Financing sustainable development
Addressing vulnerabilities

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Financer le développement durable
Traiter les vulnérabilités

Key themes for UNDP/AFD workshop
Financing the 2030 Agenda in the Least Developed Countries (LDCs):
Diversifying the Financing Tool-Box and Managing Vulnerability
Paris, 7 mars 2016

Origin of the book and relevance for LDCs

- Publication of the book « *Financing Sustainable Development. Addressing Vulnerabilities »/ « Financer le développement durable. Réduire les vulnérabilités »,* initially prepared for the Addis UN Conference on financing development
- Taking place in the Ferdi long standing research on LDCs (see list) with the book *Caught in a trap. Identifying the LDCs,* 2009*,* to be followed by its companion, *Out of the trap. Supporting the LDCs,* forthcoming for Antalya Mid-Term review of IPoA, where related issues are to be discussed in several events, including on finance
- Actually the content of the book *Financing*… is particularly relevant for the LDCs, as poor and vulnerable countries

Vulnerability at the heart of the LDC category

- LDCs designed as poor (low income) countries suffering from structural handicaps to growth (now to sustainable development), identified by a low level of human capital (HAI) and a high structural economic vulnerability (EVI); (history and rationale of the category in *Caught in the trap*, criteria and prospects of graduation in Ferdi papers for the *LDC IV Monitor*)
- Now 1/3 (17/48) of LDCs are no longer low income, but most of them, as well as the recently graduated or graduating ones, are still highly vulnerable
- Thus the FSD book mainly, but not exclusively, concerns the LDCs. But it only concerns financial support measures to LDCs, not trade-related support measures, also very important for LDCs

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The message of the book in a nutshell

- What is at stake is financing a sustainable development, in the three, economic, social and environmental (mainly climatic) dimensions of sustainability,
- Vulnerability threatens the sustainability of development and has itself three corresponding dimensions, economic, social and environmental
- So, financing a sustainable development involves to address the various sources of the three kinds of vulnerability by appropriate methods of finance, in a comprehensive strategy
- Welcome initiative of UNDP/AFD, endorsing this book message, in particular in the concept note, and aims at « diversifying the financing tool-box and managing vulnerability »

Method and structure of the book

- Issues approach rather than a toolkit approach: rather than listing instruments, the book starts from issues to be addressed, asking to a number of well known experts (45), from the North and the South, to expose their view, each one on a specific issue related to financing sustainability (in 25 complementary chapters)
- Book divided in four parts, following an overview of issues and answers
- Part I is a map of finance for sustainable development, taking into account the new sources of finance: from China, from South countries, through triangular cooperation, through the ongoing new role of MDBs, and the competing structures of governance for development finance…
- The 3 other parts are respectively focused on the 3 dimensions of vulnerability, each chapter having its own message: we here only pick up messages from 5 chapters

(I) Debt sustainability when shocks occur involves new flexible rules of debt service (ch 9)

- Flexibility in debt management according to the economic environment has a strong potential to make debt sustainable, and economic growth as well.
- Already implemented by AFD through 'counter-cyclical loans', where the debt service can be postponed in case of export shortfalls
- At the macro level Ugo Panizza suggests to index the debt repayment on GDP, so that the degree of concessionality (which could be 100% if needed, i.e. a pure grant) depends on the economic situation of the country
- A grant would thus be decided *ex post* according to *ex ante* arrangements on debt cancellation rules.

(II) Scaling up private investment in LDCs involves an increasing access to guarantees schemes (ch 14)

- Another way to cover risks, with a high potential for innovation and extension is guarantees that can be made by public entities for investments in countries where the risks are high but where the investment needs are no less
- Guarantees remain an underutilized instrument (5% of ODA mobilized through guarantees in 2014, probably even less for LDCs)
- Their use should be increased when market conditions in developing countries enable them to mobilize additional resources (regulatory framework, reliable payments systems,…)…
- By giving a proper incentive to donors through partial accounting in ODA (on the basis of differentiated discount rates? possibly limited to LDCs?)
- Guarantees for LDCs should be a complement to usual ODA, not substitute

(III) sustainable agricultural development involves appropriate schemes of credit and insurance for the poor (ch 16)

- Agricultural development in LDCs, where the share of agricultural value in GDP remains high, is strongly constrained by the climatic instabilities (as well as market instabilities) faced by poor farmers
- Innovative finance, through insurance, credit or savings, are available, the feasability of which has recently be tested and evidenced , as well as the conditions of success (examined by A. de Janvry & E.Sadoulet, from results of Ferdi workshops they organized)
- Effectiveness and sustainability of the domestic instruments may be reinforced by international subsidizing or reinsurance

(IV) Financial deepening is essential for reducing poverty (ch 17)

- More generally, private secure savings is a powerful means for allowing poor people to face risks and also invest in productive activities, even more than private credit to which access is limited, (« conduct effect » revisited),
- Access to credit will come afterwards
- Private savings of the poor may be increased by the development of banking infrastructure
- Now made easier by electronic transactions and mobile banking

(V) impact investment is needed to make small entrepreneurship sustainable (ch 20)

- Impact investment (or « investissement de mission ») combines a minimum financial return with significant social effects and externalities
- It allows small entrepreneurs to develop their activities in the formal sector and to do so durably (by reinforcing local capacities, access to credit, housing, health services, and extending formal employment,…)
- Needs to mobilize backward sources of private finance motivated not only by financial return
- Opening the way of a new development model

Many other messages on how finance can make development sustainable, for instance…

- How to boost domestic savings (ch10)
- How financing regional integration can reduce economic vulnerability (13)
- How can donors help diversifying the economies of fragile states (ch 15)
- How aid for trade can be used as a finance for the poor (ch 18)
- How pooling the risks can generate a global compact for sustainable health financing (ch 19)
- What are the principles of a sustainable mining taxation (ch 24)
- How new international resources (SDRs) can be mobilized for financing energy transition in developing countries (ch22)
- Etc…

A global approach, with pending other issues

- Many answers (and questions too) in a global framework
- With the view that there is not a general or common answer, but a need of a strategy to address vulnerabilities, the set of answers depending on the structures and policy choices of the countries
- All financial issues related to vulnerability are not examined in depth in the FSD book, but in other Ferdi works, in particular the *volume* of public finance and its a*llocation* between countries

- (The volume of development finance available for LDCs is an important issue, with the recent decrease of ODA to LDCs, deviating from official targets, with no clear future impact of the new definition of ODA
- Important to see what the new TOSSD concept will involve for LDCs)

Taking into account vulnerability in the allocation of public concessional resources between countries is a part of the strategy

- Important matter of discussion for multilateral assistance
- Ferdi proposal: LDCs identification criteria, because they refer to poverty and structural handicaps to development, in particular vulnerability (EVI), are logical criteria for aid allocation
- Reflected in the UNGA resolution 67/221 on « smooth transition » of graduating LDCs (and in EC new EDF and DCI)
- Dampens possible decrease in ODA received by an LDC after its graduation
- Channels ODA towards the LDCs, not only as a whole, but also towards the least developed ones, and the other most vulnerable
- What is valid for ODA allocation is even more so for the allocation of concessional resources for adaptation…

- …taking into account the vulnerability to climate change in the allocation of concessional resources for adaptation is fully legitimate
- will help to make poverty reduction finance and climate finance consistent
- Here the vulnerability considered should be a physical, exogeneous, vulnerability to climate change, measured by an appropriate index, other than EVI
- Would supplement the (limited) principle of 50% of the Green Fund for LDCs and vulnerable countries
- LDCs, on average highly vulnerable to climate change, and would benefit from this allocation, without substitution to ODA
- Whatever the fungibility in the use of resources