Direct economic co-benefits matter

Greening cooperation for economic development

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The world economy is shifting towards green technologies and business models. In low- and middle-income economies, the resulting opportunities are mostly underexplored. BMZ's new 2023 strategy for "Sustainable economic development, training and employment" clearly shifts gears towards a *green and inclusive* structural transformation, recognising that only a just transition approach with credible co-benefits for societies can gain societal acceptance.

To accelerate green transformation in low- and middle-income countries, it is therefore essential to provide evidence of how a greener economy can offer direct economic benefits to national economies and the majority of citizens. Benefits must go beyond a healthier environment to also include employment and income opportunities, export revenues and/or energy security. The nexus between greening and direct co-benefits should become a key feature of German development policy in this field. Ongoing cooperation portfolios now need to be adjusted to this new and timely orientation in BMZ's core strategy. We suggest the following adjustments (click here for a more detailed version):

Raising revenues for pro-poor spending via eco-social fiscal reforms: Developing and emerging economies need to increase tax revenues, e.g. for infrastructure, education and social security. It is better to tax undesirable rather than desirable things, for example, pollution instead of incomes, exports, or enterprises. Price signals are essential for a green transformation and do not need to harm the poor. Eco-social fiscal reforms that price pollution and resource depletion while removing environmental harmful subsidies are a win-win option. They can be made politically and socially acceptable if revenues are used to reduce taxes on productive assets and increase pro-poor spending. Eco-social fiscal reforms should become a priority across all German cooperation programmes aimed at economic development or climate change.

Sustainable cities as an economic stimulus package: Sub-Saharan Africa alone needs to create 15 million jobs per year – but how? Urbanisation is in full swing, especially in Africa and South Asia, requiring unprecedented levels of investment in buildings and infrastructure. This will lock in enormous carbon emissions for decades, unless city design fundamentally changes now: Towards mixed-use neighbourhoods, low carbon transit and sustainable buildings. The good news is that building with renewable materials substituting emissions-intensive steel and cement creates many new jobs, and mixed-use quarters favour small relative to big enterprises.

Business models for sustainable consumption: Middle-classes in emerging economies are booming, and their increased purchasing power often results in unsustainable consumption practices – buying cars, fast fashion, air travel. Leveraging this demand for the green economy is essential and offers great potential for partner countries. Local consumption in low- and middle-income countries is not yet a priority of German cooperation – but it should be, for example, working with retail corporations as change agents, introducing eco-design guidelines, supporting local green consumer standards and fostering sustainable start-ups.

Inclusive green finance: A green transformation requires large amounts of additional public and private investments. Fortunately, green finance instruments are expanding, and especially public banks are greening their portfolios. Yet, green finance runs the risk of exacerbating financial exclusion. Unless access to affordable finance is ensured, stricter environmental standards can jeopardise the survival of small enterprises that cannot invest in clean technology or pay for environmental certification. Policymakers can be supported in adopting an equity lens to green finance, e.g. facilitating IT-based procedures to bring down the cost of lending and insurance products for SMEs and households.

Green industrial policy: Industrial policies and technological learning have played a key role in those latecomer economies that managed to close the productivity and income gap vis-à-vis rich nations (while others fell further behind). Yet, development agencies have rarely systematically adopted a sector-wide perspective of productivity-enhancing structural transformation. With the shift to a global green economy, industrial development opportunities change, and new technological capabilities are required. Green hydrogen is one prominent example, promising opportunities for industrial development, economic diversification and technological learning in countries with rich renewable energy endowments. Yet, such benefits do not accrue automatically. Without national investments in industrial policy capabilities, hydrogen investment can easily turn into foreign-owned enclaves that encourage rent-seeking rather than technological upgrading. Germany should emphasise support for core industrial policy institutions: technology foresight agencies and think tanks as well as multi-stakeholder platforms, and Fraunhofer-type institutes for promising green technologies. In parallel, Germany should support trade measures, including trade rules that promote low-income countries' opportunities to implement effective green industrial policies.

It is evident for all above areas that the challenges in low- and middle-income economies will differ from those in high-income countries. It is, therefore, imperative that successful and locally adapted programmes are co-developed with local partners. A just green transition that harvests benefits beyond a healthier environment and is supported by societies is then achievable.

Recommended citation: Altenburg, T. / Pegels, A. (2023). Greening cooperation for economic development
(The Current Column 22 November 2023). Bonn: IDOS