FONDATION POUR LES ÉTUDES ET RECHERCHES SUR LE DÉVELOPPEMENT INTERNATIONAL

LA FERDI EST UNE FONDATION RECONNUE D'UTILITÉ PUBLIQUE.
CETTE PUBLICATION A BÉNÉFICIÉ D'UNE AIDE DE L'ÉTAT FRANCAIS AU TITRE
DU PLAN D'INVESTISSEMENT FRANCE 2030 PORTANT LA RÉFÉRENCE ANR-16-IDEX-0001.

CHAIR
International Architecture
of Development Finance

Monitoring Development Financing: a First Assessment of the 2018 Reform One More Effort?

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The reform of official development assistance (ODA) accounting implemented from 2018, combined with the creation of Total Official Support for Sustainable Development (TOSSD), represents a substantial improvement in the monitoring of development financing. In some respects, however, it remains in the middle of the road, and there is still room for improvement.

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A Necessary Reform of ODA Accounting to Measure Donors' Efforts More Rigorously

A concept developed to monitor the quantified ODA financing target established by the UNGA (0.7% of GNI) aimed at measuring donor efforts

The concept of Official Development Assistance (ODA) is 55 years old. It was born in 1969, when the OECD's Development Assistance Committee (DAC) first proposed a definition and method of accounting for ODA. This "first" was in response to a request from the United Nations General Assembly (UNGA), which wanted to set a quantified target for the international solidarity efforts of the industrialised countries, to support the development of the many countries then trapped in the "poverty trap". The emblematic target of 0.7% of gross national income (GNI) to be devoted to ODA was endorsed by the UNGA in 1971.

This definition has changed little since then. ODA is still defined as ***"all resource flows provided to countries and territories on the list of ODA recipient countries, or to multilateral institutions, which meet the following criteria:***

- ***Official aid, i.e., aid from public bodies, including national and regional governments, or bodies acting on their behalf;***
- ***Financing operations that must also: 1) have as their primary purpose the promotion of economic development and the improvement of the standard of living in developing countries and 2) be on favourable terms and include an element of concessionality[1]."***

Originally, this effort of liberalization was to be at least equal to 25% (based on a discount rate of 10%), the same rate regardless the recipient country's income level.

A concept refined over time...

Over the years, the scope of aid has been clarified, in particular by : 1) the exclusion of military aid, with a few exceptions (cost of using armed forces to deliver humanitarian aid, training or advice for security forces on respect for human rights, training for internal security and civil protection forces, peacekeeping operations up to 15%); 2) by including expenditure on civil nuclear energy, cultural development, expenditure on hosting refugees or students from developing countries, administrative expenditure on aid management, and debt cancellation operations.

This ODA monitoring system is supplemented by a limited list of eligible countries, defined by reference to a GNI per capita ceiling (currently USD 12,695). It provides for a graduation system (exclusion from the list) when er capita income exceeds this ceiling for three successive years. In 2023, the list comprised 141 countries, including 46 least developed countries (LDCs), 2 non-LDC low-income countries (LICs) and 93 middle-income countries (MICs), including 57 upper-middle-income countries (UMICs).

... but there are shortcomings due to a method of accounting for loans that includes capital and is based on a discount rate that is very generous to donors

However, this metric had a number of shortcomings that needed to be corrected: firstly, since its inception, ODA has mixed grants and concessional loans, with the latter's capital accounted for. Because of a very generous discount rate (a fixed rate of 10%), and the downward trend in rates over the last decade, the system made it difficult, even tendentious, to compare the efforts of donors, by giving an advantage to those who allocated a lot of loans, at little or no cost to the budget. Furthermore, since it was calculated on a net basis (gross ODA disbursements

1. Source: OECD: https://www.oecd.org/fr/topics/sub-issues/oda-eligibility-and-conditions/official-development-assistance--definition-and-coverage.html

in year N being reduced by repayments of loans granted in the past and reaching maturity), this method of accounting made ODA illegible, since the volume in year N could be profoundly altered by capital repayments on loans granted, sometimes decades earlier, as a result of longer grace periods. As a result, it could have a disincentive effect, with today's governments being held accountable for decisions sometimes taken by distant predecessors. Finally, as in the case of France, it could lead to serious distortions in the geographical and sectoral allocation of aid: because of the existing pressure on the overall volume of ODA, it could lead to a preference for concessional loans (because of their low short-term budgetary cost), allocated in preference to middle-income countries and productive sectors, to the detriment of subsidies generally targeted at low-income countries and/or social sectors. This has had an impact, for example, on France's significant drop in the rankings of the main donors to the Sahelian countries, all of which are LDCs, to the benefit of a sharp rise in French ODA to middle-income countries in Asia.

The first objective of the reform introduced in 2018 was to improve the reliability of the measurement of donors' national efforts by refocusing ODA on the grant equivalent, as close as possible to donors' budgetary efforts. It was also intended to encourage better targeting of ODA on poor countries, where its marginal effectiveness is highest due to the structural development handicaps of these countries, which are largely excluded from access to financial markets.

From 2018, for loans, only the grant equivalent is taken into account in calculating ODA for the year of disbursement. Conversely, when the principal of the loan is repaid, this flow is no longer deducted from the donor's net ODA.

In addition, the grant equivalent [2] is now assessed differently depending on the level of development of the recipient country: the grant element must be at least 45% for bilateral loans to LICs (with a 9% discount rate), 15% for lower middle-income countries (LMICs) (with a 7% discount rate) and at least 10% for LMICs (with a 6% discount rate).

While the use of the grant equivalent represents real progress, the reform of the accounting of concessional loans in ODA has remained imperfect by retaining the reference to a fixed reference cost for all donors, even though they do not all borrow at the same rate. As a result, this method loses its relevance by moving away from a real measure of each donor's efforts.

Proposition 1

Change the method for valuing ODA loans by indexing the reference cost of the resource to the effective market rate paid by the donor country at intervals to be determined (every year or every three years)..

The Creation of an Indicator to Measure Development Financing: the TOSSD

ODA was introduced to provide the international community with an indicator for measuring the efforts of donor countries in relation to their GDP, in line with the UNGA target of 0.7% of GNI. However, it has never been a reliable indicator for measuring development financing, due to its many limitations: restricted essentially to DAC member countries, it excludes by definition all non-concessional financing (loans, equity investments, guarantee mechanisms, etc.) and all financing allocated by non-DAC member countries, particularly through South-South co-

2. The grant element of a loan is calculated as the difference between the face value of the loan (or nominal value on the day it is disbursed) and the sum of all payments to be made by the borrower, discounted to the value on the day of disbursement.

operation. ***The 2018 reform therefore pursued a second objective, namely the creation, alongside ODA, of a new indicator to measure total public financing for sustainable development, the TOSSD.***

Measuring all sustainable development financing, including GPG financing

Tracked since the 2019 data, the TOSSD breaks down into two main pillars, supplemented by a specific category of financing. The first pillar records cross-border development financing allocated to developing countries on the DAC list, whether concessional or not, by donor countries or international organisations (IOs) through North-South, South-South or triangular cooperation. The second pillar aims to monitor financing allocated to global or regional public goods (GPGs or RPGs) and to IOs, whether concessional or not, including without cross-border flows. Finally, a third series of flows is tracked, as in the case of ODA: private financing flows mobilised with the support of public instruments. They are isolated in a third category, outside the two pillars, for the sake of transparency.

This new indicator offers a number of advantages in terms of ODA, in particular:

- ***Greater comprehensiveness:*** 1) by seeking to identify as many donors as possible, well beyond the traditional DAC member donors (while there are 32 DAC member countries, 56 countries and territories, more than 65 IOs provided declarations for the last report published on the TOSSD, including Brazil, Indonesia, Chile, Costa Rica, Peru, Thailand, etc.); 2) by understanding South-South cooperation flows, and; 3) by collating data relating to all public financing, whether concessional or not.

- ***A willingness to value the perspective of recipient countries:*** for example, through the rule of valuing contributions in kind at the price of recipient countries (and not at the actual cost borne by the donor as in ODA) or the measurement of multilateral contributions in terms of actual payments by IOs (and no longer, as in ODA, by measuring the relative contributions of donors to these IOs). In the same vein, the declared intention (decision of May 2024) to introduce, in the long term, a system for declaring funding received at the level of recipient countries, enabling reconciliation with donor declarations, would be a significant step forward in further strengthening this consideration of the perspective of recipient countries.

- ***The aim is to eventually include vulnerability in the eligibility criteria:*** the aim is to draw up a list of countries eligible for TOSSD that would differ from the DAC list, which focuses on per capita income alone, by including a vulnerability criterion in addition to this per capita income (decision taken at the last Oslo meeting in May 2024)..

Strengthening the credibility and impact of TOSSD

Despite the significant progress made in improving the monitoring of development funding, the TOSSD has one major drawback. When Pillar 2 was subdivided, it was decided to create a Pillar 2B to record funding for GPGs that does not result in a cross-border flow: in addition to traditional expenditure already included in ODA (hosting refugees or students from developing countries on the territory of the donor country), national expenditure has been added, notably in favour of the climate: efforts made to preserve forests located on national territory, subsidies for the purchase of electric vehicles, etc. While this spending undoubtedly contributes to the decarbonisation of economies and to overall mitigation efforts, it represents a dangerous departure from spending dedicated to financing economic growth or improving living conditions for populations in developing countries. This risks creating confusion and undermining confidence in the indicator, which is the opposite of the desired objective, even if we understand the desire to stick as closely as possible to the 2030 Agenda and the Sustainable Development Goals (SDGs).

Faced with this dilemma, ***our proposal would be to revise the criterion for differentiating the two pillars according not to the existence of a cross-border flow, but exclusively to the purpose of the financing***. Pillar 1 would therefore include all financing intended to help economic development or improve living conditions in developing countries, including non-concessional financing or financing carried out on the territory of the donor country (hosting refugees or students from developing countries, financing dedicated research into tropical agriculture, for example). Pillar 2, on the other hand, would list all funding allocated as a priority to the preservation of a global or regional public good, irrespective of whether it is located in a donor country or in a developing country. Thus, in the fight against global warming, all mitigation programmes aimed primarily at reducing greenhouse gas emissions would be included in this second pillar, even when they are carried out in a developing country. Indeed, the primary purpose of a mitigation project is not the development of the country where it is carried out, but to contribute to the global effort to mitigate global warming. This is the very reason why mitigation projects are largely carried out in middle-income countries, where their marginal effectiveness is at its highest: according to the latest OECD report, 70% of public climate finance from donor countries allocated to developing countries would be concentrated on MICs in 2022, with FRPs mobilising only 10% of this climate finance. Over 60% of climate finance is still targeted at mitigation programmes, with adaptation projects accounting for only 28% of funding, despite an increase in recent years.

Proposition 2

Review the categorisation of the TOSSD pillars on the basis of the criterion of the purpose of the financing, so as to concentrate in pillar 1 all financing allocated to the development of developing countries, and in pillar 2 all expenditure on financing GPGs and BPRs, regardless of their location, and in particular all expenditure on mitigation in the fight against global warming.

This concentration of climate finance on MICs can only reinforce the fears of poor countries that development finance will eventually be diverted to finance GPGs, and in particular climate, which now dominates the international agenda. This is the whole issue of the supposed additionality of climate finance, which has been constantly called for by low-income countries since the beginning of the climate COPs, and recognised as an intangible principle in all the COPs, in particular the 2015 Paris Climate Agreement. This commitment is fundamental, as it is a prerequisite for low-income countries and Small Island Developing States (SIDS) to adhere to international climate commitments.

The clarification proposed above in the definition of pillars 1 and 2 of the TOSDD would allow a first step forward in the monitoring of this emblematic commitment, by proposing a clear demarcation between the financing allocated to the development of poor countries in the strict sense, and the financing of GPGs benefiting all. However, this is not enough to guarantee adequate financing for development. Measuring additionality is a challenge that appears to be methodologically difficult[3], so we believe that

3. To date, there is no objective, approved method for measuring this additionality. The challenges are indeed, how to make a real distinction between a development project development project and a climate change adaptation project? What ODA benchmark should be used to measure additionality: the 0.7% target achieved by only 5 donors? The level of ODA in 1992, 2009 or 2015? How can we calculate the extra cost of a development project generated by the use of a low-carbon technology, compared

the solution today lies in setting ambitious development funding targets, which demonstrate the international community's determination not to sacrifice this ambition (for the development of poor countries) on the altar of the new climate priority. Indeed, the momentum of the climate negotiations should lead to the establishment of a new quantified climate financing target at the next COP, in December 2024. To ensure that this commitment is not made at the expense of development, we believe it is essential to balance it by setting new commitments on development financing.

Given the data presented above on the distribution of climate finance, showing the very small share allocated to LICs (a category which today largely overlaps with that of LDCs, with the exception of two countries), a first proposal would be to reassess the commitment made by donor countries to devote 0.15% of ODA to LDCs. This commitment could be raised to 0.25% of GNI. This change seems all the more justified given that it is precisely in these countries that ODA has the highest marginal effectiveness, given the low level of savings available in these countries and their major difficulties in accessing financial markets and foreign direct investment.

Proposition 3

Raise the commitment to devote 0.15% of ODA to LDCs to 0.25% of donor's countries GNI.

A second proposal would be to set an agreed target for financing development (pillar 1 of the revised TOSSD) for all countries submitting declarations. Such a commitment would give concrete expression to the desire of all countries to contribute to the reduction of international income inequalities, according to their capacities, and thus establish the idea of a general, but differentiated, contribution to the development of poor countries.

Proposition 4

Propose a quantified development financing target for pillar 1 of the TOSSD, defined a priori in relation to the GNI of countries.

These two proposals could usefully be presented by France and/or the European Union at the next United Nations Conference on Financing for Development.

with the cost of the same project using traditional processes? Is this latter method relevant at a time when the international community has been committed to a sustainable development agenda for the past decade?

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n° ISSN : 2275-5055

Publication director: Patrick Guillaumont

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