Join up better Global Gateway and Sustainable Finance framework

The following text is a statement by the European Development Finance Institutions (EDFI) Association on the EU's Sustainable Finance framework

Brussels, 25 June 2024

We applaud the European Union's Strategy for Financing the Transition to a Sustainable Economy, and especially its global ambition. The Union has created an invaluable standard for responsible investment. The strategy once again shows an ability by EU policymakers to (i) spur long-term thinking about the future of the planet; (ii) mainstream sustainability in banking; (iii) reorient capital flows towards sustainable pursuits; and (iv) deliver a robust and consistent framework for due-diligence and disclosures. This approach has changed the way market actors—both within and outside the European Union—make business and investment decisions.

The EU sustainable finance framework complements standards already established which lay out good practices for responsible and sustainable conduct within our investment community. Examples include the EDFI Principles for the Responsible Financing of Sustainable Development and the Operating Principles for Impact Management, as well as commitments to align with the Paris Agreement, exclude fossil fuel financing, enhance disclosures and embed climate action within our institutions.

The European Union and its Member States play a much-needed enabling role in building up a strong European ecosystem of impact investors with vast reach in Low- and Middle-Income Countries (LMICs). Impact investors are now pioneers and mobilisers in economies within the European neighbourhood as well as in Africa, Latin America and in Asia. In a unique way, impact investors harness finance and technical expertise and connect the financial resources of Europe with those development and climate opportunities in LMICs. Joining up both can bring jobs and bolster climate resilience that lead to more prosperity and stability in LMICs and in Europe.

This connector role played by impact investors can catalyse Global Gateway, the European Union's global partnership proposition. The European Union offers through Global Gateway a structured and coherent response to pressing global challenges: the elimination of extreme poverty, climate change, inequality and the decline of democracy and multilateralism. EDFI, working alongside other impact investors, is committed to contributing to and advancing this EU ambition by enhancing our role of connecting development opportunities in LMICs to the aspirations of Global Gateway.

Recently implemented and proposed EU legislation on Sustainable Finance presents risks, however, of becoming a hurdle for our investment support to Global Gateway. Our experience to date has raised concerns that these rules, as currently designed, are sometimes not suited for the societies and markets in which we operate. Analysis of the hurdles show that there are realistic ways to adapt the EU Sustainable Finance framework so that they will no longer be an obstacle, but an incentive to credible and responsible sustainable economic activities supported by European investors in emerging and developing economies.

Designed with the needs of the European marketplace in mind, **the EU Sustainable Finance framework** operates, in part, by promoting the mutual exchange of information among entities subject to the same rules. It also relies—for example, in the Taxonomy's requirement that economic activities "do no significant harm" (DNSH)—on linkages to other EU laws and regulations. While these interdependencies have the effect of creating a coherent regulatory ecosystem in the European context, they represent a challenge for European investors in LMICs, where EU regulations are not applicable and where regulatory frameworks differ from those in the European Union.

Investors seeking to apply the EU Sustainable Finance framework outside the European Union therefore face several challenges. These challenges include (i) ESG data availability; (ii) the package's reliance on European law; (iii) criteria that are not adapted to the circumstances of LMICs, and (iv) the exclusion of third-country investments from eligibility under the Taxonomy Regulation and the calculation of key performance indicators such as the Green Asset Ratio.

Availability of ESG data is a particular issue in LMICs. Companies operating in LMICs frequently do not disclose, and may not realistically be able to disclose, sufficiently extensive and reliable information for investors to comply with their obligations under the regulations. Even where adequate information is available, the stringency of regulations written for a developed market creates a risk that the significant benefits of investments in LMICs that put companies on a path towards sustainability will not be credited.

Furthermore, even where investments in LMICs satisfy European criteria, investors will not see such investments reflected in their key performance indicators. The current non-recognition of third-country investments in the Taxonomy's Green Asset Ratio calculation makes climate-focussed investments in LMICs appear as if they are not sustainable. It may discourage the pursuit of such opportunities.

These challenges risk constraining investment in LMICs and therefore the mobilisation aims of Global Gateway. This is why we believe the EU Sustainable Finance framework should be further adapted. The EU legal and regulatory framework should support the EU goal to mobilise private investment for climate, environmental, and social objectives in LMICs. Amendments to the framework can deliver a regulatory regime adapted for these purposes, and proportionate to the realities in LMICs, based on a recognition of (i) the need to enhance the flow of European investments to LMICs, as part of the Global Gateway aspirations; and (ii) the incremental nature of the process to seek interoperability as between non-EU regulatory frameworks and the EU Taxonomy.

As DFIs and impact investors operating in Europe, and around the world, we have the practical experience and expertise to contribute to ongoing dialogue around the interoperability of regulatory frameworks outside Europe with the EU Taxonomy. We have identified certain aspects of the sustainable finance package that could be adapted to enhance its usability and better support economic transformation in LMICs:

- **Broaden the incorporation of existing international standards**, such as the IFC Performance Standards on Environmental and Social Sustainability—which already enjoy widespread recognition and are referenced in the Taxonomy's Delegated Acts—as an equivalent standard for financing in LMICs.

- **Adapt the requirements related to the 'Do No Significant Harm' (DNSH) principle and minimum safeguards** to ensure that a reliance on European legislation and norms does not prevent the recognition of important investments that further sustainability in LMICs.

- **Amend the Green Asset Ratio calculation** so that the calculation includes sustainable investments made outside the European Union, while recognising that this must be part of a wider programme of regulatory change—including of the kind described here—if the Green Asset Ratio is to provide a meaningful indicator of the sustainability of LMIC investments.

- **Promote interoperability between the European Union's Taxonomy and the national taxonomies of LMICs and other developed markets**, to introduce the requisite flexibility that a just transition will require, while creating a globally coherent system for recognising sustainable investments, as recommended by the High-Level Expert Group on scaling up sustainable finance in low- and middle-income countries.

- **Create an "extended Taxonomy" with greater recognition of transition finance**, as has previously been proposed by the EU Platform on Sustainable Finance, to incentivise sustainable transformation through such mechanisms as a "traffic light" system that formally recognises investments on a pathway to sustainability, or a separate transition-related KPI, while recognising that any such extension would itself need to be adapted for investments in LMICs.

Beyond these proposed changes, we recognise that the most essential changes must happen at the level of individual companies in LMICs. Therefore, we would welcome more public financial support for technical assistance to clients of investments in LMICs, alongside support for wider financial market development and enabling environment solutions, to further improve practices and capacity to provide the data necessary for compliance with the Sustainable Finance framework. Such support will be critical for those businesses, such as SMEs in LMICs, that stand to benefit most from investment but may lack the resources necessary to allow compliance with the regulations.

For a successful delivery of Global Gateway, continued engagement between the European Union and European impact investors and the European Development Finance Institutions (EDFI) can help build a fully workable, adaptable, proportionate, and global system of rules. Doing so will enable us to fully contribute to the mobilisation of investment for LMICs and the full array of aspirations of Global Gateway.

Contacts for additional information:

James Brenton, Sustainable Finance & Impact Advisor, EDFI, james.brenton@edfi.edu
James Pieper, Senior Communications Advisor, EDFI, james.pieper@edfi.edu, +32 490 16 76 67

Notes to editors:

About EDFI: The Association of European Development Finance Institutions, or EDFI, was established in 1992 to support and promote the work of bilateral Development Finance Institutions (DFIs). With a combined portfolio of €53 billion, including over €15 billion of climate finance, EDFI's 15 member institutions share a vision of a world where the private sector offers people in low- and middle-income countries opportunities for decent work and improved lives, and where private investment flows are aligned with the Sustainable Development Goals and the Paris Climate Agreement. EDFI's mission is to promote the joint interests of its members, inform policy, and drive innovation in industry standards. Learn more at www.edfi.eu

EDFI membership: BII (United Kingdom), BIO (Belgium), Cofides (Spain), DEG (Germany), Finnfund (Finland), FMO (The Netherlands), IFU (Denmark), Norfund (Norway), OeEB (Austria), Proparco (France), SIFEM (Switzerland), Simest and CDP Development Finance (Italy), SOFID (Portugal), and Swedfund (Sweden).

About the Platform on Sustainable Finance
The Platform is an advisory body subject to the Commission's horizontal rules for expert groups. Established in October 2020, the Platform plays a key role in enabling cooperation by bringing together the best expertise on sustainability from the corporate and public sector, from industry as well as academia, civil society, and the financial industry. Learn more about the Platform on Sustainable Finance at the European Commission website.

About the High-Level Expert Group (HLEG) on scaling up sustainable finance in low- and middle-income countries
Set up by the European Commission, this group's primary tasks are to identify the challenges and opportunities that sustainable finance presents in our partner countries and provide recommendations to the Commission to accelerate private financial flows. The group was formed when the European Commission adopted, in July 2021, a Strategy for Financing the Transition to a Sustainable Economy to improve the flow of money towards financing that transitions economies to become more sustainable. This includes support to low- and middle-income countries in scaling up their access to sustainable finance by developing a dedicated EU Sustainable Finance Strategy and by promoting sustainability-related financial instruments. Learn more about the HLEG at the European Commission website.

EDFI Principles for the Responsible Financing of Sustainable Development
EDFI member institutions have endorsed a set of commitments for our approach to the responsible financing of sustainable development, encompassing responsible financing, impact management and transparency. The commitments are set out in the "EDFI Principles for Responsible Financing of Sustainable Development. Learn more.

Operating Principles for Impact Management
The Impact Principles are a framework for investors for the design and implementation of their impact management systems, ensuring that impact considerations are integrated throughout the investment lifecycle. Called the '9 Principles', they may be implemented through different types of systems, each of which can be designed to fit the needs of an individual organisation. They do not prescribe specific tools and approaches, or specific impact measurement frameworks. The expectation is that industry participants will continue to learn from each other as they implement the Impact Principles. See the principles.

EDFI Statement on Climate and Energy Finance
EDFI members agreed on a list of joint ambitions on climate and energy related finance including key commitments to mobilise private investments aligned with the Paris Agreement. The statement aims to signal real ambition for the sector while recognising the development needs of the countries European DFIs invest in. Read the statement

ends / all