developing guidelines for climate budget tagging and issuing directives in the budget call circular to reflect climate investments, and ensuring all public investments and PPP projects include an appraisal of their effect on climate adaptation and mitigation.

Table 1. Resilience and Sustainability Facility conditions

Condition	Climate reform area
1: Adopt and publish a PIM decree integrating climate considerations at each step of the project development (appraisal, selection, external audit etc.)	Disaster risk management
2: (i) Adopt at the Council of Ministers an implementation plan for the strategy for greener public transport and (ii) reflect it in the 2024 PIP budget of the Ministry of Transport, in line with the objectives of the NDC.	Fiscal planning and investment

Condition	Climate reform area
3: Adopt Senegal's PAP III (Country Development Strategy) at the Council of Ministers, which should fully reflect Senegal's National Determined Contribution (NDC).	Accelerate adaptation
4: Submit to the National Assembly two laws that establish (i) the Urban Code (CU) and (ii) the Construction Code (CC) to improve urban planning, thereby mitigating the impact of coastal erosion and urban flooding, and approve the related implementation decrees.	Accelerate adaptation
5: Adopt an electricity tariff adjustment plan based on the results of the financial audit of SENELEC, which is conducted with the support of the World Bank, with the aim of phasing out electricity subsidies by 2025.	Support decarbonization
6: Assess and quantify disaster-related fiscal risks as part of the Risk Statement Annex included in the 2025 budget law.	Fiscal planning and investment
7: Publicly disseminate key information on climate risks by the National Committee on Climate Change.	Accelerate adaptation
8: Approve an inter-ministerial decree that defines the roles and responsibilities and the procedures allowing each actor to assume their role and responsibilities for water, including the steps to take to be accountable for their actions.	Accelerate adaptation
9: Ministry of Finance to (i) develop guidelines for climate budget tagging (deadline end-2024); and (ii) to issue in the budget call circular directives in order to fully reflect the priority mitigation and adaptation public investments (end-2025).	Fiscal planning and investment
10: The Minister of Finance will issue a binding instruction to all Ministers engaged in large public investment program (PIP) to ensure that all public investments and PPP projects executed or supported by the State budget will include as part of documents required for the appraisal (i) a technical assessment of the impact of the investment on adaptation to climate change (both in the pre-feasibility study, if any, and in the feasibility study), and: (ii) the climate implications of the project, i.e. say the impact on GHG emissions.	Fiscal planning and investment

The selection of reform measures was coordinated with the World Bank, who joined the program negotiation mission and are providing ongoing technical assistance for reforms required under the RSF, described in Annex III of the first review of the programs (IMF 2023f). Extensive coordination is also evident with regard to the prior actions in the World Bank's Development Policy Financing program commencing May 2022 that are consolidated in the ECF-EFF and RSF programs (described further below), such as reforms geared towards establishing

the regulatory framework for private investment in the gas subsector and increasing transparency in government procurement processes in the electricity sector, as well as measures that bolster targeting of the most vulnerable beneficiaries and increase the total number covered in the social protection system (World Bank 2022). In addition, the IMF's Climate Public Investment Management Assessment (C-PIMA), completed in February 2023, identified several shortcomings undermining coherent climate consideration in the budget and investment process—such as a lack of effective central coordination mechanism and climate-related selection criteria. IMF technical assistance, primarily by the IMF's Fiscal Affairs Department, is envisaged to facilitate RSF measures identified in the C-PIMA. The Global Center on Adaptation also provided expertise for the refinement of adaptation policies and will provide ongoing technical assistance for adaptation reform measures.

The broader program documentation contained modest coverage of climate risks and the green transition. Outside of the coverage of RSF measures, the bulk of it is provided in Annex V of the program approval document (IMF 2023g), which dedicates five pages to explaining the architecture of climate governance in Senegal, its adaptation and mitigation priorities, risks around water security and coastal erosion, and the gas-to-power strategy. But the content is descriptive and cursory, lacking the data-driven historical coverage and climate diagnostics used in other RSF programs, such as in Bangladesh and Kenya (Stubbs and Kentikelenis 2023a). The first program review also included a paragraph describing resources committed to enhancing climate resilience under the recently signed JETP (IMF 2023f), but this coverage failed to reflect on the uncertainties of this financing. For example, two years into South Africa's JETP, only \$600 million of the committed \$8.5 billion has actually materialised (Tooze 2024). Donors explain their lack of disbursements as a result of shortcomings in South Africa's regulatory, legal, and organisational environment (Vanheukelom 2023). In addition, there was cursory recognition integrated throughout the program documentation of risks and macro-fiscal consequences of climate change. The IMF notes, for example, that it “could reduce GDP growth by 2 to 4 percentage points across Africa by 2040 [...and] Senegal is particularly vulnerable” due to its coastal population and high proportion of workers in agriculture (IMF 2023g, 21). But this coverage is not underpinned by a diagnostic toolkit, such as Debt, Investment, Growth, and Natural Disasters (DIGNAD) model simulations demonstrating benefits of investing in adaptation measures vis-à-vis several economic indicators.

Furthermore, while the debt sustainability analysis acknowledges uncertainty about climate-related spending needs, it did not include climate-related stress tests, even though the IMF is capable of delivering them to low-income countries (IMF 2021f), thereby failing to quantify benefits of climate investment vis-à-vis the country's debt profile. Another question mark pertains to the realism of the

debt sustainability analysis. While it did highlight delays to the start of hydrocarbon production as a key risk to baseline projections, it nonetheless proceeded under the assumption that there would be no delays to hydrocarbon production, in turn providing a boost to growth, exports, and fiscal revenues. But delays are the norm, not the exception, so should be factored into the baseline scenario. They have frequently occurred in Senegal since it made oil and gas discoveries, and they commonly occur in other countries with recent discoveries, like Argentina and Uganda. Inevitably, delays materialised by Senegal's first program review, with postponement of oil and gas production to the second half of 2024. It should be acknowledged, however, that outside of the debt sustainability analysis the IMF did recognise potential implications of delayed oil and gas production for government revenues and exports, presenting a half-page textbox containing four graphs. Notwithstanding this coverage, the IMF's headline economic projections provided in the standard figures and tables throughout the documentation assumed no delays, thereby offering a misleading picture of medium-term macroeconomic prospects by embedding an overly optimistic oil and gas production schedule—although for economic growth and the primary balance the IMF helpfully provided forecasts a hydrocarbon and non-hydrocarbon version.

But perhaps the most glaring omission is that the IMF fails to sufficiently acknowledge the perverse climate implications of fossil fuel extraction, which are located in sensitive geographic areas. The Sangomar oil field is in the Saloum Delta, a significant wetland habitat protected by UNESCO; and its natural resources are essential to the livelihoods of indigenous communities—who fear these wetlands may be harmed in the drilling, installation, operation, and eventual dismantling of the field (Keita 2023; Ngam and Thiam 2022). The Greater Tortue Ahmeyim is located near a 200,000-year-old cold-water coral reef ecosystem that supports many species of fish and some of West Africa's largest fishing communities, who fear the ecosystem could be damaged by natural gas by-products (Coalition for Fair Fisheries Arrangements 2021). Yet, coverage is contained to a sentence stating “Senegal will need to ensure there is a coherence between its forthcoming fossil fuel production and the need to reduce carbon emissions” (IMF 2023g, 55). With such scant content, the IMF implicitly encourages further reliance upon fossil fuels as a means to balance the government budget and redress the balance of payments. And by failing to include a more concerted treatment of climate damages, such as harm to marine and coastal ecosystems and to the livelihoods of fishermen (Greenpeace Africa 2018; Lemmerich 2024), the IMF misrepresents the true costs of hydrocarbon production.

Even ignoring its impact on climate, hydrocarbons as a source of export revenue cannot be relied upon in the long term as trade partners may transition towards a low-carbon economy—imposing carbon border taxes, for example—thereby

impacting the earnings from such exports. The IMF recognizes this risk on only one occasion, stating “hydrocarbon revenue in the medium- and long-term may turn out lower-than-projected if global transition to net zero accelerates” (IMF 2023f, 8). Another omitted economic risk relates to Senegal’s gas-to-power strategy. If gas is genuinely going to be a transition fuel and not a permanent solution, then there are likely to be significant transition risks linked to asset stranding as the country moves towards an energy matrix dominated by renewables. The lack of more concerted coverage of global spillover and domestic transition risk exemplifies how the IMF has downplayed inherent risks to the economy of hydrocarbon projects.

Fiscal policy

IMF advice on fiscal policy has the potential to impact Senegal’s progress on achieving climate commitments and addressing transition risks. With the coming on stream of hydrocarbon revenues, the IMF helped devise a fiscal strategy in its previous program—the 18-month Standby Arrangement and Standby Credit Facility that commenced June 2021—anchored on a new fiscal rule that limits the non-hydrocarbon primary balance as a share of non-hydrocarbon GDP. This rule ensures oil and gas revenues are set aside for a stabilisation fund, to shield fiscal policy from volatility in resource revenues, and for an intergenerational fund, to ensure a fair distribution of resource wealth across generations (i.e., once the resources are depleted). While safeguarding of hydrocarbon revenues is welcome, there was room for the IMF to push the envelope further by encouraging a portion of revenues be earmarked for developing the renewable energy sector. Throughout the program, the IMF prioritises debt servicing over social and environmental needs. This is exemplified by the IMF’s recommendation that “given that the government net wealth is largely negative (due to high public debt relative to limited resource wealth), reducing public debt to strengthen its sustainability would be preferable to accumulating resources into the intergenerational fund over the short and medium terms” (IMF 2023g, 50). The rationale for this advice is that the intergenerational fund may not be able to generate higher returns on investment than the government borrowing costs without taking significant investment risks—so would ultimately save the country’s financial resources. But the IMF’s advice appears economically sound because more ambitious alternatives, such as cancellation or reduction of external debt repayments to more sustainable levels (as occurred in 1996 through the Heavily Indebted Poor Countries Initiative of 1996), are overlooked. From a social standpoint, the IMF’s stance may be perceived as unpalatable as it directly confronts and demystifies the inherent injustices of the global financial system: rich Global North creditors that engaged in risky lending practices are prioritized over the future livelihood of the Senegalese people. In this light, Senegal’s foray into oil and gas production resembles a form of neo-imperial resource extraction (Nkrumah 1965).

Several conditions related to the reduction of the fiscal deficit also have the potential to impact the country's climate change efforts. The IMF calls for a fiscal consolidation that would see a decline in the primary budget deficit from 4.4% of GDP at end-2022 to 0.7% by 2025. This objective is underpinned by a series of conditions, including quarterly performance criteria on the non-hydrocarbon primary balance and on non-hydrocarbon tax revenues, as well as a prior action for the first review of the program to submit to the National Assembly the 2024 budget law reflecting these targets. Although fiscal consolidation may appear the most prudent course of action for the government's finances to move toward a sustainable path in the short-term, the absence of explicit consideration of the long-term trade-offs involved in such measures in achieving climate objectives represents a major oversight. And at a time when expenditure on climate adaptation and mitigation should be scaled up—Senegal's NDC adaptation and mitigation targets require \$13 billion in financing by 2030 (Government of Senegal 2020)—fiscal consolidation undermines the ability of the government to fulfil its climate commitments.

Fiscal consolidation is to be driven primarily by a phasing out of untargeted energy subsidies—via reductions to gasoline and diesel subsidies under the ECF-EFF and via increases to electricity tariffs under the RSF—from 4% of GDP in 2022 to 1% of GDP in 2024, and to completely eliminate them by 2025. To facilitate this process, the IMF set structural conditions under the ECF-EFF requiring the government to establish by November 2023 an independent committee with the mandate to determine and publish final consumption fuel prices based on a revised pricing formula; and to revise the current pricing formula for petroleum products to ensure that prices at the pump reflect developments international markets by December 2023. The IMF also included a condition under the RSF (condition #5) stipulating that the government adopt by June 2024 an electricity tariff adjustment plan that would see it gradually eliminated. These reforms hold implications both in terms of the shift away from dependence on fossil fuels and the extent to which this shift is consistent with a just transition. The IMF argues that reductions to energy subsidies effectively raise the price of fossil fuels to the end-user, thereby encouraging less and more efficient use of energy and incentivizing a shift to cheaper renewable sources, like wind and solar (Lagarde and Gaspar 2019).

According to the program documentation, “generated savings will be redirected to strengthening social welfare policies and, especially, increasing investment expenditures” (IMF 2023f, 54). Steps to ramp-up social protection are warranted because energy constitutes a larger proportion of poorer households' spending, such that energy subsidy reductions can place a disproportionate burden on them, and because—as the IMF points out—coverage of Senegal's social protection system remains lower than the median of the low-income developing

economies and sub-Saharan African groups. To assuage these concerns, the program includes a structural benchmark requiring the re-certification of data in the Single National Registry and a scaling up of its coverage from 500,000 to one million households by June 2024 to improve targeting of the most vulnerable individuals in the safety net system. The IMF also set as a prior action for the commencement of the ECF-EFF program that the government settle some outstanding cash transfers that had not been paid since 2021, which “would therefore help protect the most vulnerable in the context of energy subsidies phasing out” (IMF 2023g, 20). In addition, the government had already expanded the number of recipients and increased the amount paid out at the beginning of 2023 (i.e., prior to program commencement), resulting in an increase in social protection spending from CFAF 35 to 51 billion. The IMF notes in the first review that this budget allocation has further increased to CFAF 54 billion for 2024, but this may reflect a real reduction in spending if inflation remains at its current level of 9.6%, and with energy reductions disproportionately affecting the poor. Indeed, while the IMF also includes as a quarterly indicative benchmark a floor on social expenditures as a share of total government spending, this is set at 40% throughout the program thus far (i.e., up to December 2024), so does not clearly represent an increase, especially as government spending—the denominator—is being cut. IMF projections on social benefits expenditures also remain at 0.3% of GDP throughout the program.

The IMF did introduce a structural benchmark in the first review of the program requiring that the new electricity tariff structure incorporates a social tariff specifically designed for vulnerable groups. It is as yet unclear to what extent this may alleviate the burden on vulnerable households. This reflects a more general trend throughout the program documentation of a lack of detailed diagnostics surrounding the impact of energy subsidies on poorer income deciles and substantive analysis indicating how social protection measures will compensate. In addition, it is questionable whether the IMF’s push for the rapid elimination of energy subsidies is politically feasible given Senegal is in a presidential election year and has already experienced social unrest—and is only likely to be exacerbated by, in the IMF’s words in describing the Senegalese context, “a cost-of-living crisis, widespread youth unemployment, and threat to security from developments in neighbouring countries [that] are adding to this loaded political period” (IMF 2023g, 5).

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