Memo to the commissioners responsible for international partnerships and reform of the multilateral development banks

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The European Commission has revamped its strategy toward developing countries, with better coordination of European Union donors ('Team Europe'), blending of aid with private finance, less paternalism, better branding and an emphasis of financing physical infrastructure (the Global Gateway). These changes are welcome but bring risks: inability to deliver on promised financing volumes, potential conflict with the Sustainable Development Goals, and tensions with emerging and developing economies, which accuse the EU of double standards.

To address these risks, you should recommit to the SDGs as the primary objective of the Global Gateway, embed infrastructure investment in a comprehensive development strategy, create a separate instrument to fund international emissions mitigation and ensure it is amply resourced, create an institutional mechanism to coordinate Team Europe, seek member state coordination and consolidation of seats on the boards of multilateral development banks (MDBs), and use this to leverage MDB reform and operations through country climate platforms.

Maximise the impact of the Global Gateway

Defuse tensions with emerging and developing partners

Improve coordination internally and externally

State of affairs

EU member states and institutions provide close to half of global bilateral official aid and more than one third of all aid

European Union member states and institutions provide close to half of global bilateral official aid (grants and other grant equivalent subsidies) and more than one third of all aid (including multilaterals and private donors). About a quarter of the EU total comes from the EU budget, specifically, from the Neighbourhood, Development and International Cooperation Instrument – Global Europe (NDICI-GE), which amounts to about €80 billion for 2021-2027 (6.5 percent of the EU's multiannual financial framework, MFF).

Total EU net disbursements have risen significantly in recent years, from about €58 billion in 2019 (United Kingdom not counted) to almost €96 billion in 2023, driven initially by disbursements related to COVID-19 and more recently by aid to Ukraine. If disbursements to Ukraine are excluded, EU aid peaked in 2022 at €79 billion, before falling to €73 billion in 2023. In inflation-adjusted terms, 2023 EU aid to emerging and developing economies (EMDEs) other than Ukraine was slightly below its 2020 level (but above its 2019 level).

Your predecessors made significant changes to how EU development spending is allocated and branded, involving: 1) greater focus on physical infrastructure; 2) stronger, Commission-led coordination of 'Team Europe' (EU countries and development finance institutions controlled by the EU and/or its member states); 3) greater use of blended finance (use of public funds to mobilise private finance, via guarantees and risk sharing); and 4) better branding, including by shifting away from paternalistic donor-recipient relationships (European Commission, 2021). In line with these changes:

- The Directorate-General for International Cooperation and Development was renamed to DG International Partnerships (DG INTPA) in January 2021;
- The NDICI-GE Regulation (Regulation (EU) 2021/947) was adopted in June 2021. This commits the EU and its members to coordinate assistance policies and programmes, and includes risk-sharing instruments for up to €40 billion under the European Fund for Sustainable Investment Plus (EFSD+);

- A new flagship initiative, the Global Gateway, was rolled out in December 2021. This aims to mobilise funding of up to €300 billion by 2027 for – mainly infrastructure – investments in partner countries, combining funding from the EU budget, EU countries, the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) and the private sector.

The Commission has framed the main objective of the EU's international partnerships as being to promote the direct self-interest of the EU

Most of these changes have been years in the making but one is new and radical: the way in which the European Commission seeks to rationalise EU international partnerships. While development aid was previously justified through a mix of moral obligation and enlightened self-interest (such as promoting growth and political stability in trading partners), the Commission has framed the main objective of the EU's international partnerships, and specifically of the Global Gateway, as being to promote the direct self-interest of the EU at a time of geopolitical rivalry. The NDICI-GE was "*at the service of our geopolitical objectives*" in the words of one of your predecessors [1]

How much these shifts matter in practice is not yet clear (Perez *et al*, 2023). EU blending facilities have supported about 100 projects since 2021, but most are small, and so is the EU financing contribution (about €1.3 billion). A few high-profile infrastructure projects have been launched under the Global Gateway brand, including the Lobito economic corridor and the Medusa fiberoptic cable. But projects branded as part of the Global Gateway cover many other sectors, including health and education. Net disbursements to energy projects have increased but are no higher than prior to the pandemic. The share of EU-level disbursements to health and education (about 14.6 percent of total) remains almost twice as high as the share of disbursements to energy, industry, mining and transport (7.7 percent). This could be because any major change in strategy takes time to implement, but also because of some contradictions inherent in the new approach.

The external environment, meanwhile, has seen major changes

1 See 'Speech by Commissioner Urpilainen at the European Parliament plenary debate on Neighbourhood, Development and International Cooperation Instrument 2021-2027 – Global Europe', 8 June 2021, https://ec.europa.eu/commission/presscorner/detail/en/speech_21_7583.

since 2019. Most of these either place additional demands on EU international partnerships or make it harder to meet those demands:

- Most EMDEs have suffered significant setbacks in reaching the Sustainable Development Goals (SDGs). Some of these setbacks will be long-lasting, in part because food prices are expected to remain higher over the medium term than pre-pandemic levels. Improvements in SDG indicators are happening at a frustratingly slow pace. Most 2030 targets will likely be missed.
- For related reasons, fiscal space has narrowed in most EMDEs. Although a generalised debt crisis has been avoided so far, many low income and some emerging market economies are up against their borrowing limits; some have defaulted. Orderly debt restructuring has become more difficult, because it requires China – by far the largest creditor, but with comparatively little influence over the International Monetary Fund and the World Bank – to agree with Western creditors.
- The world has become even more multipolar and fragmented than was already expected in 2019. Tensions between China and the US and other democracies have continued to rise. Growth prospects have shifted, with the IMF expecting lower medium-term growth in China than it did before the pandemic. Several other developing economies are growing quickly and becoming more assertive.
- Global carbon emissions continue to rise, and biodiversity is declining at alarming rates. Nationally determined contributions to mitigate emissions pledged by EMDEs are not nearly ambitious enough to keep global temperature rises below 2 degrees above pre-industrial levels, even if advanced countries fully meet their 2050 net-zero targets.

North-south climate finance remains far too low

- North-south climate finance remains far too low. While it surpassed $100 billion a year for the first time in 2022, this includes all finance (not just grants and grant-equivalents). The climate financing commitments of advanced countries remain small compared to the costs of investing in renewables and shutting down coal (Bolton *et al*, 2024).

European influence in the development finance debate is increasingly blunted by an erosion of trust

A further complication is that European influence in the development finance debate – and more broadly its soft power – is increasingly blunted by an erosion of trust, fuelled by the hoarding of COVID-19 vaccines, perceived double-standards on Ukraine and Gaza, and the perception that the EU, far from building equal partnerships, likes to impose its norms and standards on the developing world. The imbalance between large EU voting blocks in the international financial institutions and the EU's declining share of global GDP has fuelled questions about the fairness and legitimacy of the global financial architecture and is a factor behind the creation of parallel financing structures, ranging from international reserve buffers and swap arrangements to the creation of the BRICS bank. Further structures of this type could weaken Europe's influence on development finance in core areas of interest.

Challenges

Most of your predecessors' strategic decisions go in the right direction. But they also create new challenges relating to implementation and unintended consequences. There are also rising challenges relating to emerging EU policies, reduced fiscal space and the more difficult geopolitical environment.

The Global Gateway

The Global Gateway's focus on physical investment, Team Europe and avoiding paternalism all make sense. There is also nothing wrong with openness about what the EU hopes to get out of its partnerships. That said, the new strategy carries risks.

One risk is that the new framing of international partnerships will exacerbate the perception of EU hypocrisy, further weakening EU credibility in the global south. The Commission has declared that EU aid must henceforth serve EU economic and geopolitical interests but it also continues to insist that its partnerships serve the greater good: the SDGs, democratic values, good governance. These objectives could clearly clash. For example, aid allocated based on geopolitical interests needs to give disproportionate attention

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to the preferences of ruling elites, perhaps to the detriment of democratic values, transparency and some of the SDGs.

A related risk is that the emphasis on physical infrastructure could be taken too far. There is indeed a large physical investment gap, and filling this gap should be one of the purposes of EU aid (directly, and by catalysing private finance). But physical investment alone does not achieve growth and prosperity; indeed, it may create debt traps (a lesson learned in the 1970s and again through the Belt and Road Initiative).

Finally, the Team Europe approach will not work if large EU countries prefer to run their own projects and maintain their own visibility in partner countries. The willingness of countries including Germany and France to deliver a lot more of their bilateral aid through the Global Gateway will determine whether it succeeds.

Tensions with EMDEs

The EU has begun to implement policies to bolster its industrial competitiveness and prevent carbon leakage that could hurt its EMDE partners. These include industrial policies aimed at reshoring manufacturing and the carbon border adjustment mechanism (CBAM). Even if this is implemented in an entirely non-discriminatory way (that is, foreign products are taxed exactly like domestic products), CBAM creates a new burden for certain EMDE producers. Some EMDEs see CBAM as imposing EU carbon pricing on developing countries that have a claim to 'differentiated treatment' and often have little capacity to trace carbon in value chains.

Measures such as the Deforestation Regulation (Regulation (EU) 2023/1115) add to the perception that the EU is imposing its climate strategies on the rest of the world even when these limit EMDE options for development. As the EU pushes new policies to increase its energy and economic security (for example, by expanding mining and hydrogen production in Africa to the detriment of local needs in water-scarce regions), this perception may be aggravated.

Budgetary pressure

With fiscal space slim or non-existent in many partner countries and the high cost of capital as a barrier to large-scale private finance, official aid flows will continue to be crucial, especially for low-income countries. But fiscal space has also narrowed significantly in the EU. Discussions on the size and structure of the next MFF (2028-2034) will begin immediately after you take office. There will be pressure on the EU's aid budget, even while you are being asked to pursue objectives that go beyond traditional aid: accelerating the energy transition, addressing conflict and fragility, funding projects essential to EU economic security and assisting with climate adaptation.

Making resources go further

To make limited budgets go further, your first objective should be to scale up blended finance

To make limited budgets go further, your first objective should be to scale up blended finance, particularly in renewable energy, digital infrastructure and transport infrastructure. Your predecessors worked on the foundations, but the results remain unsatisfactory. The Global Gateway is struggling to leverage the private sector investments that would scale it up to the €300 billion target[2]. And north-south private climate finance remains ridiculously low in both absolute and relative terms: just $22 billion of the $116 billion reported by the OECD for 2022 (and less than $15 billion per year during 2017-2021).

The second – related – objective is effective multilateral development bank (MDB) reform. Successive G20 and United Nations panels have argued that MDB balance sheets could be used more efficiently, lending volumes could triple and mandates could shift more decisively towards global public goods. MDBs could do more to mobilise private capital, recycle Special Drawing Rights and support coordination of the climate transition through country platforms. The G20 has been preparing a roadmap for MDB reform. With EU countries holding almost 23 percent of shares in the World Bank, the EU should be well-positioned to influence reforms. But European positions on MDB strategy are not always coordinated.

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2 This is not helped by the EU's own rules in areas such as public procurement, where the principle of non-discrimination can end up preventing the Commission from financing European companies to deliver Global Gateway projects.

You and your allies will need to shepherd multilateral development banks down a path that requires uprooting of much of the *status quo*

To make MDB reform happen, you will need to align Team Europe behind key strategic decisions. You will also need to get low- and middle-income countries to engage fully on an agenda prioritised by the EU that they sometimes view as an imposition. And you and your allies will need to shepherd MDBs down a path that requires uprooting of much of the *status quo*: creating greater financial capacity through financial innovations and more risk-taking, crowding in private finance, building project pipelines in systematic collaboration with regional and national development banks, and helping to create and increasingly operate through country climate platforms.

Geopolitical tension

Even with effective coordination within Team Europe, adequate fiscal resources and a good relationship with developing country partners, EU interests in the Global South will hit a roadblock unless the EU is able to maintain a close and collaborative relationship with G7 partners and large emerging markets such as India and Brazil, while at least maintaining a functioning business relationship with China. These relationships are essential for effective MDB reform, to resolve developing country debt crises (in which China is often the largest creditor), to accelerate the energy transition and to reduce the EU's strategic dependencies without escalating tensions with China and without forcing its partners to choose between China and the West.

Facing this challenge is a matter for the entire Commission and all of Team Europe. But international partnerships must be a well-articulated pillar of this broader strategy.

Recommendations

An effective Global Gateway

Recommit to the promotion of the SDGs as the primary objective of the Global Gateway. This includes facilitating the energy transition in partner countries to cut global emissions

The Commission must stop undermining the credibility of the Global Gateway by raising suspicions about its motives. The Global Gateway should remain investment- and infrastructure-focused and should use innovative financing instruments rather than traditional official development assistance. It can and should pursue objectives that promote both the SDGs and EU global priorities, such as climate action and reducing conflict and fragility. But projects should not be selected or designed to promote the commercial or security interests of the EU when this creates a potential trade-off with the SDGs. The EU has other instruments to promote its geopolitical aims.

Embed infrastructure projects in a broader development strategy

Filling critical physical investment gaps is necessary but not sufficient for development

Filling critical physical investment gaps is necessary but not sufficient for development. Large infrastructure projects pose fiscal and environmental risks and do not generate economic returns unless embedded in a holistic development strategy. The latter requires human development and better institutions. Furthermore, health and education are important SDGs in their own right. Spending on those SDGs should be protected.

Adequate EU-level fiscal resources

Create a new MFF instrument specifically to fund international climate mitigation, and ensure it is amply resourced

International climate mitigation finance should be massively scaled up because this is in the EU's self-interest. Carbon abatement has the same economic value for the EU wherever it happens and it is cost-effective to fund reductions outside the EU. It also makes

Funding of climate mitigation should be separate from the funding of other development goals

no sense to create a trade-off between emissions mitigation and other SDGs by forcing both into the financing envelope of the same budget line. Funding of climate mitigation should be separate from the funding of other development goals, even if both are delivered through the Global Gateway.

Active policies to defuse tensions between EU and EMDE interests

Use international partnerships and EU external action to offset the economic costs of EU climate mitigation and green industrial policies

Measures such as CBAM and the Deforestation Regulation are necessary to achieve the green transition. But they require flanking measures to help development partners make the transition. A large share of CBAM revenues should flow back to partner countries to help them reduce the carbon content of their exports and to protect their forests while still meeting their industrialisation and development goals. Some of this money should support climate adaptation. The EU should monitor whether its green industrial policies benefit EMDEs by creating supply chains that include rather than exclude them.

Seek agreement on a proportionate reduction in member state voting shares and consolidation of board seats in relevant MDBs

Anachronistically large EU voting blocks are an obstacle to MDB reform and undermine trust. The EU needs to accept a reduction in its shares, to the benefit of EMDEs, as part of a broader package to modernise and refocus MDBs. Freed-up voting shares and board seats should be offered to recipient countries based on long-available formulas. The floor on collective EU shareholdings in the World Bank Group might be set at the level of the United States, while conditions and appropriate solutions will differ at the regional development banks.

Maximum impact through improved coordination

Create institutional mechanisms to ensure alignment within the Commission and with Team Europe

Mechanisms to ensure consistency at various levels, inside EU institutions and with EU countries, are a logical next step for the Team Europe approach. Given dispersed responsibilities within the Commission, there will be a continuous need for internal alignment. A separate mechanism to achieve Team Europe consistency in order to increase the EU's collective impact in partner countries might be created under the Council of the EU, with the Commission providing secretariat functions.

Build on those mechanisms to coordinate Team Europe positions on strategic and reform decisions for the MDBs

Team Europe's shares in the MDBs, even if reduced, could be leveraged more purposefully in the EU's interests. Taking account of MDB governance, agreements reached under a Council of the EU mechanism would be transmitted to board representatives but would be advisory. Board representatives (or governors, as the case may be) would use their regular, existing caucus meetings to align positions and coordinate EU voting power to drive MDB reform.

Coordinate with the World Bank, the EIB and other European instruments, regional MDBs and national finance institutions in EMDEs, with a focus on increasing blended finance for climate mitigation, and addressing other global challenges

The World Bank and regional MDBs are critical complements of EU international partnerships, because of their expertise and balance sheets, but also because they are co-owned by EMDEs. MDBs are crucial to scaling up blended finance – for instance for climate mitigation – in which official finance subsidises private investment only to the degree that is necessary and only in conjunction with supportive national policies. The Team Europe toolkit can also be leveraged by cooperating with MDBs in other contexts, including infrastructure, human development and conflict prevention.

The Council of the EU decided in June 2021 against a

unified European Climate and Development Bank[3]. If effective coordination between the EBRD, the EIB, other EU instruments and MDBs fails, it will need to be revisited.

Cooperation within the G7 and beyond

Expand and upgrade multi-donor partnerships, including Just Energy Transition Partnerships

Effective emissions mitigation and protection of biodiversity in EMDEs requires coordination not just within Team Europe, with EMDE partners and with reformed and strengthened MDBs, but also across the G7 and other international partners who share responsibility, and should share the financial burden. Apart from the expansion of international emissions trading – handled by your climate colleague – the main means to do so is the invigoration and expansion of mitigation finance through country platforms. These exist in embryonic form: Just Energy Transition Partnerships (JETPs) with South Africa, Indonesia, Vietnam and Senegal. But they are insufficient. The financing promised is far too low, and not explicitly linked to specific policy actions. JETPs should be developed to scale and expanded to additional countries.

Just Energy Transition Partnerships should be developed to scale and expanded to additional countries

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