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POLICY PAPER
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Time for climate leadership in carbon-free export finance

– An opportunity for Sweden

Summary

In Sweden and elsewhere, export credits policies have not fully aligned with the climate goals of the Paris Agreement and with scenarios on net zero emissions pathways. Despite recent policy change limiting support to coal and oil and gas *extraction* and *exploration*, current Swedish export credit policies allow actors in the export credit system to promote and underwrite projects in the oil and gas value chain, including power plants, refineries, pipelines, and transport and storage of fossil fuels. Support to fossil fuel energy projects is at odds with Sweden's climate policies in other areas, as well as with Sweden's ambition of being one of the world's first fossil-free welfare nations. This brief argues that Swedish export credit policies should align with Swedish climate policies including the policy goal of a fossil-free Sweden, and with the temperature goals of the Paris Agreement, while recognizing the need of and ensuring a just transition. In addition, Sweden should advocate for stricter policies on export support to oil and gas in international fora, such as the OECD and the UN Climate Change Conference.

RECOMMENDATIONS TO THE GOVERNMENT OF SWEDEN

- **Domestically, ensure coherence in climate policy and adopt a whole-of-government approach to climate change, ending export finance support to overseas fossil fuel energy projects, while recognising the need for a just transition;**
- **Internationally, contribute to establishing a coalition of countries committing to stop export finance to fossil fuel energy projects ahead of the November 2021 UN Climate Change Conference (COP26) in Glasgow;**
- **Within the OECD, advocate for the introduction of a new Sector Understanding on restrictions to oil and gas export finance, as well as for strong climate provisions throughout the OECD Arrangement.**

Background: climate change and the role of financial actors

Scientists agree that, to avoid dangerous global warming, greenhouse gas emissions should quickly decline to net zero by 2050. To achieve this, signatories to the 2015 Paris Agreement have committed to making "financial flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development"[1] and solicited the help of non-state stakeholders, including financial institutions, to "address and respond to climate change."[2] State, business and financial actors thus have a clear role in addressing risks arising from climate change.

According to the August 2021 Sixth Assessment Report (AR6) of the United Nations Intergovernmental Panel on Climate Change (IPCC) global warming could exceed 2 °C already between 2040 and 2050 unless strong climate mitigation measures are quickly implemented.[3] According to the AR6, only scenarios with very low or low greenhouse gas emissions declining to net zero around or after 2050 are assessed to be likely to avoid global warming of more than 1.5 °C and 2 °C respectively. The findings of the AR6 confirm, once again, the urgency of strong policy action to limit greenhouse gas emissions.

In its report *Net Zero by 2050: A roadmap for the global energy system*, the IEA concludes that the global pathway to net zero emissions by 2050 requires "all governments to significantly strengthen and then successfully implement their energy and climate policies."[4] The pathway which according to the agency's analysis is "the most technically feasible, cost-effective and socially acceptable", leaves no room for new oil and natural gas fields and states that unabated[I] coal and oil power plants need to be phased out as soon as possible. In the same scenario, electricity generation by unabated natural gas is "allowed" to grow until the mid-2020s, but will need to soon decrease after that[5], with global natural gas use seeing a 55 per cent reduction in 2050 compared to 2020.[6] The IEA scenario depicts a narrow path to net zero emissions, and a series of milestones including the phaseout of fossil fuels and a large-scale implementation of renewable energy and energy efficiency technologies. These milestones require significant readjustments in all sectors of society, including export finance and export credit agencies.

Nonetheless, the current global climate policy landscape differs starkly from net zero scenarios: despite a temporary decline due to the Covid-19 pandemic, emissions of greenhouse gas remain unsustainably high, and investments in the current and planned production of fossil fuels are not aligned with the 1.5 °C (or well below 2 °C) temperature goal of the Paris Agreement.[7]

Export finance and climate change

Export credit actors provide credits, guarantees, or loans to exporting companies, and thus enable export deals which would have otherwise been more difficult, costly, or impossible, to execute. As such, export credit agencies play a crucial role in financing and determining the development of energy technologies in the Global South. Since export credit agencies are typically regulated by national governments, policy coherence would demand that policies governing trade promotion, export finance, overseas development aid and direct foreign investments be aligned with exporting countries' climate goals and international commitments, such as those of the Paris Agreement. However, while in some countries export credit agencies have begun to align their activity with climate goals, data from the non-governmental organization (NGO) Oil Change International show that export credit agencies are still one of the largest international public financiers of fossil fuel energy projects.[8] This is troubling given the tight timeframe to reduce emissions described by the IPCC's AR6: continued support for investments in fossil fuel energy projects can lead to global warming of more than 2 °C and to

I The term "unabated" refers to the combustion of fossil fuels without carbon capture and storage.

"carbon lock-in"[II] in low-income countries for many years to come, contributing to making the energy mix of those countries overly reliant on fossil fuels and incompatible with the 1.5 °C temperature goal. Furthermore, fossil fuel energy projects frequently lead to adverse impacts on the environment and public health.[9]

Policies governing export finance and the climate transition in Sweden

Poor policy coherence between export finance policies and national and international climate commitments has only recently received attention, and much remains to be done to align the activities of export credit agencies to climate goals. In Sweden, where the policy goal of being "one of the world's first fossil-free welfare nations" was adopted in 2015[10] and a net zero climate policy has been in place since 2017[11], the Swedish government has not yet fully aligned policies governing export credit agency Exportkreditnämnden (EKN) and state-owned export finance bank AB Svensk Exportkredit (SEK) with climate goals. EKN and SEK have been criticized for guaranteeing and financing export projects contributing to adverse impacts on health and climate.[12,13] During 2019 and 2020, EKN issued guarantees associated with oil and gas worth 965 million Swedish crowns; in the first four months of 2021, guarantees worth 120 million Swedish crowns were issued[14] for transactions related to the oil and gas sector[III].

New policies were adopted by the Swedish government in 2019 – as part of a new export strategy[15] focusing on clean-tech exports and its potential contribution to climate change mitigation in export markets – to align Sweden's export credit system with the country's climate goals. The new export strategy explicitly commits to phasing out export finance for extraction and prospecting of fossil fuels by 2022. The strategy further mandates actors in the Swedish export credit system to evaluate how Swedish export credits can contribute to a transition to climate-resilient development and avoid carbon lock-in effects in other countries. In September 2020 EKN issued the report *An export finance system that contributes to the climate transition*,[16] including recommendations for the Swedish export credit system to increase support for business deals that contribute to the climate transition and increasing transparency on the sustainability and climate areas, recommendations which were reflected in the December 2020 appropriation letter (*regleringsbrev*) from the government to EKN.[17]

Consistent with the report's recommendations and the appropriation letter, EKN and SEK in 2020 adopted criteria to evaluate support for projects that have the potential to increase greenhouse gas emissions, including by assessing whether such projects have the potential for a low-carbon transition by 2030, and whether they are compatible with global net zero emissions by 2050. During 2020, ahead of the deadline set out by the export strategy, EKN updated its sustainability policy[18] to exclude business activities related to coal, unconventional oil and gas, as well as to new developments of oil and gas fields from export finance support.[19] In August 2021 it was announced that a scientific climate council was established to provide advisory support to EKN and SEK in aligning the Swedish export finance system with the Paris Agreement's 1.5 °C goal.[20]

However, despite these positive policy developments and the strategy to provide more support for renewable energy projects, there are no government policies in place mandating Swedish export credit actors to phase out export finance for projects throughout the fossil fuels value chain. Consequently, EKN's and SEK's policies still allow for financing projects in the oil and gas value chain, such as refineries, pipelines, and oil and gas power plants.

II The Stockholm Environmental Institute defines carbon lock-in as the situation in which "once certain carbon-intensive investments are made, and development pathways are chosen, fossil fuel dependence and associated carbon emissions will be "locked in", making it more difficult to move to lower-carbon pathways."

III See Appendix. EKN's exposure to fossil fuel energy projects between January 2019 and April 2021 amounted to less than 1% of EKN's total transactions.

International context

While each state regulates the activities of national export credit agencies, there are international frameworks covering various aspects of export credits, including climate change and fossil fuels. However, existing frameworks fail to ensure a full alignment of export credit agencies with international climate goals, rather agreeing on minimum terms to avoid support for projects with the highest climate impacts.

For instance, the Organisation for Economic Cooperation and Development (OECD) has adopted an "Arrangement"[21] to create a level playing field for government supported export credits which includes "Sector Understandings" on different topics, including on coal-fired electricity generation (known as the CFSU)[22] in which member countries commit to refraining from providing export support to coal power plants over a certain capacity. The CFSU contemplates however only limited exemptions on what fossil fuel energy projects are to be excluded by export finance support, essentially merely encouraging exporters and buyers of coal-fired power plants to depart from "low-efficiency" towards "high-efficiency" technologies.

Within the European Union, the Foreign Affairs Council has agreed to discourage further investments in fossil fuel-based energy infrastructure projects in third countries and called for an end to financing of new coal infrastructure, while agreeing to promote a global phaseout of harmful fossil fuel subsidies.[23] European regulation 1233/2011[24] effectively makes the OECD Arrangement legally binding for export credit agencies of EU member states, and sets out reporting measures – including how environmental risks are to be considered by EU export credit agencies.

In April 2021, Sweden, Denmark, the Netherlands, France, Spain, Germany, and the United Kingdom (UK) created an initiative called Export Finance for Future (E3F)[25] through which they commit to align export finance to climate targets. Notwithstanding the ambitious goal, E3F's commitments fall short of a comprehensive exclusion of export finance to all fossil fuel energy projects. While it was clear that E3F countries would stop export finance directed to coal and coal power, weaker commitments were adopted in relation to oil and gas, such as initiating a review of how to best phase out export finance to fossil fuel energy projects. Above all, E3F's commitments lack clear timelines and targets.

An obligation to reduce emissions

It is increasingly recognized that there is a legal obligation for governments and other state actors to take adequate action to mitigate climate change. A legal opinion[28] focussing on the roles and responsibilities of export credit agencies in mitigating climate change was recently issued at the behest of the international NGO Oil Change International, stating that the continued support for fossil fuel energy projects by export credit agencies in the form of export credits is in principle not compatible with international law obligations, and that export credit agencies should adopt timelines to decrease and phase out support to fossil fuel energy projects. According to the same legal opinion, international law places a due diligence obligation on states, to avoid significant environmental harm and protect human rights, which in turn implies efforts to reduce emissions.

A similar argument was espoused by the Dutch Supreme Court, which in December 2019 upheld a claim brought by Dutch NGO Urgenda asking the Dutch government to review its greenhouse gas emissions reduction targets.[29] While the Court recognized the uncertainties and complexities of climate change mitigation, and acknowledged that a single state cannot solve climate change on its own, it maintained that the Dutch state has an individual responsibility to mitigate climate change, regardless of measures adopted by other states.

Recent years have seen an increase in climate change litigation: climate litigation claims against state and business actors are constantly breaking new legal ground, and it is not unlikely that governments and export credit agencies could soon face litigation for providing export finance support to fossil fuel energy projects overseas amid a recognized climate crisis.

Similarly, in May 2021, the G7 countries adopted ambitious but vaguely defined commitments "to ensure that financial flows from [public financial institutions] are aligned with the goals of the Paris Agreement." G7 countries also committed to "take concrete steps" to end financing of coal power projects by the end of 2021, and to begin phasing out support for "carbon intensive international fossil fuel energy, except in limited circumstances."[26]

At the time of writing, the most progressive policy on export credit and climate is the one adopted by the UK in March 2021. The UK policy excludes all trade promotion activities and export finance support related to fossil fuels, other than in limited circumstances,[27] making exemptions for gas powered generation under the fulfilment of certain conditions and providing a one-year transition period for small and medium sized exporters.

A just transition in export finance

It is generally accepted that the transition to a low-carbon and climate-resilient economy has the potential to stimulate economic growth and create employment opportunities.[30] However, climate transition policies, including efforts to align export finance with climate goals, also have the potential to adversely impact industry sectors, companies, communities, and jobs.[31] It is hence important to manage the impacts of policy change using a just transition perspective to ensure that equity issues are addressed. Indeed, it can be argued that transitions adopting a rights-based approach, taking into account impacts on vulnerable workers, families and communities affected by policy changes, are more likely to succeed.[32] In other words, successful climate policies are effective in managing transition risks while ensuring that equity issues are addressed during the transition.

In the case of export credits, potential negative impacts and equity issues arise both domestically and abroad. Domestically, new business and employment opportunities brought about by the climate transition will likely be created in sectors and regions other than those most impacted by a low-carbon transition.[33] At the same time, a study evaluating export finance support for domestic energy jobs in the UK, a country with a sizeable oil and gas industry, found that support for renewable technologies is more effective at creating jobs than support to the oil and gas sectors, mainly due to renewables having higher labour intensity relative to fossil fuels.[34] In addition, the study found that a phaseout of export finance to fossil fuel energy projects would not overly affect UK domestic jobs.

Fossil fuel energy infrastructure is at times seen as necessary for development in countries and regions with poor energy infrastructure or where access to energy is lacking.[35] However, the downward cost trends of renewable energy, the adverse impacts of fossil fuels on health, and considerations about energy independence of communities show that fossil fuels are far from the best solution to guarantee development and access to energy in least developed countries. On the contrary, continued investment in fossil fuel infrastructure has the potential to lock low- and middle-income countries in carbon-dependent pathways, exposing them to transition risks[IV] and to the risk of creating stranded assets and stranded communities. In this regard it is worth noting that multilateral and development finance institutions, whose main mandate is to reduce poverty and promote sustainable development, have not shied away from enacting policies limiting financing of fossil fuel energy projects, mindful that failure to mitigate climate change will disproportionally affect already marginalized groups in least developing countries[V].

From a just transition perspective, new trade promotion and export credit policies should include provisions to support workers, families, regions and communities affected by the climate transition, including through re-skilling,

IV Transition risks can be defined as the risks arising from changes in policies, practices, and technologies, as government and societal actors take action to constrain carbon-intensive activities, whether regionally or globally.

V For example, Swedish development finance institution Swedfund, whose mandate is to invest to reduce poverty, has since 2014 stopped investing in fossil fuels projects. Likewise, the European Investment Bank stated that it "will end financing for fossil fuel energy projects from the end of 2021."

education and research, and support to impacted industry sectors.[36] For example, the recent UK policy change, which determined that the UK will no longer provide any new direct financial or promotional support for the fossil fuel energy sector overseas, other than in exceptional circumstances, was accompanied by measures to support industry in this transition, including a grace period for small and medium sized enterprises, as well as a renewed focus on the trade opportunities arising from new energy markets. From the perspective of recipient countries, adopting a provision in export finance policies allowing support for electricity supply projects deemed necessary in contexts of severe energy poverty could ensure that human development and access to energy are not jeopardized.

Such provisions should however not be used as loopholes to delay necessary climate transition policies, but only be employed when no alternatives are commercially or technically available. Any exception should in addition be coupled with ambitious greenhouse gas emissions thresholds and mitigation plans.

Recommendations

Sweden has an opportunity to be a leader on policies for climate and export finance. To achieve this, Sweden should:

- Domestically, ensure coherence in climate policy and adopt a whole-of-government approach to climate change, ending export finance support to overseas fossil fuel energy projects, while recognising the need for a just transition;

- Internationally, contribute to establishing a coalition of countries committing to stop export finance to fossil fuel energy projects ahead of the November 2021 UN Climate Change Conference (COP26) in Glasgow;

- Within the OECD, advocate for the introduction of a new Sector Understanding on restrictions to oil and gas export finance, as well as for strong climate provisions throughout the OECD Arrangement.

Appendix

List of transactions related to oil and gas supported by EKN, January 2019 to April 2021. EKN's exposure to fossil fuel energy projects between January 2019 and April 2021 amounted to less than 1% of EKN's total transactions.

Year	Type of guarantee	Amount in MSEK	Sector	*Country*
2019	Supplier credit guarantee (*leverantörsgaranti*)	4	Oil	Singapore
2019	Export loan guarantee (*långivargaranti*)	715	Natural gas	Argentina
2019	Supplier credit guarantee (*leverantörsgaranti*)	153	Oil	Mexico
2019	Supplier credit guarantee (*leverantörsgaranti*)	8	Natural gas	Mozambique
2019	Supplier credit guarantee (*leverantörsgaranti*)	Not disclosed due to secrecy	Natural gas	Mozambique
2019	Counter guarantee (*motgaranti*)	Not disclosed due to secrecy	Oil	Sweden / Singapore
2019	Supplier credit guarantee (*leverantörsgaranti*)	21	Natural gas	Saudi Arabia
2020	Supplier credit guarantee (*leverantörsgaranti*)	3	Oil	Singapore
2020	Supplier credit guarantee (*leverantörsgaranti*)	Not disclosed due to secrecy	Oil	Singapore
2020	Supplier credit guarantee (*leverantörsgaranti*)	7	Oil	Singapore
2020	Counter guarantee (*motgaranti*)	20	Natural gas	Sweden/Taiwan
2020	Counter guarantee (*motgaranti*)	19	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	3	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	3	Natural gas	Sweden /Taiwan
2020	Counter guarantee (*motgaranti*)	9	Natural gas	Sweden
2021	Supplier credit guarantee (*leverantörsgaranti*)	40	Oil	Mexico
2021	Export loan guarantee (*långivargaranti*)	71	Oil/ Natural gas	Saudi Arabia
2021	Supplier credit guarantee (*leverantörsgaranti*)	9	Oil/ Natural gas	Saudi Arabia

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