Increasing affordable and long-term financing: the role of effective development cooperation

Expert Group Meeting on Economic and Social Survey of Asia and the Pacific 2024

Session 1

31 October 2023

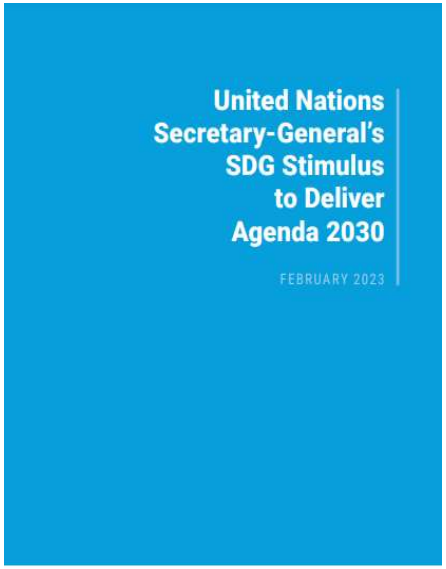
Lin Zhuo

Macroeconomic Policy and Financing for Development Division

ESCAP
Economic and Social Commission for Asia and the Pacific

Context

- High public debt level
- Tightening global financing environment
- High risk of debt distress
- Huge development financing gap
- Increasing access to affordable, long-term financing for the SDGs cannot be achieved solely through domestic policy actions
- Strong and effective **international development cooperation** is indispensable



United Nations

- Address rising debt servicing costs
- Scale up affordable long-term development financing
- Expand contingency financing

Objectives: Increasing affordable and long-term financing

A new set of metrics to be used by the international community

Going Beyond GDP Metrics

Propose a new set of metrics that extend beyond the traditional GDP and national income levels to be used by the international community in determining both the provision and allocation of concessional development financing in the form of grants, loans and debt relief

What can the two important actors, MDBs and CRAs do to help bridge the financing gap?

Unleash MDBs' potential to leverage from "billions to trillions"

Drawn from the recent G20 Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks, Chapter 4 explores practical solutions to address the underutilized potential of MDBs in supporting the SDGs.

Credit Rating Reforms

Suggest policy options to address structural limitations of CRAs

Going Beyond GDP Metrics

GDP does not adequately capture development needs in the SDGs era

Traditional metrics

- The calculation of ODA commitments are linked to gross national income (GNI) per capita
- Access to development financing including access to ODA through concessional finance windows, as well as the cost of capital, from multilateral development banks is generally linked to GNI per capita
- While decisions on allocation of bilateral ODA are more often made based on strategic development priorities, the interest charges are still tied to recipient countries' GNI per capita

Fill the gap

- GDP fails to capture the human and environmental destruction of some economic activities
- GDP growth does not necessarily mean an increase in living standards

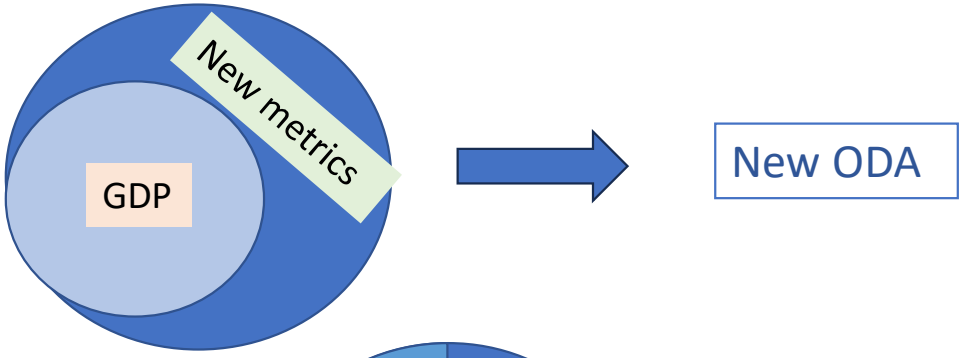
New measurements

- Multi-dimensional Structural Vulnerability Index
- System of Environmental-Economic Accounting (SEEA)
- Historical and current CO2 emissions
- Historical and current levels of natural resource use
- Offshoring of production with potentially large environmental damage
- Pros and cons of using each proposed indicator, data availability, weight given to each indicator will be discussed

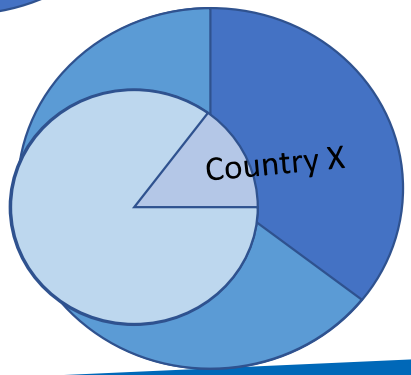
This new set of metrics can be applied in at least three areas

Provision of ODA	Allocation of development financing	Debt Sustainability Analysis

- The use of beyond-GDP/GNI measures may affect the size of total ODA commitments



- ODA targets or commitments for some major donor countries may be changed based on alternative measures

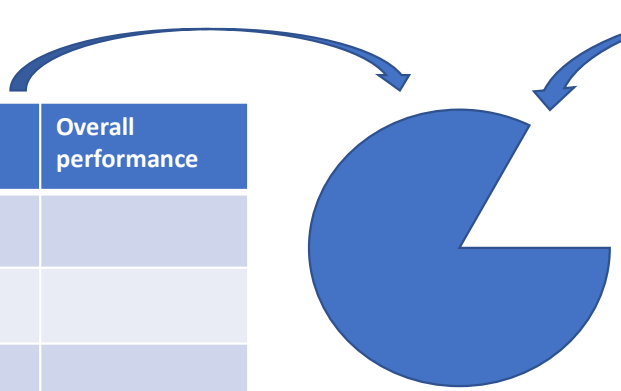


This new set of metrics can be applied in at least three areas

Provision of ODA	Allocation of development financing	Debt Sustainability Analysis

- Development financing includes grants, (concessional) loans and public debt relief
- The proposed alternative measures ,whether individually or multiple indicators at once, would affect the size of concessional financing received and the debt servicing costs borne by different Asia-Pacific countries

	Indicator A * Weight a	Indicator B * Weight b	Indicator X Weight x	Overall performance
Country X	…	…	…	
Country Y	…..			
…….	……..			



Indicator X	Interest rate
Value between a and b	…
Value between	……..

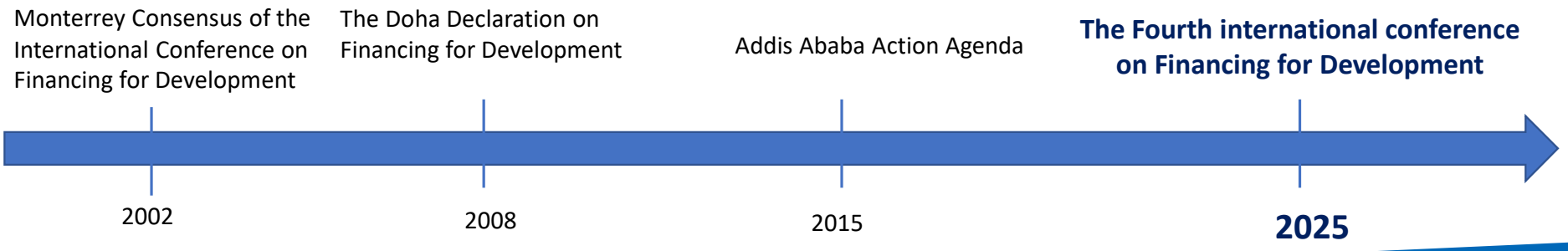
This new set of metrics can be applied in at least three areas

Provision of ODA	Allocation of development financing	Debt Sustainability Analysis

- Public debt/**GDP** ratio, what if the denominator is not GDP but SDG adjusted GDP, for instance, carbon emission adjusted GDP?
- Some countries with high public debt to GDP ratio might be adjusted down and move from high risk to medium risk
- The reclassification/lower of risk will lower cost of financing for a given country
- Beyond-GDP measures in stress test scenarios? e.g. economic growth rates that are adjusted for natural resource.

And change how international financial institutions and donor countries allocate development funds and provide public debt relief

- A paradigm shift is needed, primarily relying on GDP as a metric of progress does not respond anymore to our world and the challenges it faces - which are multi-dimension.
- Strong political commitment is required to develop an alternative framework that informs how decisions around provision and allocations of concessional finance are made.
- Now is the time to seek the political momentum ahead of the next international conference on financing for development.



ESCAP
Economic and Social Commission for Asia and the Pacific

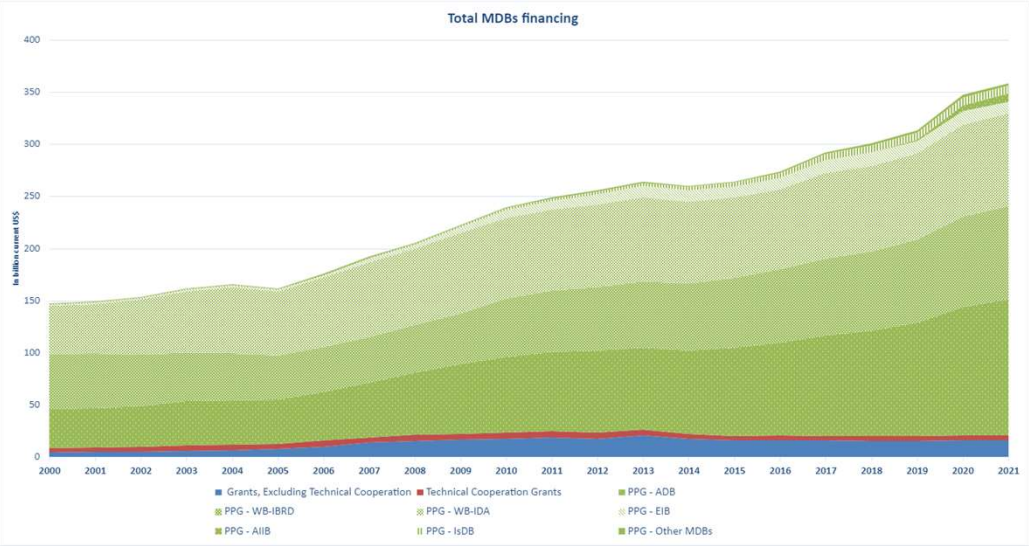
Questions

- Overall structure of the new metrics, how can sustainable and green development be integrated?
- Use cases of the new metrics
- Selection of indicators
- Expected difficulties at the operational level and possible solutions

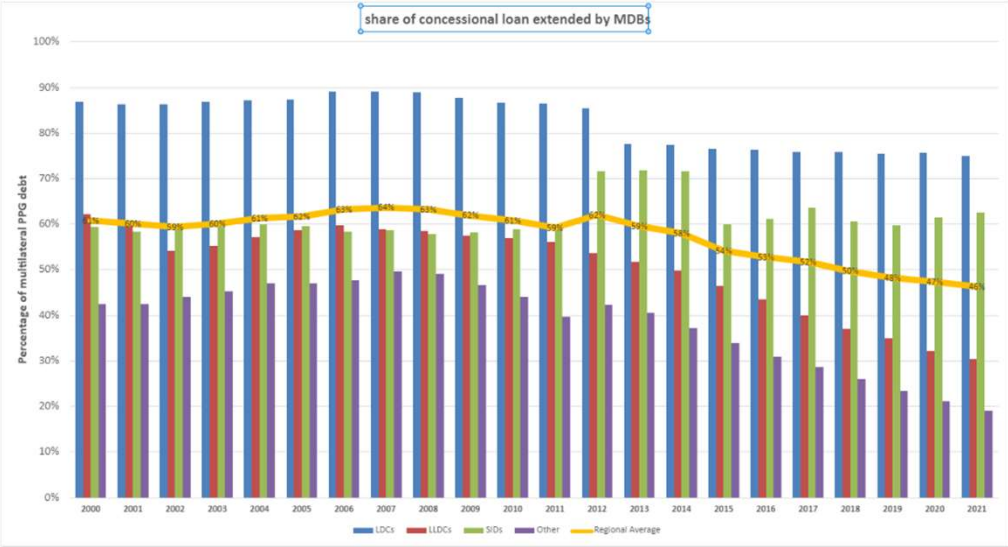
Unleash MDBs' potential to leverage from "billions to trillions"

MDBs' lending is insufficient to support SDGs and the proportion of concessional loans has been gradually declining.

The largest share of financing provided by the MDBs to developing Asia and the Pacific economies are in the form of grants and loans



The share of concessional loans owed to multilateral creditors has exhibited a gradual decrease from 62% since the year 2012 to 46% in 2021



ESCAP
Economic and Social Commission for Asia and the Pacific

Policy recommendation 1: Boost MDBs' lending capacities

Optimize MDBs Balance Sheet

- Integrate callable capital in Capital Adequacy Frameworks
- Reduce excessive reliance on CRAs in setting risk appetite
- Improve CRA rating methodologies on MDB credit rating
- Improve Capital Adequacy governance
- Adopt operational and financial innovations

  e.g. merge of concessional window and non-concessional equity, risk transfer instruments, MDB SDR hybrid capital

Raise more equity capital from shareholders

Policy recommendation 2: Improve MDBs' lending terms

- Lower interest rates and longer term of maturities
- Revise concessional lending criteria
- Adapt policy conditionalities to development needs
- Increase MDB lending in local currency
- Reduce administrative burdens
- Design new products to meet clients' needs

Policy recommendation 3: Strengthen MDBs systemic coordination

- Establish a governance framework that periodically performs a MDB system-wide review
- Share common standards and benchmarks for project preparation
- Enhance co-financing structures that unlock investments at scale
- Deepen country-level collaboration
- Promote regional development bank complementarity
- …

A joint statement by the heads of MDBs highlighting the collective role all MDBs need to play and committed to strengthen their collaboration



Questions

- What's your view on the G20 Independent Review of Multilateral Development Banks' Capital Adequacy Frameworks? How much progress have most MDBs (and AIIB) made in following the advice from the Review? How does MDB as a system plan to work together?

- In terms of raising more equity capital from shareholders possible, what is the major obstacle? Is it the fiscal constraints of shareholders or the fear of losing voting power? What are the possible solutions?

- What are the current allocation formula? What are the factors used to reward performing countries in the allocation? What are the difficulties in using the proposed new metrics in deciding concessional lending?

- Many MDBs are committed in providing loans in local currency but available data shows share of USD lending MDBs is increasing to Asia Pacific countries. Why and what can be done more?

- What do you think ADB and the AIIB should and can do to promote cooperation, develop complementary portfolios in terms of sectoral exposure and geographical coverage?

Credit Rating Reforms

A sovereign credit rating is vital for issuing debt securities and it influences both perceived risks and borrowing costs of a given country.

- Credit ratings encourage financial sector development and are crucial in attracting investors.
- A downgrade in credit rating does not only increase the cost of borrowing but also limits access to international capital markets.



Many challenges related to developing country sovereign credit ratings are not new but few of the structural reforms were implemented. Strong commitments from the international community are required.

Current critiques

- Lack of transparency
- Overestimating risks in developing countries
- Short-termism
- Procyclicality
- Perceived bias toward government interventions
- Uncompetitive market structure

Policy Recommendations

- Enhance transparency
- Incorporate ESG metrics and adopt a longer-term approach based on economic fundamentals
- Reduce mechanistic reliance on credit ratings
- Increase dialogues between governments and CRAs
- Boost competition – a regional CRA? a public CRA?

Questions

- Alternative tools to external credit ratings
- Feasibility of the establishment of an Asian CRA for the assessment of sovereign debt
- Application of the UNDP report to the context of Asia and the Pacific

Next steps

November – January

- Incorporate feedback received today
- Fill the incomplete sections and revise the complete sections
- Ensure coherence of the overall chapter, sharpening the messages



February

- Send the draft to the Editorial Board

Early April

- Launch of the report

April to June

- Outreach: Subregional and country-level policy dialogues

THANK YOU

Follow us:


unescap


unitednationsescap


www.unescap.org


unescap


unescap


united-nations-escap



ESCAP

Economic and Social Commission
for Asia and the Pacific