Ninety Second Sovereign Debt News Update: South Africa Concludes $1 Billion Hydrogen Fund Agreement for the Implementation of the $8.5 Billion Climate Finance Pact

By:

The African Sovereign Debt Justice Network

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South Africa is well-positioned to potentially become a major producer of green fuel, which is anticipated to eventually replace natural gas owing to its abundant wind and solar resources and industrial capability. Pursuant to this potential, South Africa's President Cyril Ramaphosa, Netherlands Prime Minister Mark Rutte, and Denmark Prime Minister Mette Frederiksen concluded a Heads of Agreement to launch a new SA-H2 Fund, which has a goal to raise $1 billion (R18 billion) for green hydrogen. Supported by the finance investment firm Climate Fund Managers (CFM) and Invest International (II) of the Netherlands, Sanlam Limited of South Africa (Sanlam), the Development Bank of Southern Africa (DBSA), and the Industrial Development Corporation of South Africa (IDC), in collaboration with other strategic partners, the SA-H2 is a blended finance fund that will facilitate and accelerate the development of a green hydrogen sector and circular economy in South Africa. According to one source, the inclusion of Denmark and the Netherlands strengthens South Africa's efforts to reduce coal dependency, which currently accounts for over 80% of its electricity generation.

The planned fund comes as South Africa prepares to implement an $8.5 billion climate finance pact with some of the world's richest countries as it seeks to transition away from the use of coal. As reported in the Fifty-Fifth Sovereign Debt News Update in November 2022, South Africa clinched a $8.5-billion climate finance deal with France, Germany, the European Investment Bank, the UK and the US. The deal was hailed as a prototype for helping other coal-dependent developing countries transition to cleaner energy sources.

There have been delays to the implementation of the deal. The implementation of South Africa's landmark pact has been delayed by how to incorporate recommendations that it do more to spell out how coal-dependent workers and communities will be shielded from the impact of a green transition. According to Rudi Dicks, head of the project management office in the Presidency, the South African government's Just Energy Transition Implementation Partnership now aims to produce a plan on how it will spend the money to shift the country away from using coal by the end of August 2023.

The fund, which is a first for South Africa, is expected to add a blended finance facility and is intended to catalyse more private-sector investment in the industry. The fund will also receive contributions from the DBSA and the Industrial Development Corp. of South Africa Ltd., which are both state finance institutions, Sanlam Ltd., and the Hague-based Climate Fund Managers BV. According to the chief executive officer of the Development Bank of Southern Africa (DBSA), Boitumelo Mosako, the fund's goal is to catalyse more private-sector investment in the industry.

It is imperative to note the developing trend by African governments in the uptake of blended finance as a solution to tackling the climate crisis. In addition to Netherlands and Denmark, Germany is also pouring massive resources into creating a global market for green hydrogen, including a $1 billion H2Global project that promotes hydrogen partnerships, particularly on the African continent. Some of the hydrogen partnership deals by Germany include with South Africa, Morocco, Niger, Angola, and Namibia. One source claims that in the case of Namibia, the green hydrogen derisking bloc also includes German capital, as well as a collaboration between Capricorn Investment (founded by Jeff Skoll of eBay), the local public pension fund, and the mining pension fund.

Once established, the South Africa's hydrogen fund will join the SDG Namibia One Fund as the second-of-its-kind, regional blended finance fund to develop and fund green hydrogen projects. The SDG Namibia, which similarly aims to secure $1bn in funding to be raised directly in Namibia or indirectly via other channels, is a partnership between Climate Fund Managers, Invest International, and the Environmental Investment Fund of Namibia. The Dutch Development Bank and Sanlam Infraworks own Climate Fund Managers, while Invest International is a financing institution owned by the Dutch Ministry of Finance. The Namibia Green Hydrogen and Derivatives Strategy, which sets out the government's action plan to establish Namibia as a major global hydrogen producer by 2025, notes that Namibia could enjoy a significant competitive advantage due to a favourable combination of solar and wind conditions, along with the coastal location of its renewable resources. The competitive advantage of this strategy lies in the production of green hydrogen derivatives such as ammonia, methanol, e-kerosene and green hydrogen-based hot briquetted iron. Such investments by the Namibian government in hydrogen developments have been necessitated by the need to achieve more energy self-sufficiency and to reduce its strong reliance on energy from crisis-laden South Africa and its coal-fired power stations. Against this backdrop, one scholar has cautioned that "*private investors in African green hydrogen projects threaten yet another (green) commodity trap for countries in the Global South*."

Climate change currently presents an urgent imperative to transform the world's energy system. However, a significant increase in the volume and accessibility of low-cost financing is required in order to achieve both climate and other development goals. This is especially true for countries in the Global South, which are increasingly in debt distress. Heavily indebted African countries reportedly can no longer afford fossil fuel subsidies. Senegal, like

Nigeria and Angola, is eliminating costly fossil fuel subsidies. This was once not politically feasible, but due to crushing debt, a rise in borrowing rates, and rising fuel prices, it has become necessary. At the recently held Paris Summit for a New Global Financing Pact, a Just Energy Transition Partnership (JETP) was launched for Senegal to mobilize public and private finance toward transitioning the country's energy system. First developed for South Africa, the JETPs provide an energy transition plan supported by both public and private investors.

Undoubtedly, South Africa has set the pace for other coal-dependent African nations going the green transition path. While sustainable energy practices are encouraged, the cost of financing a just transition should not add to the already existing debt crisis. Acknowledging the blended-financing nature of this deal, there are valid concerns on how it leverages private sector financing. This is particularly so considering how private sector financing advances profit maximization at the expense of development and hinders loan transparency and accountability. Caution is therefore required to ensure that African governments do not fall into climate-related debt traps.

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