International NGO Forum on Indonesian Development

Review of Financing for Sustainable Development 2022 Report: Bridging the Finance Divide

MAY 2022

Background

On Tuesday, 12 April 2022, the Inter-Agency Working Group on Financing for Development, composed of more than 60 UN system agencies and international partner organisations, launched the new report on financing for sustainable development: 'Closing the Financing Gap'. This report is the sixth since its inception in 2016.

Linked to Goal 17, this report identifies a financial divide between developing and developed countries for recovery to respond to crises and investment in sustainable development. The risk of debt distress caused or exacerbated by the pandemic and the recent war in Ukraine, which now affects 60% of least developed countries (LDCs) and other low-income countries, has resulted in an inability to raise sufficient resources and borrow affordably for investment. This is despite the provision of large-scale emergency financing and the G20's Debt Service Suspension Initiative (DSI), which have at least prevented a wider, systemic debt crisis.

The pandemic and the war in Ukraine have generated a global economic context of inflationary pressures, supply disruptions, commodity price volatility, and interest rate hikes by several central banks. These impacts have consequently destabilised domestic financial conditions and growth in developing economies (GDP per capita is expected to remain below 2019 levels by the end of 2023 for 20% of them), and have also resulted in a high cost of financing sustainable development. They have further exacerbated pre-existing poverty and inequality by disproportionately affecting vulnerable groups (low-skilled and informal workers, women, youth, and migrant workers).

Developed countries adopted aggressive macroeconomic policies to respond to the COVID-19 pandemic by financing a large-scale response at historically low-interest rates while developing countries were unable to finance an appropriate response to this historic shock. While household incomes and financial markets in the former were stabilised, those in the middle- and low-income countries (MICs, LICs) and least-developed countries (LDCs) were in difficulties.

Gender equality, one of the main goals of the 2030 Agenda (SDG 5), must be ensured more than ever. Despite progress with gender-sensitive statistical systems in countries that prioritize gender in their national planning and policies, the effects of the pandemic on labour markets and social protection have exacerbated existing inequalities, particularly in developing countries. Therefore, gender-responsive budgeting and fiscal policies are essential for achieving gender equality and women's empowerment.

In light of the disparities between developed and developing countries, and in order to overcome this financial divide for the overall achievement of the SDGs, the report makes several policy recommendations, both at the domestic and international levels.

This paper was written by Romain Segouin (SDGs and Human Rights Intern at INFID). You can download the Financing for Sustainable Development 2022 report at www.developmentfinance.un.org/fsdr2022

First, the report mentions domestic public resources and systemic issues.

According to the report, the ability to borrow affordably depends on national actions, including good governance, public financial management and institutional frameworks. To this end, Integrated National Financial Frameworks (INFFs) are presented as an excellent tool for good governance by aligning financing policies and strategies with investment priorities and sustainable development strategies. Indeed, through four elaboration stages in line with the Addis Ababa Action Agenda, INFFs allow national authorities to consider strengths and vulnerabilities in achieving sustainable development priorities. As a result, public investment decisions would be guided by a national medium-term sustainable development strategy and plan, and development cooperation would be more effective in expressing the needs of developing countries to the international community and improving the transparency of financial flows.

To reverse the recovery gap and achieve the SDGs, due to investor perceptions and uncertainty about repayment capacity, developing countries need reliable access to long-term, affordable and stable finance from concessional and non-concessional sources (public, private, domestic, and international). In particular, the report argues that counter-cyclical fiscal policies could be established in advance of the crisis to reduce the extent of short-term damage and medium-term scarring. In addition, an effective tax system, for example, through general taxation and social security contributions, could reduce inequalities or lead to the creation of universal social protection (only 46.9% of the world's population had access to at least one social protection benefit in 2020).

At the national level, policymakers should follow a systemic approach to each infrastructure sector, rather than a project-by-project approach. A long-term vision is needed to transform developing economies in line with the achievement of the 2030 Agenda.

On the revenue side, mobilizing additional public investment funding means improving income taxes' progressivity, reducing distortions arising from tax exemptions, and using technology to improve tax administration. On the expenditure side, spending and protecting investments in the SDGs, as well as improving the efficiency of spending and the quality of public procurement. The efficient use of resources and productive use of revenues is also required and logically imply strengthening transparency, accountability, risk management, and good governance practices.

Secondly, the report mentions international development cooperation.

The report calls on the developed countries to meet their Official Development Assistance (ODA) commitments - $100 billion per year from public and private sources to support climate action. Despite the record level reached in 2020, rising by 3.5 per cent in real terms to $161.2 billion, the ODA volume is below the United Nations target regarding the commitment to provide 0.7 per cent of ODA per gross national income (GNI). At this moment, only six donors met or exceeded the target: Denmark, Germany, Luxembourg, Norway, Sweden, and the United Kingdom. In this implementation, the report considers grant finance as a priority, at the difference of loans. Besides not evenly distributed, the contributions are focused more on terrestrial and freshwater biodiversity than on marine biodiversity. Moreover, despite progress in recent years, only 53 per cent of the current bilateral allocable ODA for climate change integrated gender equality objectives.

As the pandemic has shown the interconnected links between the economic, social, and environmental pillars of sustainable development, the impacts of climate and other risks have to be incorporated into the decision-making. In this order, the OECD Development Assistance Committee (OECD DAC) members recently agreed to align ODA with the Paris climate goals, and the Group of Seven (G7) countries announced the end of their international support for coal power.

On the basis of the Glasgow Climate Pact, the agreement reached at the COP26, the developed countries are called to at least double their collective provision of adaptation finance from 2019 levels by 2025. To achieve the goals of international environmental agreements, and to limit climate change to 1.5 degrees Celsius, Member States need to align their fiscal systems with sustainability goals. To be feasible and effective, the report mentions the policy measures that could be implemented by the states: pricing of carbon emissions, the investments in renewable energies, the adoption of consistent corporate sustainability reporting standards, and credible norms for sustainable investment products.

In addition, it recognizes the merits of South-South cooperation to tackle climate change adaptation and mitigation, as well as its response to the pandemic.

Nevertheless, in the past two years, private equity funds acquired $60 billion worth of oil, gas, and coal assets, more than their investments in renewable energies. In 2020, fossil fuels still accounted for 85 per cent of global primary energy consumption. Despite that, the investment in the global energy transition by the public and private sectors reached US$755 billion in 2021, including $360 billion in modern renewable energy (more than 50 per cent in solar photovoltaic (PV) energy). The report also recognizes the progress made in hydrogen production by several countries. In spite of the evidence that the energy transition is one of the most critical sustainability transitions for achieving sustainable development, the investments in sustainable energy sources at the global level are then clearly insufficient. Indeed, to limit the rise in global temperatures to 1.5°C by 2050, the report considers that sustainable energy investments need to quadruple in developing countries.

The states are not alone in achieving the Sustainable Development Goals (SDGs) and the Paris Agreement regarding the important role played by the Multilateral Development Banks (MDBs). Despite progress in recent years, through for example, the exclusion of the coal, oil, and gas projects funded by the European Investment Bank (EIB) and IADB, in 2020, except the World Bank Group, all of them failed to meet their climate finance targets to adopt policies that exclude fossil fuel. The World Bank Group has moreover published its updated Climate Change Action Plan for 2021-2025, intended to align all new operations with the Paris Agreement by mid-2023.

Thirdly, the report refers to international trade as an engine for development.

It refers to the framework adopted in December 2021 by members of the World Trade Organisation (WTO) on addressing current and future pandemics from a trade perspective. This framework addresses several issues, such as transparency and monitoring, collaboration with organizations and stakeholders, trade facilitation, regulatory coherence and cooperation, and tariffs. The Covid-19 pandemic has illustrated the inadequacy of existing practices to respond to such crises and therefore makes it necessary to strengthen trade cooperation between different categories of countries for more resilient trade. However, the report shows that the pandemic has positively impacted e-commerce sales, which are expected to reach $4.9 trillion in 2021, a 16.3% increase over 2020.

In addition, the impacts of the pandemic have given states the will to be more organized in the future. In this regard, global trade flows could be affected by regional trade agreements (RTAs) concluded at the regional level. For example, the Regional Comprehensive Economic Partnership (RCEP) between 15 Asia-Pacific countries was concluded in January 2022.

In the Addis Agenda, adopted in 2015, states committed to strengthening the voice of developing countries in international economic decision-making and global economic governance. Although developing country representation in financial institutions has increased significantly in recent years, voting shares have been largely constant, and developed countries continue to hold a "de facto veto" in their decision-making councils through their predominance in most standard-setting bodies. This is, therefore, a major challenge for the coming years.

Fourth, the report addresses technology and innovation issues.

Based on the Addis Agenda, new technologies and digitalization present opportunities to bridge the current gaps in SDG achievement between developed and developing countries. According to the report, policymakers at national and international levels need to mobilize the funding and capacity building required to use these technologies.

The gap between the categories of countries, besides financing, is also present in the digital aspect. Policymakers must ensure universal and affordable access to the Internet. Indeed, in 2021, 4.9 billion people, or 63% of the world's population, are expected to use the internet. Some explanations are given, such as the unaffordability of the smartphone which costs 25% or more of the average monthly income of 2.5 billion people. The pandemic has clearly demonstrated this difference and exacerbated inequalities, according to the Q2 2020 estimation, concerning the workforce able to work from home in high-income countries (27%) compared to low-income countries (13%). A similar finding was made on e-learning, following the closure of schools, as more than 700 million students worldwide do not have access to the internet at home, about 800 million do not have a computer at home, and 56 million students live in areas not covered by a mobile service.

However, the report highlights the progress made in Southeast Asia in promoting digital skills by adopting policy measures to improve the digital literacy of their citizens and the digital skills of their workforce. In this respect, Indonesia has made digital skills and literacy one of the priorities of its G20 presidency in 2022 and has implemented a National Movement for Digital Cyber-Skills Literacy, as well as a scholarship program for digital talent.

Finally, the report refers to debt sustainability and data monitoring.

Given the impacts of the pandemic and conflicts, there is a need to improve the borrowing conditions of developing countries in international financial markets. While the gross public debt of developed countries remained stable between 2012 and 2019, MICs, LDCs and LICs increased by 15 percentage points. In 2021, 9 and 6 percentage points respectively have been added, instead of 18 percentage points for developed countries. Least developed countries (LDCs) and other low-income countries use 14% of their revenue to pay interest on their debt instead of 3.5% for developed countries. Developing countries must be assisted in adopting legal frameworks for debt management, including the definition of public debt and the regulation of debt disclosure statistics, as well as clarification of the borrowing authority. The Common Framework for the treatment of debt beyond the Debt Service Suspension Initiative (DSSI) is, therefore, a significant advancement in international debt architecture.

The international community also urgently needs to address the data challenge, including the effective implementation of the World Bank's Sustainable Finance Policy, the IMF's new Debt Limitation Policy, the G20 Operational Guidelines for Sustainable Finance, and the OECD's Debt Transparency Initiative. All these instruments aim to improve debt transparency.

Despite the importance of data and statistics for monitoring the Sustainable Development Goals (SDGs) as well as for policy making, data and statistical systems are underfunded, and some countries do not provide data on the SDG indicators. Three instruments launched in 2021, the Global Data Facility (GDF), the Berne Network Development Clearinghouse, and the Complex Risk Analysis Fund (CRAF'd), aim to strengthen coordination and mobilize funding on this issue. Within the INFF framework, a national data plan could provide an integrated data system for implementing national sustainable development strategies.

The GDP, which measures economic prosperity, currently seems limited and inadequate as it does not include the dimensions of well-being and environmental sustainability. The measurement of environmental sustainability is carried out by the SEEA ecosystem accounting, adopted by the United Nations Statistical Commission in 2021, which brings together economic and environmental information in a common framework.

In conclusion, the following key global and national lessons can be drawn from this report.

Across the world, there is a clear setback in the implementation of the SDGs due to the recovery of COVID-19 and the consequences of the Ukraine war. While developed countries are borrowing economic recovery funds at lower interest rates, 3 out of 5 developing countries are perceived to be at high risk of debt and have subsequently been forced to cut budgets for education, infrastructure, and other capital expenditures to ensure recovery. To close the recovery gap and anticipate future challenges, including climate change, official development assistance (ODA) providers in developed countries need to increase and meet ODA commitments, particularly for LDCs, with higher grant volumes. Further efforts are also needed with regard to the International Monetary Fund's (IMF) Special Drawing Rights (SDRs) allocations, which reached a new record high this year, as well as with regard to the comprehensive sharing of tax information at the international level to address tax evasion and eliminate illicit financial flows.

The last crisis and the current one, despite their various negative impacts, are nevertheless an opportunity to change or drastically strengthen practices, especially at the national level. Funding is already available but not always well used, and the ability of developing countries to borrow at an affordable cost is mainly a result of this. National action is often lacking, particularly in the areas of good governance, public financial management, and institutional frameworks. In this respect, Integrated National Financial Frameworks (INFFs), which will improve governance and transparency by providing medium-term guidance for public investment decisions, are seen as the ideal way to overcome this divide between developing and developed countries. To effectively implement a plan or strategy, countries also need to improve their data capacity through monitoring and accountability approaches. The gender equality perspective, among current inequalities, must be accompanied by corresponding budgets and policies, as well as the development of an appropriate tax system.

NGO in Special Consultative Status
with the Economic and Social Council of the United Nations
Ref. No: D1035

Jl. Jatipadang Raya Kav.3 No.105 Pasar Minggu, Jakarta Selatan,
12540 021 7819734, 7819735 | office@infid.org | www.infid.org