Highlights of the outcomes of the 4th High-level Dialogue on Financing for Development in Asia and the Pacific

Statement by the Chair, Hon Ravi Karunanayake, Minister of Finance of Sri Lanka

1. The Fourth High-Level Dialogue on Financing for Development in Asia and the Pacific, held in Bangkok, Thailand, on 28 and 29 April 2017, was co-hosted by the Economic and Social Commission for Asia and the Pacific (ESCAP) and the Ministry of Finance of Sri Lanka. Ministers and senior government officials from 37 countries, together with experts and representatives of international organizations, other organizations in the United Nations system, and eminent experts attended the Dialogue.

2. The participants highlighted the central role of tax policy and public expenditure management in effectively pursuing the 2030 Agenda for Sustainable Development. Key priorities should include strengthening tax systems and administration; increasing the effectiveness and efficiency of public expenditure; deploying tax policies to mitigate inequalities and promote environmental sustainability; strengthening municipal finance to cope growing urbanisation challenges, including those related to environment; and tackling harmful tax competition, base erosion, profit shifting and other tax avoidance by building broad international and regional partnerships.

3. The participants highlighted the importance of a strong collective response to address tax challenges of the region in view of the 2030 Agenda. In this regard, they emphasized the need for a broad-based discussion among policy makers, tax administrators, and relevant regional and subregional organizations in the Asia-Pacific region. Particularly, they highlighted the potential of ESCAP to leverage its intergovernmental mechanisms and existing platforms, in close collaboration with development partners, to facilitate such discussions. The participants also pointed out the importance of facilitating the exchange of knowledge and policy lessons and experiences, and coordinating capacity building initiatives in areas such as:

    - Tax and public expenditure policies for inclusive and sustainable development;
    - International tax reforms and their implications for developing countries in the region;
    - Specific local challenges such as municipal public finance for urbanization; and
    - Cross-cutting issues such as social contracts for responsible and efficient public spending and taxpayer consent for sustainable revenue mobilization.

4. Noting that public resources alone will be insufficient to meet the region's significant infrastructure development needs, the participants underscored that mobilizing private financing through public-private partnerships (PPPs) and by deepening and integrating capital markets is essential to increase financing for sustainable and resilient infrastructure. Measures should include innovative financial products, such as climate bonds, credit enhancement mechanisms, catastrophic insurance schemes and currency/interest rate risk hedging instruments, as well as reform of financial regulation.

5. Participants recognized the support provided by ESCAP and its expertise in building PPP capacity and creating enabling PPP environments and noted a proposal inviting ESCAP to lead an Asia-Pacific PPP Unit network to promote sharing of PPP country experiences. They also noted the need to incorporate sustainability considerations into various PPP schemes. Participants also emphasized the

need to improve selection, allocate sufficient resources to preparation and streamline delivery of infrastructure projects in order to do more with less. Likewise they underlined the importance of proper asset management in order to preserve the value of existing assets and the possibility of recycling existing assets to finance new ones.

6. The participants recognized the importance of greater financial inclusion and noted that this requires a well-designed financial regulatory framework which balances the objectives of increasing access to finance and maintaining financial stability. In that regard, they highlighted the need for capacity building in setting and implementing new regulations for promoting financial inclusion, for which ESCAP, as an intergovernmental platform covering the entire region, could play an important role.

7. Participants noted that ESCAP could examine how countries may further develop and deepen national capital markets for sustainable and resilient infrastructure financing, and create mechanisms to integrate national capital markets across countries while preserving financial stability.

8. The participants recognized that these issues could be further explored by the ESCAP Secretariat through its intergovernmental meetings, particularly the forthcoming meeting of the Committee on Macroeconomic Policy, Poverty Reduction and Financing for Development, scheduled for November 2017.

9. During the deliberations, the participants discussed in detail the following financing for development issues that are particularly relevant as means of implementation of the 2030 Agenda in the Asia-Pacific region.

Enhancing role of public finance for sustainable development

10. The participants highlighted the central role of public finance for an effective pursuit of the 2030 Agenda for Sustainable Development and called for the prioritization of public resource mobilization, along with public finance reforms and effectiveness and efficiency of public expenditure as key pillars of the Asia-Pacific region’s implementation strategy. In particular, the participants pointed out that the developing Asia-Pacific region has one of the world’s lowest tax-to-GDP ratios, averaging 17.6% of GDP compared to the global developing country average of 21.3% and OECD countries average of 26.4% excluding social contributions. The participants noted, however, that the tax-to-GDP ratio should not be taken as the absolute indicator of public finance performance.

11. The participants observed that for a number of countries with close-to-single-digit tax-to-GDP ratios, the revenue gap as compared to the needs of the 2030 Agenda is significant, and therefore it is important to increase compliance and broaden the tax base by reducing tax exemptions and the size of the informal economy. Participants also noted the importance of improving the effectiveness of tax administrations for this purpose.

12. The participants identified financing for sustainable urbanization as a primary challenge for many developing countries of the region. They advocated comprehensive but prudent reforms to rationalize the fiscal governance regime of large metropolitan areas and mega cities, consolidate

fiscal positions of municipal governments, and explore a diversified mix of revenue sources and policy tools, such as property tax to realize the full potential of Asia-Pacific cities.

13. Emphasizing the importance of rethinking and recalibrating tax and public expenditure policies in view of the new principles and demands articulated in the 2030 Agenda, the participants called for proactive efforts to better leverage these policies to address the region's growing income and wealth gaps and environmental concerns. They also highlighted the need for taxes to be considered fair and that tax revenues are efficiently and transparently allocated to socially and environmentally desirable spending.

14. The participants noted that in an increasingly interlinked world, impacts of tax policies and practices transcend national borders. This requires tax coordination across countries. The participants expressed concerns regarding intensification of tax competition in the region. Pointing to the potential flaws of a one-size-fit-all approach to tax incentives and related policies, participants suggested that policy diagnosis and recommendations take into account developing country contexts, such as capacity constraints in cost-benefit evaluation of tax incentives and the presence of large informal sectors.

15. The participants discussed current reforms of international tax policies at the global level and their implications for domestic tax policy making. They welcomed global efforts to protect tax bases of developing countries, but advocated greater capacity support for Asia-Pacific developing countries to effectively engage in these processes.

16. The participants emphasized the need for a strong collective response to base erosion and profit shifting and the risk of harmful regional tax competition. In this regard, participants called for regional organizations to collaborate with existing regional tax cooperation mechanisms and specialized stakeholders, such as ADB, IMF and OECD, to facilitate broad-based regional discussion for knowledge exchange, policy coordination and capacity development on tax matters. In this regard, participants highlighted the important role of the intergovernmental mechanisms and existing platforms of ESCAP.

Engaging the Private Sector for Infrastructure Development

17. The participants noted that many countries in the region are in the process of developing legal, regulatory and institutional frameworks for PPP and called for an effective use of existing mechanisms and tools to better support countries in these efforts. In this regard, they highlighted the importance of political support at the highest level for the success of a PPP programme. They also recognized the importance of promoting exchange of PPP best practices among countries at different stages of development, and recognized the work of ESCAP in this regard.

18. The participants stressed that a key bottleneck for the growth of PPP in the region is a lack of capacity in governments, which runs the risk of unfeasible projects being pursued along with inappropriate risk and reward allocation. Continued work in this area is thus essential and the participants welcomed the valuable support provided by ESCAP in this area. They also applauded the collaborative approach among development partners.

19. The participants noted that implementing PPP projects at a multi-country level is a complex endeavor. By having more than one country involved, cross-border projects face augmented

challenges, in particular for countries where domestic private sector development is limited. To address these challenges, the participants discussed different policy options and recognized that regional platforms should be further leveraged to facilitate cross-border project identification, reduce political risks, promote good governance and explore possible financing mechanisms. Regarding financing mechanisms, the participants noted that hybrid models, which blend public and private finance, can offer a solution to projects not fully viable on commercial terms. They also indicated that fiscal risks of PPP projects should be carefully monitored.

20. The participants discussed the importance of expanding the use of PPP beyond transport and energy infrastructure to include social infrastructure, such as schools and hospitals. They highlighted the need for consultations among all relevant stakeholders to ensure that infrastructure development is inclusive and sustainable.

Building resilient and sustainable infrastructure

21. Participants highlighted that public and private finance must be scaled-up significantly across the region from present levels in order to build resilient and sustainable infrastructure. This is important as having such infrastructure will ultimately reduce the costs of asset maintenance and the costs of disaster impact while meeting long-term demand. For this reason, investors are increasingly taking the view that sustainable infrastructure investments are sound investments.

22. Participants highlighted that financial regulation will play an important role to ease the risks for private investors and overcome the major challenges for the financial system to unlock private finance for sustainable and resilient infrastructure investment. Supporting the formation of long-term pools of risk capital and enhancing financial innovation, are important elements to achieve the scale-up.

23. Participants observed that green bonds for sustainable infrastructure have potential to further tap institutional wealth. However, investors still require adequate returns that reflect the risks involved. Sustainable infrastructure finance can also be enhanced through mandated commercial bank portfolio targets, de-risking or other voluntary measures. To unlock cross-border capital flows for infrastructure investment, regional financing facilities can be considered to achieve economies of scale and build integration dividends.

24. In view of the limited financial resources currently available for infrastructure development, participants stressed that the focus should be on development outcomes of infrastructure plans. Governments should therefore prioritize investment that has the largest development impact across all three pillars of sustainable development using robust measurement and evaluation systems. They should also ensure that sufficient resources are allocated to the maintenance of infrastructure in order to preserve the value of the asset. Efforts should be made to support developing countries in building practical tools to conduct analyses that incorporate the three dimensions of sustainable development and quantify positive and negative externalities. Effectively engaging multiple relevant stakeholders in consultations for both the selection of new projects and for the monitoring and evaluation of existing projects will be necessary as well. In addition, price signals can be used to spread asset use more evenly (i.e. reduce peak demand) as this would reduce the need for additional capital investment.

25. Participants highlighted the need to enhance financial innovation, for example, to find innovative ways to scale-up investment for sustainable infrastructure, to develop private sector credit enhancement instruments, or to make better use of impact investment. They also noted the importance of PPP project risk management through innovative financial products, such as hedging instruments to address currency and interest rate risks. Participants noted the role of ESCAP to collect and share examples of good practice and to identify and address the capacity gaps in least developed countries and Small Island developing States.

Promoting Financial Inclusion

26. The participants stressed the importance of enhancing access to financial services both to reduce poverty and to promote economic growth and employment generation through the dynamism of small and medium enterprises (SMEs). In this regard, they recognized the enormous potential of FinTech companies in enhancing financial inclusion. However, they also pointed out to potential risks to financial stability that can arise if the expansion in the access to credit in the economy occurs too rapidly. Risks include excessive indebtedness of low-income borrowers, illegal deposit mobilization, fraud, high transaction costs, and exploitation of customers.

27. To prevent these risks, participants emphasized the need to develop appropriate supervision and regulatory frameworks to support the extension of financial inclusion. In this regard, some participants noted the usefulness of a proportionate approach to regulation, which adjusts prudential norms according to the risk profile and systemic importance of particular banks and microfinance institutions. They highlighted the need for capacity building in setting and implementing new regulations for promoting financial inclusion, for which ESCAP, as an intergovernmental platform covering the entire region, could play an important role.

28. The participants also highlighted the importance of extending financial education to new users of financial services and to strengthen consumer protection regimes. They also emphasized the importance of building stronger financial infrastructure, in particular to ensure that financial transactions take place in a timely and secure manner.